Thursday 26 May 2005

BABCOCK INTERNATIONAL GROUP PLC

2004/5 PRELIMINARY RESULTS

Babcock International Group PLC, the Support Services company, announces its preliminary results for the year ended 31 March 2005:

	2004/5	2003/4	% Change
Sales	**£760.0m**	£452.0m	68
Operating profit (1)	**£41.0m**	£25.5m	61
Profit before tax	**£28.4m**	£19.8m	43
Profit before tax-adjusted (2)	**£35.1m**	£23.1m	52
Earnings per share (3)	**14.20p**	13.60p	4.4
Dividend	**4.00p**	3.35p	19.4

(1) Before goodwill amortisation (2005: £6.6 million, 2004: £3.3 million), discontinued operations losses (2005: £nil, 2004: £0.3 million) and operating exceptionals (2005: £1.5 million credit, 2004: £nil), (2) Before goodwill amortisation, exceptional items (2005: pre-tax £(0.1) million, 2004; £nil) (3) Before exceptional items (2005: £0.3 million credit, 2004: £nil) and goodwill amortisation.

Business Highlights:

- Successful acquisition and integration of Peterhouse – earnings enhancing in year one
- Babcock-led consortium appointed preferred bidder on Royal School of Military Engineering PFI
- 5 year extension to contract for management of HM Naval Base Clyde expected imminently – worth £400 million
- Continued growth in sales and profits in existing businesses
- Sales up by 68%, profit before tax up 43%
- Earnings per share up by 4.4% despite increased tax charge
- Full year dividend raised by 19.4% - final payment up 26% to 2.65p
- Order book as at 25 May £1.2 billion up from £1.1 billion last year

Commenting, Peter Rogers, Chief Executive, said:

"This has been another excellent year for Babcock, with sales increasing by 68% and adjusted profit before tax growing by 52%. Notable achievements during the year included our appointment as preferred bidder on the Royal School of Military Engineering PFI contract and the award of a five year extension to the contract for the management of HM Naval Base Clyde, which is expected imminently, a year earlier than anticipated.

"We have now established a solid foundation to take the company forward, with a broadened customer base. This follows on from the successful acquisition of Peterhouse, which has exceeded our expectations at the time of transaction. We are well positioned in a number of growing markets and our skills in project planning design and engineering are now well-recognised in the sectors in which we operate.

"This is the third successive year of double digit sales and profit growth and Babcock is well positioned to achieve continued growth going forward."

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CHAIRMAN'S STATEMENT

Four years ago we embarked on a process to convert Babcock from an engineering conglomerate to a support services business. I said last year, that the year ending March 2004 completed the first phase of this transformation, which was predicated upon being a major service supplier to the defence sector. The second phase was to broaden our customer base so that we were not overly reliant on any one market sector. The acquisition of Peterhouse, concluded in June 2004, marked the start of this second phase. The acquisition has been extremely successful and the businesses are now largely integrated into Babcock. The synergies anticipated were achieved as quickly as we could possibly have hoped, and hence the acquisition was earnings enhancing in the year ended March 2005, somewhat earlier than had been predicted in the Offer documents. Equally our cash management skills have reduced the debt taken on to acquire the Peterhouse business very rapidly, such that our debt at March 2005 was only £63 million.

The results to March 2005 continue to support our strategy. Profit before tax before goodwill and exceptional items increased by 52% following on from an increase the previous year of 28%. Operating profit, before goodwill and exceptional items, increased by 63% year on year, but this was by no means all due to the Peterhouse acquisition. The existing Babcock businesses also increased their operating profit by a reassuring 18%.

The success of the strategy is also marked by the better balance of our sales. Sales to the Ministry of Defence fell from 70% of turnover in the year to March 2004 to approximately 50% in 2004/5. The defence sector remains an important part of our business but the presence in higher growth sectors such as telecommunications and power transmission gives the results more robustness. Our South African business also continues its dynamic growth, and we have positioned Rosyth to withstand the sharp decline in the refit business without undermining its ability to resource adequately the assembly and integration of the new aircraft carriers.

Earnings per share before goodwill and exceptional items in the year to March 2005 increased by 4.4% to 14.2p per share. With a comparable year on year tax charge the increase would have been 15%. The Directors have been conscious throughout this major transformation of Babcock of the need for tight controls on cash, but with a much larger and better balanced business we feel that shareholders should be rewarded by a substantial increase in dividends whilst maintaining a conservative cover. Over the medium term we intend to target dividend cover, based on full year earnings excluding goodwill amortisation and exceptional items, in the range 2.5 – 3.0 times based on current accounting principles. As a consequence, the Board is recommending a 26% increase in the final dividend to 2.65p per share, which will take the total dividend for the year up to 4p per share, an increase over last year of 19.4%.

The introduction of IFRS as the method of accounting for UK companies does not have a significant effect on the 2004/05 earnings of Babcock, although there is some redistribution between operating profit and interest. IFRS accounting will be introduced in the year ending March 2006.

The Report and Accounts will show our compliance with the Combined Code and a number of minor changes as a result of the Higgs recommendations. In the few cases where we do not comply fully with the Combined Code we shall explain our reasoning in the Report and Accounts. However, a number of our Non-Executive Directors have held their positions for long periods by the standards of Higgs recommendations. Notwithstanding, therefore, their outstanding contribution to the company over this period of time, we shall be implementing a programme of change amongst the Non-Executive Directors. However, we feel it important that this be carried out in a controlled manner such that we do not lose the substantial benefit of their experience. This change will therefore be carried out progressively over the next couple of years.

The two most important decisions a Board can make in large companies is to choose the strategy and to identify and select the best people to implement that strategy. I think the history over the last five years suggests that we have made both decisions with some skill, and the increase in shareholder value over those five years is a testimony to that. Over the five years ending March 31 2005, £100 invested in Babcock would have yielded a return of 124% more than a similar investment in the FTSE All-Share index.

