Babcock is an international defence company operating in our focus countries of the UK, Australasia, Canada, France and South Africa, with exports to additional markets with potential to become focus countries.

Our Purpose, *to create a safe and secure world, together*, defines our strategy. We support and enhance our customers' defence and security capabilities and critical assets through a range of product and service solutions. We meet our customers' requirements of value for money, increased availability, modernisation and flexibility.

We made excellent progress in our first year of turnaround; securing the balance sheet and focusing the Group through portfolio alignment and by reorganising around a new operating model and people strategy.

Supported by our ESG strategy, we are now better positioned to take advantage of the opportunities created by the strengthening global market for defence.

Please scan this code to watch a video explaining how our purpose informs all that we do and how the work we deliver is helping Babcock to create a safe and secure world, together.

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## 2022 FINANCIAL HIGHLIGHTS

### Revenue
**£4,102m**

2021: £3,972m
(Restated, see page 24)

### Statutory operating profit/(loss)
**£227m**

2021: £(1,737)m
(Restated, see page 25)

### Underlying operating profit/(loss)
**£238m**

2021: £(28)m

### Statutory cash generated from operations
**£42m**

2021: £475m
(Restated, see page 162)

### Underlying free cash flow
**£(191)m**

2021: £170m
(Restated, see page 30)

### Net debt/EBITDA (covenant basis)
**1.8x**

2021: 2.4x

**Adjustments between statutory and underlying**

The Group uses various alternative performance measures, including underlying operating profit, to enable users to better understand the performance and earnings trends of the Group. The Directors believe the alternative performance measures provide a consistent measure of business performance year to year and they are used by management to measure operating performance and as a basis for forecasting and decision-making. The Group believes they are also used by investors in analysing business performance.

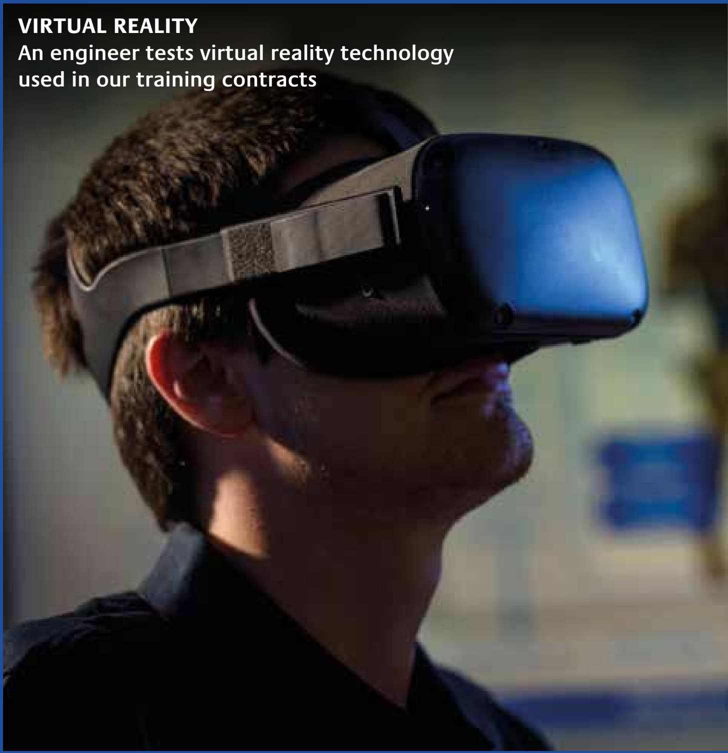
This presentation allows for separate disclosure and specific narrative to be included concerning the adjusting items. This helps to ensure performance in any one year can be clearly understood by users of the financial statements. These alternative performance measures are not defined by IFRS and therefore there is a level of judgement involved in identifying the adjustments required to calculate the underlying results. As the alternative performance measures used are not defined under IFRS, they may not be comparable to similar measures used by other companies. They are not intended to be a substitute for, or superior to, measures defined under IFRS.

**Forward-looking statements**

Statements in this Annual Report, including those regarding the possible or assumed future or performance of Babcock or its industry, as well as any trend projections or statements about Babcock's or management's beliefs or expectations, may constitute forward-looking statements. By their nature, forward-looking statements involve known and unknown risks and uncertainties as well as other factors, many of which are beyond Babcock's control. These risks, uncertainties and factors may cause actual results, performance or developments to differ materially from those expressed or implied by such forward-looking statements. No assurance is given that any forward-looking statements will prove to be correct. The information and opinions contained in this Annual Report do not purport to be comprehensive, are provided as at the date of the Annual Report and are subject to change without notice. Babcock is not under any obligation to update or keep current any information in the Annual Report, including any forward-looking statements.

## FY22 HIGHLIGHTS

- Portfolio – focused the group: Generated gross proceeds of £447 million from four completed disposals, above our targeted minimum of £400 million. Disposal of part of our Aerial Emergency Services (AES) business signed in July 2022 after year end for a cash consideration of c.£115 million. Footprint expanded in Australia with acquisition of the remaining 50% interest in our Australian Naval Ship Management (NSM) joint venture
- Operating model – implemented: Streamlining processes and structures and improving controls drove a c.£20 million benefit in FY22 (c.£40 million annualised), as expected. Internal business reporting lines flattened. We continue to focus on improved execution to deliver efficiencies
- People strategy - culture transforming: New people strategy developed, including roll-out of Group Principles and agile working
- ESG strategy – developing: Expanded our corporate commitments to incorporate broader environmental targets and created new policies and guidance to support the governance of our sustainability programmes
- Growth – developing opportunities: Good order momentum including the signing of export agreements with Indonesia and Poland for the Arrowhead 140 (AH140) naval ship design (the base for the UK's Type 31 programme) and new defence contracts in Australia, France and the UK



**VIRTUAL REALITY**
An engineer tests virtual reality technology used in our training contracts

**QUEEN ELIZABETH CLASS**
One of the UK's new QEC aircraft carriers in Portsmouth

# Our business today

## Creating a safe and secure world, together

Babcock is an international defence company operating in our focus countries of the **UK, Australasia, Canada, France** and **South Africa,** with exports to additional markets with potential to become focus countries.

Our work supports our public sector and blue chip customers on complex long-term programmes and critical services. We provide through-life technical and engineering support, specialist training, asset management and the design and manufacture of a range of defence and specialist equipment. We meet our customers' key requirements of value for money, increased availability, modernisation and flexibility.

## WHAT WE DO

We provide engineering, support and systems and deliver critical services to defence and civil markets.

### Deliver complex programmes and critical services

We provide through-life technical and engineering support for our customers' assets, delivering improvements in the performance, availability and programme cost. We also deliver critical services to our defence and civil customers, including engineering support to land defence and air base operations, specialist training and asset management, equipment supply and maintenance to the resources sector, and engineering support to the nuclear power industry.

### Design, manufacture and integrate

We design and manufacture a range of defence and specialist equipment, from naval ships and weapons handling systems to liquid gas handling systems. We also provide integrated, technology-enabled solutions to our defence customers in areas such as secure communications, electronic warfare and air defence.

## REVENUE PROFILE

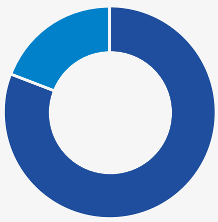
### By location


- 63% UK
- 37% International

### By market

- 55% Defence
- 45% Civil

### By customer



- 81% Public
- 19% Private

## BACKLOG PROFILE

### By market


- 72% Defence
- 28% Civil

## DELIVERED ACROSS OUR FOUR SECTORS

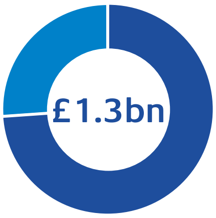
### Marine

**31% of FY22 revenue**

- UK and international warship through-life support: design, build, assemble, maintain, upgrade
- International submarine through-life support
- Global naval exports: ship design, military equipment and engineering support
- Energy and marine equipment and support

See page 42

**FY22 revenue**




74% Defence
26% Civil

### Nuclear

**24% of FY22 revenue**

- Support all UK nuclear submarines and infrastructure
- Own or manage key infrastructure and naval bases
- Nuclear submarine dismantling
- UK civil nuclear new build, generation support and decommissioning projects
- UK and international nuclear services

See page 44

**FY22 revenue**


84% Defence
16% Civil

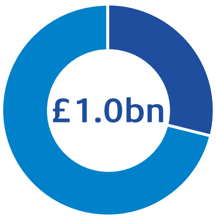
### Land

**25% of FY22 revenue**

- Asset management and engineering support for British Army vehicles
- Technical training and support for the British Army
- Emergency services technical training and fleet management
- South Africa engineering and equipment businesses

See page 46

**FY22 revenue**




29% Defence
71% Civil

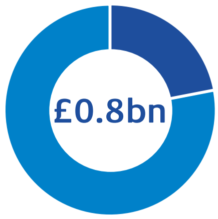
### Aviation

**20% of FY22 revenue**

- UK and French pilot training and support
- Military aircraft engineering and airbase support
- Military and emergency services aircraft maintenance, repair and overhaul
- Air ambulance, search and rescue and firefighting services

See page 48

**FY22 revenue**




22% Defence
78% Civil

## FURTHER INFORMATION ON

**Strategy and business model**
See page 6-9

**Markets**
See page 10

**Culture change**
See page 18

**ESG strategy**
See page 54

# Our strategy

Our Purpose, *to create a safe and secure world, together*, defines our strategy. We support and enhance our customers' defence capabilities and critical assets through a range of product and service solutions. We meet our customers' requirements of increased availability, affordability and capability.

In last year's report, we said our strategy had three elements: the UK naval business; UK value-add services and International. As we have developed and shaped the business over the first year of our turnaround, we have determined that our international presence is an inherent part of our overall strategy and so should not be considered separately. Our strategy focuses on naval engineering, support and systems, and on critical services in our core defence and civil markets. In this section we share our thinking and outline our strategic priorities.


## Naval engineering, support and systems

- To deliver high-value, technical and engineering support for ships and submarines to UK and other navies
- To own, maintain and develop critical naval infrastructure
- To design, build and export world class naval platforms and equipment
- To deliver affordable digital support and solutions which enhance our customers' capabilities

### Drivers

- Global threat environment and geopolitics
- Rising global defence spending
- Infrastructure and equipment modernisation trends
- UK National Shipbuilding Strategy
- Digitalisation of defence and security environment
- Requirement for integrated, technology-driven solutions

### Babcock Sectors

- Marine
- Nuclear (naval)


## Critical services: defence and civil

- To provide high-value engineering and support services in land and aviation defence, civil nuclear and other critical sectors
- To deliver technical training services in defence and security sectors
- To maintain and provide complex assets and equipment
- To provide integrated solutions to our customers by bringing together the right technology and suppliers

### Drivers

- Increased asset complexity across all defence domains and public service sectors
- Nuclear energy is a key component of the UK Government's decarbonising strategy
- Tight budgets driving need for innovative asset management solutions and outsourced services
- Outsourcing specialist equipment services

### Babcock Sectors

- Nuclear (civil)
- Land
- Aviation

| Delivering | | |
|---|---|---|
| Availability | Affordability | Capability |

*We report through four operating sectors, read more about them in our operational reviews on page 42*

Find out more about our Arrowhead 140 export programme by scanning this code.

## Good progress on FY22 priorities

During the year, we delivered the strategic actions, set out below, required to strengthen the Group, creating a stable platform to execute our strategy.

### Portfolio

- Gross proceeds of £447 million
- Net debt/EBITDA reduced to 1.8x
- Strategic acquisition of the remaining 50% interest in our Australian Naval Ship Management (NSM) joint venture

### Operating model

- New operating model established
- Managed COVID-19 challenges
- Achieved target in-year operating model savings
- Operating margin 5.8% (from 5.5%)

### People

- Established our Purpose and Principles
- Created a flatter management structure
- Harmonised policies and processes
- Managed senior leadership changes and restructuring
- Focused on sharing best practice and innovation

### ESG

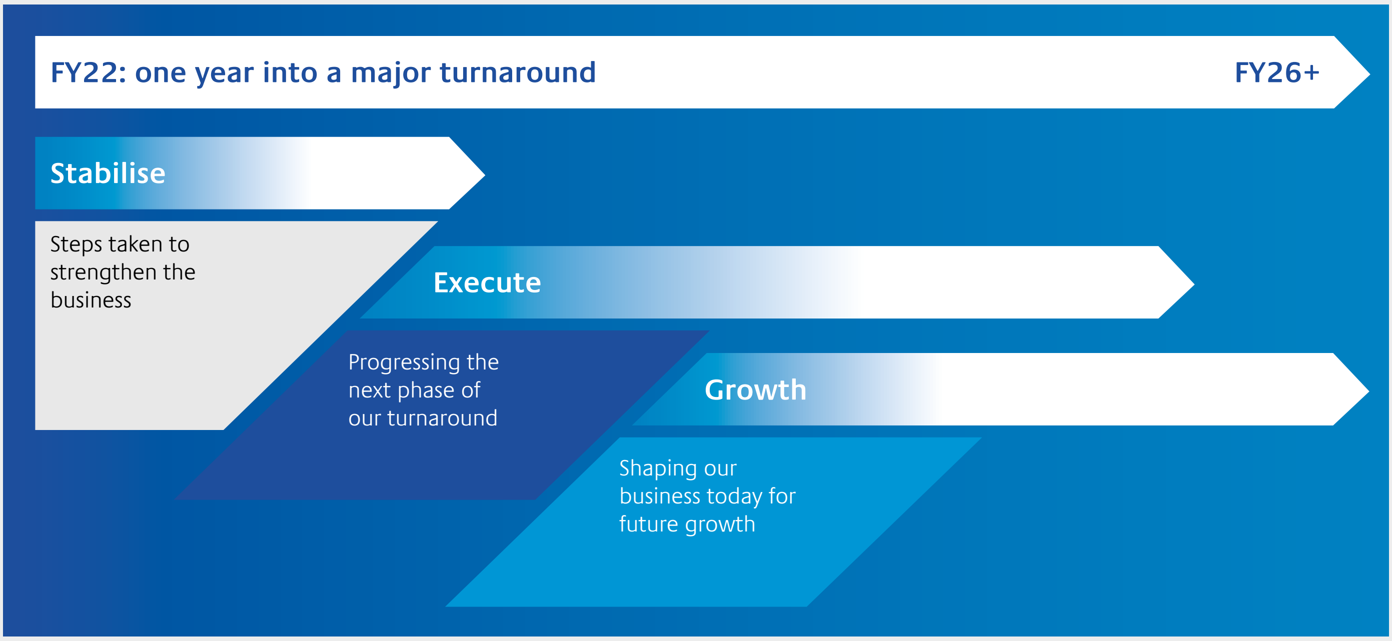
- Matured integration of ESG into programmes
- Developed sector sustainability programmes
- Expanded our ESG commitments
- Committed to set ambitious science-based targets

### Growth

- Contract backlog £9.9 billion
- Global AH140 exports
- Significant new defence communications business globally
- Launched iSupport for naval operations

*Read more about our strategic progress in our CEO Review on page 13*

## Our turnaround strategy continues




### Delivering

| Improved outcomes for our customers | A better place to work | Returns for our shareholders |
|---|---|---|

*Read more about our priorities for FY23 and beyond in our CEO Review on page 13*

# Our business model

We provide a range of products and service solutions to enhance our customers' defence capabilities and critical assets. Our business model is underpinned by a deep understanding of technology integration and engineering, infrastructure management and specialist training. We help our customers around the world to cost effectively improve the capability, reliability and availability of their most critical assets.

## Our key strengths and resources

### Our people

We rely on our people, and their experiences and skills, to deliver for our customers and solve challenges every day. We aim to better support and empower our workforce of over 28,000.

*See our People Strategy on page 19*

### Customer relationships

We are a trusted partner, critical to our customers' ability to solve complex problems. Through long-term programmes and contracts, we work collaboratively with our customers to understand their needs and identify solutions that add value.

### Our assets

We own critical national infrastructure in the UK including the Rosyth and Devonport Royal dockyards. We also operate a range of customer-owned critical assets, for example, naval and air force bases and company-owned assets including complex engineering facilities and aircraft for the delivery of emergency services and military training.

### Our technology and know-how

We use our technology and our highly specialised engineering know-how to solve customer challenges. We have a deep understanding of our customers' assets and are able to integrate technologies and capabilities to support their needs and provide services that add value.

### Safety and regulatory compliance

This underpins all work. We and our customers operate in heavily regulated environments where the health, safety and wellbeing of all stakeholders is the number one priority.

## What we do

### Deliver complex programmes and critical services

We provide through-life technical and engineering support for our customers' assets, delivering improvements in the performance, availability and programme cost. We also deliver critical services to our defence and civil customers, including engineering support to land defence and air base operations, specialist training and asset management, equipment supply and maintenance to the resources sector, and engineering support to the nuclear power industry.

### Design, manufacture and integrate

We design and manufacture a range of defence and specialist equipment from naval ships and weapons handling systems to liquid gas handling systems. We also provide integrated, technology-enabled solutions to our defence customers in areas such as secure communications, electronic warfare and air defence.

## How we do it

### 1 Foundations

We work collaboratively with government departments, public bodies, highly regulated industries and blue chip companies, and are embedded on crucial long-term programmes. We focus on markets and customers with outsourcing models that require value-add engineering-based support and product development. Our five main markets are the UK, Australasia, France, Canada and South Africa, with operations in and exports to other countries.

### 2 Bidding and business development

We continually monitor opportunities across our markets, using strong reference cases and deep sector expertise to identify ways to solve new and existing customers' challenges and support their programmes. We have a multi-gate review process for contract bids to help ensure we only bid on value-creating work.

### 3 Contracting

A significant proportion of our business is carried out on a long-term contract or multi-year framework basis. Our backlog of £9.9 billion of contracted work provides a base level of revenue for the years ahead, supplemented by new business wins, framework call-offs, contract extensions and variations, and short-cycle work. Revenue is recognised as we deliver on our contracts and performance obligations are satisfied. We have an established review process to manage contract risk.


### 7 Investment and capability

Revenue is recognised as we deliver on our contracts and performance obligations are satisfied. The cash we generate funds selective reinvestment into the business, principally through capital expenditure to develop our unique infrastructure, equipment, IT systems and engineering talent.

### 6 Partnerships and collaboration

Partnering and collaboration are key to our success of bringing market- leading capabilities to our customers. We bring together organisations to deliver engineering and technology-based products and support solutions that add value to our customers and increase access to markets.

One example of this is our new collaboration with Elbit Systems UK and QinetiQ to deliver support to the UK's Maritime Electronic Warfare Systems Integrated Capability (MEWSIC), where we are the Prime contractor.

### 4 Sustainability

Our ESG strategy is a key component of how we deliver and increase the sustainability of our business. Our business has a significant impact on society and the environment and sustainability is an integral part of our corporate strategy and how we do business.

### 5 Technology-based solutions

We apply technology-based solutions to solve complex customer problems. We invest in technologies that optimise asset utilisation, advance manufacturing, enhance support capabilities and add value to customers. Our data analytics, digital design and integration capabilities reduce costs and increase the customer's ability to adapt to technology developments.

## Creating stakeholder value

### Customers

Delivering for our customers and partnering with them on the challenges they face.

### Investors

Creating shareholder value through growth, cash generation and the efficient allocation of capital. Delivering shareholder returns through dividends and increased share value.

### Employees

Creating a better place to work where employees are valued and motivated at all times.

### Regulatory and industry bodies

Never compromising on safety and complying with regulations at all times.

### Supply chain

Creating jobs and nurturing investment through collaboration with our supply chain.

### Communities

Providing jobs and investment across the UK and ensuring we act responsibly at all times in the interests of local communities around our sites.

*See page 52 for details on how we engage with stakeholders*

# Defence and civil nuclear

We are increasingly focused on defence, which remains our largest and most important market.

We have a critical role in the defence and security of the UK, Australia, New Zealand, Canada and France and we design and manufacture equipment and systems for several other nations including the US and South Korea.

Our defence customers all have increasingly complex requirements, driven by:

- An increasingly unstable geopolitical environment, evolving threats and unpredictable crises
- Budget pressure and requirements to deliver value for money
- The need to develop and apply new technology to keep up with customer needs and rapidly changing threats
- Supply chain and inflation concerns
- Customer ESG requirements

Following the Russian invasion of Ukraine many European countries have increased or pledged to increase their defence budgets and altered their defence posture to increase force readiness e.g. double the number of NATO battle groups in Eastern Europe. The crisis may also lead to increased defence spending across the Indo-Pacific, as assessments of Chinese intentions are updated, and the Middle East. Investor ESG concerns around defence companies have also been challenged as commitment to defence is shown to be necessary to preserving the liberal democratic order which is a prerequisite for addressing the ESG agenda.

As a result, UK and targeted international defence markets continue to offer significant resilience, alongside increased short, medium and long-term potential, both through increased spend in our existing markets and expansion into new markets.

The UK, US and Australian governments announced the creation of a major defence collaboration (AUKUS), not least to counter the increased threat in the Indo-Pacific. This collaboration covers not only the joint development of conventionally armed, nuclear-powered submarines for Australia, but also other areas including, electronic warfare (EW), information sharing, defence innovation, autonomous systems, artificial intelligence, and undersea capabilities.

## UK defence

### Market position

Our primary defence market is the UK where we provide critical support to all of the UK's armed forces. We remain the UK's second largest defence supplier with around 8% of total MOD procurement spend and, as part of the Strategic Partnering Programme, we are working with the UK Government and MOD across multiple critical programmes to ensure the increasingly complex needs of our armed forces are met.

UK defence spending rose to £42 billion in 2021, £2.5 billion higher than 2020, an increase of around 0.3%, adjusted for inflation, with an estimated £19 billion spent on MOD equipment and support, a decrease of around 10% on the prior year. Around 18% of the total defence spend (around £7.5 billion) was designated to supporting MOD equipment, which was similar to last year. In November 2020, the Government announced a £16.5 billion increase in defence spending over four years, and detailed plans in 2021's Integrated Review and Defence Command Paper. There was no change to these plans announced in either the Autumn 2021 or Spring 2022 budgets.

#### UK defence spend 2021 £42 billion

| | |
|---|---|
| 32.0% | Personnel |
| 18.0% | Specialist Military Equipment |
| 18.0% | Equipment Support |
| 12.0% | Infrastructure |
| 13.0% | Property, Equipment, R&D and inventory |
| 7.0% | Other |

Source: MOD Departmental resources: 2021

### Opportunities

The 30-year shipbuilding pipeline, detailed in the National Shipbuilding Strategy relaunched in March 2022 offers, long term opportunities for ship build and support. We have had some success securing export orders for our Arrowhead 140 design and see further opportunities. There is also growing emphasis on underwater capability, defence communications, Intelligence, Surveillance and Reconnaissance (ISR) and EW, all of which present opportunities for Babcock. The continued commitment to the Continuous At Sea Deterrence may require two streams of nuclear ballistic submarine maintenance in future combined with two streams of attack class submarine support while both classes transition. The war in Ukraine may drive a reprioritisation of spending to increase availability and forward basing of armoured vehicles. Over the longer term, the F35 and Tempest programmes may present further opportunities for support to operational training.

### Risks

In FY22, £2.1 billion of our revenue came from direct MOD spend, an increase of 12%. Increased spending from the our MOD customers is spread across major critical programmes such as Type 31 and new areas of digital defence.

We are the second largest defence supplier to the UK Government, and participate in a wide range of its critical defence programmes. We recognise that this represents a significant reliance on the UK MOD. We routinely review reputational and execution risk on the volume of critical programmes in which we are involved (see Group principal risks, see page 76).

The continually evolving international geopolitical and threat environment may see reprioritisation of budgets away from traditional large, complex platforms to smaller, uncrewed platforms and cyber.

### National Shipbuilding Strategy

The National Shipbuilding Strategy Refresh was launched in March 2022. The strategy is based on five central pillars: create a 30-year pipeline of over 150 vessels; accelerate innovation, including related to net zero and AI; increase financial support to shipbuilders; and establish a UK Shipbuilding Skills Taskforce. We are currently building five Type 31 frigates and are well positioned for other near term programmes including FSS and Type 32, as well as other longer term opportunities the strategy offers for ship build and support.

