

DELIVER

Consistent with the plans we laid out in November 2015, we have enhanced the financial disclosures for all our reporting segments to include gross margin, R&D and other costs below gross margin, as well as restructuring charges. In addition, within Civil Aerospace we have provided additional revenue segmentation and a trading cash flow breakdown. These disclosures apply to both 2014 and 2015 and should help further analysis of trading performance.

Order book and order intake

During the year our order book increased by £2.7bn to £76.4bn. Key orders included our record single order from Emirates for 200 Trent 900 engines which contributed \$6.1bn to the order book. Throughout the year new order intake in our Marine business was very weak, driven by significant market deterioration in offshore. Overall, orders were lower in Defence and Nuclear, although we view the prospects for these businesses as unchanged, reflecting long-term orders won in previous years.

Underlying trading

Underlying Group revenue declined 1% in 2015 compared to 2014 on a constant currency basis. This reflects a 5% decline in revenue from original equipment, partially offset by a 4% increase in services revenue, led by Civil Aerospace. By business on a constant currency basis, Civil Aerospace revenue increased 3%, Defence Aerospace revenue decreased 5%, Power Systems revenue decreased 3%, Marine revenue decreased 16% and Nuclear revenue increased 9%.

Underlying profit before financing of £1,492m (2014: £1,681m) was 11% lower on a constant currency basis, led by a significant reduction in Marine profit, driven by weak offshore markets in particular. Civil Aerospace was down year-on-year, although performance was helped by around £222m of retrospective benefits (2014: £150m) led by refining the basis for taking account of risk in our forecasts of

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We have significantly enhanced this year's Annual Report with additional disclosures to increase transparency and understanding.”

David Smith
Chief Financial Officer



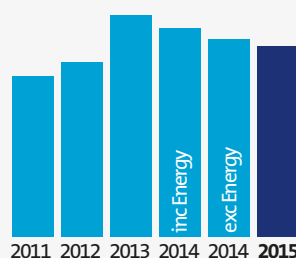
GROUP TRADING SUMMARY

£m	2014	Underlying change	Acquisitions & disposals	Foreign exchange	2015
Order book	73,674	2,725	—	—	76,399
Underlying revenue	13,864	(96)	—	(414)	13,354
<i>Change</i>		-1%	—	-3%	-4%
Underlying OE revenue	7,418	(363)	—	(331)	6,724
<i>Change</i>		-5%	—	-5%	-9%
Underlying services revenue	6,446	267	—	(83)	6,630
<i>Change</i>		+4%	—	-1%	+3%
Underlying gross margin	3,523	(251)	—	(90)	3,182
<i>Gross margin %</i>	<i>25.4%</i>	<i>-160bps</i>	—	—	<i>23.8%</i>
Corporate and administrative costs	(1,069)	11	—	54	(1,004)
Restructuring costs	(149)	107	—	3	(39)
Research and development costs	(730)	(64)	—	29	(765)
Joint ventures and associates	106	10	—	2	118
Underlying profit before financing	1,681	(187)	—	(2)	1,492
<i>Change</i>		-11%	—	—	-11%
Underlying operating margin	12.1%	-130bps	—	—	11.2%

Underlying revenue

£13,354m

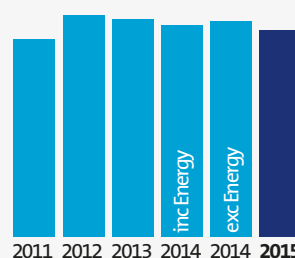
2014 exc	£13,864m
2014 inc	£14,588m
2013	£15,505m
2012	£12,209m
2011	£11,277m



Underlying operating margin

11.2%

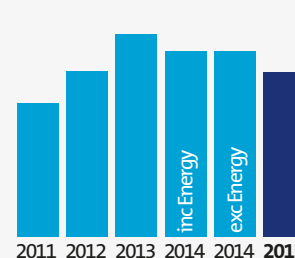
2014 exc	12.1%
2014 inc	11.5%
2013	11.8%
2012	12.0%
2011	10.7%



Underlying profit before financing

£1,492m

2014 exc	£1,681m
2014 inc	£1,678m
2013	£1,831m
2012	£1,495m
2011	£1,206m



future revenue on long-term contracts, and the reversal of previously recognised impairment on contractual aftermarket rights (CARs) and release of a related provision. Defence Aerospace delivered an improved year-on-year profit which included one-time contract benefits, led by contract extensions and reduced long-term costs. Power Systems was down year-on-year in line with our expectations on a constant currency basis as the business managed well within a number of weaker markets. Marine, as expected, was sharply lower, reflecting the weak oil & gas offshore sector and Nuclear was in line, after excluding the positive R&D credit.