I am sure that shareholders would wish me to thank all employees who have contributed to such an outstanding performance and I believe that, with the acquisition of Peterhouse, we shall continue to improve value for our shareholders.

CHIEF EXECUTIVE'S OPERATING STATEMENT

The 2004/05 Financial Year has been both successful and highly active for Babcock. The acquisition and integration of Peterhouse, and subsequently Turner & Partners, the start of the South West Regional Prime Contract, the first year of the contract at RAF Valley, significant reorganisation in our marine-based business and movement to preferred bidder on RSME all took place during the Financial Year. The result of all this activity is that sales from continuing operations have risen by £322 million or 74% and operating profit from continuing operations before goodwill and exceptional items has risen by £15.5 million or 61%.

The integration of the former Peterhouse businesses continued to occupy significant amounts of management time but synergy benefits totalling £9 million compared to the £5.3 million contained in the Offer documents had been identified by 31 March 2005.

Most significantly the development of a better balanced portfolio of businesses, most of which are in growing markets, has laid solid foundations which should allow the company to continue double digit sales and profit growth in the coming years.

Defence Services

Sales £245.1m (2004 : £171.5m) Operating profit £17.8m (2004 : £11.6m)
(32% of Group Sales)

Growth in sales was largely driven by the April 1, 2004 start of the South West Regional Prime (SWRP) Contract. We expect further growth in sales during the current year as the contract will be fully operational throughout the period. Naval Services also showed some growth in turnover and margin as the scope of the contract increased and our confidence in delivering the contracted cost reduction targets improved. The announcement by the Ministry of Defence that the contract will be extended by an additional 5 years, which is expected imminently, will further enhance the order book.

We continue to deliver excellent service to the customer across the range of businesses. At HM Naval Base Clyde customer satisfaction surveys show that, despite the significant cost savings we are achieving, our customers rate our service as significantly better than that which was being delivered previously. Similarly, we have been complimented on our activities in relation to contracts at RAF Valley, RAF Lyneham and on SWRP on each of which we are also delivering substantial savings to the customer.

A notable step forward in the second half of the year was the award of Preferred Bidder Status on the Royal School of Military Engineering (RSME) PFI to the Holdfast consortium led by Babcock. We had been sole bidder for almost three years and internal difficulties in the Ministry of Defence (MoD) had prevented the project moving forward. We are now aiming, with the MoD, to achieve financial close during the 2006/07 Financial Year.

We are involved in the MoD's Marine Services PFI as part of the Starfish Marine consortium, one of two bidders for this large project. Other significant bids on which we are working include the Eastern Regional Prime Contract and Projects for managing the ministry estates in Cyprus and Gibraltar. We are also working towards submitting bids on a number of opportunities in the 'Building Schools for the Future' programme.

The major project on which we are currently bidding (again as leader of the Holdfast Consortium) is the Defence Training Review which is a PFI for the management and delivery of approximately half of the three services non-military training. The award of this contract should take place during the 2006/07 financial year.

Technical Services

Sales £160.2m (2004 : £180.0m) Operating profit £13.1m* (2004 : £14.8m)
(21% of Group sales)
* before exceptional charge of £5.5m (2004 : £nil)

This is the business based at Rosyth. We carried out significant reorganisation during the year in recognition of the fact that the allocated programmed for warship refit is coming to an end in March 2006 and in further recognition of the fact that the market for warship refit will be somewhat smaller over the next few years. The reorganisation so far has enabled us, we believe, to become the lowest cost warship refit yard in the UK and we are therefore confident of our ability to compete in the reduced market. We won 8 of the last 13 competitive bids during the year and we are confident of our ability to continue to bid both successfully and profitably.

We have moved the businesses based at Rosyth from a position two years ago where they were almost wholly dependent for profits on the warship refitting programme to a position in which they would be a profitable group of businesses even in the unlikely event of the refit market dropping to zero. A regrettable consequence of this reorganisation is the reduction in the Rosyth workforce from some 1800 people to under 1200 by March 2006.

We are continuing to participate in the programme for construction of the new aircraft carriers. While no contracts have yet been awarded, other than for design, we remain confident that Rosyth will be the location selected for the assembly and integration of the two ships, on the grounds of the excellent facilities and the skills of the workforce. These have also played a large part in the success of the modular construction work we are carrying out for Heathrow Terminal 5.

We are participating in discussions with the MoD on the ISOLUS programme – which is a programme for the dismantling and storage of defuelled nuclear submarines. Any contract awarded under the ISOLUS programme will be for over 20 years.

The Supply Chain Services, Design and Technology and nuclear businesses are all profitable in their own right. We are continuing to bid for naval refit work and are seeking opportunities to expand the scope of the Engineered Products business.

Engineering and Plant Services

Sales £113.0 (2004 : £86.5m) Operating profit £5.5m (2004 : £3.5m)
(15% of Group sales)

The African business has continued its outstanding progress during the year with sales at over £100 million for the first time and profits exceeding £5 million. The growth resulted mainly from the growth in the Construction Equipment business which sells Volvo equipment largely to the mining and construction industries. Our market share continued to increase and the parts aftermarket is growing as the number of Volvo vehicles on the ground continues to expand. Increasing sales in the aftermarket will give opportunities for further margin improvement.

The African engineering business continued its excellent progress with profitability again improving. The need to continue increasing both active generation capacity and infrastructure support in Africa will provide a more stable environment for the engineering business than has been the case for a number of years.

Eagleton, our pipeline business in Houston Texas, had another challenging year as the market continued at very low levels, although towards the end of the year there were clear signs of increased activity driven by the continuing high price levels for oil and gas.