## Australia and New Zealand defence

### Market position

Babcock supports the armed forces of both Australia and New Zealand. For the Royal Australian Navy we provide support to both Collins Class submarines and surface ships including ANZAC class frigates, Canberra class Landing Helicopter Docks (LHD) and LHD landing craft. In March 2022, we acquired the remaining 50% of Naval Ship Management (NSM) from our joint venture partner. NSM has evolved into a strategic maritime sustainment partner to Australia and the acquisition will strengthen the breadth of our support to the Australian Defence Force's maritime capability and provide additional capability for Australia's current and future maritime programmes. We have also been selected as preferred bidder to upgrade and sustain the Australian Defence High Frequency Communication System (DHFCS). This builds on our proven DHFC experience in the UK and New Zealand and reinforces our core capabilities in delivering technology-led, cutting-edge solutions to support complex electronic defence programmes.

Babcock has a long-standing partnership with the NZDF in support of the Royal New Zealand Navy, which was further strengthened with the award of the NZDF's main strategic maritime partnering contract in February 2022. Babcock will provide asset management services, including engineering, project management, production and operational support, to the entire Royal New Zealand Navy fleet, from frigates through to small boats including RHIBs.

### Opportunities

Australia's Defence Strategic Update and Force Structure Plan indicates an increase in defence spending and procurement over the next decade in response to evolving threats in the Indo-Pacific, with Babcock well positioned to support a number of key programmes.

The UK, US and Australian governments announced the creation of AUKUS. This presents opportunities for Babcock in the joint design, build and support of conventionally armed, nuclear-powered submarines for Australia, but also electronic warfare, information sharing, defence innovation, and additional undersea capabilities.

### Risks

Competition is strong, but we are developing our in-country capability and credibility.

## Canada defence

### Market position

Babcock delivers the Victoria In Service Support Contract (VISSC) to sustain the Royal Canadian Navy's (RCN) Victoria class submarines. Working with the RCN, Babcock has transferred the skills and expertise required to provide through life support and maintenance to submarines from the UK to Canada.

### Opportunities

We continue to target large military aviation training opportunities in Canada. Post-Ukraine, Canada is highly likely to further increase its defence spending, in addition to agreed increases already underway. Canadian Defence Minister Anand has indicated an 'aggressive' increase to defence spending to reach the NATO 2% of GDP target. This may present new opportunities for Babcock.

### Risks

A preference for well-established native competition could limit Babcock's exposure to further opportunities given our relatively modest footprint in the country. Our current work is based around one contract and we do not own any infrastructure. This is highlighted as one of the Group's principal risks, see page 76.

## France defence

### Market position

We have grown our position in military aviation training France through the award of the Mentor 1 contract for fast jet pilot training and strengthened our position in the military rotary wing maintenance, repair and overhaul (MRO) market, including the provision of search and rescue aircraft and services for the French Navy.

### Opportunities

Defence spending in France continues to grow with clear opportunities in military aviation training and MRO, and land vehicle MRO. There may also be some marine opportunity for the support of non-complex vessels and equipment, equipment management, maritime autonomy and training.

### Risks

Similarly to Canada, France has well established domestic defence suppliers, often with some element of state ownership. As a British company with limited infrastructure, we may struggle to compete for some opportunities.

## Civil nuclear

### Market position

Babcock is now the only major UK-owned nuclear services partner for Government and is unique in covering both the defence and civil sectors. We provide complex services across civil nuclear new build, operations and decommissioning in the UK, and also provide more limited services in Canada and Japan.

### Opportunities

Nuclear power is a key part of both the UK's Net Zero strategy and its energy security post-Ukraine. The Government's Energy Security Strategy published on 6 April 2022 announced a new body called Great British Nuclear.

By 2050 this body aims to bolster the UK's nuclear capacity to up to 24 GW of electricity, or 25% of projected demand, through up to eight new reactors, with one being approved each year until 2030.

It also confirmed advanced plans to approve two new reactors at Sizewell in Suffolk during this parliament. Subject to technology readiness, Small Modular Reactors (SMR's) will form a key part of the nuclear project pipeline. We are well positioned to take advantage of opportunities in these areas.

### Risks

The decommissioning market has become increasingly difficult following the NDA's decision in 2020 to insource the major programmes across Magnox and Dounreay. In addition, historically it has been hard to secure the necessary commitments to make new nuclear power stations a reality.

# Babcock's transformation is far-reaching and comprehensive

**Ruth Cairnie**
Chair

*Read Ruth's biography on page 94*

In last year's report I gave a full account of the developments arising from the steps we had taken to address the historic underperformance of the Group.

We had reset our financial baseline, refreshed our strategy, launched a new operating model and introduced improved governance and controls.

The first full year of our turnaround has continued the implementation of these improvements. The Board is very satisfied with the progress made against the five strategic actions we had identified for FY22, including generating more than our target of £400 million from divestments intended to focus the Group. Our progress is covered in more detail in the CEO report (page 13).

Our financial results for the year are encouraging. Underlying operating profit of £237.7 million was a 13% organic increase on last year, excluding one-off contract profitability and balance sheet (CPBS) adjustments in FY21, supported by the expected improved performance from our new operating model and a reduction in the impact of COVID-19. Statutory operating profit of £226.8 million compares to a loss of £1,736.7 million in FY21, which included charges from the CPBS review and asset impairments. Our underlying free cash flow was slightly ahead of expectations at £(191.3) million, driven by timing benefits and advance payments.

Statutory revenue grew by 3% to £4,101.8 million. On an organic basis, revenue grew by 5% with good volume recovery in the Land and Aviation sectors.

We have had some notable commercial successes through the year, demonstrating the relevance of our capabilities to our target customers. These included the signing of a £3.5 billion Future Marine Support Programme (FMSP) contract that continues our work for the UK Royal Navy, further work on defence aviation training in France, and new contracts for next-generation tactical communications and information systems in the UK and Australia.

The Board was delighted at the early successes from the Arrowhead 140 frigate export programme, the Babcock design based on the Type 31 we developed for the UK, in Indonesia and Poland.

The transformation of Babcock is intended to be far-reaching and comprehensive, and is grounded in our corporate Purpose: *to create a safe and secure world, together.* This Purpose has been communicated extensively within the Group this year and feeds through into all aspects of our strategy. It is supported by our six new Principles (see page 20) launched this year through substantial engagement with our workforce; these Principles embody the new ways of working and shift towards the more people-focused and accountable culture that we believe is essential to meet the needs of all our stakeholders. I am delighted by how positively our people have been responding.

Alongside and integral to the launch of our Principles and focus on culture is the role of sustainability. We believe that it is right for our stakeholders to expect to hold us to account for our approach and progress. Importantly, as evidenced by the tragic events in Ukraine, we believe the defence industry plays a major part in assuring the stability of sovereign nations; without stability, it is impossible to drive the necessary environmental, social and governance (ESG) improvements to create a safe and secure world.

We have progressed our ESG strategy, expanding our corporate commitments to incorporate broader environmental targets, and we have created new Group policies and guidance. Our social value activities support the needs of the local communities where we operate, which are so critical to our future success (see page 63). On climate action, we are continuing to progress our decarbonisation programme and are on track to submit science-based emission targets (see page 57).

The Board's primary focus in FY22 was to stabilise the business. Overall, we have made excellent progress against our goals for the year, driving tangible positive change across the Group against a background of increasing geopolitical uncertainty.

The second year of our turnaround will build on the strategic actions taken in FY22, with a focus on execution and growth. As we continue to make further progress, the Board is confident of delivering on its expectations of increasingly profitable growth and improved cash flow for FY23 and into the medium term. Babcock is returning to strength.

**RUTH CAIRNIE**
**Chair**

# Strong progress in our first year of turnaround

## David Lockwood
Chief Executive Officer

*Read David's biography on page 94*

### One year ago we defined the actions we needed to take in FY22 to stabilise the business and lay the foundations for the future.

In this, our first year of turnaround, I am pleased to report that we have made strong progress on all our strategic priorities. Overall, our financial performance in FY22 was in line with our expectations, with cash flow slightly better than anticipated. Additionally, we took significant actions to improve balance sheet quality, including the reduction of certain working capital items such as supply chain financing, debt factoring and the practice of deferring period-end creditors.

Led by our Purpose, to create a safe and secure world, together, we have taken action to secure our business; stabilising the balance sheet and focusing the Group through portfolio alignment. We have reorganised around a new operating model and people strategy, which has been further supported by our developing ESG strategy. We are now well-positioned to take advantage of the opportunities created by the strengthening global market for defence.

## Stabilise – strategic actions update

At the start of FY22 we identified five strategic actions for the first year of our turnaround, designed to stabilise the Group both financially and operationally, and to position us for improved execution and growth:

1. Align our portfolio
2. Implement our new operating model
3. Roll out our new people strategy
4. Develop our new ESG strategy
5. Explore growth opportunities

We made strong progress against our priorities, making the changes that will drive improved delivery for our customers, a better experience for our employees and improved returns for shareholders.

**Portfolio**: We reviewed the businesses in our portfolio to determine strategic fit and the value to shareholders of their presence in our portfolio. The divestment of four businesses (our Oil and Gas aviation business, Frazer-Nash Consultancy Ltd, UK Power and our 15.4% stake in the AirTanker Holdings Limited joint venture) generated gross proceeds of £447.3 million, exceeding our target of at least £400 million. In addition, in July 2022 we signed a conditional agreement the sale of some of our aerial emergency services (AES) businesses for a cash consideration of c.£115m. This achieved our key portfolio objectives: to reduce complexity, focus the Group on our chosen markets and strengthen the balance sheet. In March 2022, we expanded our footprint in Australia with the acquisition of the remaining 50% interest in our Australian Naval Ship Management (NSM) joint venture for £33.1 million. Our portfolio actions have enabled us to reduce our gearing to 1.8x net debt to EBITDA, in line with our year-end target of below 2.0x.

**Operating model**: Our new operating model is now established and is driving efficiencies throughout the business. We are already realising benefits from our ongoing work to streamline processes, increase standardisation and improve controls. In FY22 we achieved our target in-year operating model savings of c.£20 million and an annualised savings rate of c.£40 million, while restructuring costs of £36 million were slightly below our original expectations. This progress contributed to the increase in underlying operating margin to 5.8%. The new model increases visibility and shortens communication lines – both essential for an agile business, and important enablers for collaboration. We will continue to embed these new ways of working, with a particular focus on operational excellence and execution in FY23.

**People strategy**: With c.28,000 skilled employees in the Babcock Group, our people strategy is critical to our future success. Aligned with our Purpose, to create a safe and secure world, together, we rolled out six Principles that underpin the ongoing cultural transformation that is key to driving sustainable improvement: Be curious; Be Kind; Be Courageous, Think: Outcomes; Collaborate; and Own and Deliver. Across the Group we are harmonising our people policies and fostering a culture that shares capability, talent, innovation and best practice. We will continue to seek to optimise our legal entities and structures as we continue to roll out our people strategy.

**ESG strategy**: We have made good progress on our ESG strategy. We have matured our plans to reduce harmful emissions from our operations, and to integrate sustainability into programme design and contract terms. Each of our sectors are developing their own sustainability plans in support of Group-led programmes and to meet stakeholders' needs. We have evolved our strategy to meet our commitment to achieve net zero carbon emissions for our estate, assets and operations by 2040. In April 2021, we signed the Business Ambition Pledge and committed to a 2030 science-based target in line with a 1.5°C pathway. We are on track to meet our goal and over the next 12 months we aim to submit our targets for approval by the science-based targets initiative (SBTi).

**Growth**: FY22 was a pivotal year for new business development. Our strategy, which combines asset support and sustainment with a range of value-add products and technical services, drove good business momentum. We signed two export agreements for our AH140 naval ship design, which is the base for the UK's Type 31 programme: a licence order for two ships for Indonesia and selection by Poland for its new MIECZNIK (Swordfish) three-ship frigate programme. We secured several major defence communications contracts including a c.£150 million logistics support contract for the UK's next-generation tactical communications and information systems and a c.£100 million contract for the UK MOD's new Defence Strategic Radio Service (DSRS). In addition, we were selected as capability partner to upgrade and sustain the Defence High Frequency Communication System (DHFC) to support the Australian armed forces over the next 10 years. This award is a great example of collaboration across the Group and with international partners to develop high-value-add solutions for our customers.

The strong progress made on the five strategic actions for FY22 has achieved what we set out to do in the first year of our turnaround. We have met the immediate need to stabilise the business, strengthen the balance sheet and set our performance baseline. We have successfully laid the foundations for the future. In the second year of our turnaround we will increase our focus on execution and growth, and continue to drive cultural change across the Group.

## Execution

With improvement underway across many areas of the Group, our focus for FY23 is on driving further operational excellence. We will continue to invest in controls and process improvement, our facilities, our people, and our IT systems. This will enable us to drive efficiencies, increase business resilience and improve operational delivery and risk management, ultimately increasing the Group's profitability and cash conversion.

## Growth

We have laid the foundations for sustainable profitable growth. The markets we address offer favourable medium-term growth, with opportunities in our core defence market increasing as a result of the current heightened geopolitical uncertainty. We continue to target opportunities for defence and critical services in our focus countries – the UK, France, Canada, Australasia and South Africa – and exports to additional markets, for example, selection of the AH140 design by Poland for its MIECZNIK frigate programme.

The tragic conflict unfolding in Ukraine has created significant additional geopolitical volatility and governments have reprioritised defence and national security. In the short term, opportunities are emerging for our defence support capabilities, driven by the need for force readiness. Over the longer term, our government customers must balance requirements for large-scale equipment modernisation and force expansion with the reality of constrained budgets. Our business model supports and enhances customers' defence and security capabilities and critical assets through a range of products and service solutions. We are ideally placed to address their core requirements of availability, affordability and capability:

- **Availability** – Our customers require high utilisation of complex assets, from ships and submarines in our Marine and Nuclear sectors to military and emergency services aircraft and vehicles in Aviation and Land. Our fleet support and sustainment models are increasingly geared to higher-value-add availability-based solutions designed to optimise asset utilisation and reduce lifetime costs.

- **Affordability** – Our customers are also demanding value for money on support programmes and new platforms. Our deep understanding of our customers' needs, and our ability to bring suppliers and technologies together to deliver an integrated solution, enable us to provide the affordability and flexibility they require.

**LYNEHAM, UK**
**Getting hands on at a visit to our training contract at MOD Lyneham.**


**BABCOCK CANADA**
**A visit to our Canada submarine programme**

- **Capability** – Our customers operate in complex and ever-changing environments, which drives a continual need to adapt and enhance capability. We apply our understanding of technology integration, infrastructure management and specialist training to improve their capability, whether it be through product, support or training solutions.

We are growing our defence digital capabilities to develop a range of technology-based products and solutions that reduce acquisition and operational costs and increase flexibility. For example, our iSupport360 solution enables the optimisation of support to maritime and other complex equipment. Building on our success in winning the MEWSIC, LeTacCIS and DHFC contracts in FY22, we will continue to develop our ability as a technology integrator, bringing together industry partners to design innovative and cost-effective capabilities in areas such as secure communications and electronic warfare.

We are experiencing significant international interest in AH140, the export variant of our Type 31 frigate, driven by the demand for affordable and flexible naval power. Its modular construction offers a wide range of programme options, including capability (systems), construction and supply chain, and acquisition model – from a basic licence agreement to high levels of build programme participation for Babcock. Following our successes in Indonesia and Poland, we are in active discussions regarding further AH140 export opportunities. The digital design and build model for Type 31 is also an important enabler for the UK Government's recently refreshed 30-year National Ship Building Strategy and positions us well for future opportunities in the UK.

Also in defence, increased operational tempo and a growing incumbent fleet are driving demand for surface ship support and maintenance. After the year-end we signed a four-year contract to deliver through-life support to the Marinha do Brasil's flagship vessel, NAM Atlântico, formerly the UK Royal Navy platform HMS Ocean, as part of its global support programme.

## Inflation

The Group's main exposure to inflation is via rising employment costs – particularly where we have existing contracts which were agreed in a low-inflation environment and include inflation risk. At the same time, our employees are suffering the rapidly rising cost of living, with the issue most acute in the UK of all our markets. The Group is seeking to manage the short-term impact of inflation through increased efficiencies, and to limit the taking of commercial risk of future inflation in new contracts where it cannot be mitigated.

We are therefore delighted that over the last few months we have engaged collaboratively with our employees and trade unions in the UK to agree a fixed-sum pay increase for FY23 that will benefit all but the most highly paid employees. This innovative and progressive pay deal has been designed to disproportionately benefit our lower-paid employees, who are most exposed to rising costs. It has now been agreed and implemented for 85% of the UK workforce (around 65% of the total workforce) giving us better visibility of employment costs for the year ahead. This will increase our labour costs by some £25 million per annum above our original expectations. The Group expects to offset this cost increase through a variety of measures, including the acceleration of improvements in contracting and procurement practices, and the removal of inefficient processes as we further embed our new operating model.

Outside of wage inflation, in many of our markets the recent increase in input-cost inflation coupled with shortages of supply, has increased the cost, and in some areas the availability, of materials and components. In such an environment, supplier resilience is also an emerging risk. Our newly formed Procurement and Supply Chain organisation is monitoring our supply chain to identify and mitigate any such issues as early as possible.

## Health and safety performance in the year

The appointment of a Global Safety, Health and Environmental Protection Director, and formation of a central team, has brought additional focus to the safety improvement programme. We have strengthened our governance and introduced an electronic global safety information management system. The Group's Total Recordable Injury Rate (TRIR) in FY22, which includes work-related injuries requiring medical treatment, has reduced from 0.89 injuries for every 100,000 hours worked to 0.75 over the year, with a reduction in the number of these types of accidents of 18% against 2021. However, we have also seen a 5% increase in work-related injuries that resulted in personnel needing at least one day away from work. We continue to work hard to reduce the number of injuries and illnesses as a result of our activities.

## Summary of financial performance in FY22

Revenue of £4,101.8 million grew by 5% organically, driven largely by recovery across the Group from prior-year COVID-19 impacts and growth in Marine and Nuclear.

Underlying operating profit of £237.7 million was a 13% organic increase on last year (excluding one-off CPBS adjustments in FY21), supported by improved performance from our new operating model and lower COVID-19 business interruption, particularly in Marine, Land and Aviation. This was partly offset by a £22 million programme write-off in the Nuclear sector. Underlying operating margin improved to 5.8% (FY21: 5.5%) driving a 7% increase in underlying basic EPS to 30.7 pence (FY21: 28.8 pence, excluding one-off CPBS adjustments).

Statutory operating profit of £226.8 million compared to a £1,736.7 million loss in the prior year, which included £(1,815.5) million from the CPBS review.

Cash performance was heavily impacted by the settlement of past factors as previously communicated, including pension deficit catch-up payments and efforts to normalise period-end working capital. Underlying free cash flow of £(191.3) million was slightly ahead of our expectations, driven by lower net capex and a tax cash inflow from the settlement of open years with the authorities. Also, the favourable timing of customer receipts and prepayments enabled the Group to pay-off around £70 million more previous deferred creditors than originally planned, as well as £23.3 million of scheduled FY23 pension payments and settling the c.£15 million Italian fine.

**DEVONPORT, UK**
**A visit to Devonport Royal Dockyard.**

## Trading in first quarter of FY23

Trading in the quarter ended 30 June 2022 was in line with expectations. Net debt excluding operating leases was £625 million, higher than at 31 March 2022, reflecting timing of pension deficit payments.

## Outlook

We are pleased with the strong progress made in FY22 to stabilise the Group and begin the process of driving improvements in the areas we identified at the beginning of the year. In particular, the material steps we have taken to address the balance sheet and the quality of our cash flow mean that we ended the year in a far stronger position than we began.

With the business stabilised, we are in a stronger position, both financially and operationally, with the prospects for the business similarly improved. Although we are not immune to the various macro challenges, such as inflation, that continue to impact and shape the markets in which we operate, we will be as agile as we can be in response.

The second year of our turnaround will be as important as the first as we to build further on the foundations laid for a better Babcock in FY23. We will continue the drive to achieve efficiencies from better execution, including the expected c.£20 million further restructuring benefit, and to capture the increasing opportunities for growth in our core markets.

As we look ahead, and as we continue to make operational progress through the disciplined execution of our strategy, the Board is confident of delivering on its expectations of increasingly profitable growth and improved cash flow for FY23. Looking further ahead, we believe our strategy and focus on operational execution will significantly improve the Group's growth, profitability and cash generation over the medium term.

**BECKTON, UK**
**A visit to the London Fire Brigade training centre.**

## Delivering for all our stakeholders

Over the medium and long-term, we are focused on delivering value for all our stakeholders, including:

- **Improved outcomes for our customers:** consistent delivery and partnering with customers to solve their challenges
- **A better place to work for our employees:** an open, collaborative and diverse workplace that engages our employees
- **Returns for our shareholders:** a return to growth with improving margins and better cash conversion

We have made strong progress to position the Company for future success. There is still much to do, but we have all the elements in place to take advantage of the many opportunities which lie before us.

**DAVID LOCKWOOD**
**Chief Executive Officer**

## OTHER INFORMATION

### Dividend

No ordinary dividends have been paid or declared for the financial year ended 31 March 2022.

### AGM

We will be holding our Annual General Meeting on 19 September 2022.

### Board changes

In January 2022 we welcomed John Ramsay to the Board as a Non-Executive Director. John became Chair of the Audit Committee in February 2022.

Myles Lee and Victoire de Margerie retired as Non-Executive Directors at the AGM in September 2021 after six and five years of service respectively. Russ Holden will retire as a Non-Executive Director in July 2022 after two years of service, and our 2022 AGM will see Non-Executive Director and Remuneration Committee Chair Kjersti Wiklund retire from the Board after four years of service.

# Led by our Purpose

Our Purpose is to ***create a safe and secure world, together*** – this is why we exist as a business, and why we do what we do. It defines and underpins our new ways of working, how we create value for our shareholders and how we improve delivery for our customers. It informs the decisions we make and how we treat each other.

Our Purpose and Principles were formally launched this year to support the major cultural shift the business is making. They were developed with the help of our people and are designed to unite us as a company, inspire our thinking, guide our actions, and encourage us to support each other in achieving our vision of a safe, strong, sustainable Babcock.

We are embedding our Principles across the business and applying them to the way we operate. We have built awareness through increased communication and direct engagement with our front-line leaders.

We have helped managers, teams and individuals to explore how to bring the Purpose and Principles to life, through 'town hall' meetings, vlogs, videos, workshops, webinars, team discussions and focused weeks. Our people have embraced the new Principles by sharing personal stories of the Principles in action, and why they are important to them. We will continue to collect and share these stories across the business.

The next phase of this work is to embed the Principles into all of our people processes, and transform at pace how we recruit, lead, develop, recognise, reward and manage the performance of our people.

Our Principles put people at the core of everything we do and they will continue to guide how we all work together, from the front-line to the Board.

*You can see our Principles on page 20*

## Our new operating model

To further unlock our potential, we developed and implemented a new operating model during 2021. The resulting changes saw us reduce headcount, remove layers, and simplify how we work together, underpinned by our Principles.

One of the most significant changes in the period was the move to a centrally coordinated functional model, impacting areas such as HR, Finance, Procurement and Supply Chain, Communications and IT. This new way of working has empowered us to operate as one Babcock, driving accountability, efficiency and consistency across the Group.

Coupled with the new operating model and the cultural reset, we have focused on reducing complexity in the business to make us more efficient. By integrating the Group, we have increased our ability to respond quickly to changing market conditions, sharing capability and solving challenges across Babcock. The roll-out of our new People Strategy has begun and will strengthen our ability to be flexible, enabling us to move talent, innovation, and best practice around the Group and to support our people with an agile and inclusive workplace and an increased focus on output and delivery.

These changes have reinforced our commitment to being a purpose-led business, which will help to transform the experience of our people and customers, and will drive improved performance across the Group.

## Harnessing expertise

Over the past year we have accelerated our knowledge-transfer and sharing programmes to harness the engineering and technical expertise of our people and to strengthen and expand our own skills and networks.

Through our Innovation Lunch and Learn programme, our people and partners have come together to deliver over 60 hours of shared training and insight on core programmes to enable a safe and secure workplace for collaboration and learning.