The R&D charge increased 11% over 2014 on a constant currency basis, largely reflecting ongoing investments in Civil Aerospace for the Trent 1000 TEN and Trent XWB-97, together with higher spending on the Trent 7000 and corporate jet programmes. In addition, we increased investment in future technology demonstrator programmes and improved emissions solutions for Power Systems applications. In addition, capitalisation of R&D declined significantly largely due to the entry

into service of the Trent XWB-84 in January 2015 and increased recognition of entry fees.

Underlying financing charges were £60m (2014: £61m). Underlying profit before tax was £1,432m (2014: £1,620m). The underlying tax charge was £351m, with an effective tax rate of 24.5% (2014: 24.0%).

Free cash flow

Cash capital expenditure in 2015 reduced to £479m (2014: £616m), largely reflecting lower spend on new aerospace facilities. Cash taxes were £160m (2014: £265m excluding Energy). The cash cost of defined benefit pension schemes in excess of the earnings charge was £46m (2014: £154m excluding Energy).

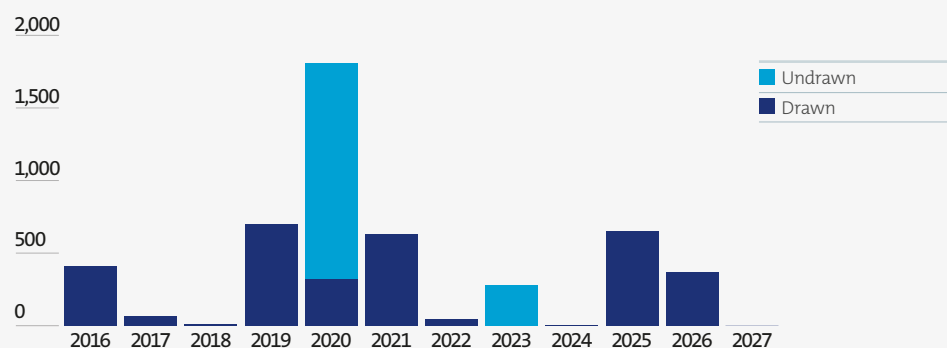
Overall, the free cash inflow for the year was £179m (2014: inflow of £447m, adjusted for Energy). The significant decline from 2014 primarily reflects lower trading margins and adverse working capital movements. The TotalCare net asset movement year-on-year was slightly higher than expectations.

Net debt

The Group is committed to maintaining a robust balance sheet and a strong, investment-grade credit rating, which it believes are important when selling products which will be in service for decades. Standard & Poor's updated its rating in January 2016 to A/negative outlook and Moody's maintained a rating of A3/stable.

At the end of 2015, the Group's net cash balance reduced from £666m to a net debt position of £111m, reflecting the £179m positive free cash inflow, share repurchases totalling £414m and shareholder payments of £421m. Other items include residual payments related to the divestment of the Energy business and non-cash foreign exchange movements. On 6 July 2015, we announced that we had curtailed the share buyback associated with the Energy business sale at the to-date total of £500m, including the shares purchased in 2014. During the year we refinanced our revolving credit facility, increasing it to £1.5bn, and issued two new US bonds, totalling US\$1.5bn.

Debt retirement (£m)



FINANCIAL REVIEW CONTINUED

Results broadly in line with the expectations set out in July 2015

UNDERLYING INCOME STATEMENT

£m	2015	2014	Change
Revenue	13,354	13,864	-510
Gross profit	3,182	3,523	-341
Commercial and administrative costs	(1,004)	(1,069)	+65
Restructuring	(39)	(149)	+110
Research and development costs	(765)	(730)	-35
Share of results of joint ventures and associates	118	106	+12
Profit before financing	1,492	1,681	-189
Net financing	(60)	(61)	+1
Profit before tax	1,432	1,620	-188
Tax	(351)	(388)	+37
Profit for the year	1,081	1,232	-151
Earnings per share (EPS)	58.73p	65.42p	-6.69p
Payment to shareholders	16.37p	23.10p	-6.73p
Gross R&D investment	(1,240)	(1,249)	+9
Net R&D charge	(765)	(730)	-35