Networks

Sales £61.5m (2004 : £n/a) Operating profit £4.1m (2004 : £n/a) [for period of 9.5 months]
(8% of Group sales)

Since the acquisition of Peterhouse, the Networks businesses (which trade under the 'Eve' name) have performed somewhat better than we had anticipated. In the telecoms business, the launch of 3G technology by the network operators is taking place on a more gradual basis than many had expected, but has been in line with our expectations at the time of the acquisition. With the purchase of Turner and Partners we continue to win contracts for the acquisition design and construction of new sites thereby strengthening the core business as well as adding valuable skills. The combination of the skills of Eve and Turners is proving attractive to customers. A number of contracts with the major operators have been secured, including Vodafone, Orange and 3.

The transmission business continues to deliver an excellent performance with the volume of work continuing to rise, at a slightly faster rate than our original expectations. The volume of pre-sanction engineering work also continues to rise, which is usually a predictor of the volume of contracts to be let over the next two years.

Eve Trakway had a reasonable winter and spring period as its share of the industrial market grew and is now profitable. We have invested in further capacity in this business to ensure we maintain our ability to provide outstanding levels of service to our customers.

Rail

Sales £167.0m (2004 : £n/a) Operating profit £8.3m* (2004 : £n/a) [for period of 9.5 months]

(22% of Group sales)

* before operating exceptional credit of £8.8m

The rail business (First Engineering) has met our original expectations at the time of acquisition. Although the market for signalling was somewhat slower than we had anticipated the track renewals business remained extremely busy throughout our period of ownership. There are clear signs that the rate of placement for signalling and communication contracts will increase over the coming months while track renewals will continue to perform well. The high output renewals contract is continuing to develop well and First Engineering is now responsible for the Facilities Management (Mechanical and Electrical Maintenance) for all Network Rail's major stations.

Significant first steps have been taken to align overheads with the new structure of First Engineering following the handing back of maintenance work to Network Rail in June 2004. Further savings are planned including the consolidation of all Glasgow operations into a single building at Hamilton International Park at the end of the 2005/06 Financial Year.

Health, Safety and Environmental

Sales £13.2m (2004 : £n/a) Operating loss £1.2m (2004 : £n/a) [for period of 9.5 months]
(2% of Group sales)

The two smallest businesses acquired with Peterhouse are in the process of disposal. Neither IETG nor ESS (flow monitoring and safety equipment and training) is regarded as core and we are aiming for completion of the processes before the end of September.

Summary and Prospects

As I said in November, credit is due to the operational management of the businesses for a strong performance, despite the inevitable distractions of the acquisition and integration of Peterhouse. The forecast integration savings have been achieved and we expect that further savings will be realised.

During the last year we have positioned Babcock to take advantage of the growing markets in which we operate. We now have a balanced portfolio of businesses and customers. We have continued to grow sales and profits in existing businesses by over 10% a year while successfully integrating a significant acquisition.

We are well placed to continue the growth in both sales and profits in the coming years and to become a major force in the public sector outsourcing markets and in other technically demanding markets.

FINANCIAL REVIEW

Results of operations – summary analysis

To assist in understanding how events have impacted the Group, we have set out in the tables below an analysis of existing and acquired operations, as such all operating profit numbers quoted in the table are before charging goodwill amortisation and operating and non-operating exceptional items.

	Turnover		Operating profit		Net margin		Growth	
	2004/05	2003/04	**2004/05**	2003/04	**2004/05**	2003/04	**T/over**	**Op. profit**
	£m	£m	**£m**	£m	**%**	%	**%**	**%**
Defence Services	**245.1**	171.5	**17.8**	11.6	**7.3%**	6.8%	**43%**	**53%**
Technical Services	**160.2**	180.0	**13.1**	14.8	**8.2%**	8.2%	**(11)%**	**(12)%**
Engineering & Plant	**113.0**	86.5	**5.5**	3.5	**4.9%**	4.0%	**31%**	**57%**
Unallocated			**(6.4)**	(4.4)				
Existing	**518.3**	**438.0**	**30.0**	**25.5**	**5.8%**	5.8%	**18%**	**18%**
Networks	**61.5**	-	**4.1**	-	**6.7%**	-	-	-
Rail	**167.0**	-	**8.3**	-	**5.0%**	-	-	-
HS&E	**13.2**	-	**(1.2)**	-		-	-	-
Unallocated			**(0.2)**					
Acquisitions	**241.7**	-	**11.0**	-	**4.6%**	-	-	-
Disposals	-	14.0	-	(0.3)	-	-	-	-
Total pre-goodwill and exceptional items	**760.0**	**452.0**	**41.0**	**25.2**	**5.4%**	5.6%	**68%**	**63%**

Sales and operating profits from continuing businesses were substantially increased from those of last year as a result of both organic and acquisition related growth and, as we reported at the interim stage, the performance of the existing businesses and that of the newly acquired Peterhouse businesses has been strong. The acquired businesses met our expectations for the nine months that they formed part of the Babcock group.

Turnover was 68% above that of the previous year or 18% up after excluding the effect of acquisitions. Operating profit increased by 63% to £41 million, representing a net margin of 5.4% against 5.6% last year. On existing businesses, operating profit increased 18% with margins in line with last year at 5.8%.

Existing businesses

Within the existing businesses, Defence Services performed strongly both in turnover and operating profit with net margins up from 6.8% to 7.3% driven by a combination of the start of South West Regional Prime and further growth in the HM Naval Base Clyde contract. Conversely and as anticipated, revenues declined in Technical Services in the face of lower naval re-fit activity but timely realignment of the cost base enabled margins to be sustained at 8.2%. Continued strong growth in the African operations on improved margins yielded turnover in excess of £100 million and an operating profit improvement of over 50%.