Our Big Ideas programme has seen over 600 new ideas on cost savings, the environment and safety, and identified where and how we can continue to innovate across our business.

## Inclusion and Diversity

We believe being an inclusive business which supports its people and values difference is central to living our Purpose. It is key to creating the right foundations to attract and retain the best, diverse talent. We have recently appointed our first Global Head of Inclusion and Diversity, to develop our approach and to review, design and implement ways of working that empower our people.

*See more about our approach to Inclusion and Diversity on page 64*

## Our People Strategy

Our People Strategy clearly defines our ambition for the future. It recognises the work we have undertaken and, more importantly, identifies the steps needed to achieve our ambition to make Babcock a more efficient, agile, inclusive, sustainable and people-focused business.

We plan to achieve this by providing our people with the tools, flexibility and support they need to unlock their potential and develop the skills required in this ever-changing world.

Underpinned by our Principles, our People Strategy sets out our overarching vision for Babcock and focuses on **five key People goals** to achieve this vision.

**Our People Strategy has five key goals:**

### 1 Demand great leadership
Individuals are supported, valued and engaged to succeed.

### 2 Redefine our ways of working
We build a strong, safe, unified, global business.

### 3 Grow our capability
Everyone can learn, progress and unleash their potential.

### 4 Improve our people experience
People feel part of Babcock; listened to, trusted and able to make a difference.

### 5 Raise the performance bar
We deliver better outcomes for our business, people, customers and communities.

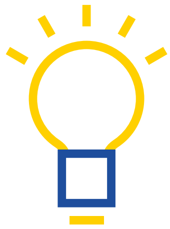
Work is ongoing across these areas, and we are developing a set of metrics that will measure our progress against these goals to ensure we are delivering for our customers, communities and our people.

Our ambition is to attract and retain the best possible people by engaging with our employees, promoting their wellbeing, investing in their development, recognising their commitment and ensuring our employee packages are competitive.

Babcock will be an inclusive and diverse company, a great place to work where people feel part of an integrated, more global business. This will be reflected in how we operate across geographical and business lines, the value we demonstrate in collaborating and the diversity of our leadership and employees across the Group.

## Our People Strategy

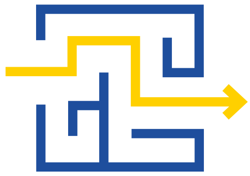
# Our Principles



## be curious

We believe in positively challenging the status quo and asking, 'How might we?'

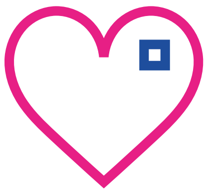
Principles in action on page 50



## think:outcomes

We believe in measuring success by the results we deliver and the positive impact we make.

Principles in action on page 51



## be kind

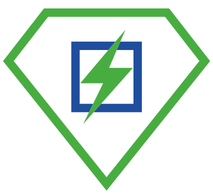
We believe in being kind to ourselves, kind to each other and kind to the planet.

Principles in action on page 90

## collaborate

We believe that Babcock is greater than the sum of its parts.

Principles in action on page 91



## be courageous

We believe in being brave, ambitious and determined.

Principles in action on page 140

## own & deliver

We believe everybody has a part to play in Babcock's and our customers' success.

Principles in action on page 141

# Using innovation and technology to deliver for our customers

Over the past year we've really focused on laying the foundations to drive and deliver innovation in every aspect of our business. We knew that whilst there were areas in which we excelled, we needed to engage our people to ensure that successes and opportunities were shared across our entire Group.

We know innovation is vital to our delivery and our future performance, so we have taken every opportunity to collaborate with our customers, wider stakeholder community, and across our people as we develop our digital and data strategies.

Whilst we've made significant inroads over the past year, we will continue to develop, integrate and collaborate to achieve even more.

## Investment in digital and data

We have been working to create a backbone of data and digital capabilities, using technology where it makes a difference and driving innovation and value for our customers, whatever the engineering challenge.

We've developed our **iSupport360 approach**, which provides real-time monitoring of assets and operations across our business, using a suite of technologies that give us predictive insight and real-time analytics through modelling and simulation, digital twinning and automation of repetitive tasks and processes.

The benefits of collaborating in this way, are that we harness the deep technical skills of our people wherever they are in the world, working across one platform (iSupport360). The assets may be different, the engineering challenge may be different, so getting to the right solution means collaborating to harness the deep engineering and technical expertise we're renowned for. We'll continue to progress on iSupport360 over the coming year.

Our focus is not just on the technology itself, but on how it can improve availability and affordability for our customers and on keeping our front line and our communities safe. In October we showcased what the future of army training could look like at **Army Warfighting Experiment 2021**, the flagship innovation experimentation programme for the British Army. Against a backdrop of increasingly complex and digital battlespace environments, our teams combined techniques such as artificial Intelligence, virtual reality and adaptive learning, to integrate new and existing data which enables us to build an information-rich picture to assess soldier and team performance.

Whilst our customers increasingly turn to us for innovative technology solutions, the challenge of adapting our existing assets to new and emerging technologies requires just as much innovation and commitment, as we highlighted in last year's report. So over the past year we have been harnessing our technology expertise and knowledge transfer to develop and build digital twins for both legacy and new assets, piloted on the Bulldog armoured platform in our Land defence business.

We're already seeing the far-reaching benefits and impact of this pilot. The creation and 'retrofitting' of digital twins onto legacy assets gives us real insight into areas such as future failures, and means we are now able to recognise issues such as previously undiagnosed design faults, and remedy them. The technology we've been developing for the Bulldog programme gives us the potential to save our customers around £60 million over the next 10 years, and also enables us to transform asset support across our entire business, unlocking platform availability for end users and further reducing equipment maintenance and support costs.

## Advanced manufacturing

Since April 2021 we have invested in our advanced and additive manufacturing programme, leading to a new partnership with Plymouth Science Park which launched in February this year.

This partnership, involving access to a brand new manufacturing centre, will enable us to make a step change in our approach to disruptive technologies such as additive manufacturing, allowing us to direct-print metal parts for the first time.

The project builds on our existing plastic additive manufacturing capability, which allowed us to produce personal protective equipment during the COVID-19 pandemic, and our strong relationships with the academic and technology community across the south west of the UK, as well as the local community around Devonport dockyard.

Over the next year, we will be collaborating with our customers to expand this major capability in additive methods, for example to include direct metal laser sintering, which enable us to create high-priority equipment, such as armoured vehicle brake parts.

Ultimately, the collaboration will accelerate our real-world application of additive technologies and help us address the challenges of obsolescence and support chain resilience shared by other engineering communities — especially where we maintain complex and critical equipment over long lifecycles.

Over the coming year we will also use the facility to strengthen our manufacturing and Maintenance, Repair and Overhaul (MRO) skills, working directly with Plymouth Science Park, and through our own internal engagement programmes.

## Digital facility

We have made real progress in establishing our digital facility programme in Rosyth, with a new automated production line for our T31 frigate, focused on three key aspects:

1. **Automating** our traditional shipbuilding methods, driving significant efficiencies.
2. **Digitising** the shop floor, transforming our IT infrastructure and rolling out mobile devices to our people, so they can access data in real time at the point it's required.
3. **Systems integration** from design to project controls and right through to commissioning. We have successfully implemented the design and are building the digital thread working in collaboration with our customer, the UK's Royal Navy.

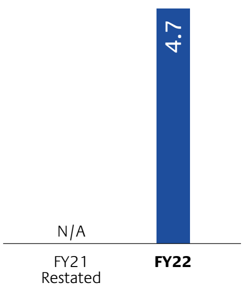
# How we will measure our progress

We have six financial and three non-financial key performance indicators (KPI). The six financial metrics are alternative performance measures, which we use to monitor the underlying performance. These are not defined by International Financial Reporting Standards (IFRS) and are therefore considered to be non-GAAP (Generally Accepted Accounting Principles) measures. The Group has defined and outlined the purpose of its alternative performance measures in the Financial Glossary starting on page 39.

## 2022 RESULTS

### Organic revenue growth (%)

**4.7%**



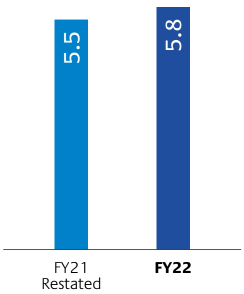

#### Definition
The movement in revenue compared to that of the previous year excluding the impact of FX, contribution from acquisitions and disposals over the prior and current year, and one-off CPBS adjustments in FY21. See note 1 of the accounts for details of our revenue recognition policy and page 165 for an analysis of one-off CPBS adjustments to FY21 revenue.

#### Commentary
Revenue was higher across all sectors organically, driven by recovery from COVID-19 impacts in the prior year across the Group, and growth in Marine and Nuclear.

#### Link to glossary
Organic growth

### Underlying operating margin (%)

**5.8%**



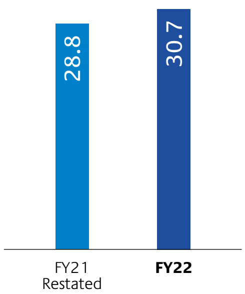

#### Definition
Underlying operating profit, expressed as a percentage of revenue. For FY21, we excluded one-off CPBS adjustments from profit and revenue as this gives the most useful comparator. See page 25 for a reconciliation of statutory to underlying operating profit and an analysis of one-off CPBS adjustments to FY21 underlying operating profit.

#### Commentary
Group margin was higher year on year driven mainly by continued COVID-19 recovery across the Group and operating model cost savings.

#### Link to glossary
Underlying operating margin

### Underlying EPS (p)

**30.7p**



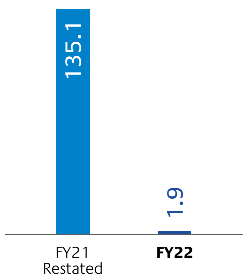

#### Definition
Underlying earnings, after tax divided by the weighted average number of ordinary shares. For FY21, we excluded the one-off CPBS adjustments as this gives the most useful comparator.

#### Commentary
Excluding one-off CPBS adjustments in FY21, underlying earnings per share increased 7% in the year, reflecting higher profit before tax and a higher effective tax rate of 26% (FY21: 21%), due to a one-off tax adjustment relating to prior periods.

#### Link to glossary
Underlying basic earnings per share

### Underlying operating cash conversion (%)

**1.9%**




#### Definition
Underlying operating cash conversion is defined as underlying operating cash flow after capital expenditure as a percentage of underlying operating profit. For FY21, we have excluded the one-off CPBS adjustments on underlying operating profit as this gives the most useful comparator.

#### Commentary
Underlying operating cash conversion in FY22 was driven by low operating cash flow as a result of planned working capital outflows, although overall it was slightly higher than expected due the timing of customer receipts and prepayments.

#### Link to glossary
Underlying operating cash conversion

### Net debt/EBITDA (covenant basis)

**1.8x**


#### Definition
Net debt to EBTIDA as measured in our banking covenants. This uses net debt (excluding operating leases) divided by underlying earnings before interest, tax, depreciation and amortisation plus JV dividends received. For FY21, we excluded the one-off CPBS adjustments. This definition makes a series of adjustments to both Group net debt and Group EBITDA, see page 33 for a reconciliation.

#### Commentary
Our net debt to EBITDA (covenant basis) decreased to 1.8 times at 31 March 2022 driven by the reduction in net debt, principally from disposals, which was proportionally greater than the decrease in EBITDA + JV and associate dividends.

#### Link to glossary
Net debt/EBITDA (covenant basis)

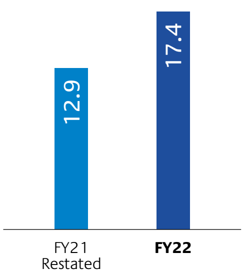
### Our approach

We went through the process of the contract profitability and balance sheet review (CPBS) in FY21 to set our approach to running the Group, including creating the right baseline for future performance. We show our financial-based KPI performance for two years, excluding one-off CPBS adjustments in FY21 to provide a meaningful measurement and ongoing baseline, and reflect how we assess operational performance. Previously we presented the data including one-off CPBS adjustments.

## NON-FINANCIAL

### Underlying return on invested capital, pre-tax (ROIC) (%)

**17.4%**




#### Definition

Underlying return on invested capital is defined as underlying operating profit plus share of JV profit after tax, excluding one-off CPBS adjustments in FY21, divided by the sum of Net debt, shareholders' funds and retirement deficit or surpluses.

#### Commentary

The increase in underlying ROIC reflects higher underlying operating profit and share of JV profits after tax, and lower invested capital due to reduced debt and change in our IAS 19 pension from deficit to surplus.

#### Link to glossary

Return on invested capital (pre-tax) (ROIC)

### Total injuries rate

**0.75**


#### Definition

Reported number of recordable work-related injuries and illnesses per 200,000 working hours (200,000 represents 100 employees working 40 hours for 50 weeks per year).

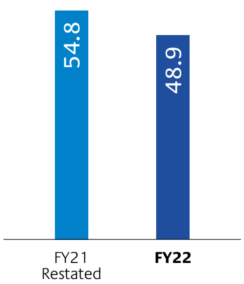
#### Commentary

We have moved to an internationally recognised HSE accident categorisation method in order to be able to benchmark vs peers.

Total Recordable Injury rate, which includes work related injuries requiring medical treatment or above, has reduced from 0.89 to 0.75 over the year, which is a reduction of 18% vs 2021. (See page 63 - 64 for more details).

### $CO_2e$ emissions ($tCO_2e$/£m)

**48.9**




#### Definition

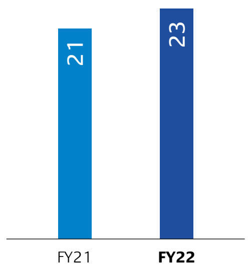
Estimated tonnes of $CO_2e$ emitted as a direct result of revenue generating operations. We now report energy consumption and carbon emissions per calendar year (01 January to 31 December). The transition has allowed more time to collate, analyse and report our environmental data, which has improved the accuracy and completeness of our data sets.

#### Commentary

During the year, estate rationalisation, strategic divestments, 'low-hanging fruit' energy conservation measures and improvements to our energy management practices resulted in a reduction of both our carbon baseline and FY22 operational emissions. (See page 57 for more details).

### Senior management gender diversity (%)

**23%**




#### Definition

Senior managers are defined as employees (excluding Executive Directors) who have responsibility for planning, directing or controlling the activities of the Group (Exco) or a strategically significant part of the Group (Sector/Functional leadership teams) and/or who are directors of subsidiary business units (Business Unit leadership).

#### Commentary

There has been an improvement in female gender representation at the senior management level that has resulted in an increase from 21% to 23% over the past year. (See page 65 for more details on gender diversity statistics).

### Link to management remuneration

Our remuneration policy, as detailed on pages 118 to 124, includes reference to underlying EPS, underlying operating cash flow and underlying ROCE, a measure similar to ROIC.

### Operational performance measures

In the operational reviews on pages 42 - 49, we use our first two KPIs (revenue growth and underlying operating margin) to measure sector performance.

# Financial Review

DAVID MELLORS
Chief Financial Officer

## Overview

We are encouraged by our financial performance in the first year of our turnaround. We delivered year-on-year profit improvement and a cash outturn that was ahead of our expectations. The actions we have taken have significantly strengthened the balance sheet and improved the quality of cash flows. We have met, and in some cases exceeded, the financial targets we set ourselves a year ago, including delivering £20 million savings from the implementation of our new operating model, generating more than £400 million of proceeds from our disposals, and reducing gearing to our FY22 target of below 2.0x.

## Group statutory results

| | 31 March 2022 £m | 31 March 2021 (restated)* £m |
|---|---|---|
| **Revenue** | 4,101.8 | 3,971.6 |
| **Operating profit/(loss)** | 226.8 | (1,736.7) |
| Other income | 6.2 | – |
| Share of results of joint ventures and associates | 20.1 | (13.1) |
| Investment income | 0.8 | 0.9 |
| Other net finance costs | (71.6) | (62.1) |
| **Profit/(loss) before tax** | 182.3 | (1,811.0) |
| Income tax benefit/(expense) | (14.4) | 8.0 |
| **Profit/(loss) after tax for the year** | 167.9 | (1,803.0) |
| **Basic EPS** | 32.5p | (357.0)p |
| **Diluted EPS** | 32.1p | (357.0)p |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

In the year ended 31 March 2022, we reflected prior period restatements to FY21 that arose from further scrutiny of prior periods and benefited from refreshed challenge from the new auditors. These include adjustments for non-cash items in pensions, impairment and derivative accounting, as well as changes in the judgement of certain pass-through revenue now being treated as net within cost of sales. The impact of these restatements on revenue and underlying operating profit for the year ended 31 March 2021 was £0.2 million and £0.3 million respectively.

### Statutory performance

Revenue of £4,101.8 million was 3% higher than last year, driven by recovery across the Group's businesses that were impacted by COVID-19 and the one-off CPBS reduction in revenue of £88.3 million in FY21 which did not repeat in FY22. Offsetting this was the net year-on-year reduction from disposals and a slight adverse impact from foreign exchange.

Statutory operating profit of £226.8 million compared to a £1,736.7 million loss in the prior year, which included charges from the CPBS of £274.7 million (of which £250.0 million was one-off and £24.7 million was recurring), and asset impairments of £1,566.3 million. Statutory operating profit in FY22 includes profit as a result of acquisitions and disposals of £172.8 million (FY21: £49.7 million loss), £123.6 million impairment of goodwill and intangible assets relating to the AES businesses that were subject to a signed disposal agreement in July 2022, amortisation of acquired intangibles of £21.4 million (FY21: £40.2 million) and £33.8 million restructuring (FY21: £8.4 million). See Note 2 of the financial statements.

Other income of £6.2 million (FY21: £nil) related to pre-completion guarantee fees received in relation to one of the divested businesses during the year. The share of results of joint ventures (JVs) and associates was higher than the prior year, mainly due to the CPBS loss in FY21 of £37.1 million. Other net finance costs increased to £71.6 million (FY21: £62.1 million), with lower net interest costs due to lower average debt and reduced IFRS 16 lease interest, more than offset by a £7.1 million higher pension finance charge and a one-off, non-cash finance charge on derivative instruments of £9.6 million. Profit before tax was £182.3 million (FY21: £1,811.0 million loss). Basic earnings per share, as defined by IAS 33, was 32.5 pence (FY21: (357.0) pence) per share. A full income statement can be found on page 159.

# Underlying results

## Statutory to underlying

As described in the 'Financial Glossary – alternative performance measures' on page 24, the Group provides underlying measures to better understand the performance and earnings trends of the Group. Underlying operating profit and underlying earnings per share exclude certain specific adjusting items that can distort the reporting of underlying business performance, as set out in Note 3 of the financial statements on page 180. The reconciliation from the IFRS statutory income statement to underlying income statement is shown below:

| | 31 March 2022 | | | 31 March 2021 (restated)* | | |
|---|---|---|---|---|---|---|
| | Underlying £m | Specific adjusting items £m | Statutory £m | Underlying £m | Specific adjusting items £m | Statutory £m |
| **Revenue** | 4,101.8 | – | 4,101.8 | 3,971.6 | – | 3,971.6 |
| **Operating profit/(loss)** | 237.7 | (10.9) | 226.8 | (27.9) | (1,708.8) | (1,736.7) |
| Other income | 6.2 | – | 6.2 | – | – | – |
| Share of results of joint ventures and associates | 20.1 | – | 20.1 | (13.1) | – | (13.1) |
| Investment income | 0.8 | – | 0.8 | 0.9 | – | 0.9 |
| Other net finance costs | (62.0) | (9.6) | (71.6) | (62.1) | – | (62.1) |
| **Profit/(loss) before tax** | 202.8 | (20.5) | 182.3 | (102.2) | (1,708.8) | (1,811.0) |
| Income tax (expense)/benefit | (43.9) | 29.5 | (14.4) | (21.8) | 29.8 | 8.0 |
| **Profit/(loss) after tax for the year** | 158.9 | 9.0 | 167.9 | (124.0) | (1,679.0) | (1,803.0) |
| **Basic EPS** | 30.7p | | 32.5p | (24.6)p | | (357.0)p |
| **Diluted EPS** | 30.4p | | 32.1p | (24.6)p | | (357.0)p |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

## Specific adjusting items

Specific adjusting items within operating profit of £(10.9) million (FY21: £(1,708.8) million) includes profit resulting from acquisitions and disposals of £172.8 million (FY21: £49.7 million loss), a further £9.7 million of costs incurred in relation to the Group's divestment programme for disposals that have not completed, operating model and restructuring costs of £33.8 million (FY21: £8.4 million), and exceptional charges of £118.1 million (FY21: £1,590.5 million). Exceptional items in FY22 include £123.6 million impairment of goodwill and intangible assets relating to the AES businesses that were subject to a signed disposal agreement in July 2022, offset by a £3.6 million release of provisions relating to the Italy fine and £1.8 million release of onerous contract provisions. Exceptional items in FY21 were dominated by asset impairments as a result of the CPBS. As previously stated, we intend to restrict the use of exceptional items in future periods.

## Underlying results excluding one-off CPBS adjustments in FY21

For the most useful comparison to FY21, we focus on the last years' underlying operating profit excluding one-off CPBS adjustments. We believe this to be the most helpful measure for stakeholders to judge our performance this year. Going forward we will not report on this basis as there will be no CPBS year-on-year impact.

| | | 31 March 2022 £m | | 31 March 2021 (restated)* £m |
|---|---|---|---|---|
| **Revenue** | | 4,101.8 | | 3,971.6 |
| *of which one-off CPBS adjustments* | | – | | 88.3 |
| *Revenue excluding one-off CPBS adjustments in FY21* | | 4,101.8 | | 4,059.9 |
| **Underlying operating profit/(loss)** | | 237.7 | | (27.9) |
| *of which one-off CPBS adjustments* | – | | (250.0) | |
| *Underlying operating profit excluding one-off CPBS adjustments* | *237.7* | | *222.1* | |
| *Underlying margin excluding one-off CPBS adjustments* | *5.8%* | | *5.5%* | |
| Other income | | 6.2 | | |
| Share of results of joint ventures and associates | | 20.1 | | (13.1) |
| *of which CPBS one-off impacts* | – | | *(31.5)* | |
| *Share of results of JVs and associates excluding one-off CPBS adjustments* | *20.1* | | *18.4* | |
| Investment income | | 0.8 | | 0.9 |
| Other net finance costs | | (62.0) | | (62.1) |
| **Underlying profit/(loss) before tax** | | 202.8 | | (102.2) |
| Income tax | | (43.9) | | (21.8) |
| **Underlying profit/(loss) after tax** | | 158.9 | | (124.0) |
| Non-controlling interests | | 3.7 | | – |
| **Underlying profit attributable to shareholders** | | 155.2 | | (124.0) |
| **Underlying basic EPS** | | 30.7p | | (24.6)p |
| *Underlying basic EPS excluding one-off CPBS adjustments*** | *30.7p* | | *28.8p* | |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement
** Estimated in FY21 based on an underlying effective tax rate of 21%

## Revenue performance

| | 31 March 2021 (restated)* £m | One-off CPBS in FY21 £m | 31 March 2021 (excl. one-off CPBS adj.) £m | FX impact £m | Acquisitions & disposals £m | COVID-19 recovery (estimated) £m | Other trading £m | 31 March 2022 £m |
|---|---|---|---|---|---|---|---|---|
| Marine | 1,230.6 | 8.6 | 1,239.2 | (0.6) | (24.3) | (10.2) | 55.2 | 1,259.3 |
| Nuclear | 975.9 | 2.2 | 978.1 | – | – | 0.4 | 31.2 | 1,009.7 |
| Land | 910.7 | 60.7 | 971.4 | – | (27.1) | 103.2 | (32.0) | 1,015.5 |
| Aviation | 854.4 | 16.8 | 871.2 | (22.0) | (75.4) | 38.5 | 5.0 | 817.3 |
| Total | 3,971.6 | 88.3 | 4,059.9 | (22.6) | (126.8) | 131.9 | 59.4 | 4,101.8 |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

Revenue for the year was £4,101.8 million, 5% higher than last year on an organic basis excluding one-off FY21 CPBS adjustments, foreign exchange and the impact of acquisitions and disposals. All sectors grew organically driven by recovery from COVID-19 impacts in the prior year, with further underlying growth in Marine from the ramp-up of new and early-stage contracts, including Type 31, and in Nuclear, from additional submarine infrastructure activity. See sector operational reviews on pages 42 to 49.