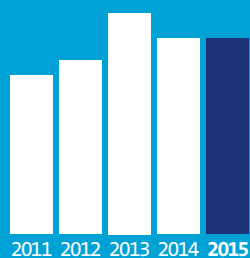
SEGMENTAL ANALYSIS

£m	Revenue			Gross profit			Profit before financing		
	2015	2014	Change	2015	2014	Change	2015	2014	Change
Civil	6,933	6,837	+96	1,526	1,675	-149	812	942	-130
Defence	2,035	2,069	-34	579	567	+12	393	366	+27
Aerospace Division	8,968	8,906	+62	2,105	2,242	-137	1,205	1,308	-103
Power Systems	2,385	2,720	-335	635	742	-107	194	253	-59
Marine	1,324	1,709	-385	260	425	-165	15	138	-123
Nuclear	687	638	+49	111	119	-8	70	50	+20
Other	96	46	+50	64	8	+56	52	(2)	+54
Intra-segment	(106)	(155)	+49	7	(13)	+20	7	(13)	+20
Land & Sea Division	4,386	4,958	-572	1,077	1,281	-204	338	426	-88
Central costs							(51)	(53)	+2
Group	13,354	13,864	-510	3,182	3,523	-341	1,492	1,681	-189

Reported revenue

£13,725m

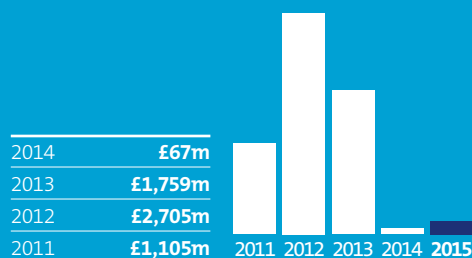
2014	£13,736m
2013	£15,513m
2012	£12,161m
2011	£11,124m



Reported profit before taxation

£160m

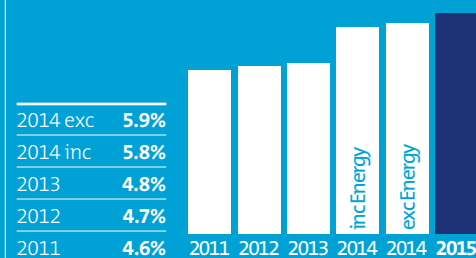
2014	£67m
2013	£1,759m
2012	£2,705m
2011	£1,105m



Net R&D as a proportion of underlying revenue

6.2%

2014 exc	5.9%
2014 inc	5.8%
2013	4.8%
2012	4.7%
2011	4.6%



Underlying income statement

The 'Other' category in the segmental analysis includes residual retained assets relating to the Energy business which were not included in the sale to Siemens in 2014 and a one-off intellectual property settlement of £58m. The value of these is not material to the Group.

Underlying profit before financing and taxation is discussed in the Business review on pages 22 to 41.

Underlying financing costs were stable versus 2014. An increase in net interest of £13m was offset by changes in other underlying financing costs. An underlying foreign exchange gain of £34m is included, arising from realised gains on foreign exchange contracts settled to translate overseas dividends into sterling.

Underlying taxation was £351m, an underlying tax rate of 24.5% compared with 24.0% in 2014.

Underlying EPS was lower reflecting the reduction in underlying profit after tax, partially offset by a reduction in the average number of shares as a result of the share buyback.

At the Annual General Meeting on 5 May 2016, the Directors will recommend an issue of 71 C Shares with a total nominal value of 7.1p for each ordinary share. Together with the interim issue on 4 January 2016 of 92.7 C Shares for each ordinary share with a total nominal value of 9.27p; this is the equivalent of a total annual payment to ordinary shareholders of 16.37p for each ordinary share. Further details are included on page 178.

Reported results

Consistent with past practice and IFRS accounting standards, the Group provides both reported and underlying figures. We believe underlying figures are more representative of the trading performance, by excluding the impact of year-end mark-to-market adjustments, principally the GBP:USD hedge book. In addition, financing of post-retirement benefits, effects of acquisition accounting and impairment of goodwill are also excluded. Adjustments between underlying profit and reported profit in the income statement are set out in more detail in note 2 to the Consolidated Financial Statements. This basis of presentation has been applied consistently.