Acquisitions

The former Peterhouse businesses, included for nine months, added £11 million in operating profit on £242 million of turnover, a net margin of 4.6%. The Networks business benefited from ongoing growth in both the high voltage power supply market and the mobile phone transmission market and operating margins totalled 6.7%. The latter included a contribution to operating profit of £0.5 million from Turner and Partners, which was acquired in September 2004. In Rail the strong growth recorded in track renewals more than offset any softness in other rail activities to deliver turnover of £167 million and, following adjustment of the cost base (post the transfer of rail maintenance work to Network Rail in June 2004) an operating margin of 5%. Conversely, the performance of the non-core Health, Safety and Environmental businesses was worse than anticipated, losing £1.2 million in market conditions weakened by delays in expenditure on the regulated assets of the utility companies that are the division's key customers.

Reconciliation to statutory profit and loss

The following table reconciles the results quoted above to the figures reported in the statutory accounts.

	Turnover		Operating profit		Net margin		Growth	
	2004/05	2003/04	**2004/05**	2003/04	**2004/05**	2003/04	**T/over**	**Op. profit**
	£m	£m	**£m**	£m	**%**	%	**%**	**%**
Total pre-goodwill and exceptional items	**760.0**	452.0	**41.0**	25.2	**5.4%**	5.6%	**68%**	63%
Operating exceptional items:								
On acquisitions			**7.0**	-				
On existing			**(5.5)**	-				
Total			**1.5**	-				
Amortisation of goodwill:								
On acquisitions			**(3.4)**	-				
On exisiting			**(3.2)**	(3.3)				
Total			**(6.6)**	(3.3)				
Statutory operating results	**760.0**	452.0	**35.9**	21.9	**4.7%**	4.8%	**68%**	**64%**
Share of joint ventures			**0.3**	0.1				
Non-operating exceptional items			**(1.6)**	(1.7)				
Profit on ordinary activities before interest			**34.6**	20.3				

Exceptional items

The following have been treated as exceptional charges to operating profit.

	Cash £m	**Non-cash £m**	**Total £m**
Reorganisation of marine design and goodwill impairment	**(0.8)**	**(4.7)**	**(5.5)**
Exceptional gain on termination of rail maintenance contracts	**8.8**		**8.8**
Peterhouse rationalisation costs	**(1.8)**		**(1.8)**
Disposals - non-operating	**(1.2)**	**(0.4)**	**(1.6)**
	5.0	**(5.1)**	**(0.1)**

Reorganisation costs and goodwill impairment charges of £5.5 million were incurred in respect of the marine design businesses within Technical Services following the decision to scale down and refocus this division's operations.

Agreement was reached with Network Rail for compensation and other payments to be made by them in respect of the early termination and hand back of rail maintenance contracts formerly run by First Engineering, the Peterhouse subsidiary responsible for rail operations. The net gain after costs of redundancies and other restructuring charges totalled £8.8 million.

Costs incurred in restructuring and integrating the Peterhouse businesses into the group totalled £1.8 million.

Costs totalling £1.6 million in respect of disposals have been charged as a non-operating exceptional item in the year.

Goodwill

Additions to goodwill arose in respect of the acquisitions of Peterhouse Group plc (£81.0) million and Turner and Partners (£7.0 million). Amounts amortised and written off as a result of impairment were £6.6 million and £4.7 million respectively. The impairment write off was made as a result of a scaling down of the activities of the marine design businesses.

Interest and taxation

	2004/05 £m	2003/04 £m
Profit on ordinary activities before interest	**34.6**	20.3
Interest	**(6.2)**	(2.2)
Exceptional gain on financial asset	**-**	1.7
Net interest and similar income/(charges)	**(6.2)**	(0.5)
Profit before tax	**28.4**	19.8
Taxation	**(7.7)**	(3.4)
Profit after tax	**20.7**	16.4

The net interest charge rose to £6.2 million following an increase in net debt arising on acquisition of Peterhouse and for which a new £140 million financing facility was arranged. The total interest charge was covered over 6 times by operating profit before goodwill amortisation and exceptional items.

Pre-tax profit increased 43% to £28.4 million and by 52% to £35.1 million excluding goodwill amortisation and exceptional items.

The group’s effective tax rate for the year was 24%. This compares to a rate of 15.7% last year, which benefited from the utilisation of prior years tax losses. The expected rate for 2005/06 is approximately 26%.

Earnings per share

Basic earnings per share, before goodwill and exceptional items, increased 4.4% to 14.20 pence, despite a significantly higher tax charge and an enlarged issued share capital. After adjusting for the effect of the larger tax charge, underlying growth in earnings per share was 15%.

Cash flow

We continue to underpin good and improving profit performances with strong cash generation and one of our key performance indicators for all operations is the conversion rate of operating profit into cash from operations, after taking into account capital expenditure. The conversion rate for 2004/05 was 115% compared to 120% last year.

After interest and tax payments free cash flow was £30.5 million, (2004; £24.4 million). Capital expenditure, before receipts from assets sold, totalled £5.7 million or less than 1% of turnover and less than 1 times depreciation. On average over the medium term we target to spend no more than 1.5% of turnover or 1 times depreciation, whichever is the greater, on capital assets.

Net debt increased to £62.9 million from £15.4 million last year principally as a result of the acquisition of Peterhouse (cash impact £64.7 million) and Turner and Partners (£4 million) although higher interest payments (£6.1 million against £0.4 million last year) and tax payments (£4.7 million against £1.6 million) both of which benefited from one off gains last year, also impacted. The group has access to a £140 million three year credit line arranged at the time of the Peterhouse acquisition of which £78 million had been drawn down at 31 March 2005.