The main variances year-on-year (compared to revenue before one-off CPBS adjustments in FY21) are:

- **FX impact (1)%** – this primarily relates to foreign exchange translation on the results of our European Aviation businesses
- **Acquisitions and disposals (3)%** – this reflects lower net revenue from the sale of Cobras (sold in October 2020 – Land), Oil and Gas aviation (sold in August 2021 – Aviation), Frazer-Nash Consultancy Ltd (sold in October 2021 – Marine), UK Power (sold in December 2021 – Land), and a modest contribution from the NSM acquisition in March 2022 (Marine)
- **COVID-19 recovery 3%** – this reflects our estimate of revenue recovered in our businesses that were impacted by COVID-19 in FY21, most notably across our South African contracts and civil training business in the Land sector, and aerial emergency services (AES) activities in the Aviation sector. The COVID-19 revenue impact in Marine is negative, reflecting the ventilators project in FY21 that did not repeat in FY22
- **Other trading 2%** – excluding COVID-19 recovery factors, there was growth in Marine from further ramp-up of work on the Type 31 frigate programme, new contracts in Mission Systems and demand for LGE products, and in Nuclear, driven by the continued ramp-up in submarine infrastructure programmes. On the same basis, Land decreased, with higher activity in Rail more than offset by the impact of the loss of the Heathrow baggage contract in the prior year and the Eskom support contract in South Africa in FY22

## Underlying operating profit performance

| | 31 March 2021 (restated)* £m | One-off CPBS in FY21 £m | 31 March 2021 (excl. one-off CPBS adj.) £m | FX impact £m | Acquisitions & disposals £m | COVID-19 recovery (estimated) £m | Pension movements £m | Other trading £m | 31 March 2022 £m |
|---|---|---|---|---|---|---|---|---|---|
| Marine | 56.2 | 28.9 | 85.1 | (1.1) | (4.6) | 15.9 | (2.9) | 5.6 | 98.0 |
| Nuclear | 63.8 | 23.4 | 87.2 | – | – | 2.1 | (0.3) | (26.6) | 62.4 |
| Land | (17.5) | 69.3 | 51.8 | 0.1 | (3.2) | 12.8 | 0.1 | (2.8) | 58.8 |
| Aviation | (130.4) | 128.4 | (2.0) | (3.6) | (1.7) | 8.1 | – | 17.7 | 18.5 |
| Total | (27.9) | 250.0 | 222.1 | (4.6) | (9.5) | 38.9 | (3.1) | (6.1) | 237.7 |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

Underlying operating profit of £237.7 million was 7% higher than last year excluding the one-off FY21 CPBS adjustment of £(250) million. Organic growth of 13% was driven mainly by COVID-19 recovery across the Group and operating model cost savings of c.£20 million, achieving our target annualised savings of c.£40 million. By sector, profit improvement in Marine, Land and Aviation more than offset a decline in Nuclear, as a consequence of a programme write-off of £22 million.

The underlying operating margin was 5.8%, up from 5.5% on the same basis (excluding one-off CPBS adjustments in FY21). Three sectors improved their operating margin: Marine by 90bp to 7.8%, Land by 50bp to 5.8% and Aviation by 250bp to 2.3%. Nuclear margin decreased 270bp to 6.2% due to the programme write-off.

The main variances year-on-year (compared to underlying operating profit before one-off CPBS adjustments in FY21) are:

- **FX impact (2)%** – this primarily relates to foreign exchange translation on the results, most notably South Africa and Southern Europe
- **Acquisitions and disposals (4)%** – this is the lower net contribution following completed transactions in the period
- **COVID-19 recovery 18%** – this is the estimate of profit linked to the recovery of activity in business impacted by the pandemic based on an analysis of direct and indirect impacts. The Group saw material profit improvements from recovery of operations and reduced operating costs associated with COVID-19, particularly in Land, Marine and Aviation. Subject to any material unforeseen pandemic-related developments, we do not expect to report separately on its impact in future periods
- **Pension movements (1)%** – this reflects slightly higher IAS 19 pension costs this year split across our sectors
- **Other trading (3)%** – Excluding COVID-19 recovery factors, sector performance was boosted by c.£20 million operating model benefits which more than offset increased business development costs relating to certain large bids and costs of implementing a stronger control environment. In Marine, initial licence fees from the Indonesian AH140 design order and a favourable contract settlement resulted in a strong performance in the second half, while the increase in Aviation profit was driven primarily by the significant milestone achievements in two defence contracts in France and restructuring benefits. Nuclear profit decreased due to the £22 million contract write-off, which more than offset the higher contribution from infrastructure work

Further analysis of our revenue and underlying operating profit performance is included in each sector's operating review on pages 42 to 49.

## Share of results of joint ventures and associates
The Group's share of results in JVs and associates was a profit after tax of £20.1 million in the year (FY21: £13.1 million loss). The improvement year-on-year was due largely to the impact of one-off CPBS charges in FY21 that did not repeat (£(31.5) million) and recovery from COVID-19 impacts, primarily in our Aviation and Land JVs.

The Group's main JVs and associates at 31 March 2022 were:

- Ascent in our Aviation sector, which trains RAF pilots in the UK under the UK Military Flying Training System (UKMFTS) air training contract
- AirTanker Services in our Aviation sector, which operates A330 Voyager aircraft to support air-to-air refuelling, air transport and ancillary services for the UK Ministry of Defence

During the year we sold our 15.4% stake in the AirTanker Holdings Ltd. asset JV. Babcock retains its 23.5% shareholding in AirTanker Services Limited, as described above. In March 2022, we purchased the remaining 50% share in our Naval Ship Management (NSM) JV in our Marine sector, which maintains part of Australia's naval fleet.

## Underlying finance costs
Underlying net finance costs were flat at £62.0 million (FY21: £62.1 million) with lower net interest costs due to lower average debt and reduced IFRS 16 lease interest, offset by a £7.1 million higher pension finance charge and a £9.5 million non-cash charge due to a change in the revaluation methodology of cross currency interest rate swaps.

## Tax charge
The tax charge on underlying profits/(losses) was £(43.9) million (FY21: £(21.8) million) representing an effective underlying rate of 24% (FY21: 21%), compared to the originally expected 23% due to the country profit mix. The underlying effective tax rate is calculated on underlying profit before tax excluding the share of income from JVs and associates (which is a post-tax number).

The Group's effective rate of tax for FY23 will be dependent on country profit mix and the timing of the completion of the AES disposal announced in July 2022. The current assumption is expected to be around 25%. In the medium term, we expect our effective tax rate to increase in conjunction with UK corporation tax rate increases.

## Underlying earnings per share
Underlying earnings per share for the year was 30.7 pence (FY21: (24.6) pence). Excluding one-off CPBS adjustments in FY21, underlying earnings per share increased 7% from 28.8p, reflecting growth in underlying operating profit and other income of £6.2m (guarantee fees earned before completion on one of the FY22 disposals), partly offset by the non-cash finance charge on derivative instruments of £9.6 million and the slightly higher effective tax rate due to the country profit mix.

## Exchange rates
The translation impact of foreign currency movements resulted in a decrease in revenue of £22.6 million and a £4.6 million decrease in underlying operating profit. The main currencies that have impacted our results are the South African Rand and the Euro. The currencies with the greatest potential to impact our results are the Euro, the South African Rand and the Canadian Dollar:

- A 10% movement in the Euro against Sterling would affect revenue by around £40 million and underlying operating profit by around £2 million per annum
- A 10% movement in the South African Rand against Sterling would affect revenue by around £25 million and underlying operating profit by around £2.5 million per annum
- A 10% movement in the Canadian Dollar against Sterling would affect revenue by around £15 million and underlying operating profit by around £1 million per annum

## Disposal programme
Our plan for disposals has been assessed and does not meet the criteria for any assets to be classed as held for sale under IFRS 5.

# Cash flow and net debt

## Statutory cash flow summary

| | 31 March 2022 £m | 31 March 2021 (restated)* £m |
|---|---|---|
| **Profit/(loss) for the year** | 167.9 | (1,803.0) |
| Net cash flows from operating activities | 6.8 | 427.4 |
| Net cash flows from investing activities | 338.6 | (24.4) |
| Net cash flows from financing activities | (122.7) | (1,223.9) |
| **Net increase/(decrease) in cash, cash equivalents and bank overdrafts** | 222.7 | (820.9) |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

### Cash flows from operating activities

Net cash flow from operating activities of £6.8 million was lower compared to last year (FY21: £427.4 million) as expected, driven by a working capital outflow of £(178.9) million (FY21: £333.2 million inflow, which included impacts from the CPBS review) and higher pension deficit payments.

Notwithstanding these outflows, the Group performed better than expected on cash generation from the timing of customer receipts and prepayments, and used this to further accelerate the unwinding of both past working capital management practices (principally deferred creditors, debt factoring) as well as pension deficit repair and payment of the Italian fine of c.£15 million).

### Cash flows from operating activities

Net cash flow from investing activities of £338.6 million increased compared to last year (FY21: £(24.4 million)), primarily due to net cash inflow from disposals and acquisitions of £404.2 million (FY21: £90.6 million).

### Cash flows from financing activities

Net cash flow from financing activities of £(122.7) million principally reflects lease principal payments in the year of £113.0 million (FY21: £140.6 million). The Group repaid bank loans of £31.7 million compared to £1,154 million in FY21.

A full cash flow statement can be found on page 162.

## Movement in net debt

| | 31 March 2022 £m | 31 March 2021 (restated)* £m |
|---|---|---|
| **Net increase/(decrease) in cash in the year** | 222.7 | (820.9) |
| Cash flow from the decrease/(increase) in debt | 55.1 | 1,202.1 |
| **Change in net funds resulting from cash flows** | 277.8 | 381.2 |
| Net additional lease obligations | (93.8) | (82.3) |
| New leases – granted | 41.9 | 13.9 |
| Disposal of subsidiaries | 137.1 | – |
| Other non-cash movements and changes in fair value | (14.2) | 4.2 |
| Foreign currency translation differences | 12.8 | 44.6 |
| **Movement in net debt in the year** | 383.7 | 361.3 |
| Opening net debt | (1,352.4) | (1,713.7) |
| **Closing net debt** | (968.7) | (1,352.4) |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

## Underlying cash flow and net debt

Our underlying cash flows are used by management to measure operating performance as they provide a more consistent measure of business performance year to year.

| | 31 March 2022 Underlying £m | 31 March 2021 Underlying (restated)* £m |
|---|---|---|
| **Operating profit** | 226.8 | (1,736.7) |
| Add back: specific adjusting items | 10.9 | 1,708.8 |
| **Underlying operating profit** | 237.7 | (27.9) |
| One-off CPBS adjustments | – | 250.0 |
| **Underlying operating profit excl. one-off CPBS adjustments** | 237.7 | 222.1 |
| Depreciation & amortisation | 74.4 | 108.0 |
| ROU asset depreciation | 123.1 | 140.2 |
| Non-cash items | 0.6 | 9.1 |
| Working capital movements | (173.9) | 128.9 |
| Provisions | (9.3) | 3.4 |
| Net capital expenditure | (135.2) | (171.1) |
| Lease principal payments | (113.0) | (140.6) |
| **Underlying operating cash flow** | 4.4 | 300.0 |
| *Cash conversion % excl. one-off CPBS adjustment* | *1.9%* | *135.1%* |
| Pension contributions in excess of income statement | (151.7) | (73.5) |
| Interest paid | (45.0) | (67.4) |
| Tax received | 10.0 | 18.4 |
| Dividends from joint ventures and associates | 41.6 | 36.8 |
| Cash flows related to exceptional items | (50.6) | (44.7) |
| **Underlying free cash flow** | (191.3) | 169.6 |
| Net acquisitions and disposals of subsidiaries | 417.2 | 90.6 |
| Acquisitions/investments in joint ventures and associates | (18.1) | (8.8) |
| Dividends paid (including non-controlling interests) | (1.1) | (0.8) |
| Purchase of own shares | – | (2.2) |
| Lease principal payments | 113.0 | 140.6 |
| Leases acquired with subsidiaries | (0.5) | – |
| Leases disposed of with subsidiaries | 137.1 | – |
| Other non-cash debt movements | (2.4) | – |
| Fair value movement in debt | (11.8) | 10.0 |
| Net new lease arrangements | (71.2) | (82.3) |
| Exchange movements | 12.8 | 44.6 |
| **Movement in net debt** | 383.7 | 361.3 |
| Opening net debt | (1,352.4) | (1,713.7) |
| **Closing net debt** | (968.7) | (1,352.4) |
| Add back: operating leases | 412.0 | 582.1 |
| **Closing net debt excluding operating leases** | (556.7) | (770.3) |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

## Underlying cash performance

### Underlying operating cash flow

Underlying operating cash flow for the year after capital expenditure was £4.4 million, compared to £300.0 million inflow in the prior year, primarily due to working capital outflows and lower net capex (see below). The Group used favourable timing of customer receipts and prepayments to further accelerate the unwind of the past practice of period-end working capital management (principally creditor deferrals and debt factoring), pension deficit repair and to pay the Italian fine of c.£15 million, while keeping net debt/EBITDA (covenant basis) below our target of 2.0x. This represented operating cash conversion of 1.9% (FY21: 135.1%) on the underlying operating profit (excluding one-off CPBS adjustments).

### Movements in working capital

The movement in working capital for the year was a £(173.9) million outflow compared to an inflow of £128.9 million last year. The outflow includes the unwind of VAT payments deferred from the previous financial year (£56 million), a reduction in deferred creditors (£130 million) and debt factoring in Southern Europe (by £40 million to £62 million) as we move away from the practice of period-end management of working capital, as well as an increase in amounts recoverable under contract in our Aviation business. The outflow in the year was partly improved by favourable timing of customer receipts and prepayments against long-term contracts that will reverse in FY23.

### Capital expenditure

Gross capital expenditure increased to £203.2 million (FY21: £176.5 million), including £12.4 million of purchases of intangible assets (FY21: £19.6 million). The increase reflects further investment in submarine infrastructure in Devonport, including in 9 Dock, and commencement of enterprise resource planning (ERP) roll-out in Nuclear. Net capex reduced to £135.2 million (FY21: £171.1 million) due to higher proceeds from disposals (£68.0 million (FY21: £5.4 million)), primarily reflecting the disposal and sale and leaseback of aircraft in our Aviation sector. We expect that gross capital expenditure will remain at an elevated level in FY23 as we continue to upgrade our facilities and IT equipment.

### Lease principal payments

Lease principal payments of £113.0 million in the year (FY21: £140.6 million) represents the capital element of payments on lease obligations. This is reversed out below underlying free cash flow as the payment reduces our lease liability.

### Pensions

Pension cash outflow in excess of the income statement charge (excluding exceptional charges for curtailment losses) was £151.7 million (FY21: £73.5 million). As stated above, the Group accelerated a payment of £23.3 million in the year, originally scheduled for FY23. We expect the cash outflow in excess of the income statement charge to be around £100 million in FY23.

### Interest

Net cash interest paid, excluding that paid by JVs and associates, decreased to £45.0 million (FY21: £67.4 million) due to lower net debt, a reduction in interest on leases as a result of the Group's disposal programme and repayment of the US Private Placement debt facility in FY21.

### Taxation

Cash tax in the year was an inflow of £10.0 million, compared to our previous expectation of an outflow of around £30 million, following the settlement of several open years' tax computations with the authorities. We currently expect a cash tax outflow of approximately £20 million in FY23.

### Dividends from joint ventures and associates

During the period the Group received £41.6 million in dividends from its JVs and associates (FY21: £36.8 million). The increase year-on-year reflects close-out dividends on the termination of the ALC and Dounreay JVs, and the final dividend from NSM pre-acquisition. Following the disposal of our 15.4% share in AirTanker Holdings Ltd, we expect dividends from JVs and associates to be around £5 million in FY23.

### Exceptional cash flows

Cash outflows related to exceptional items were £50.6 million compared to £44.7 million last year. These costs included £34 million restructuring costs, which came in slightly below our initial expectations, and the early settlement of the Italy fine of £15 million. In FY23, we anticipate exceptional cash outflows of up to £10 million, principally operating model restructuring costs for which the charge was taken in FY22 or prior.

### Underlying free cash flow
There was an underlying free cash outflow of £(191.3) million (FY21: £169.6 million inflow) reflecting the items set out above including the working capital outflow and pension deficit payments partly offset by lower net capital expenditure.

### Acquisitions and disposals
The net cash inflow from acquisitions and disposals after costs was £417.2 million. This included gross proceeds of £447.3 million (net of cash disposed) from the sale of Oil and Gas (£10.0 million), Frazer Nash Consultancy (£286.8 million), Power (£45.8 million) and our 15.4% shareholding in AirTanker Holdings Limited (£95.6 million), and £(15.5) million cash consideration (net of cash acquired) for the acquisition of the remaining 50% of NSM Limited. Related disposal costs were £17.5 million and there were £9.6 million of costs relating to disposals that have not completed in the year, which was partly offset by a £6.2 million inflow from pre-completion guarantee fees received in relation to a disposal.

### New lease arrangements
In addition to net capital expenditure, and not included in free cash flow, £71.2 million (FY21: £82.3 million) of additional leases were entered into in the period. These represent new lease obligations and so are included in our main net debt figure but do not involve any cash outflows at inception.

### Net debt
The Group's net debt at FY22 was £968.7 million, or £556.7 million excluding operating leases. The reduction in net debt, excluding lease obligations, of £213.6 million reflects the free cash outflow and net divestments set out above, including £137.1 million of leases disposed of with subsidiaries. Our net debt includes balances related to the use of supply chain financing in the Group with extended credit terms. At 31 March 2022 the amount included was £12 million (FY21: £25 million). We are phasing out the regular use of supply chain financing across the Group.

### Funding and liquidity
At 31 March 2022, the Group's net cash balance was £757 million. This combined with the undrawn amount under our committed revolving credit facilities (RCF) gave us liquidity headroom of around £1.7 billion.

As of 31 March 2022, the Group had access to a total of £2.4 billion of borrowings and facilities of mostly long-term maturities. These comprised:

- €550 million bond maturing 6 October 2022 (in April 2021 this was hedged at £482 million)
- New £300 million 3-year RCF maturing 20 May 2024 (signed on 20th May 2021)
- Existing £775 million RCF maturing 28 August 2025; of which £730 million now matures on 28 August 2026
- £300 million bond maturing 5 October 2026
- €550 million bond, hedged at £493 million, maturing 13 September 2027

### Capital structure
An important part of the transformation of Babcock is the strengthening of the balance sheet. While there are several facets to balance sheet strength, the primary measurement relevant to Babcock is the net debt/EBITDA gearing ratio within our debt covenants, which was 1.8x for FY22. The covenant level was temporarily lifted to 4.5x in May 2021, but reverts to 3.5x from September 2022. Having achieved our previous target of leverage under 2.0x, the ratio could increase above 2.0x in the short term, reflecting final pension deficit catch-up payments of c.£100 million and the unwind of the remaining creditor deferrals (c.£35 million). The bulk of these non-recurring cash flows are expected within the first half of FY23. Thereafter, we expect leverage to reduce and are now implementing a medium-term gearing ratio target of 1.0x to 2.0x.

## Subsequent events
On 19 July 2022, we signed a conditional agreement with Ancala Partners for the sale of part of our aerial emergency business including net lease liabilities of £209 million, for a gross cash consideration of £115 million. These businesses provide aerial emergency medical services, firefighting and search & rescue to customers and communities in Italy, Spain, Portugal, Norway, Sweden and Finland. Completion of the agreement is subject to certain regulatory and other conditions. The deal is expected to complete by the end of the calendar year, subject to the satisfaction of the relevant conditions.

## Net debt to EBITDA (covenant basis)

This is the measure used in the covenant in our RCF and makes a number of adjustments from reported net debt and EBITDA. The covenant level is 3.5 times – which was amended to 4.5 times until 31 March 2022. As set out above, our net debt to EBITDA (covenant basis) decreased to 1.8 times for FY22 driven by the reduction in net debt, which was proportionally greater than the decrease in EBITDA + JV and associate dividends.

| | 31 March 2022 £m | 31 March 2021 (restated)* £m |
|---|---|---|
| **Underlying operating profit excl. one-off CPBS adjustments** | 237.7 | 222.1 |
| Depreciation and amortisation | 74.4 | 108.0 |
| Covenant adjustments[1] | (12.9) | (11.5) |
| **EBITDA** | 299.2 | 318.6 |
| JV and associate dividends | 41.6 | 36.8 |
| **EBITDA + JV and associates dividends (covenant basis)** | 340.8 | 355.4 |
| **Net debt excluding operating leases** | (556.7) | (770.3) |
| Covenant adjustments[2] | (60.0) | (94.7) |
| **Net debt (covenant basis)** | (616.7) | (865.0) |
| **Net debt/EBITDA** | 1.8x | 2.4x |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

1. Various adjustments made to EBITDA to reflect accounting standards at the time of inception of the original RCF agreement. The main adjustments are to the treatment of leases within operating profit and pension costs
2. Removing loans to JVs, finance lease receivables and adjusting for an average FX rate for the previous 12 months

## Interest cover (covenant basis)

This measure is also used in the covenant in our RCF, with a covenant level of 4.0x.

| | 31 March 2022 £m | 31 March 2021 (restated)* £m |
|---|---|---|
| **EBITDA (covenant basis) + JV and associate dividends** | 340.8 | 355.4 |
| Finance costs | (60.2) | (55.6) |
| Finance income | 9.6 | 12.6 |
| Covenant adjustments | (1.5) | (0.7) |
| **Net Group finance costs** | (52.1) | (43.7) |
| **Interest cover** | 6.5x | 8.1x |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

## Return on invested capital, pre-tax (ROIC)

This measure is one of the Group's key performance indicators.

| | 31 March 2022 £m | 31 March 2021 (restated)* £m |
|---|---|---|
| **Underlying operating profit** | 237.7 | (27.9) |
| Share of JV PAT | 20.1 | (13.1) |
| **Underlying operating profit plus share of JV PAT** | 257.8 | (41.0) |
| Underlying operating profit excl. one-off CPBS impacts | 237.7 | 222.1 |
| Share of JV PAT excl. one-off CPBS impacts | 20.1 | 18.4 |
| **Underlying operating profit plus share of JV PAT excl. one-off CPBS adjustments** | 257.8 | 240.5 |
| Net debt excluding operating leases | 556.7 | 770.3 |
| Operating leases | 412.0 | 582.1 |
| Shareholder funds | 701.5 | 229.0 |
| Retirement deficit/(surplus) | (191.6) | 278.9 |
| **Invested capital** | 1,478.7 | 1,860.3 |
| **ROIC (pre-tax)** | 17.4% | (2.2)% |
| **ROIC excl. one-off CPBS adjustments (pre-tax)** | 17.4% | 12.9% |

* Refer to Note 3 of the financial statements for details regarding the prior-year restatement

## Pensions

The Group has a number of defined benefit pension schemes. The principal defined benefit pension schemes in the UK are the Devonport Royal Dockyard Pension Scheme, the Babcock International Group Pension Scheme and the Rosyth Royal Dockyard Pension Scheme (the Principal schemes). The nature of these schemes is that the employees contribute to the schemes with the employer paying the balance of the cost required. The contributions required and the assessment of the assets and the liabilities that have accrued to members and any deficit recovery payments required are agreed by the Group with the trustees of each scheme who are advised by independent, qualified actuaries.

The Group's balance sheet includes the assets and liabilities of the pension schemes calculated on an IAS 19 basis. At 31 March 2022, the net position was a surplus of £191.6 million compared to a net deficit of £278.9 million at 31 March 2021. These valuations are based on discounting using corporate bond yields.