PROFIT BEFORE TAXATION

£m	2015	2014
Underlying profit before tax	1,432	1,620
Mark-to-market of derivatives and related adjustments	(1,065)	(1,258)
Movements on other financial instruments	8	(87)
Effects of acquisition accounting	(124)	(142)
Exceptional restructuring	(49)	(39)
Acquisitions and disposals	2	8
Impairment of goodwill	(75)	—
Post-retirement scheme financing	32	(29)
Other	(1)	(6)
Reported profit before tax from continuing operations	160	67

Mark-to-market adjustments are principally driven by movements in the GBP:USD exchange rate which moved from 1.56 to 1.48 during 2015.

Movements in other financial instruments relate entirely to financial risk and revenue sharing arrangements. The put option on the non-controlling interest in Power Systems was exercised in 2014, so this had no impact in 2015.

The effects of acquisition accounting in accordance with IFRS 3 are excluded from underlying profit so that all businesses are measured on an equivalent basis. Impairment of goodwill principally relates to the Marine business.

Costs associated with the substantial closure, or exit from, a site, facility or activity are classified as exceptional restructuring and excluded.

Profits and losses arising on acquisitions and disposals during the year are excluded.

Net financing on post-retirement schemes is excluded from underlying profit.

Appropriate tax rates are applied to these adjustments, the net effect of which was an increase of £275m in the reported tax charge (2014: £237m increase, including a £64m reduction in the amount of recoverable advance corporation tax recognised).

The 2014 reported results also included £142m relating to discontinued operations.

Balance sheet

Intangible assets (note 9) represent long-term assets of the Group. These assets decreased by £159m in the year, with additions of £408m being more than offset by amortisation of £407m, impairments to goodwill of £75m (including £69m Marine impairment reported in the first half) and exchange losses of £134m (largely relating to euro-denominated intangible assets arising from the acquisition of Rolls-Royce Power Systems AG).

The CARs balance increased by £156m to £405m. The increase included £50m arising from the reversal of previously recognised impairments. During the year, following analysis of the first major overhauls of Trent 1000 engines, the recoverable amount of certain CARs has been reassessed. This demonstrated that aftermarket cash flows from these engines are better than originally assumed, arising from both operational and contractual performance improvements. Accordingly, cumulative impairments prior to 2015 of £50m have been reversed. This has resulted in the capitalisation of £22m of CARs in 2015 that would otherwise have been impaired, including £16m recognised in the interim results.

FINANCIAL REVIEW CONTINUED

SUMMARY BALANCE SHEET

£m	2015	2014
Intangible assets	4,645	4,804
Property, plant and equipment	3,490	3,446
Joint ventures and associates	576	539
Net working capital	(501)	(1,134)
Net funds	(111)	666
Provisions	(640)	(807)
Net post-retirement scheme (deficits)/surpluses	(77)	555
Net financial assets and liabilities	(1,883)	(855)
Other net assets and liabilities	(483)	(827)
Net assets	5,016	6,387
Other items		
US\$ hedge book (US\$bn)	28.8	25.6
TotalCare assets	2,994	2,492
TotalCare liabilities	(783)	(687)
Net TotalCare assets	2,211	1,805
Customer financing contingent commitments:		
Gross	269	388
Net	54	59

Carrying values of intangible assets are assessed for impairment against the present value of forecast cash flows generated by the intangible asset. The principal risks remain: reductions in assumed market share; programme timings; increases in unit cost assumptions; and adverse movements in discount rates. Other than noted above, there have been no significant impairments in 2015.

Property, plant and equipment (note 10) increased by £44m. Capital expenditure of £494m was largely offset by depreciation of £373m, disposals of £34m and foreign exchange movements of £32m.

Investments in joint ventures and associates (note 11) increased modestly, principally as the share of retained profit exceeded dividends received.

Net post-retirement scheme (deficits)/surpluses (note 19) decreased by £632m, comprising a reduction of £692m in the UK and an increase of £60m overseas.

The reduction in UK schemes is principally due to relative movements in assumptions used to value the underlying assets and liabilities in the UK schemes in accordance

with IAS 19. While the corporate bond yields used to measure the liabilities remained broadly stable, gilt yields which are the principal driver of asset valuations increased, reducing the value of the assets. The schemes adopt a low risk investment strategy that reduces funding volatility (for which both assets and liabilities are measured on a gilt basis); interest rate and inflation risks are largely hedged and the exposure to equities is around 9% of scheme assets.

The increase in overseas schemes arose largely due to higher discount rates in Germany and the US.

Provisions (note 18) largely relate to warranties and guarantees provided to secure the sale of OE and services. The decrease is largely a result of the utilisation of warranty and restructuring provisions.