Cost of capital and return on investment

The group's weighted average cost of capital, which for 2004/05 was 8.7%, is used as one measure in assessing the financial viability of its investments. The after-tax return before goodwill amortisation and exceptional items for 2004/05 was 16%, compared with 20% last year, a decline arising principally from the inclusion of less than a full years operating profit for Peterhouse and Turner and Partners.

Pensions

The group maintains a number of defined benefit pension schemes some of which were acquired with the Peterhouse businesses. In accounting for these schemes the group applies SSAP24 in its consolidated accounts and the transitional rules of FRS17 for disclosure purposes. The balance sheet position under both SSAP24 and FRS17 at 31 March 2005 is as set out in the following table.

	SSAP24		FRS17	
	2004/05 £m	2003/04 £m	**2004/05 £m**	2003/04 £m
Balance sheet surplus/(deficit)	**98.2**	67.2	**(20.4)**	2.0
Related tax (liability)/ asset	**(29.9)**	(20.7)	**5.8**	(0.9)
Net surplus/(deficit)	**68.3**	46.5	**(14.6)**	1.1

Since last year end the inclusion of schemes taken on from Peterhouse has increased the SSAP24 balance sheet surplus substantially with the net surplus standing at £68.3 million at the end of this year. Conversely, under FRS17 the net position has deteriorated from a small surplus last year to a net deficit of £14.6 million at 31 March 2005. The contrast in the valuation status reflects the fundamental difference in assumptions between the two bases; whereas SSAP24 adopts a long term view of funding, FRS17 takes a fair or market value approach to pension fund assets and liabilities, which is likely to lead to increased volatility in balance sheet values. All of the group's principal defined benefit schemes were in actuarial surplus for funding purposes at the last valuation dates. The methodology and assumptions used to calculate the pension assets and liabilities under FRS17 are substantially consistent with the requirements of IAS19, which will be adopted by the Group with effect from 1 April 2005.

Treasury

The Group's policies, which have been reviewed and approved by the Board, cover all significant areas of treasury activity including foreign exchange, interest rates, liquidity and credit risk. The Treasury Committee, which comprises the Group's Chief Executive, Finance Director and Financial Controller, with authorities delegated by the Board, is responsible for ensuring that the Group operates within the policies agreed by the Board.

The Group finances its operations through a combination of retained profits, new equity and bank borrowings. It is policy to ensure that the Group has sufficient financial resources to support the business and to leave a comfortable margin between those facilities and likely peak borrowings during the year. As such, substantial committed facilities are maintained and are currently a £140 million bank facility, which has a maturity date of June 2007.

Interest rate risk is managed through the maintenance of a mixture of fixed and floating rate debt and interest rate caps, each being reviewed on a regular basis to ensure the appropriate mix is maintained.

The Group's main exposures to foreign currency fluctuation arise through its activities in South Africa where both translational and transactional exposures exist. It is group policy not to cover the effects of exchange rate fluctuation on translation of the results of foreign subsidiaries into the groups base currency, sterling. All material transactional exposures arising through trading in currencies other than the operation's base currency must be eliminated by the use of forward currency cover contracts as soon as they are known of.

All treasury transactions are carried out only with prime rated counter-parties as are investments of cash and cash equivalents. The Group's revenue is derived mainly from government or government backed institutions or blue chip corporates and as such credit risk is considered small.

International Financial reporting standards (IFRS)

Under European legislation, we are required to adopt IAS and IFRS in preparing our Financial Statements from 1 April 2005 onwards. As a result, these Financial Statements are the last prepared under UK Generally Accepted Accounting Principles (UK GAAP).

Application of a particular standard issued by the International Accounting Standards Board (IASB) is dependent on the European Union endorsing that standard. To the extent that some standards may remain to be endorsed we have assumed that they will be so endorsed when applying them in the restatement of results for 2004/05.

The group has today issued a separate announcement to the Stock Exchange summarising the effects of the adoption of the new standards on key elements of the Group's Profit and Loss Account and on Group Net Assets. This announcement is also available on our web site at www.babcock.co.uk.

Although the majority of the work on the transition from UK GAAP to IAS/IFRS has been completed, certain areas of the standards are still subject to change. Consequently, further and more detailed information on the impact on Profit and Loss Account and Balance Sheet line items will be given within the next two months. The estimates provided in the announcement have not been audited.

The major areas of impact were outlined in our 2003/04 Financial Review and were identified as pensions accounting, goodwill and intangibles with particular reference to acquisition accounting, deferred tax, finance leases and foreign exchange hedging. Further analysis since then has shown that finance leases and foreign exchange hedging are unlikely to have a material impact but accounting for share based payments will affect earnings although not necessarily to a significant extent.

The key points to note are that the Group's cash flow and its ability to pay dividends will be unaffected but that there is likely to be more volatility in the balance sheet as a result of the use of the fair value concept, particularly in applying the new standard relating to pensions, which will also result in a realignment of operating profit and interest income.

Although the presentational requirements of IFRS will differ from those currently applied under UK GAAP, the Group will continue to provide details of underlying earnings, which under IFRS will be defined as earnings before significant non-recurring items and before amortisation of acquired intangibles.