The fair value of the assets and the present value of the liabilities of the Group pension schemes at 31 March were as follows:

| | 2022 | | | | 2021 (restated) | | | |
|---|---|---|---|---|---|---|---|---|
| | Principal schemes £m | Railways scheme £m | Other schemes £m | Total £m | Principal schemes £m | Railways scheme £m | Other schemes £m | Total £m |
| **Fair value of plan assets** | | | | | | | | |
| Growth assets | | | | | | | | |
| Equities | 31.6 | 14.3 | 30.6 | 76.5 | 55.0 | 12.5 | 23.0 | 90.5 |
| Property funds | 364.0 | 0.1 | 5.1 | 369.2 | 437.1 | 2.1 | 4.7 | 443.9 |
| High yield bonds/emerging market debt | 44.1 | – | 0.4 | 44.5 | 348.4 | – | – | 348.4 |
| Absolute return and multi-strategy funds | 46.0 | 182.9 | 31.8 | 260.7 | 428.5 | 194.6 | 25.4 | 648.5 |
| Low-risk assets | | | | | | | | |
| Bonds | 1,924.1 | 77.2 | 77.5 | 2,078.8 | 1,422.9 | 54.7 | 83.4 | 1,561.0 |
| Matching assets | 2,094.0 | 1.3 | 101.8 | 2,197.1 | 1,682.7 | 1.7 | 108.5 | 1,792.9 |
| Longevity swaps | (283.5) | – | (10.2) | (293.7) | (250.9) | – | (10.7) | (261.6) |
| **Fair value of assets** | 4,220.3 | 275.8 | 237.0 | 4,733.1 | 4,123.7 | 265.6 | 234.3 | 4,623.6 |
| Percentage of assets quoted | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| Percentage of assets unquoted | – | – | – | – | – | – | – | – |
| **Present value of defined benefit obligations** | | | | | | | | |
| Active members | 756.0 | 65.7 | 35.8 | 857.5 | 857.6 | 126.1 | 39.4 | 1,023.1 |
| Deferred pensioners | 1,066.2 | 93.5 | 132.7 | 1,292.4 | 1,227.3 | 107.4 | 152.4 | 1,487.1 |
| Pensioners | 2,170.4 | 167.9 | 53.3 | 2,391.6 | 2,205.1 | 136.1 | 51.1 | 2,392.3 |
| **Total defined benefit obligations** | 3,992.6 | 327.1 | 221.8 | 4,541.5 | 4,290.0 | 369.6 | 242.9 | 4,902.5 |
| **Net (liabilities)/assets recognised in the statement of financial position** | 227.7 | (51.3) | 15.2 | 191.6 | (166.3) | (104.0) | (8.6) | (278.9) |

## Analysis of movement of pensions in the Group statement of financial position

| | 2022 | | | | 2021 (restated) | | | |
|---|---|---|---|---|---|---|---|---|
| | Principal schemes £m | Railways scheme £m | Other schemes £m | Total £m | Principal schemes £m | Railways scheme £m | Other schemes £m | Total £m |
| **Fair value of plan assets (including reimbursement rights)** | | | | | | | | |
| **At 1 April** | | | | | 3,989.2 | 241.4 | 180.7 | 4,411.3 |
| Restatement (note 3) | | | | | (47.0) | – | 10.1 | (36.9) |
| At 1 April (restated) | 4,123.7 | 265.6 | 234.3 | 4,623.6 | 3,942.2 | 241.4 | 190.8 | 4,374.4 |
| Interest on assets | 82.3 | 5.2 | 4.7 | 92.2 | 91.6 | 5.7 | 4.6 | 101.9 |
| Actuarial gain on assets* | 77.0 | 13.1 | (1.7) | 88.4 | 231.5 | 26.3 | 40.0 | 297.8 |
| Employer contributions | 182.5 | 2.6 | 5.1 | 190.2 | 102.5 | 2.8 | 3.5 | 108.8 |
| Employee contributions | 0.2 | – | – | 0.2 | 0.2 | – | – | 0.2 |
| Benefits paid | (245.4) | (10.7) | (5.4) | (261.5) | (244.3) | (10.6) | (4.6) | (259.5) |
| Settlements | – | – | – | – | – | – | – | – |
| **At 31 March** | 4,220.3 | 275.8 | 237.0 | 4,733.1 | 4,123.7 | 265.6 | 234.3 | 4,623.6 |
| **Present value of benefit obligations** | | | | | | | | |
| **At 1 April** | | | | | 3,790.8 | 297.5 | 177.8 | 4,266.1 |
| Restatement (note 3) | | | | | – | – | 10.1 | 10.1 |
| **At 1 April** | 4,290.0 | 369.6 | 242.9 | 4,902.5 | 3,790.8 | 297.5 | 187.9 | 4,276.2 |
| Service cost | 25.6 | 2.0 | 3.5 | 31.1 | 24.1 | 2.0 | 2.0 | 28.1 |
| Incurred expenses | 6.6 | 0.5 | 0.3 | 7.4 | 6.4 | 0.7 | 0.2 | 7.3 |
| Interest cost | 83.8 | 7.3 | 4.8 | 95.9 | 86.4 | 7.0 | 4.5 | 97.9 |
| Employee contributions | 0.2 | – | – | 0.2 | 0.2 | – | – | 0.2 |
| Experience (gain)/loss* | 70.6 | (14.2) | (2.4) | 54.0 | (20.5) | 0.6 | (2.2) | (22.1) |
| Actuarial loss/(gain) – demographics* | (11.5) | (3.5) | – | (15.0) | 8.5 | (0.6) | (0.7) | 7.2 |
| Actuarial (gain)/loss – financial* | (227.3) | (23.9) | (21.9) | (273.1) | 629.7 | 73.0 | 55.6 | 758.3 |
| Benefits paid | (245.4) | (10.7) | (5.4) | (261.5) | (244.5) | (10.6) | (4.4) | (259.5) |
| Past service costs | – | – | – | – | 1.4 | – | – | 1.4 |
| Curtailment | – | – | – | – | 7.5 | – | – | 7.5 |
| **At 31 March** | 3,992.6 | 327.1 | 221.8 | 4,541.5 | 4,290.0 | 369.6 | 242.9 | 4,902.5 |
| **Net surplus/(deficit) at 31 March** | 227.7 | (51.3) | 15.2 | 191.6 | (166.3) | (104.0) | (8.6) | (278.9) |

* Remeasurement of net retirement benefit obligations resulted in a gain of £322.5 million (2021: £445.6 million)

## Accounting valuations

The IAS 19 valuation for accounting purposes showed a market value of assets of £4,733.1 million, net of longevity swaps and the MOD indemnity for BNSPS, in comparison to a valuation of the liabilities of £4,541.5 million. The total net accounting surplus, before allowing for deferred tax, at 31 March 2022, was £191.6 million (2021: deficit of £278.9 million), representing a 104.2% funding level. A summary of the key assumptions used to value the largest schemes is shown below. The most significant assumptions that impact on the results are the discount rate and the expected rate of inflation. As the IAS19 accounting valuation uses corporate bond yields as a discount rate, the net surplus (deficit) position can materially differ from an actuarial valuation, which typically uses gilts based discount rates.

| | Devonport Royal Dockyard Scheme | | Babcock International Group Scheme | | Rosyth Royal Dockyard Scheme | |
|---|---|---|---|---|---|---|
| | 2022 | 2021 | 2022 | 2021 | 2022 | 2021 |
| Discount rate % | 2.7 | 2.0 | 2.7 | 2.0 | 2.7 | 2.0 |
| Inflation rate (RPI) | 3.7 | 3.2 | 3.7 | 3.2 | 3.7 | 3.2 |
| Inflation rate (CPI) | 3.2 | 2.7 | 3.2 | 2.7 | 3.2 | 2.7 |
| Rate of increase in pensions in payment % | 3.2 | 2.7 | 3.5 | 3.1 | 3.7 | 3.2 |
| Total life expectancy for current pensioners aged 65 (years) | 85.9 | 85.7 | 86.8 | 87.1 | 85.0 | 84.8 |

An estimate of the actuarial deficits of the Group's defined benefit pension schemes, including all longevity swap funding gaps, calculated using each Scheme's respective technical provisions basis, as at 31 March 2022 was approximately £400 million (2021: c.£600 million), such valuations use discount rates based on UK gilts – which differs from the corporate bond approach of IAS 19 above. This technical provision estimate is based on the assumptions used within the latest agreed valuation prior to 31 March 2022 for each of the three main schemes and does not fully allow for the impact of RPI reform which will be fully reflected in future technical provisions valuations.

## Governance

The Group believes that the complexity of defined benefit schemes requires effective governance and supports an increasingly professional approach. Each of the largest schemes have independent trustees and professional trustees with specialist investment expertise.

## Pensions management

The Group continues to review its options to reduce the risks inherent in its schemes. It has employees earning benefits in the Babcock International Group Pension Scheme, the Devonport Royal Dockyard Pension Scheme, the Babcock Rail Ltd Shared Cost Section of the Railways Pension Scheme, the Cavendish Nuclear section of the Magnox Group section of the Electricity Supply Pension Scheme and the Babcock Clyde Section of the Citrus Pension Plan, as well as employees in local and central government schemes. All the occupational defined benefit pension schemes have been closed to new members for some years.

The Group also provides an occupational defined contribution pension scheme used to comply with the automatic enrolment legislation across the Group for all new employees and for those not in a defined benefit pension scheme. Over 75% of its UK employees are members of the defined contribution pension scheme. The Group pays contributions to this scheme based on a percentage of employees' pay. It has no legal obligations to pay any additional contributions. All investment risk in the defined contribution pension scheme is borne by the employees.

## Investment strategy

In recent years, the Group has agreed investment strategies with the trustees of the Babcock International Group Pension Scheme and the Rosyth Royal Dockyard Pension Scheme designed to target these schemes being self-sufficient by 2026, and with the trustees of the Devonport Royal Dockyard Pension Scheme designed to target self-sufficiency for this scheme by 2030. The schemes also operate within agreed risk budgets to ensure the level of risk taken is appropriate. To implement the investment strategies, each of the three largest schemes' Investment Committees has divided its scheme's assets into growth assets, low risk assets and matching assets, with the proportion of assets held in each category differing by scheme reflecting the schemes' different characteristics and funding strategies. The matching assets are used to hedge against falls in interest rates or rises in expected inflation. The level of hedging is steadily increased as the funding level on the self sufficiency measure increases, such that as at 31 March 2022 approximately 90% of the schemes' liabilities (as measured on a self-sufficiency basis) across the three largest schemes are protected against adverse changes in interest rates and inflation.

## Actuarial valuations

Actuarial valuations are carried out every three years in order to determine the Group's cash contributions to the schemes. The valuation dates of the three largest schemes are set so that only one scheme is undertaking its valuation in any one year, in order to spread the financial impact of market conditions. The valuation of the Devonport Royal Dockyard Pension Scheme as at 31 March 2020 was completed in the last financial year, the valuation of the Rosyth Royal Dockyard Pension Scheme as at 31 March 2021 has been completed since the year end, and work has commenced on the valuation of the Babcock International Group Pension Scheme at 31 March 2022.

## Cash contributions

| For year ending 31 March | 2023 (expected) £m | 2022 £m | 2021 £m |
|---|---|---|---|
| Future service contributions | 19.9 | 21.1 | 24.2 |
| Deficit recovery | 88.3 | 135.2 | 51.6 |
| Longevity swap | 15.6 | 16.8 | 16.3 |
| **Total cash contributions — employer** | 123.8 | 173.1 | 92.1 |

Cash contributions made by the Group into the defined benefit pension schemes, excluding expenses and salary sacrifice contributions, during the last financial year are set out in the table above.

## Income statement charge

The charge included within underlying operating profit for the year to 31 March 2022 was £38.5 million, of which £31.1 million related to service costs and £7.4 million related to expenses. We expect charges of around £33 million in the year to 31 March 2023, split between £26 million of service costs and £7 million of expenses. In addition to this, there was an interest charge of £3.7 million for the year to 31 March 2022 and, for 2023, we expect an interest credit of £6.6 million on the surplus.

## Treasury

Treasury activities within the Group are managed in accordance with the parameters set out in the treasury policies and guidelines approved by the Board. A key principle within the treasury policy is that trading in financial instruments for the purpose of profit generation is prohibited, with all financial instruments being used solely for risk management purposes. The treasury team is only permitted to enter into financial instruments where it has a high level of confidence in the hedged item occurring. Both the treasury department and the sectors have responsibility for monitoring compliance within the Group to ensure adherence to the principal treasury policies and guidelines. The Group's treasury policies in respect of the management of debt, interest rates, liquidity and currency are outlined below. The Group's treasury policies are kept under close review, particularly given the ongoing economic and market uncertainty.

## Debt

### Objective

With debt as a key component of available financial capital, the Group seeks to ensure that there is an appropriate balance between continuity, flexibility and cost of debt funding through the use of borrowings, whilst also diversifying the sources of these borrowings with a range of maturities and rates of interest, to reflect the long-term nature of the Group's contracts, commitments and risk profile.

### Policy

All the Group's material borrowings are arranged by the treasury department, and funds raised are lent onward to operating subsidiaries as required. It remains the Group's policy to ensure the business is prudently funded and that sufficient headroom is maintained on its facilities to fund its future growth.

### Updates

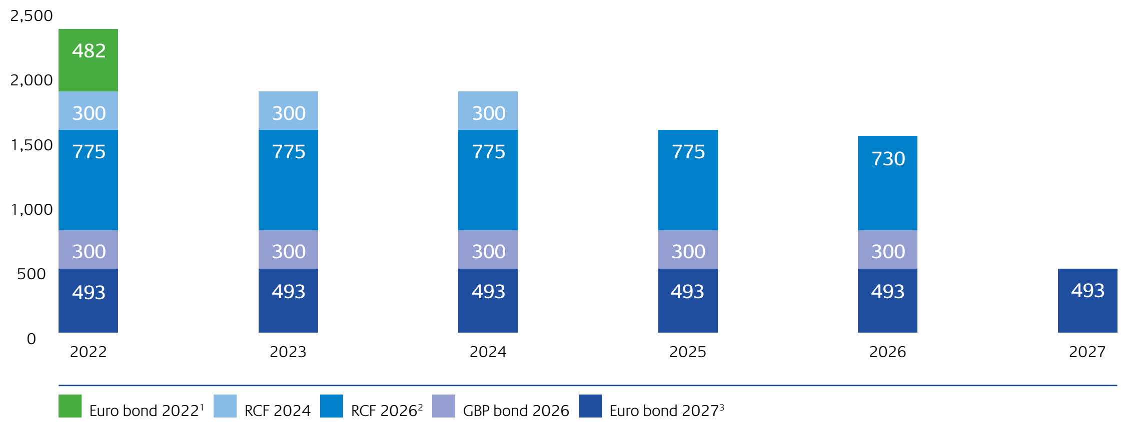
The Group continues to keep its capital structure under review to ensure that the sources, tenor and availability of finance are sufficient to meet its stated objective.

During the financial year, the Group signed a new three-year Revolving Credit Facility (RCF) of £300 million that expires in May 2024. This is in addition to the Group's existing £775 million RCF. At the same time, the Group clarified the definition of underlying results used in the RCF covenant calculations to ensure that any one-off impacts from the Group's contract profitability and balance sheet review ('CPBS') do not impact the calculation and agreed with lenders a temporary amendment to the net debt to EBITDA ratio covenant permitted level to 4.5 times for the measurement periods ending 30 September 2021 and 31 March 2022 after which the permitted level returns to the original 3.5 times. The Group also extended the maturity of £730 million of its existing £775 million RCF to 2026.

The Group's other main corporate facilities comprise of the following: a £300 million Sterling bond, maturing October 2026, a €550 million bond, maturing October 2022, and a €550 million bond, maturing September 2027. Taken together, these debt facilities provide the Group with a total of around £2.4 billion of available committed facilities and bonds.

The Group is planning to repay the bond maturating in October 2022 using cash from disposals.

## Debt maturity profile[4] (£m)




1. Euro bond 2022 €550m hedged at £482m.
2. £730m of £775m RCF extended to 2026.
3. Euro bond 2027 €550m hedged at £493m.
4. Chart shows notional value of the debt.

## Interest rates

### Objective
To manage exposure to interest rate fluctuations on borrowings by varying the proportion of fixed rate debt relative to floating rate debt to reflect the underlying nature of the Group's commitments and obligations. As a result, the Group does not maintain a specific set proportion of fixed versus floating debt, but monitors the mix to ensure that it is compatible with its business requirements and capital structure.

### Policy
Interest rate hedging and the monitoring of the mix between fixed and floating rates is the responsibility of the treasury department and is subject to the policy and guidelines set by the Board and updated from time to time.

### Performance
As at 31 March 2022, the Group had 66% fixed rate debt (31 March 2021: 70%) and 34% floating rate debt (31 March 2021: 30%) based on gross debt of £2,290.1 million (31 March 2021: £2,340.0 million).

## Liquidity

### Objective
I. To maintain adequate undrawn committed borrowing facilities
II. To monitor and manage bank credit risk, and credit capacity utilisation
III. To diversify the sources of financing with a range of maturities and interest rates, to reflect the long-term nature of Group contracts, commitments and risk profile

### Policy
All the Group's material borrowings are arranged by the treasury department and funds raised are lent onward to operating subsidiaries as required.

Each of the Group's sectors provides regular cash forecasts for both management and liquidity purposes. These cash forecasts are used to monitor and identify the liquidity requirements of the Group and ensure that there is sufficient cash to meet operational needs while maintaining sufficient headroom on the Group's committed borrowing facilities.

The Group adopts a conservative approach to the investment of its surplus cash. It is deposited with financial institutions only for short durations, and the bank counter-party credit risk is monitored closely on a systematic and ongoing basis.

A credit limit is allocated to each institution taking account of its credit rating and market information.

### Performance
The Group continues to keep under review its capital structure to ensure that the sources, tenor and availability of finance are sufficient to meet its stated objectives. As noted above, the Group signed a new £300 million RCF and extended the maturity of £730 million of its existing RCF to 2026 during the financial year. Surplus cash during the year was invested in short term deposits diversified across several well rated financial institutions in accordance with policy.

## Foreign exchange

### Objective
To reduce exposure to volatility in earnings and cash flows from movements in foreign currency exchange rates. The Group is exposed to a number of foreign currencies, the most significant being the Euro, US Dollar, South African Rand and increasingly the Australian Dollar, Canadian Dollar, Norwegian Krone and Swedish Krona.

### Policy — Transaction risk
The Group is exposed to movements in foreign currency exchange rates in respect of foreign currency denominated transactions. To mitigate this risk, the Group's policy is to hedge all material transactional exposures, using financial instruments where appropriate. Where possible, the Group seeks to apply IFRS 9 hedge accounting treatment to all derivatives that hedge material foreign currency transaction exposures.

### Policy — Translation risk
The Group is exposed to movements in foreign currency exchange rates in respect of the translation of net assets and income statements of foreign subsidiaries and equity accounted investments. It is not the Group's policy to hedge through the use of derivatives the translation effect of exchange rate movements on the income statement or balance sheet of overseas subsidiaries and equity accounted investments it regards as long-term investments. However, where the Group has material assets denominated in a foreign currency, it will consider some matching of those aforementioned assets with foreign currency denominated debt.

## Financial Glossary – Alternative performance measures

The Group provides alternative performance measures, including underlying operating profit, to enable users to better understand the performance and earnings trends of the Group. These measures are considered to provide a consistent measure of business performance from year to year. They are used by management to assess operating performance and as a basis for forecasting and decision-making, as well as the planning and allocation of capital resources. They are also understood to be used by investors in analysing business performance.

Further information on the Group's Specific Adjusting Items, which is a critical accounting judgement, can be found in Notes 2.

The Group's alternative performance measures are not defined by IFRS and are therefore considered to be non-GAAP measures. The measures may not be comparable to similar measures used by other companies, and they are not intended to be a substitute for, or superior to, measures defined under IFRS.

The Group's alternative performance measures are consistent with the year ended 31 March 2021, except for Contract Backlog, which is redefined to be consistent with the revenue accounting policy change in Note 3 of the preliminary financial statements.

| Measure | Closest equivalent IFRS measure | Definition and purpose | Adjustments to reconcile to IFRS measure (and reference to reconciliation) |
|---|---|---|---|
| **Revenue measures** | | | |
| Revenue excluding the one-off CPBS adjustment | Revenue | Revenue excluding the impact of the one-off CPBS adjustment in FY21<br>• To eliminate the non-recurring element of the CPBS review from FY21 revenue to provide a better measure of growth | One-off CPBS revenue impact<br>• See table on page 25 to 27 |
| Organic growth | Revenue growth year-on-year | Growth excluding the impact of foreign exchange (FX), and contribution from acquisitions and disposals over the prior and current year, and the one-off CPBS adjustment in FY21<br>• Used to measure the year-on-year movement in Group revenue<br>• It is a good indicator of business growth<br>• Group KPI | FX, contribution of acquisitions and disposals in the current and prior year |
| Contract backlog | IFRS15 | Contracted revenue excluding variable revenue, expected contract renewals, expected revenue from framework agreements and impact of termination for convenience clauses<br>• Used to measure revenue under contract as a good indicator of revenue visibility | |
| **Profit measures** | | | |
| Underlying operating profit | Operating profit | Operating profit before the impact of Specific Adjusting Items[1]<br>• Underlying operating profit is the headline measure of the Group's performance | Specific Adjusting Items[1]<br>• See table on page 25<br>• See note 2 |
| Underlying operating margin | No direct equivalent | Underlying operating profit as a percentage of revenue<br>• To provide a measure of operating profitability, excluding one-off items<br>• Operating margin is an important indicator of operating efficiency across the Group<br>• Group KPI | Ratio – N/A |
| Underlying net finance costs | Net finance costs | Net finance costs excluding Specific Adjusting Items[1]<br>• To provide an alternative measure of underlying finance costs excluding items such as fair value measurements which can fluctuate significantly on inputs outside of management's control | Specific Adjusting Items[1]<br>• See table on page 25 |
| Underlying profit before tax | Profit before tax | Profit before tax adjusted for<br>• The summation of the impact of all adjusting items on profit before tax | Specific Adjusting Items[1]<br>• See table on page 25 |
| Underlying effective tax rate | Effective tax rate | Tax expense excluding the tax impact of Specific Adjusting Items[1], as a percentage of underlying profit before tax (being the summation of the impact of all adjusting items on profit before tax) excluding the share of post-tax income from joint ventures and associates<br>• To provide an indication of the ongoing tax rate across the Group, excluding one-off items | Specific Adjusting Items[1]<br>• See table on page 25 |

| Measure | Closest equivalent IFRS measure | Definition and purpose | Adjustments to reconcile to IFRS measure (and reference to reconciliation) |
|---|---|---|---|
| **Profit measures continued** | | | |
| Underlying basic earnings per share | Basic earnings per share | Based on the Group's underlying profit before tax. It includes the Group's post-tax share of results of joint ventures and associates | Specific Adjusting Items[1]<br>• See table on page 25<br>• See Note 10 |
| Underlying operating profit (excluding one-off CPBS adjustment) | Operating profit | Underlying operating profit excluding one-off CPBS adjustment in FY21<br>• Eliminates the non-recurring element of the CPBS review to provide a better measure of underlying operating profit in FY21 | |
| Underlying operating margin (excluding one-off CPBS adjustment) | No direct equivalent | Underlying operating profit divided by revenue, both excluding one-off CPBS adjustment in FY21<br>• Eliminates the non-recurring element of the CPBS review to provide a better measure of underlying operating margin in FY21 | Ratio – N/A |
| Underlying basic (earnings per share excluding one-off CPBS adjustment) | Basic earnings per share | Underlying earnings per share excluding the impact of the one-off CPBS adjustment in FY21<br>• Eliminates the non-recurring element of the CPBS review in FY21 to provide a better measure of underlying earnings growth in the year | Specific Adjusting Items[1] |
| EBITDA | Operating profit | Underlying operating profit excluding one-off CPBS adjustments in FY21, plus depreciation and amortisation, and various covenant adjustments linked to the Revolving Credit Facility including the treatment of leases within operating profit and pension costs<br>- Used as the basis to derive the gearing ratio net debt/EBITDA, which is a key measure of balance sheet strength and the basis of our debt covenant calculations | Specific Adjusting Items[1]<br>Depreciation and amortisation<br>Covenant adjustments<br>• See table on page 33 |
| **Balance sheet** | | | |
| Net debt | No direct equivalent | Cash and cash equivalents and short-term investments, less bank and other borrowings, operating leases and net derivative financial instruments<br>• Used as a general measure of the progress in generating cash and strengthening of the Group's balance sheet position | • See table on page 29<br>• See table on page 30 |
| Net debt (excluding operating leases) | No direct equivalent | Net debt excluding lease liabilities as defined by IAS 17, the relevant standard at the inception of the banking facility. This net debt figure also includes finance lease (as defined by IAS 17) receivables and payables, loans from the Group to joint ventures and supply chain financing balances (of FY22: £12 million, FY21: £25 million)<br>• Used by management to monitor the strength of the Group's balance sheet position and to ensure the Group's capital structure is appropriate<br>• Used by credit agencies | • See table on page 29<br>• See table on page 30 |