Net financial assets and liabilities (note 17) include the fair value of derivatives, financial RSSAs and C Shares. The increase in liabilities primarily reflects the impact on the US\$ hedge book of the GBP:USD exchange rate falling to 1.48 from 1.56 at the beginning of the year.

The Group hedges transactional foreign exchange exposures to reduce volatility. The most significant exposure is net US\$ income. The US\$ hedge book increased by 12.5% to US\$28.8bn, which represents around five years of net exposure and has an average book rate of £1 to US\$1.59.

Net TotalCare assets relate to long-term service agreement contracts in the Civil Aerospace business, including the flagship services product TotalCare. These assets represent the timing difference between the recognition of income and costs in the income statement and cash receipts and payments.

The net asset increased in 2015 by £406m (2014: £463m), reflecting accounting for new 'linked' engines of £521m (2014: £588m) and retrospective TotalCare accounting adjustments of £222m (2014: £150m) taken in the year, offset by cash flows and other items of £337m (2014: £275m).

Customer financing facilitates the sale of OE and services by providing financing support to certain customers. Where such support is provided by the Group, it is almost exclusively to customers of the Civil Aerospace business and takes the form of various types of credit

and asset value guarantees. These exposures produce contingent liabilities that are outlined in note 18. Contingent liabilities represent the maximum aggregate discounted gross and net exposure in respect of delivered aircraft, regardless of the point in time at which such exposures may arise. During 2015, the Group's gross exposure on delivered aircraft reduced by £119m, mainly due to guarantees expiring.

Summary funds flow

Movement in working capital includes an increase in the net TotalCare asset of £406m and a reduction in the amount of net customer deposits of £143m. The reduction in customer deposits is largely in the Marine business as a result of lower order intake in the offshore market and lower government spend.

Expenditure on property, plant and equipment and intangible assets: the decrease reflects reductions in additions to property, plant and equipment (£174m), participation fees and certification costs (£86m) and capitalised development costs (£45m), offset by increased expenditure on contractual aftermarket rights (£68m) and foreign exchange movements of £51m.

Pensions: contributions to defined benefit pension schemes in 2015 reduced by £63m, which included a reduction in the UK deficit funding payments of £36m and the non-recurrence of discretionary increase contributions of £33m. The total operating charge increased by £43m largely due to past service credits of £8m in 2015 compared to £31m in 2014. Funding of defined benefit schemes is expected to be similar in 2016.

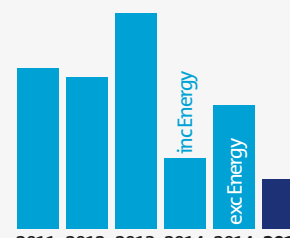
Shareholder payments: the reduction reflects the fact that no dividend was paid by Power Systems to Daimler AG (2014: £76m), offset by an increase in the redemption of C Shares of £15m.

Discontinued operations in 2015 reflect a sales price adjustment of £42m paid in 2015 on the 2014 disposal of the Energy business and wind-down costs.

Free cash flow

£179m

2014 exc	447					
2014 inc	254					
2013	781					
2012	548					
2011	581					
		2011	2012	2013	2014	2015



SUMMARY FUNDS FLOW

£m	2015	Previously reported	2014	Excluding Energy	Change
			Energy		
Opening net funds	666	1,939			
Closing net funds	(111)	666			
Change in net funds	(777)	(1,273)			
Underlying profit before tax	1,432	1,617	(3)	1,620	-188
Depreciation and amortisation	613	600	18	582	+31
Movement in net working capital	(544)	(509)	(152)	(357)	-187
Expenditure on property, plant and equipment and intangible assets	(887)	(1,114)	(30)	(1,084)	+197
Other	(229)	88	(17)	105	-334
Trading cash flow	385	682	(184)	866	-481
Contributions to defined benefit post-retirement schemes in excess of PBT charge	(46)	(152)	2	(154)	+108
Tax	(160)	(276)	(11)	(265)	+105
Free cash flow	179	254	(193)	447	-268
Shareholder payments	(421)	(482)	—	(482)	+61
Share buyback	(414)	(69)	—	(69)	-345
Acquisitions and disposals	(3)	(965)	—	(965)	+962
Net funds of businesses acquired	—	(30)	—	(30)	+30
Discontinued operations	(121)	—	193	(193)	+72
Foreign exchange	3	19	—	19	-16
Change in net funds	(777)	(1,273)	—	(1,273)	