BABCOCK INTERNATIONAL GROUP PLC
GROUP PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 31 MARCH 2005

		Year ended 31 March 2005			Year ended 31 March 2004		
	Note	**Before goodwill and exceptional items £m**	**Goodwill and exceptional items £m**	**Total £m**	Before Goodwill and exceptional items £m	Goodwill and exceptional items £m	Total £m
Existing operations		**518.3**	**-**	**518.3**	438.0	-	438.0
Acquisitions		**241.7**	**-**	**241.7**	-	-	-
Continuing operations		**760.0**	**-**	**760.0**	438.0	-	438.0
Discontinued operations		**-**	**-**	**-**	14.0	-	14.0
Group turnover	3	**760.0**	**-**	**760.0**	452.0	-	452.0
Cost of sales		**(647.7)**	**-**	**(647.7)**	(385.0)	-	(385.0)
Gross profit		**112.3**	**-**	**112.3**	67.0	-	67.0
Net operating expenses		**(71.3)**	**(5.1)**	**(76.4)**	(41.8)	(3.3)	(45.1)
Existing operations		**30.0**	**(8.7)**	**21.3**	25.5	(3.3)	22.2
Acquisitions		**11.0**	**3.6**	**14.6**	-	-	-
Continuing operations	3	**41.0**	**(5.1)**	**35.9**	25.5	(3.3)	22.2
Discontinued operations		**-**	**-**	**-**	(0.3)	-	(0.3)
Group operating profit	3	**41.0**	**(5.1)**	**35.9**	25.2	(3.3)	21.9
Share of operating profit of joint ventures	3	**0.3**	**-**	**0.3**	0.1	-	0.1
Loss on sale of operations	4	**-**	**(1.6)**	**(1.6)**	-	(1.7)	(1.7)
Profit on ordinary activities before interest		**41.3**	**(6.7)**	**34.6**	25.3	(5.0)	20.3
Net interest and similar (charges)/income		**(6.2)**	**-**	**(6.2)**	(2.2)	1.7	(0.5)
Profit on ordinary activities before taxation		**35.1**	**(6.7)**	**28.4**	23.1	(3.3)	19.8
Tax on profit on ordinary activities	5	**(8.1)**	**0.4**	**(7.7)**	(3.4)	-	(3.4)
Profit on ordinary activities for the financial year		**27.0**	**(6.3)**	**20.7**	19.7	(3.3)	16.4
Equity minority interests				**(0.1)**			-
Profit for the financial year				**20.6**			16.4
Equity dividends paid and proposed	7			**(9.4)**			(4.9)
Retained profit for the financial year				**11.2**			11.5
Earnings per share							
- Basic	6			**10.87p**			11.31p
- Diluted	6			**10.86p**			11.28p
Earnings per share before exceptional items and goodwill							
- Basic	6			**14.20p**			13.60p
- Diluted	6			**14.18p**			13.57p

BABCOCK INTERNATIONAL GROUP PLC
GROUP BALANCE SHEET
AT 31 MARCH 2005

	As at 31 March 2005	As at 31 March 2004 (as restated) £m
Fixed assets		
Intangible assets		
Development costs	**0.2**	0.7
Goodwill		
- Goodwill	**156.1**	81.5
- Negative goodwill	**(2.9)**	(4.7)
	153.2	76.8
	153.4	77.5
Tangible assets	**37.9**	12.2
Investments		
Investments in joint ventures		
- Share of gross assets	**4.8**	2.4
- Share of gross liabilities	**(4.4)**	(2.7)
- Loans to joint ventures	**0.2**	0.9
	0.6	0.6
Other investments	**0.1**	0.1
	192.0	90.4
Current assets		
Stocks	**41.3**	29.7
Debtors – due within one year	**180.4**	75.2
Debtors – due after more than one year	**98.1**	64.0
	278.5	139.2
Cash and bank balances	**33.1**	17.5
	352.9	186.4
Creditors – amounts due within one year	**(307.5)**	(134.7)
Net current assets	**45.4**	51.7
Total assets less current liabilities	**237.4**	142.1
Creditors – amounts due after more than one year	**(8.4)**	(16.0)
Provisions for liabilities and charges	**(55.0)**	(29.0)
Net assets	**174.0**	97.1
Capital and reserves		
Called up share capital	**125.0**	90.1
Share premium account	**69.3**	38.6
Capital redemption reserve	**30.6**	30.6
Profit and loss account	**(51.0)**	(62.2)
Shareholders' funds – equity interests	**173.9**	97.1
Equity minority interests	**0.1**	-
	174.0	97.1

BABCOCK INTERNATIONAL GROUP PLC
SUMMARISED GROUP CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 MARCH 2005

	Note	**Year ended 31 March 2005 £m**	Year ended 31 March 2004 (as restated) £m
Cash inflow from operating activities	8	**43.2**	28.0
Returns on investments and servicing of finance		**(6.1)**	(0.4)
Taxation		**(4.7)**	(1.6)
Capital expenditure and financial investment		**3.9**	(1.8)
Acquisitions and disposals		**(29.7)**	1.4
Equity dividends paid		**(7.0)**	(4.5)
Cash (outflow)/inflow before financing		**(0.4)**	21.1
Management of liquid resources		**(5.6)**	0.2
Financing		**20.6**	(19.2)
Increase in cash in the period	9	**14.6**	2.1

BABCOCK INTERNATIONAL GROUP PLC
GROUP STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
FOR THE YEAR ENDED 31 MARCH 2005

	Year ended 31 March 2005 £m	Year ended 31 March 2004 £m
Group profit for the financial year	**20.3**	16.4
Profit on joint ventures	**0.3**	-
Profit for the financial year	**20.6**	16.4
Currency translation differences on foreign currency net investments and related loans	**-**	0.6
Total recognised gains and losses relating to the year	**20.6**	17.0

BABCOCK INTERNATIONAL GROUP PLC
RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS
FOR THE YEAR ENDED 31 MARCH 2005

	Note	**Year ended 31 March 2005 £m**	Year ended 31 March (as restated) 2004 £m
Shareholders' funds at start of year, as previously reported		**101.1**	87.3
Prior year adjustment	**11**	**(4.0)**	(3.9)
Shareholders' funds at start of year, as restated		**97.1**	83.4
Ordinary Shares issued in the year		**65.6**	1.7
Total recognised gains and losses relating to the period		**20.6**	17.0
Dividends		**(9.4)**	(4.9)
Movement on Employee Share Ownership Plan		-	(0.1)
Net movement in shareholders' funds		**76.8**	13.7
Shareholders' funds at the end of year		**173.9**	97.1

BABCOCK INTERNATIONAL GROUP PLC
NOTES TO THE PRELIMINARY STATEMENT
FOR THE YEAR ENDED 31 MARCH 2005

1 Basis of Preparation

The financial information set out above does not comprise the company's statutory accounts. Statutory accounts for the previous financial year ended 31 March 2004 have been delivered to the Registrar of Companies. The auditors' report on those accounts was unqualified and did not contain any statement under section 237(2) and (3) of the Companies Act 1985. The accounting policies have all been applied consistently throughout the year and the preceding year with the exception of UITF38 (see note 11).