1. Refer to Note 2

| Measure | Closest equivalent IFRS measure | Definition and purpose | Adjustments to reconcile to IFRS measure (and reference to reconciliation) |
|---|---|---|---|
| Net debt (covenant basis) | No direct equivalent | Net debt (excluding operating leases), excluding loans to Joint Ventures, finance lease receivables and adjusting for an average FX rate for the previous 12 months<br>• Used by debt investors<br>• Used by credit agencies | • See table on page 33 |
| Net debt/ EBITDA (covenant basis) | No direct equivalent | Net debt (covenant basis) divided by EBITDA<br>- A measure of the Group's ability to meet its payment obligations<br>• Used by analysts and credit agencies<br>• Group KPI | Ratio – N/A<br>• See table on page 33 |
| Return on invested capital (pre-tax) (ROIC) | No direct equivalent | Underlying operating profit plus share of JV PAT, divided by the sum of net debt, shareholders' funds and retirement deficit (surplus)<br>• Used as a measure of profit earned by the Group generated by the debt and equity capital invested, to indicate the efficiency at which capital is allocated<br>• Group KPI | Ratio – N/A<br>• See table on page 33 |
| Return on invested capital excluding one-off CPBS adjustments (pre-tax) | No direct equivalent | Underlying operating profit plus share of JV PAT excluding one-off CPBS adjustments, divided by the sum of net debt, shareholders' funds and retirement deficit (surplus)<br>• Used as a measure of profit earned by the Group excluding the one-off impact of CPBS adjustments generated by the debt and equity capital invested, to indicate the efficiency at which capital is allocated | Ratio – N/A<br>• See table on page 33 |
| **Cash flow measures** | | | |
| Net capital expenditure | No direct equivalent | Property, plant and equipment and intangible assets, less proceeds on disposal of property, plant and equipment<br>- Includes underlying operating cash flow to calculate underlying operating cash conversion | |
| Underlying operating cash conversion | No direct equivalent | Underlying operating cash flow after capital expenditure as a percentage of underlying operating profit<br>• Used as a measure of the Group's efficiency in converting profits into cash | Ratio – N/A |
| Underlying free cash flow | No direct equivalent | Underlying free cash flow includes cash flows from exceptional items and the capital element of lease payment cash flows (rather than net new lease commitments, which are reflected as a debt movement)<br>• Provides a measure of cash generated by the Group's operations after servicing debt and tax obligations, available for use in line with the Group's capital allocation policy | • See page 30 |

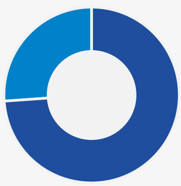
# Marine

| | FY22 | FY21 (Restated) |
|---|---|---|
| Contract backlog | £2.5bn | £2.5bn |
| Revenue | £1,259.3m | £1,230.6m |
| Underlying operating profit | £98.0m | £56.2m |
| *of which CPBS one-off adjustment* | *–* | *£(28.9)m* |
| *Underlying operating profit excluding CPBS one-off adjustment* | *£98.0m* | *£85.1m* |
| *Underlying margin excluding CPBS one-off adjustment* | *7.8%* | *6.9%* |

Revenue
**£1,259m**

Underlying operating profit
**£98m**

### Revenue profile



74% Defence
26% Civil

## What we do

**We ensure the UK Royal Navy goes to sea safely** by supporting their ships and crews around the world

**We support navies around the world** through the delivery of complex ship and submarine sustainment programmes

**We deliver marine technology solutions** to improve our customers' complex, safety-critical operations

## Financial review

Revenue of £1,259.3 million increased 2% (excluding the one-off CPBS adjustment in FY21). Organic growth of 4% was driven by increased activity on the Type 31 programme, initial AH140 export revenue, new contracts in Mission Systems and strong demand for our LGE products. This more than offset the year-on-year impact of COVID-19, including the contribution from the ventilators project in the UK last year and the end of our Royal Naval training contract in FY21.

Underlying operating profit (excluding one-off CPBS adjustments) increased 15% to £98.0 million, or 22% on an organic basis. The main drivers were increased revenue, including COVID-19 recovery and growth in Mission Systems and LGE contracts, operating model efficiencies, a favourable contract settlement and the Indonesia AH140 licence fee, which more than offset significant bid costs on new large opportunities, including Indonesia, Poland and in the UK. As a result, underlying operating margin (excluding one-off CPBS adjustments) improved to 7.8% (FY21: 6.9%).

The disposal of Frazer-Nash Consultancy Ltd completed in August 2021 for a gross consideration of £291.7 million. In March 2022, we acquired the remaining 50% of the Australian Naval Ship Management (NSM) business from joint venture partners for £34 million.

Contract backlog was flat at £2.5 billion, with the addition of two large contracts in Mission Systems combined and growth in LGE orders, replacing revenue traded on long term contracts. At 1 April 2022, Marine had around £0.8 billion of FY23 expected revenue under contract, and an additional c.£460 million under framework agreements, both in line with the FY21 position.

## Operational review

### UK defence

The Type 31 (Inspiration Class) frigate programme remains on schedule, with three major milestones achieved during the year: the first steel cut for HMS Venturer, its subsequent keel laying, and the topping out of our advanced manufacturing facility in Rosyth. The investment across our Rosyth site aims to ensure capability and capacity to support future shipbuilding opportunities. In April 2022, we were awarded a 10-year contract to provide dry-dock maintenance work for the Royal Navy's Queen Elizabeth Class (QEC) aircraft carriers. The contract strengthens Rosyth capabilities in design, build, assembly and support of large ships.

Warship support activity at Devonport was higher year-on-year, with work on the Type 23 frigate programme ahead of last year, which included COVID-19 disruption. We continued to provide the UK's Royal Navy with fleet-time support, deployed support, and deep maintenance, with life extension and refit activity on a number of warships. We also supported the Royal Navy's Carrier Strike Group across multiple platforms and locations, including work on HMS Richmond in Japan, as well as the Type 23, Type 45, the QEC Class and Sandown Class.

We saw several positive developments in our Missions Systems business, including securing a c.£110 million contract to deliver the new Defence Strategic Radio Service to critical military operations and a c.£100 million 13-year contract for the UK MOD for the design, manufacture, delivery and in-service support to the Maritime Electronic Warfare Systems Integrated Capability (MEWSIC). Babcock will act as prime contractor, working with collaboration partners, Elbit Systems UK and QinetiQ.

We achieved full operational capacity in our new Morpheus Logistic Support Contract, which forms part of the UK's Land Environment Tactical Communications and Information Systems programme to deliver next generation tactical communications and information systems for the British Army. We also extended our contracts for Dreadnought launch weapons and signal ejector systems to include further scope on boats two to five.

### International defence

We support international defence markets from our UK operations and from our businesses in Canada, Australia, New Zealand, Oman and South Korea.

### Revenue and underlying operating profit bridge:

| | FY21 (Restated) £m | One-off CPBS adj £m | FY21 Restated (excl. one-off CPBS) £m | FX impact £m | Acquisition and disposals £m | COVID-19 recovery (estimated) £m | Pensions charge £m | Other trading £m | FY22 £m |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | 1,230.6 | 8.6 | 1,239.2 | (0.6) | (24.3) | (10.2) | – | 55.2 | 1,259.3 |
| Underlying operating profit | 56.2 | 28.9 | 85.1 | (1.1) | (4.6) | 15.9 | (2.9) | 5.6 | 98.0 |

In **Australia**, we completed the acquisition of the remaining 50% stake in our Naval Ship Management (NSM) business from our JV partners in March 2022. The NSM acquisition strengthens Babcock's support to the Australian Defence Force's future maritime support model, Plan Galileo. With the signing of a new sustainment contract in New Zealand (see below), Babcock is now the Australasia region's leading warship sustainment enterprise.

In December, we were selected by the Australian Government as the preferred tenderer to upgrade and sustain the Defence High Frequency Communication System (DHFC) to support the Australian armed forces over the next 10 years, with a further four-year extension option, each of two years.

In **New Zealand**, In February 2022, the Defence Force awarded Babcock a new seven-and-a-half year Maritime Fleet Sustainment Services contract to provide full service asset management and engineering to the Royal New Zealand Navy.

In **Canada**, Babcock is continuing to deliver on the Victoria Class In-Service Support Contract (VISSC), supporting Canada's fleet of four submarines. Babcock completed the deep maintenance period of HMCS Corner Brook and is preparing to commence work on the deep maintenance period for HMCS Victoria. Additionally, the Government of Canada has further extended VISSC to June 2025.

In **South Korea**, we signed a Memorandum of Understanding (MoU) with Hyundai Heavy Industries for the CVX Aircraft Carrier Programme opportunity. In March, we signed a further MoU with Daewoo Shipbuilding and Marine Engineering Co Ltd (DSME) to focus on international opportunities, and support system integration on future programmes. The business is benefitting from investment in an assembly, maintenance, repair and overhaul facility in Busan, where Babcock currently assembles equipment for the fifth boat in the Janbogo-III submarine programme.

In **Oman**, our joint venture operation in Duqm with the Oman Drydock Company has completed a first of its kind double engine replacement for a UK Royal Navy Type 23 Class frigate. This enables the Royal Navy to sustain operations within the region and is a clear example of Babcock's global reach. During the period, two packages of work were also completed on US Navy vessels.

In September, we won our first export contract for the AH140 frigate (which Type 31 is based on) through a design licence agreement with PT PAL Indonesia. The design licence will enable PAL to build two frigates in Indonesia with bespoke design modifications for the Indonesian Navy. The second export success came in March 2022, when our design was selected by Poland and Babcock was selected as the design technology partner for Poland's MIECZNIK (Swordfish) frigate programme. Babcock will co-operate with Polish state-owned defence contractor PGZ and other members of the MIECZNIK consortium to adapt the AH140 design and construct the vessels at the PGZ shipyard in Gdynia.

In **Brazil**, we were awarded a four-year contract to deliver through life support to the Marinha do Brasil's flagship vessel, NAM Atlântico, formerly the UK Royal Navy platform HMS Ocean, as part of our global programme.

Our Energy and Marine (LGE) business saw good growth in orders and revenue, with increased commercial vessel work and continued strong demand for liquefied gas handling and re-liquefaction systems across the LPG and LNG markets. The business won many projects in the year from shipyards in South Korea, China and other major international ship-owners.

**NAVAL SHIP MANAGEMENT, SYDNEY, AUSTRALIA**
**Babcock acquired the remaining 50% share of its NSM joint venture in March 2022**

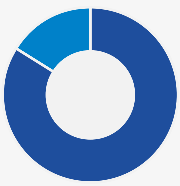
# Nuclear

| | FY22 | FY21 (Restated) |
|---|---|---|
| Contract backlog | £2.8bn | £0.4bn |
| Revenue | £1,009.7m | £975.9m |
| Underlying operating profit | £62.4m | £63.8m |
| *of which CPBS one-off adjustment* | *–* | *£(23.4)m* |
| *Underlying operating profit excluding CPBS one-off adjustment* | *£62.4m* | *£87.2m* |
| *Underlying margin excluding CPBS one-off adjustment* | *6.2%* | *8.9%* |

**Revenue**
**£1,010m**

**Underlying operating profit**
**£62m**

### Revenue profile



| | |
|---|---|
| 84% Defence | |
| 16% Civil | |

### What we do

**We have supported the Continuous At Sea Deterrent** for over 50 years

**We sustain the entirety** of the UK's submarine fleet

**We take a leading role in all civil nuclear:** from new build, to operational support, to decommissioning

## Financial review

Revenue increased 3% to £1,009.7 million (excluding the one-off CPBS adjustment in FY21). This was driven by the continued strong ramp up in submarine infrastructure programmes, which more than offset lower volumes through transition to the new FMSP contract, a £22 million programme write-off and civil nuclear projects which completed in FY21.

Underlying operating profit (excluding one-off CPBS adjustments) fell by 28% to £62.4 million. The key impact in the year was a £22 million programme write-off, which offset higher contribution year-on-year from infrastructure work and operating model savings. As a result of this, and lower initial profit recognition at the start of the FMSP contract, underlying margin for the year fell to 6.2%.

The sector's contract backlog of £2.8 billion (FY21: £0.4 billion) is up significantly due to the signing of the FMSP contract. At 1 April 2022, Nuclear had around £860 million of FY23 expected revenue under contract (FY22: £260 million) and an additional c.£110m under framework agreements (FY21: £640 million).

## Operational review

### Defence

Overall, our defence activity increased driven by the continued ramp-up of the long-term Devonport infrastructure programme to support future demand. The largest current project, the design and enabling work to refurbish 10 Dock and its supporting infrastructure, is underway along with other major projects to support the first deep maintenance period of the Astute Class submarine at Devonport in the next few years. We continue to work on the Revalidation Assisted Maintenance Period (RAMP) programme for the Trafalgar Class and the life extension of the Vanguard Class. We also continue to work with our Submarine Enterprise partners in supporting the design and build programmes for the future classes of submarine, including the Dreadnought Class.

In September 2021, the Future Maritime Support Programme (FMSP) was signed. This five-year contract for around £3.5 billion replaces the previous Maritime Support Delivery Framework (MSDF), and continues our support spanning UK naval base operations at HMNB Devonport and HMNB Clyde and engineering and planning at our Bristol hub, all undertaken alongside surface ship fleet support at Devonport in our Marine sector. We continue to work with our UK MOD customer to ensure the provision of future capability and resilience and to improve decision making across the Submarine Enterprise. The new contract has been identified as a 'Qualifying Defence Contracts' (QDC) and falls under Single Source Contract Regulations (SSCR).

Following the AUKUS announcement to acquire nuclear-powered submarine technology without nuclear armaments, Australia will no longer proceed with the Attack class conventional submarine contract with Naval Group. As a result, our participation in the Attack class programme has ended. Babcock recognises the strategic importance of the AUKUS agreement and continues to be ready to support any future requirement.

### Civil

Momentum in the civil nuclear market is building and the business continues to position for future opportunities. During the year, we secured a five-year extension to the multi-year Design Services Alliance (DSA) engineering framework, worth around £200 million, and a two-year extension to the Pile Fuel Cladding Silo (PFCS) project, both at Sellafield. We continue to support EDF and project volumes are in line with expectations. In new build, Hinkley Point C announced a delay to the project principally because of the impact of COVID-19 on the civil works, which has further delayed the ramp up of our Mechanical, Electrical and HVAC (MEH) Alliance scope further.

Small work packages from the Magnox programme are now being contracted and initiated. During the period we secured two contracts at Hinkley Point A, where we will lead the installation, setting to work and inactive commissioning for the projects as the principal contractor.

## Revenue and underlying operating profit bridge:

| | FY21 (Restated) £m | One-off CPBS adj £m | FY21 Restated (excl. one-off CPBS) £m | FX impact £m | Acquisition and disposals £m | COVID-19 recovery (estimated) £m | Pensions charge £m | Other trading £m | FY22 £m |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | 975.9 | 2.2 | 978.1 | – | – | 0.4 | – | 31.2 | 1,009.7 |
| Underlying operating profit | 63.8 | 23.4 | 87.2 | – | – | 2.1 | (0.3) | (26.6) | 62.4 |

In July 2021, we signed a memorandum of understanding with Rolls-Royce to collaborate on the Small Modular Reactor (SMR) programme to help develop roles across manufacturing, licensing, design and delivery. Babcock, in collaboration with U-Battery, has developed a full-size mock-up of the main vessels of an advanced modular reactor at our Whetstone manufacturing facility. The mock-up intends to demonstrate the potential simplicity in construction and transport of an SMR, making a valuable contribution to the UK's net zero efforts. We also signed a memorandum of understanding with X-Energy, a US reactor and fuel design engineering company, to act as its deployment partner for High Temperature Gas Reactors in the UK. The three technologies are complementary and align with the UK Governments plans to transition to net zero carbon by decarbonising electricity generation and building a hydrogen economy in the UK.

Increasing volatility of national power generation driven by global developments during the year has prompted nations to look at producing and securing their sources of low emission power. In the UK, the Government has backed new nuclear energy supply to deliver both UK energy security of supply and contribute to their target of net zero emissions by 2050. In addition to new policy developments, it has committed around £2.3 billion of funding to support new nuclear programmes. This is a core focus area for our civil nuclear business, and we are well positioned to take advantage of these opportunities.

Internationally, we are now supporting Ontario Power Generation with its decommissioning planning for the Pickering Nuclear Generating Station in Canada. In Japan, relationships continue to strengthen whilst new additional international opportunities are being identified in our focus countries.

VANGUARD CLASS SUBMARINE

# Land

| | FY22 | FY21 (Restated) |
|---|---|---|
| Contract backlog | £2.3bn | £2.4bn |
| Revenue | £1,015.5m | £910.7m |
| Underlying operating (loss) / profit | £58.8m | £(17.5)m |
| *of which CPBS one-off adjustment* | *–* | *£(69.3)m* |
| *Underlying operating profit excluding CPBS one-off adjustment* | *£58.8m* | *£51.8m* |
| *Underlying margin excluding CPBS one-off adjustment* | *5.8%* | *5.7%* |

Revenue
**£1,016m**

Underlying operating profit
**£59m**

### Revenue profile


### What we do

**We ensure the British Army can focus on their missions safely** by supporting vehicles

**We enable the British Army to do their job** with our technical training programmes

**Our people support the British Army** by contributing to front-line support and joining reserve forces

## Financial review

Revenue increased 5% to £1,015.5 million (excluding the one-off CPBS adjustment in FY21). Organic growth of 7% includes recovery from prior year COVID-19 impacts, particularly in South Africa and in our civil training businesses, and higher activity in Rail. This was offset by lower volume on the DSG contract due to project completions, the loss of the Heathrow baggage handling contract in the prior year, and the end of the Eskom power station service contract in the final quarter of FY22.

Underlying operating profit (excluding one-off CPBS adjustments) grew by 14% to £58.8 million or by 19% on an organic basis. The increase reflects a strong recovery from COVID-19 impacts (£12.8 million), operating model efficiencies and growth in Rail, which more than offset lower DSG volume and the loss of the Heathrow contract. As a result, underlying margin improved to 5.8%.

The sector's contract backlog at £2.3 billion (FY21 restated: £2.4 billion), has been adjusted for reclassification of pass-through (principal versus agent) revenue of c.£580 million. The decline reflects small business wins offset by trading and disposals. At 1 April 2022, Land had around £500 million of FY23 expected revenue under contract (FY22: £540 million) and an additional c.£150 million under framework agreements (FY21: c.£120 million).

## Operational review

### Defence

Overall, Land defence activities were broadly flat with further volume recovery from COVID-19 impacts across a number of contracts, offset by lower volumes on the DSG contract.

In line with customer requirements, the DSG transformation programme has been fully implemented and we are now leading several key programmes of improvement focussed on specific outputs for the Army which see us integrating expertise from OEMs, SMEs, and the wider supply chain to improve overall programme potential.

Defence training saw some recovery in activity levels compared to last year. After a highly successful campaign in 2021, we will be participating in the British Army's 2022 Army Warfighting Experiment to demonstrate the integration of a range of innovative collective training capabilities. In the period we were awarded a three-year extension for the Defence College of Technical Training for EMTC 2, the provision of training design and delivery.

### Emergency services

Activity was broadly flat in the period with the first year of the Met Police training contract offset by slightly lower volumes in London Fire Brigade (LFB) contracts. The Police Education and Qualification Framework (PEQF) programme originally launched through a COVID-secure delivery model was returned to operational programme delivery in September 2021.

### South Africa

South Africa grew strongly in the year as activity recovered from COVID-19 impacts. In the final quarter of the year, Eskom made the decision to not extend the engineering services contract which we have run for many years to support state power generation. The impact of the loss of the contract is expected to be around £60 million in revenue for FY23.

### Other civil markets

The Rail business saw growth in volumes on track renewals and signalling framework while our civil training business saw higher activity compared to last year which was affected by COVID-19 related disruption. Our Power business, which we divested in December 2021, contributed revenue of around £62 million and an operating profit of around £5 million in FY22.

## Revenue and underlying operating profit bridge:

| | FY21 (Restated) £m | One-off CPBS adj £m | FY21 Restated (excl. one-off CPBS) £m | FX impact £m | Acquisition and disposals £m | COVID-19 recovery (estimated) £m | Pensions charge £m | Other trading £m | FY22 £m |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | 910.7 | 60.7 | 971.4 | – | (27.1) | 103.2 | – | (32.0) | 1,015.5 |
| Underlying operating profit | (17.5) | 69.3 | 51.8 | 0.1 | (3.2) | 12.8 | 0.1 | (2.8) | 58.8 |

**ARMY WARFIGHTING EXPERIMENT**
**Our vehicle and training expertise is demonstrated during the British Army's annual Army Warfighting Experiment.**

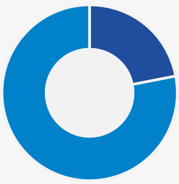
# Aviation

| | FY22 | FY21 |
|---|---|---|
| Contract backlog | £2.3bn | £2.9bn |
| Revenue | £817.3m | £854.4m |
| Underlying operating (loss) / profit | £18.5m | £(130.4)m |
| *of which CPBS one-off adjustment* | *–* | *£(128.4)m* |
| *Underlying operating profit excluding CPBS one-off adjustment* | *£18.5m* | *£(2.0)m* |
| *Underlying margin excluding CPBS one-off adjustment* | *2.3%* | *(0.2)%* |

Revenue
**£817m**

Underlying operating profit
**£19m**

Revenue profile*



22% Defence
78% Civil

## What we do

**We save lives** with our aerial emergency medical and search and rescue services

**We protect communities** with our firefighting operations

**We support the defence of nations** by supporting air forces in the UK and overseas

## Financial review

Revenue decreased by 6% to £817.3 million (excluding one-off CPBS adjustments in FY21), primarily due to the disposal of our Oil and Gas business in August 2021 and the impact of foreign exchange. Organic growth was 5% was driven by COVID-19 recovery and the ramp-up of defence contracts in France, offset partly by the completion of fixed wing aerial emergency services (AES) contracts in the Nordics and lower activity in Italy.

Underlying operating profit (excluding one-off CPBS adjustments) increased to £18.5 million (FY21: £(2.0) million loss). Profit performance improved due to operating model efficiencies, the achievement of certain programme milestones and recovery from COVID-19. FY22 was still slightly affected by lower flying hours and costs associated with additional COVID-19 related safety measures.

The sector's contract backlog declined to £2.3 billion (FY21: £2.9 billion), primarily as a result of the removal of £580 million backlog of the Oil and Gas aviation business, sold in August 2021. Excluding disposals, FY21 restated contract backlog was £2.3 billion. At 1 April 2022, Aviation had around £580 million of FY23 expected revenue under contract (FY21: £700 million (excluding disposals)).

## Operational review

### Defence

International defence grew in the year, driven by activity on new contracts and ramp up of the H160 contract which delivers search and rescue aircraft for the French Navy. In June 2021, we were awarded the Mentor contract, which involves the provision and support of an additional nine PC-21 aircraft and related equipment to the French Air Force, bringing the fleet size to 26. The contract expands the scope of our existing military training operations and is expected to be worth up to c.€500 million over 11 years, including options. c.€170 million was booked in FY22.

Additionally in the year, we teamed with Leonardo in Canada to work together on a new business opportunity for the Future Aircrew Training programme (FAcT).

Activity across UK defence including RAF station support, Hawk and LAFT contracts was flat year-on-year as expected, with further recovery from COVID-19 impacts offsetting the completion of some contracts. In the period, our military business secured a two-year extension to our Hades site support contract with the RAF, and a four-year extension for the delivery of the light aircraft flying training programme LAFT2. In addition, an expansion of requirements has been awarded from the Ascent JV to deliver further support to pilot training through the UK Military Flying Training System (UKMFTS).

### Aerial emergency services

Revenue across the majority of our aerial emergency services businesses ended the year flat, in line with expectations, with improvements in profitability as a result of operating model efficiencies and some COVID-19 recovery. Performance in aerial emergency medical services has seen some good recovery this year. Modest growth in Italy, with Scandinavia flat, was offset by lower volumes in Spain over the year. Southern European bases have all remained open and experienced varying increases in profitability. Renewal contracts have been won across the UK, Italy and Sweden. The Norway fixed wing contract has matured to a steady operational state with investment in a new maintenance facility in Tromso.

Our firefighting operations saw higher activity levels in Canada and key areas in Spain compared to last year, with Italy reporting expected flying hours. We have also utilised five Super Puma helicopters in Spain, converted from oil and gas operations. These aircraft deliver much greater water capacity than existing helicopters and are able to deliver a significantly larger number of firefighters to wildfires than was previously possible. Our Italy firefighting contract has been extended by two years.

### Oil and gas

The sale of the Oil and Gas business completed in August 2021, contributed revenue of around £79 million and an operating profit of around £2 million in FY21.

## Revenue and underlying operating profit bridge:

| | FY21 (Restated) £m | One-off CPBS adj £m | FY21 Restated (excl. one-off CPBS) £m | FX impact £m | Acquisition and disposals £m | COVID-19 recovery (estimated) £m | Pensions charge £m | Other trading £m | FY22 £m |
|---|---|---|---|---|---|---|---|---|---|
| Revenue | 854.4 | 16.8 | 871.2 | (22.0) | (75.4) | 38.5 | – | 5.0 | 817.3 |
| Underlying operating profit | (130.4) | 128.4 | (2.0) | (3.6) | (1.7) | 8.1 | – | 17.7 | 18.5 |


**F-AIR 21**
**Our Pilatus aircraft on the flightline ready to be flown as part of our French military flying training contract.**

# be curious

We believe in challenging the status quo and being curious.

As part of this mindset, a job-swap programme was implemented allowing colleagues to understand other roles and get a better overview of the way things work for different people and processes.

One such swap allowed a desk-based employee to experience an operational role.

Their usual job was ordering aircraft parts, but as part of the maintenance team for the day they were able to see how the parts they ordered were used and how to ensure all health and safety checks were complete before the aircraft took to the skies.

This experience helps our teams understand that they're all part of the bigger picture and that everyone and every role is critical to our success.

# think:outcomes

We believe in measuring success by the results we deliver and the positive impact we make.

Whilst discussing safety performance in a regular team meeting, our people decided to look at things differently.

Instead of focusing on how to intervene properly and what can be done once something has happened, they began to consider the outcomes before tasks were even planned.

This means they've reduced the need to intervene, put new mitigations in place as appropriate and it has given the whole team the opportunity to understand many new processes and activities that they might have not been involved in previously.

Thinking outcomes can help us shape our thinking towards everything, including safety.

# Building relationships

Building strong and lasting relationships with our diverse global stakeholder groups is vital to our success. The Board recognises the responsibility we have to our stakeholders, and the impact of our actions, which is why we've increased our focus on stakeholder engagement. Through continued two-way dialogue, we demonstrate a strong commitment to effective stakeholder engagement.

## CUSTOMERS

### Why they matter to us

Understanding the needs and challenges of our customers allows us to help them to succeed. We work in partnership with public and private customers across the globe, enabling them to deliver critical programmes and services, adding value to their operations. We seek to solve their challenges through excellent operational performance and the introduction of innovative solutions and technology to support their longer-term needs.

We build and maintain long-term relationships with our customers to promote the future success of the Group.

### What matters to them

- Safety
- Operational excellence
- Innovation and expertise
- Reliability
- Value for money
- Collaboration
- Deep understanding of their needs, both now and in the future
- Sustainability performance and agenda

### How Babcock engages

- Regular ongoing relationship engagement at all levels
- Contract negotiation and execution
- Strategic Partnership Programme
- Collaborating on joint initiatives
- Attendance at key industry events
- Provision of information on sustainability goals

## INVESTORS

### Why they matter to us

The support of our equity and debt investors and continued access to capital is vital to the long-term success of the Company. We work to ensure that we provide clear and transparent information to the market which allows investors and potential investors to make informed decisions, via market updates, information published on our website, appropriate access to management and an active IR and Treasury team.

### What matters to them

- Shareholder value
- Financial and operational performance
- Strategy and business development
- Capital structure
- Dividend policy
- Transparency of communication
- Governance and management
- Sustainability strategy

### How Babcock engages

- Annual Report and Financial Statements and AGM
- Results materials and presentations
- Investor relations team
- Treasury team with banks and noteholders and credit rating agencies
- Dedicated investor section on Babcock website
- Investor roadshows with management and IR team
- Chair engagement with top shareholders
- Consultation with large shareholders on remuneration policy
- Investor site visits
- Stock exchange announcements and press releases

## SUPPLIERS

### Why they matter to us

To support our global business operations and strategy we require an efficient and highly effective supply chain. This means we need to foster trusted and collaborative relationships with suppliers who share our appetite to drive improvement through innovation and best practice.

Our external supply chains are an important part of our performance and by working collaboratively with suppliers we can ensure continuity of supply, minimise risk and bring innovative solutions to our customers.

### What matters to them

- Good working relationships
- Access to opportunities
- Prompt payment and predictable supplier cash flows

### How Babcock engages

- Regular open and honest two-way communications
- Supplier Code of Conduct
- Supplier conferences, workshops and 'lunch and learns'
- Supplier due diligence
- Involvement in Security supply chain development programme SC21

## REGULATORS

### Why they matter to us

We manage complex assets in highly regulated sectors: nuclear, defence and aviation. We are committed to providing safe and effective operations. We have to maintain positive and constructive relationships with regulators in order to be able to operate, to help shape policy in our markets and to position for future opportunities.

### What matters to them

- Regulations, policies and standards
- Governance and transparency
- Trust and ethics
- Safety and compliance of operations
- Sustainability
- Site-specific issues

### How Babcock engages

- Regular engagement (national, local and official level)
- Briefing on key issues
- Dedicated compliance teams
- Response to direct queries
- Co-ordinated safety improvement programmes

## EMPLOYEES

### Why they matter to us

Our success is led by our employees. We continue to strengthen our employee value proposition by enhancing our engagement and promoting an agile global workplace.

We are committed to creating an inclusive and diverse organisation where employees can develop their full potential. We focus on developing and supporting a truly engaged workforce, living our principles and working on shared goals, united by our common Purpose.

### What matters to them

- Remuneration and reward
- Professional development
- The Group's aims, goals, priorities and reputation
- Employee engagement
- Health, safety and wellbeing
- An empowering culture
- Inclusion and diversity
- Our ESG agenda
- Employee networks

### How Babcock engages

- Employee forums and meetings
- Global engagement platforms
- Weekly CEO and senior management vlogs
- Access to the CEO via a dedicated email
- Weekly global news round-up videos
- Regular internal updates
- Cascade briefings
- A dedicated onboarding app
- Apprentice and Graduate programmes
- Regular training
- Access to independent whistleblowing process
- Senior management and Board visits
- Free confidential employee support helpline

## COMMUNITIES

### Why they matter to us

We are committed to the communities in which we operate and the broader interests of the customers we serve. As good corporate citizens, we want to make a genuine difference by supporting our local communities and helping them rebuild following COVID-19.

We have a responsibility to ensure that we support the communities in which we operate both economically and socially; community engagement and social value creation is a key aspect of our ESG strategy. Where we have major sites of operation, and are one of the largest employers in the local area, it remains important for us to add value to these communities.

### What matters to them

- Employment and economic contribution
- Health, safety and wellbeing
- Engagement in local education and STEM activities
- Sustainability and the local environment
- Support for indigenous people
- Support for armed forces community
- Community engagement

### How Babcock engages

- Sponsorship and donations
- Employee volunteering
- University partnerships
- STEM Ambassadors
- Employer of service leavers, veterans and reserves
- Engagement with local community programmes

## S172(1) STATEMENT

The Directors confirm that they, both individually and collectively, have acted in a way that they consider, in good faith, to be most likely to promote the long-term success of the Company for the benefit of the Shareholders as a whole, while having regard for all stakeholders. By considering key stakeholder groups and aligning our activities with our strategic plan, as well as the Company's culture and values, we aim to act fairly, transparently and in the best interests of the Company over the long term.

More information on how stakeholders are factored into our decision-making and the Board's engagement with stakeholders can be found in the Governance section in the Chair's introduction on page 92 and on pages 99 to 101, which form part of this Statement. Further information on how the Board addressed the different matters set out in s172(1) in performing their duties during the year can be found as follows:

| S172 factor | Relevant disclosures |
|---|---|
| a. the likely consequences of any decision in the long term | Our strategy (page 6)<br>Business model (page 8)<br>Led by our Purpose (page 18) |
| b. the interests of the Company's employees | Our People Strategy (page 19)<br>Ensuring the safety and wellbeing of our people (pages 63 to 66) |
| c. the need to foster the Company's business relationships with suppliers, customers and others | Being a collaborative, trusted partner across the supply chain (pages 69 to 72)<br>Innovation and technology (page 21) |
| d. the impact of the Company's operations on the community and environment | Making a positive impact on the communities in which we operate (pages 67 and 68)<br>Environmental (pages 57 to 62) |
| e. the desirability of the Company maintaining a reputation for high standards of business conduct | ESG Strategy: Governance (page 71) |
| f. the need to act fairly between members of the Company | Investors (page 52) |

# ESG Strategy

Sustainability is an integral part of our corporate strategy and how we do business and it underpins our corporate Purpose: *to create a safe and secure world, together*. We have done a lot in the past year to drive our sustainability programme across the Group, ensure progress towards our corporate commitments and deliver our five ESG priorities shown below.

During the year we progressed our corporate environment, social and governance (ESG) strategy, which focuses on the operations and strategy of the Group. We expanded our corporate commitments to incorporate broader environmental targets, see pages 57-59. We also created new Group policies and guidance to support appropriate governance of our sustainability programmes.

## Our ESG priorities

1. **We will reduce emissions and set science-based targets to get to net zero across our estate, assets and operations by 2040**

   *See page 57*

2. **We will integrate environmental sustainability into programme design to minimise waste and optimise resources**

   *See page 59*

3. **We will ensure the safety and wellbeing of all our people**

   *See page 63*

4. **We will make a positive difference to the communities we're proud to be part of and provide high-quality jobs that support local economies**

   *See page 67*

5. **We will be a collaborative, trusted partner across the supply chain, helping to tackle common challenges**

   *See page 69*

Sectors and regions have developed their own sustainability programmes, which support the Group-led programmes and stakeholders' needs.

Our sustainability strategy will continue to evolve with the interests of our stakeholders, as well as those of the Company. This year we asked some of our key stakeholders for their views on our material topics to ensure that we focus on issues that matter most to them. The findings will help influence our sustainability agenda and our priorities (see Materiality assessment on following page).

### Progress against our ESG priorities

Climate action is a key focus: we are continuing to progress our decarbonisation programme (Plan Zero 40) across the Group. Aligned with the Plan Zero 40 pathway announced last year, we commenced baselining our carbon footprint and are on track to submit carbon reduction targets to the Science-Based Targets initiative by April 2023. These are to be achieved by 2030 and will set us on course for decarbonising our estate, assets and operations to reach our overarching goal of net zero emissions by 2040.

During 2021, the Board and Executive Committee agreed Group strategic priorities for climate action and we incorporated Task Force on Climate-related Financial Disclosures (TCFD) risk management and scenario planning into both our strategic planning cycle and corporate risk management framework. This year we are enhancing our level of disclosure against the TCFD requirements (see pages 60-62 for more detail).

Sustainability is central to our thinking and we are integrating it into programme design to ensure optimal use of resources and to minimise waste. We are using data and digital techniques to inform our through-life thinking and support effective and efficient asset operation and management.

We want to create a better working environment at Babcock and ensuring the safety and wellbeing of our employees is at the heart of all that we do. In the context of our new unifying corporate Purpose, we ran a Group-wide safety stand-down to focus on and re-emphasise our Care and Learn safety commitments.

We aim to provide a workplace which is inclusive and where each individual feels supported and respected. Inclusion and Diversity (I&D) is therefore a key focus and this year we hired additional senior women into our senior leadership team, increasing female representation at the end of the year to 21%. We are pleased that our Mean Gender Pay Gap has narrowed year-on-year from 12.5% to 11.8%. (See Babcock's 2021 Gender Pay Gap report on our corporate website.)

We recently appointed our first Global Head of I&D to develop our approach and review, design and implement activities that will enable Babcock to become a more inclusive business that values difference.

We want to have a positive impact on the communities in which we operate, to be a good neighbour and contribute to the local economy through social value initiatives. This year we developed a Group-wide Sponsorship and Donations policy which is aligned to our corporate Purpose and is supported by local activity. In January the Executive Committee also agreed to launch a Group-wide volunteering programme, which will allow every employee to volunteer for one day per year.

We have engaged the consultancy Oxford Economics to conduct a comprehensive study of Babcock's economic impact including how the Company delivers social value as outlined in the Government's Social Value Model.

We continue to actively collaborate through industry partnerships, academia and our supply chain to meet global challenges such as climate change.

## Our sustainability charter


**Environment**

A We use innovative solutions to reduce our energy needs, while focusing on cleaner energy and other natural resources.

B We integrate environmental sustainability into our programme design, optimise use of resources and minimise waste through increased re-use and recycling.

**Social**

C We play an active part in our local communities to enhance development and inspire the next generation.

D The safety and wellbeing of our people is our priority. We encourage a diverse and inclusive employee base where each person feels respected and able to fulfil their potential.

**Governance**

E We partner with our supply chains to identify innovative solutions and ensure timely delivery of quality products and services.

F We believe that ethical behaviour underpins our sustainability activities. We have robust processes and controls to identify opportunities and manage corporate risks.

## Materiality assessment

Last year we conducted an internal materiality assessment to highlight the issues we believed mattered most to our stakeholders and to Babcock (see table below). This year we extended the materiality assessment to capture the views of some of our key stakeholder groups and ensure that our strategy evolves with their interests and needs, and aligns with our priorities.

To capture the views of our employees we ran an employee opinion poll in March, to identify the top three priority sustainability issues they think we should be focusing on in order *'to create a safe and secure world, together'*.

We also asked our investors for their views on sustainability priorities. Below we have highlighted the three topics cited by these respective groups.

Employees:

- Climate action: We are facing a global climate crisis and our people recognise we need to play our part in averting this
- Waste: Our employees believe we need to reduce the amount of waste generated, be more efficient and adopt circular economy principles
- Health and safety: Our employees recognise we must protect the wellbeing of all who interact with Babcock

Investors:

- Sustainable supply chains: In an increasingly unpredictable macro environment, supply chain resilience is key. Also, embedding sustainable practices within the supply chain will be an important factor in achieving our net zero target
- Governance, accountability and culture: These are key to delivering benefits from the operating model and to fully integrate ESG in the business to achieve our sustainability ambitions
- Talent and development: Babcock requires skilled employees. Our workforce is ageing and there is concern that we could struggle to deliver planned growth or take advantage of emerging opportunities

This year we intend to survey our key suppliers and several customer stakeholders within contracts across the sectors and regions.

### Our Purpose: *to create a safe and secure world, together*

| Material issues | Environment | Social | Governance |
|---|---|---|---|
| | **Biodiversity and ecological impact** | **Community engagement** | **Business ethics and integrity** |
| | **Climate change** | **Health, safety and wellbeing** | **Data and cyber security** |
| | **Waste** | **Talent and development** | **Governance, accountability and culture** |
| | **Water consumption** | **Local economic contribution** | **Sustainable supply chains** |
| | | **Employee inclusion and diversity** | **Innovation and technology** |
| | | | **Collaboration** |

## ESG and our shareholders

We recognise that parts of our business model are of increasing relevance to investors looking through an ESG lens: most notably that we operate in defence and nuclear markets.

Babcock has been supporting the UK's commitment to the Continuous At Sea Deterrent for over 50 years while also delivering complex and critical civil nuclear through-life engineering. We will continue to support our UK customer, both with their defence agenda and their commitment to generate low emission power from nuclear energy.

This year we further our ESG disclosure on key sustainability interests. During the year, critical ESG topics were raised in the market allowing funds to identify and filter equities to minimise exposure to defence and nuclear industries, and enabling compliance with new investment policies.

Below we talk through key points identified by our shareholders on common issues and material areas of focus:

Environmental: In addition to new disclosure this year, we add further road-mapping to achieving our target of net zero for harmful emissions from our estate, assets and operations by 2040. The target is also linked to our KPI on $CO_2$e emissions for measuring our progress on page 23.

Social: The health, safety and wellbeing of our employees, customers and the community comes first at all times. This has been a year of change with our new People strategy and the setting of solid foundations to build upon as we continue to improve our safety performance, inclusion and diversity, gender pay gap, talent development and community outreach. See pages 63 to 68.

Governance: Governance starts at the top. We have continued to support the Company's turnaround by making improvements to the governance of the Group at Board level, which is covered in our Chair's report (page 92) and our Audit Committee Chair's report (page 108). Our approach to risk management is discussed on page 76, and the Group-level response to our new governance over contract bids is covered on pages 8 and 9.

This year we have continued to develop our approach to ESG reporting. Building on last year's work, we have enhanced the level of transparency and provided further insight into a range of economic, social and environmental impacts including working towards full disclosure to the TCFD requirements, as per Listing Rule LR9.8.6R.

## Investor FAQs:

### Are you involved in nuclear weapons?

- We do not design, manufacture, maintain or deal in nuclear weapons or their components

### Are you involved in nuclear delivery platforms?

- In the UK, nuclear delivery platforms are generally defined as the UK's SSBN (Ship Submersible Ballistic Nuclear) fleet of Vanguard Class submarines and in future, its replacement programme, the Dreadnought Class
- We manufacture and assemble components for the joint UK and US SSBN submarine replacement programme
- We also design and manufacture handling and ejector systems for the future UK Dreadnought Class submarines
- These two areas of manufacture represent less than 2% of FY22 revenue

### Are you involved in any other nuclear defence activities?

- Babcock has been supporting the UK's most critical defence capability, the Continuous At Sea Deterrent, for over 50 years
- We own and operate critical infrastructure and have technical knowledge of the defence nuclear market
- We provide maintenance, through-life support and life-extensions for the UK's fleet of nuclear-powered submarines. This relates to the fleets of both SSBNs and SSNs (Surface Ship Nuclear – nuclear-powered)
- As part of our civil nuclear business we also deliver infrastructure projects for AWE
- These areas of support for the wider UK defence nuclear programme represents the defence revenue in our Nuclear sector, approximately 21% of FY22 revenue

### Are you involved in other weapons?

- We do not make or deal in other weapons
- We do, however, design and manufacture weapons handling and launch systems for international naval platforms used by the UK, Spain, Republic of Korea and Australia
- We also have contracts to maintain the UK Royal Navy's naval weaponry
- These areas of support and manufacture represents less than 2% of FY22 revenue

### Are you involved in nuclear power?

- Yes: nuclear power provides a reliable source of low-carbon electricity and is a critical component of countries' national energy strategies as they move towards net zero carbon
- Our civil nuclear business is involved in new build, power generation support, fuel route management and decommissioning in the UK nuclear market
- We also use our technical knowledge and reference cases to undertake consultancy work in Canada and Japan, albeit at a small volume currently
- Work related to these areas represents approximately 4% of FY22 revenue

### Do you have dedicated ESG remuneration targets?

- Three of the Group's key performance indicators are linked to our ESG strategy: (i) Total injuries rate, (ii) $CO_2$ emissions, and (iii) Senior management gender diversity
- We have two main targets as part of our ESG strategy: (i) to be net zero (Scope 1 and 2) by 2040, and (ii) for at least 30% of our senior management to be female by 2025

# ENVIRONMENTAL

## 1 Reducing emissions and setting science-based targets to get to net zero

Across our operations we interact with a diverse range of environments and we are committed to reducing our impact on the environment. We seek to deliver to the highest standards of environmental management and protection, truly embedding our Principle of ‘be kind’ to ensure our impacts are minimised. We take our responsibilities seriously and ensure we are playing our part in the transition to a more sustainable future for all.

Our Group-wide Environmental Protection Working Group (EPWG) is working to conduct a holistic assessment of Babcock’s approach to environmental management. We currently have 25 ISO14001 Environmental Management Systems (EMS) across the organisation which capture over 75% of our global operations, and we have several more EMS seeking accreditation over the coming 12 months. We are committed to ensuring all Babcock operations are to be delivered within an EMS by 2024, delivering advanced environmental training to all relevant employees by 2025 and have set new targets for waste, water and bio-diversity (see page 59).

### Babcock Group energy consumption and emissions

| | | Dec-18 | Dec-19 | Dec-20 | Dec-21 |
|---|---|---|---|---|---|
| **UK / UK offshore** | | | | | |
| Scope 1: Direct emissions from owned/controlled operations | $tCO_2e$ | 74,819 | 69,450 | 52,693 | 42,515 |
| Scope 2: Indirect emissions from the use of electricity and steam | $tCO_2e$ | 78,903 | 66,881 | 52,791 | 45,069 |
| Scope 3: Emissions – business travel, electric transmission and distribution | $tCO_2e$ | 18,198 | 15,265 | 8,246 | 7,981 |
| **Total emissions** | **$tCO_2e$** | **171,920** | **151,596** | **113,730** | **95,566** |
| **Underlying energy consumption used to calculate emissions** | **kWh** | **561,818,680** | **531,968,134** | **418,292,992** | **365,816,822** |
| **Global (excluding UK / UK offshore)** | | | | | |
| Scope 1: Direct emissions from owned/controlled operations | $tCO_2e$ | 93,333 | 99,579 | 110,591 | 100,644 |
| Scope 2: Indirect emissions from the use of electricity and steam | $tCO_2e$ | 2,461 | 6,743 | 4,569 | 4,426 |
| Scope 3: Emissions – business travel, electric transmission and distribution | $tCO_2e$ | 457 | 410 | 213 | 68 |
| **Total emissions** | **$tCO_2e$** | **96,251** | **106,732** | **115,373** | **105,139** |
| **Underlying energy consumption used to calculate emissions** | **kWh** | **391,772,490** | **417,537,009** | **459,580,840** | **417,483,548** |
| **Babcock Group total (UK / UK offshore and global)** | | | | | |
| Scope 1: Direct emissions from owned/controlled operations | $tCO_2e$ | 168,152 | 169,029 | 163,285 | 143,160 |
| Scope 2: Indirect emissions from the use of electricity and steam | $tCO_2e$ | 81,364 | 73,624 | 57,360 | 49,496 |
| Scope 3: Emissions – business travel, electric transmission and distribution | $tCO_2e$ | 18,654 | 15,675 | 8,459 | 8,050 |
| **Total emissions** | **$tCO_2e$** | **268,170** | **258,328** | **229,103** | **200,705** |
| **Underlying energy consumption used to calculate emissions** | **kWh** | **953,591,170** | **949,505,142** | **877,873,832** | **783,300,370** |
| **Underlying energy consumption** | **GJ** | **3,432,928** | **3,418,219** | **3,160,346** | **2,819,881** |
| **Fiscal year revenue FY19 - FY22** | **£m** | **4,474.8** | **4,428.5** | **4,182.7** | **4,101.8** |
| **Intensity ratio** | **$tCO_2e$/£1m Revenue** | **59.9** | **58.3** | **54.8** | **48.9** |

Our emissions data is reported in line with the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard under the ‘Operational Control’ approach. The reporting period for our energy consumption and carbon emissions is the calendar year (01 January to 31 December), this is opposed to financial year as we have previously reported. The transition to calendar year reporting has allowed more time to collate, analyse and report our environmental data, which has improved the accuracy and completeness of our data sets. Figures for UK operations follow conversion factors published by BEIS. Non-UK operations utilise emission factors applicable to the fuel source and location. Appropriate conversion factors have been used to calculate the underlying energy consumption figures. Scope 1, 2 and 3 sources have been divided by the annual revenue to provide the intensity ratio ($tCO_2e$ per £m). Emissions data for prior years have been adjusted to include data unavailable last year, and emission figures for this year include an element of estimated data. Prior year revenue figures have not been restated for removal of pass through revenue, identified in the financial review, to remain consistent with the emissions data recorded in prior years. Certain data, estimated to be immaterial to the Group’s emissions, has been omitted as it has not been practical to obtain (including operations in Oman, South Korea and USA). Metering and monitoring improvements are being implemented to capture these data streams. During the reporting period estate rationalisation, strategic divestments, ‘low-hanging fruit’ energy conservation measures and improvements to our energy management practices have resulted in a reduction of both our carbon baseline and FY22 operational emissions. We are progressing well on our journey to net zero and aim to accelerate our carbon reduction over the coming years.