2 Board Approval

The Board approved the Annual Report on the 25 May 2005. The auditors have given an unqualified opinion on the accounts for the year ended 31 March 2005, which will be delivered to the Registrar following the Annual General Meeting.

3 Segmental analysis

	Year ended 31 March 2005				Year ended 31 March 2004			
	Group turnover £m	**Group operating profit/(loss) before goodwill and exceptional items £m**	**Goodwill and exceptional items £m**	**Group operating profit/ (loss) £m**	Group turnover £m	Group operating profit/(loss) before goodwill and exceptional items £m	Goodwill and Exceptional items £m	Group operating profit/ (loss) £m
Existing operations								
Defence Services	**245.1**	**17.8**	**-**	**17.8**	171.5	11.6	-	11.6
Technical Services	**160.2**	**13.1**	**(5.5)**	**7.6**	180.0	14.8	-	14.8
Engineering & Plant Services	**113.0**	**5.5**	**-**	**5.5**	86.5	3.5	-	3.5
Unallocated costs, other income and goodwill	**-**	**(6.4)**	**(3.2)**	**(9.6)**	-	(4.4)	(3.3)	(7.7)
	518.3	**30.0**	**(8.7)**	**21.3**	438.0	25.5	(3.3)	22.2
Acquisitions								
Networks	**61.5**	**4.1**	**-**	**4.1**	-	-	-	-
Rail	**167.0**	**8.3**	**8.8**	**17.1**	-	-	-	-
HS&E	**13.2**	**(1.2)**	**-**	**(1.2)**	-	-	-	-
Unallocated costs, other income and goodwill	**-**	**(0.2)**	**(5.2)**	**(5.4)**	-	-	-	-
	241.7	**11.0**	**3.6**	**14.6**	438.0	25.5	(3.3)	22.2
Total continuing operations	**760.0**	**41.0**	**(5.1)**	**35.9**	438.0	25.5	(3.3)	22.2
Discontinued	**-**	**-**	**-**	**-**	14.0	(0.3)	-	(0.3)
Group total	**760.0**	**41.0**	**(5.1)**	**35.9**	452.0	25.2	(3.3)	21.9

The turnover, not included above, relating to joint ventures was £3.1 million (2004: £3.5 million). The share of operating profit of £0.3 million (2004: profit £0.1 million) from joint ventures represents a £0.2 million with the Technical Services segment (2004: loss £0.1 million), a profit with the Defence Services segment of £0.2 million (2004: £0.2 million) and a loss of £0.1 million from the Networks segment (2004 £nil). The inter segment sales in 2005 and 2004 were not material.

4 Exceptional items and goodwill

Within existing businesses an operating exceptional loss of £5.5 million was realised representing £0.8 million of restructuring costs and £4.7 million of goodwill write-off on the downsizing of the group's marine design subsidiaries. Within acquired businesses an operating exceptional profit of £7.0 million is made up of £8.8 million income from the transfer of rail maintenance contracts back to Network Rail offset by costs of the transfer and restructuring costs within the rail business, and £1.8 million of operating exceptional costs for the closure of the Peterhouse head office.

The regular goodwill amortisation (excluding exceptional charges) is £6.6 million (2004: £3.3 million).

In 2005 the non-operating exceptional loss of £1.6 million is made up of the following; a loss of £1.2 million provided in the period for disposal costs of previously disposed of businesses, and a loss of £0.4 million recognised on the sale of CMR Consultants Limited and a write-down of the carrying value of FBMA which was sold on 10 October 2004. Tax includes an exceptional credit of £0.4 million relating to the above.

In 2004 the non-operating exceptional charge of £1.7 million was made up of a loss on sale of Swedish Materials Handling businesses of £2.5 million, offset by a profit on the sale of a non-trading subsidiary containing a financial asset of £0.8 million. Net interest and similar income/(charges) includes an exceptional gain of £1.7 million arising on the disposal of a financial asset.

5 Taxation

The effective rate of tax in respect of continuing profits before goodwill exceptional items and discontinued activities is approximately 24%. This is lower than the statutory 30% rate due to the net effect of permanent differences and the difference between the UK rate and the effective overseas rate.

6 Earnings per share

The basic earnings per share has been calculated on the profit for the period of £20.6 million (2004: profit of £16.4 million) and the weighted average number of ordinary shares in issue throughout the period of 189,193,887 (2004: 145,022,090).

The diluted earnings per share has been calculated after taking account of 258,810 dilutive share options where the exercise price is less than the average market price of the company's own shares during the period.

The basic and diluted earnings per share before exceptional items and goodwill have been calculated using the same weighted average number of ordinary shares in issue as above and after adjusting for goodwill amortisation of £6.6 million (2004: £3.3 million), operating exceptional items of £1.5 million profit, the loss on the sale of operations of £1.6 million (2004: £1.7 million), and the exceptional interest income of £nil (2004: £1.7 million) and an exceptional tax credit of £0.4 million (2004: £nil).

7 Equity Dividends

A dividend of 2.65p per 60p ordinary share (2004: 2.1p per 60p ordinary share) will be paid, subject to shareholders approval, on 8 August 2005 to shareholders registered on 8 July 2005. An interim dividend of 1.35 per 60p ordinary share (2004: 1.25p per 60p ordinary share) was paid on 21 January 2005.

8 Reconciliation of group operating profit to cash flow from operating activities

	Year ended 31 March 2005 £m	Year ended 31 March 2004 £m
Group operating profit	**35.9**	21.9
Depreciation, amortisation and impairment charges	**19.7**	8.2
Increase in stocks	**(5.0)**	(8.5)
(Increase)/decrease in debtors	**(22.2)**	13.7
Increase/(decrease) in creditors	**8.6**	(7.1)
Increase/(decrease) in provisions	**5.3**	(0.1)
Loss/(profit) on sale of fixed assets	**0.9**	(0.1)
Net cash inflow from operating activities	**43.2**	28.0

9 Movement in net debt

	Year ended 31 March 2005 £m	Year ended 31 March 2004 £m
Increase in cash in the year	**14.6**	2.1
Increase/(decrease) in liquid resources in the year	**5.6**	(0.2)
Cash flow from the (increase)/decrease in debt and lease financing	**(19.8)**	20.5
Change in net funds resulting from cash flows	**0.4**	22.4
Loans and finance leases acquired with subsidiaries	**(47.2)**	-
New finance leases	**(0.9)**	(0.1)
Translation differences	**0.2**	(0.5)
Movement in net debt in the year	**(47.5)**	21.8
Net debt at 1 April	**(15.4)**	(37.2)
Net debt at 31 March	**(62.9)**	(15.4)

10 Changes in net debt

	At 1 April 2004 £m	Cash flow £m	New finance leases £m	Subsidiaries disposed/ acquired £m	Exchange movement £m	**At 31 March 2005 £m**
Cash in hand and at bank	14.6	(17.9)	-	27.9	-	**24.6**
Overdrafts	(11.3)	15.2	-	(10.6)	-	**(6.7)**
	3.3	(2.7)	-	17.3	-	**17.9**
Debt	(20.5)	(23.1)	-	(37.3)	0.1	**(80.8)**
Finance leases	(1.1)	3.3	(0.9)	(9.9)	0.1	**(8.5)**
	(21.6)	(19.8)	(0.9)	(47.2)	0.2	**(89.3)**
Liquid resources	2.9	5.6	-	-	-	**8.5**
Total	(15.4)	(16.9)	(0.9)	(29.9)	0.2	**(62.9)**

11 Prior year adjustment

The financial statements for the year ended 31 March 2004 have been restated following the adoption of UITF Abstract 38 “Accounting for ESOP Trusts”. Shares held by the Babcock International Group PLC ESOP Trust, previously shown in the balance sheet as fixed asset investments, are now required to be shown as a deduction from shareholders’ funds.

The impact of the treatment above is to reduce investments by £4.0m at 31 March 2004.

The consolidated cash flow statement has been restated to reflect the reallocation of the cash payments for the purchase of shares from “capital expenditure and financial investments” to “financing”. (There is no material impact on profit before tax in either the current or prior period.

12 Acquisitions and disposals

On 14 June 2004 Babcock acquired Peterhouse Group Plc, the following is a summary of the provisional acquisition balance sheet:

The net assets acquired and the related costs were as follows:

	Peterhouse book value £m	Peterhouse Provisional fair value adjustments £m	Peterhouse Provisional fair value £m
Tangible fixed assets	37.8	(7.7)	30.1
Investments	5.1	-	5.1
Total fixed assets	**42.9**	**(7.7)**	**35.2**
Stocks	5.2	1.6	6.8
Debtors	104.8	12.7	117.5
Cash	27.8	-	27.8
Creditors	(103.0)	(0.3)	(103.3)
Finance lease	(9.9)	-	(9.9)
Borrowings	(37.3)	-	(37.3)
Net current assets	(12.4)	14.0	1.6
Provisions for liabilities and charges	(14.8)	(3.6)	(18.4)
Net assets acquired	**15.7**	**2.7**	**18.4**
Fair value of consideration:			
Cash			31.7
Shares			64.7
Costs			3.0
			99.4
Goodwill arising			81.0

On 14 June 2004 the percentage of acceptances received was 55.7% with the remaining acceptances received over the following months. The change in percentage ownership in this period did not materially affect the fair value of assets acquired or the resultant goodwill reflected above.

On 10 September 2004 the group acquired Turner and Partners. Turner and Partners has been classified in Networks.

On 13 July 2004 the group sold CMR Consultants Limited, and on 10 June 2004 the group sold Babcock Defence Services Australia Pty Limited.

13 International financial reporting standards

Following the EU's adoption of Regulation No. 1606/2002 on the use of International Financial Reporting Standards (IFRS) by EU-listed companies, the group is implementing IFRS from 1 April 2005. The first financial information to be reported by the group in accordance with IFRS will be for the first six months ending 30 September 2005 but the requirement to present comparative information means that a balance sheet as at 31 March 2004 and primary statements for 2005 prepared in accordance with IFRS will also be required. The group has continued to report its consolidated accounts in accordance with UK GAAP for 2005.

A separate announcement will be made today to the Stock Exchange as to the principal areas affected by the transition to IFRS.

14 AGM

The Annual General Meeting will be held at London Marriott Hotel, Marble Arch, 134 George Street, London W1H 5DN, on Tuesday 19 July 2005, at 11.30 am.

Copies of the 2005 Annual Report and Accounts will be distributed to all holders of the company's ordinary shares on or before 16 June 2005. Copies will also be available at the company's registered office: 2 Cavendish Square, London W1G 0PX. In addition, this report will be available on the company's website: www.babcock.co.uk