## Plan Zero 40

We are committed to addressing the global climate crisis and leading the transition to net zero. Under the direction of our carbon strategy, Plan Zero 40, over the past 12 months we have made significant progress on our journey to net zero.

We have collaborated with a number of climate experts including Frazer-Nash and Energy Systems Catapult and developed our approach to decarbonisation. We have commenced the development of comprehensive and deliverable carbon reduction plans within our 'Pathfinder Boundaries' and are on schedule to scale the reduction plans across our global operations by the end of 2023.

We have developed a specialist central team to support the organisation and effectively manage the transition to net zero and are investigating opportunities to finance our net zero journey.

In April 2021, we signed the Business Ambition Pledge and committed to a 2030 science-based target in line with a 1.5°C degree pathway. We are on track to meet our goal and over the next 12 months we aim to submit our targets for approval by the Science Based Targets initiative (SBTi).

Within our carbon reduction plans we are identifying carbon reduction, energy efficiency and renewable energy opportunities across our operations.

At Rosyth Dockyard we have identified the opportunity for renewable energy systems with generating capacity of over 10MW, which will meet a significant percentage of the energy demand for the site, reduce the footprint of our operations and provide resilience to fluctuating energy prices. We have also conducted estate-wide renewable energy surveys to identify the opportunity for the installation of solar photovoltaics.

We are also seeking accreditation to the Carbon Trust's new 'Route to Net Zero Standard' by the end of April 2023.

During 2021 Babcock conducted a strategic review of our estate and built environment. The review identified cost savings and environmental improvements which could be delivered through estate rationalisation. We have subsequently proceeded to consolidate our estate which has delivered a reduction in our carbon baseline and operational emissions, along with delivering a broad range of environmental and organisational efficiencies.

## Scope 3 emissions

Given the diverse and complex nature of Babcock's operations, Scope 3 emissions presents a range of challenges. We have, however, made significant progress investigating and mapping our Scope 3 emissions. This includes assessment of our Scope 3 upstream emissions utilising the Environmentally Extended Input Output (EEIO) approach, hotspot analysis of our supply chain and publication of our new Supplier Sustainable policy.

Our work to date is driving proactive engagement and will ensure sustainable and low-carbon considerations are embedded throughout the value chain.

We have commenced investigations into our Scope 3 downstream footprint and have completed an initial assessment as a pathfinder. We are working to conduct further downstream assessments to identify hotspots across our global operations and are on track to develop a detailed understanding of our Scope 3 footprint with associated net zero pathway by 2025.

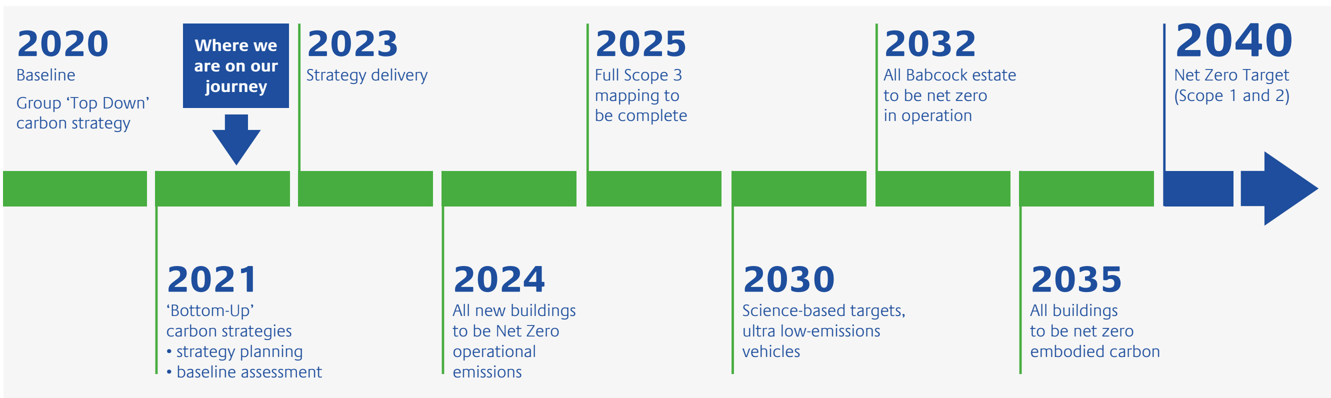
We are taking proactive action and collaborating with our customers, peers and suppliers to ensure there is a consistent approach to calculating and managing Scope 3 emissions across the defence and aerospace industry. We are active members of a range of industry forums investigating sustainable solutions and alternative fuels.

Reducing the impacts of our products and services is a key aim for the organisation. As a priority, the Group Executive Committee is ensuring the delivery of appropriate training and development for our employees and stakeholders, embedding circular economy principles and leading on the development of 'Green Ports'. We are working in collaboration with industry and academic partners to investigate approaches to environmental lifecycle assessments and whole-life models.

## Sustainable transport

Sustainable transport is an important factor in our transition to net zero. Our Sustainable Transport strategy addresses our key transportation impacts including: the Babcock fleet, business travel, employee commuting and transportation & distribution (upstream and downstream). We are developing specific transportation targets in line with our ambitions under Plan Zero 40 and our science-based targets. We are seeking to transition our fleet to 100% ultra low-emission vehicles (ULEVs) by 2030 and have a range of programmes aimed at raising awareness and promoting varying modes of sustainable transport.

## Our journey



As a flagship, we have recently launched an electric vehicle (EV) salary sacrifice scheme for our UK operations.
This scheme will promote and accelerate the uptake of EVs across our workforce, which will lead to a reduction in the footprint and impact of our operations.

### Raise awareness of environmental and sustainability issues

We understand our people are key to embedding sustainability into our operations. Over the past year we have effectively engaged with our workforce and wider stakeholder groups to educate and raise awareness of environment and sustainability issues. In the run-up to and throughout COP26 we hosted a series of events including ‘lunch and learn’ briefings and a presentation/Q&A with Olympic gold medallist Hannah Mills.
We also ran a climate podcast series with appearances from Babcock’s CEO David Lockwood and the Ministry of Defence’s Lt Gen Richard Nugee. We have exciting plans to continue and enhance our engagement over the coming year.

### Data management

Data is the cornerstone of our Environmental strategy and journey to net zero. We use data to understand our impacts, inform our decisions and communicate our position in a transparent manner.

Throughout 2021 we implemented a range of improvement measures to our data management system to ensure high accuracy and completeness. As a priority we are investigating the development of an environmental data management system which will form the basis of our approach.

## 2 Integrating environmental sustainability into programme design

### Climate action Executive Committee priorities

As part of Babcock’s TCFD governance workstream, climate action priorities have been agreed by the Group Executive Committee and are underway to ensure the assessment and management of climate-related risks. See page 60.

### Waste

Consumption of materials and resources is a significant contributor to Babcock’s environmental footprint and we understand our responsibility to minimise the impacts of our operations. We continue to deliver improvements to our waste management practices and to minimise waste sent to landfill.

Within our Marine business we have adopted innovative technology, such as robotic welding, which reduces waste along with providing a wide range of additional benefits. Within our Aviation business we harnessed data to inform the scheduling and planning of our touring pilots and reduced wasted travel and expense by over 50%.

We have set three waste targets;

- Preparing waste management plans across all significant sites by 2024
- Zero controlled waste to landfill by 2025
- Eliminate the use of unavoidable single-use plastic by 2027

### Water

Water is a key resource across our global operations and we understand the need to reduce our impacts and manage our water consumption responsibly. Across the organisation, local environmental teams are working to identify water reduction opportunities and to incorporate water reduction technologies such as rainwater harvesting, leak detection and flow restriction in our new developments.

Within our African operations, water scarcity poses a significant challenge and we have taken proactive steps to reduce our impacts through rainwater harvesting to recycling water for irrigation and flushing toilets. For example in Botswana our teams created wash bays that recycle and filter the runoff water for reuse, which has achieved a 60% reduction in water consumption.

- We have set a target to prepare water management plans across all significant sites by 2024

### Biodiversity

Maintaining and enhancing biodiverse ecosystems is a fundamental aspect of our Environmental strategy and we aim to ensure we preserve and enhance natural capital. Our local environmental specialists ensure that environmental considerations are embedded throughout our operations and our impacts are minimised.

We have set two biodiversity targets;

- Conduct biodiversity assessments across all significant sites by 2024
- Deliver a10% biodiversity increase across the estate by 2030

## Task Force on Climate-related Financial Disclosures

This year we have been working towards full disclosure to the Task Force on Climate-related Financial Disclosures (TCFD) requirements, as per Listing Rule LR9.8.6R. We have appropriate governance with respect to climate change, integrated risk management and scenario planning in our strategic planning cycles and we have set some initial targets. As we work towards full disclosure, we will assess how climate change scenarios impact on the organisation's business strategy, financial planning and budgeting. For further details see FY23 priority table, page 62.

### Governance

#### Board oversight of climate-related risks and opportunities

In FY21 the Board, in order to progress the ESG programme and meet the expectations of our stakeholders, approved Babcock's carbon initiative (Plan Zero 40), our list of identified ESG material issues and our phased approach to full TCFD implementation.

Group-wide ESG matters are now an integral part of Board strategic discussions. In FY22, the Board reviewed progress on Plan Zero 40 and TCFD through updates from the Group Head of Sustainability. See page 97 for further details on our governance framework.

Climate-related risks and opportunities are to be reported to the Executive Committee on a quarterly basis.

#### Management's role in assessing and managing climate-related risks and opportunities

The executive with responsibility for TCFD reporting is the Chief Corporate Affairs Officer. TCFD workstreams are championed by the Group Head of Sustainability and activities are overseen by the Corporate ESG Committee, which meets quarterly and includes representatives from the Executive Committee. Progress on TCFD activities is reported to this Committee, and any actions/activities required to further climate-related risk management activities are agreed by the Committee. Executive Committee members who are members of the Corporate ESG Committee are indicated on page 97.

TCFD actions and activities are managed at the Group and sector level by 'TCFD Sponsors' with oversight from the Group Head of Sustainability and support from each sector risk lead and/or relevant environmental, technical or facilities team. The sponsors are typically Finance Directors/Heads of Finance, which ensures that TCFD activities are overseen by individuals with sufficient seniority, and authority, to delegate tasks and monitor progress. Sponsors also hold responsibility for ensuring that climate-related risks and opportunities within their sector are understood, financially quantified and delegated for management on an ongoing basis.

Plan Zero 40 is being led by the Group environmental team, with sectors accountable for developing their bottom-up carbon reduction plans. For further details on decarbonisation, see page 58.

Additionally, during the year the Edinburgh University Centre for Business and Climate Change facilitated an Executive Education session with the Executive Committee on climate change.

### Strategy

We have analysed climate-related risks and opportunities across all of our business operations against three climate scenarios. These are based on an evolution and customisation of scenarios developed by the Network for Greening the Financial System (NGFS). We customised these scenarios to include location-specific information relating to areas where we carry out our operations. Additional criteria were also developed to capture the longer-term nature of climate-related risks and opportunities.

#### Orderly: 'Net Zero 2050' (warming limited to 1.5°C)

- Early high levels of transition risks with reduced subsequent physical risks

#### Disorderly: 'Delayed Transition' (warming limited to 2°C)

- Delayed transition risks with higher subsequent physical risks

#### Hothouse World: 'Current Policies' (warming of 3°C+)

- Limited or no transition risks but runaway physical risks

These scenarios were adopted as they were determined to be in line with Babcock's most likely possibilities across the business. Due to the disparate geographies that we operate in, the most relevant scenario for each sector or region varies, particularly in relation to policy retention. The UK, European countries and New Zealand are broadly seen to have a high amount of legislation that addresses climate change, with a legal commitment to achieve net zero by 2050. Canada and South Africa are aspirational for the transition but more locked into traditional carbon-intensive economies. Australia is much further behind in this area. As a result, transition risks in the UK are different from those in the Australian region. Some sectors also have operations exposed to different types of transition risk depending on their geographic spread.

Our process for identifying and assessing the impact of future potential scenarios included interviews with senior executives across all of our sectors and regions, as well as a number of workshops. More than 100 stakeholders have been involved across Babcock, providing coverage of nearly all business functions. This confirmed the materiality of climate-related issues. Based on analysis of the impact of these risks on Babcock's operations, the following areas will influence our sector/regional strategies and business model:

- Extension of risk management timescales to accommodate the longer-term nature of climate-related risks
- Development of robust green credentials to continue to attract top talent
- Implementation of flexible and adaptable governance structures and processes to accommodate regulation change
- Implementation of renewable energy sourcing and energy-efficiency measures across sites and facilities
- Implementation of a contracting approach that includes climate considerations
- Collaboration with supply chain to understand/mitigate suppliers' climate impacts

#### Risks

An analysis of climate-related risks relevant to Babcock has shown that many risks and opportunities are in the medium term (2030-2040) and long term (2040-2100), giving Babcock time in the short term to implement activities to mitigate.

Details of our most significant climate-related physical and transition risks, proximity, impact and control measures introduced can be seen in the graphic on the next page.

Our most significant physical risk is dockyard disruption and we have assessed the risk of increased flooding and storm surges. The highest risk is seen in a 3°C scenario, where we expect to see more extreme weather patterns.

From our assessment of transition risk, we believe increased climate-related regulation will have an impact on supply chain disruption. The lowest risk is in the 3°C scenario which assumes that only current climate policies are implemented, therefore transition risks globally will be negligible.

## Examples of key risks and control measures

| Risk title | Risk description | Proximity | Scenario 1.5°C | Scenario 2°C | Scenario 3°C+ | Control measures |
|---|---|---|---|---|---|---|
| **Dockyard disruption** | Dockyards owned / operated by Babcock may be flooded due to an increase in sea level and higher frequency of extreme weather, resulting in storm surges. | Short (2020-2030) | | | | Our Devonport site is currently undertaking a significant infrastructure rebuild and climate-related risk is being factored into rebuild decisions. In the medium to longer term as the site develops, for the design of rebuild and new facilities we will consider climate-related risk in line with the latest ONR standards. |
| | | Medium (2030-2040) | | Moderate | | |
| | | Long (2040+) | Moderate | | Severe | |
| **Supply chain disruption** | Increased climate-related regulation, such as taxes on fossil fuels, may affect Babcock's supply chain cost base or viability of supply chain companies. | Short (2020-2030) | Moderate | | | Our Sustainable Procurement policy has been implemented, which considers our suppliers and sub-contractors' ability to meet our requirements against 12 sustainability priorities. We will consider the plans of our suppliers in our sourcing decisions and actively monitor and manage sustainability performance in the supply chain. Further details can be found in our Sustainable Procurement policy. We have invested in an AI monitoring solution for our supply chain, see page 69. |
| | | Medium (2030-2040) | | Moderate | | |
| | | Long (2040+) | | | Insignificant / Moderate | |

Impact
Insignificant / Moderate · Moderate · Major · Severe

Plan Zero 40 is our chief mitigation mechanism to combat transition risk, which is highest in countries with a strong net zero policy, such as the UK.

### Opportunities
We also recognise there will be opportunities in the transition towards a greener economy. Through our Liquid Gas Equipment (LGE) business, we aim to continue to develop our ammonia fuel gas supply system, as well as solutions for the transportation and storage of $CO_2$ in line with customer and legislative requirements. This will ensure that we are optimising efficiency while developing zero-carbon solutions.

We're collaborating cross-industry and working with academia on several programmes such as the MarRI-UK hydrogen Fuel Cell-BATTERY Ship Advanced Power-Energy Management Solution for Zero Emission Marine Propulsion Systems. In our PHOENIX II contract, we manage in excess of 15,000 White Fleet vehicles and are working with the customer to deliver its commitment to achieve both the 2022 and 2027 UK Government's 'Road to Zero' targets. The targets require a transition of 25% of the M1 Classified Fleet (predominantly cars) to ULEVs by the end of 2022, and then 100% of M1 and N1 (predominantly vans, 4x4s) fleets to zero tailpipe emission vehicles by the end of 2027.

In 2021, we integrated the climate-related risks and opportunities flowing from our TCFD scenario workshops into our strategic planning process. Each sector, region and function has detailed its strategies for managing the priority risks and realising opportunities over the strategic plan period (five-year outlook).

## Risk management
Our process for identifying and assessing climate-related risks and opportunities utilised the existing Babcock risk management framework.

The horizons against which the climate-related risks were assessed are as follows:

- Short term (present to 2030)
- Medium term (2030 to 2040)
- Long term (2040 to 2100)

Once all relevant climate-related risks and opportunities had been identified, assessed and scored across the relevant time horizons, individual climate-related risk registers were created for each sector. These registers have been delegated to individual owners by TCFD sponsors and are required to be submitted on a quarterly basis inclusive of relevant mitigation or controls in place. On an annual basis, owners will be required to review the initial scoring of each item to assess the effectiveness of control measures. The Group Risk policy has been updated to reflect integration of the new process.

## Metrics and targets
Babcock has developed the following metrics, with associated targets and timescales, to measure our progress towards reducing our exposure to climate-related risk. We plan to develop and disclose further metrics and targets in the next financial year.

- Establish baseline and submit carbon reduction targets to the Science Based Targets initiative by April 2023
- Complete an assessment of climate-related risk of all critical Babcock infrastructure by December 2024
- Complete a review of climate-related changes to working conditions covering all employees who are exposed at geographical locations. Our target for this review is April 2023
- Ensure climate-related impacts are considered in all new business bid / no bid decisions and associated contract negotiations / KPIs
- 100% of electricity for Babcock facilities to be sourced from renewable supplies by 2030, as far as reasonably practicable
- Complete an assessment of all our critical suppliers' climate-related risks and associated impact on Babcock in autumn 2022

## TCFD progress vs priorities

| | FY22 progress | FY23 priorities |
|---|---|---|
| **Governance** | • Group Executive Committee and the Board completed the 'Chapter Zero' survey<br>• Group Executive Committee completed the Executive Education session run by Edinburgh University<br>• ESG updates to the Board included climate action<br>• In FY22 the Remuneration Committee included specific ESG objectives and measures in the FY23 annual bonus, see page 114 | • Board to continue the discussion on the topic of sustainability |
| **Strategy** | • Climate-related risks and opportunities have been integrated into 'business as usual' processes, through inclusion of climate-related questions within the Group enhancement strategy process undertaken by each sector and region | • Further assess approach to scenario analysis and assess organisational resilience<br>• Further define financial implications of climate-related risks and opportunities and seek to include mitigation steps in strategic planning<br>• Ensure climate-related impacts are considered in all material new business decisions and associated contract negotiations/KPIs |
| **Risk management** | • Physical and transitional climate-related risks and opportunities have been identified and scored through sector and region workshops in the short, medium and long term using Babcock's approach to risk<br>• Climate-related risk management has been integrated into Babcock's overall risk management process through the addition of a climate-related risk register | • Assess progression of climate-related risk registers and ongoing management<br>• Further validation of financial impacts<br>• Complete an assessment of critical suppliers' climate-related risks and associated impact on Babcock by autumn 2022 |
| **Metrics and targets** | • Progressed 11 pathfinder boundary projects and baselining phase | • Establish baseline and submit carbon reduction targets to Science Based Targets initiative by April 2023<br>• Progress on Plan Zero 40 by scaling across the rest of the organisation |

Technology plays a critical role in our efforts to minimise the environmental impact of our business. Scan this code to watch a video to find out more about the work we are doing in this area.

# SOCIAL

## 3 Ensuring the safety and wellbeing of our people

### 'Home Safe Every Day'

Our safety mission is to enable our people to go 'Home Safe Every Day', and to support this we have a series of commitments to one another that we call 'to Care and to Learn'. This has been a year of change and the setting of solid foundations to build upon as we continue to improve our safety performance.

### Governance

The appointment of a Global Safety, Health and Environmental Protection Director and formation of a central team has brought additional focus to the safety improvement programme. Supported by working groups of specialists and alongside a transformed Corporate Safety Leadership Team that includes Operational Directors from across Babcock, we have strengthened our governance. We have introduced a suite of corporate standards that form the Babcock safety framework and developed a scorecard of leading and lagging performance indicators to help monitor the business. These form part of the Babcock safety and management system and enable us *to create a safe and secure world, together*.

### Achievements and improvements

Babcock has introduced an electronic global safety information management system that supports event and audit management. This has standardised processes across Babcock and increased transparency. The global system enables sharing of lessons across our operations, to collectively improve our safety outcomes and will continue to grow with the additions of risk management functionality.

Our annual safety conference, held virtually in November 2021, shared and celebrated the successes of personnel for the sectors and direct reporting countries with a theme of 'Care and Learn'.

Babcock also held a safety stand-down in January 2022, where teams took time out from operations to discuss how *to create a safe and secure world, together* by improving their working environment. The commitments 'to Care and to Learn' were reiterated in many of the conversations, with a focus on doing the right thing.

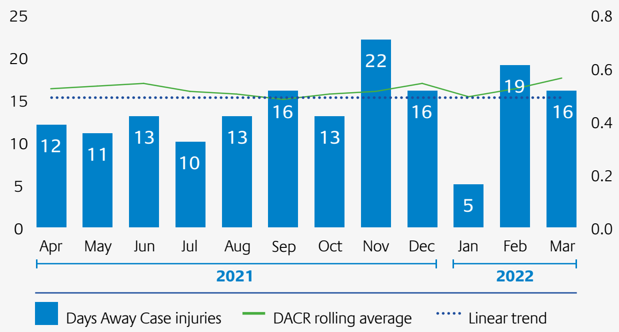
### Proactive reporting – Reporting safety issues before they cause harm

During the year, we have moved to an internationally recognised HSE accident categorisation method in order to be able to benchmark against peers. Whilst the change means that direct statistical comparison with previous years is not meaningful, it will enable future benchmarking of safety performance.

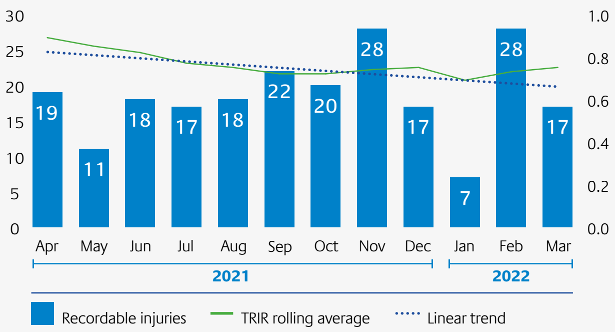
The Group's Total Recordable Injury Rate (TRIR),[1] which includes work-related injuries requiring medical treatment or above, has reduced from 0.89 to 0.75 over the year, with a reduction in the number of these types of accidents of 18% against 2021. The Days Away Case Rate (DACR) across the whole of Babcock has increased from 0.52 to 0.56.[2] This led to a 5% increase in work-related injuries that resulted in personnel requiring at least one day away from work. We continue to work hard to reduce the number of injuries and illnesses as a result of our activities.

In addition to recording all accidents, we have introduced metrics to track the level of proactive reporting. The focus is to encourage our people to report High-Potential Occurrences (HIPO), High-Potential Near Misses (HPNM) and safety observations, to enable us to learn from and correct these before they can cause harm. This indicator of positive reporting is an important element of an engaged safety culture and we have seen a gradual and consistent increase in proactive reporting across Babcock.

**Days Away Case injuries**



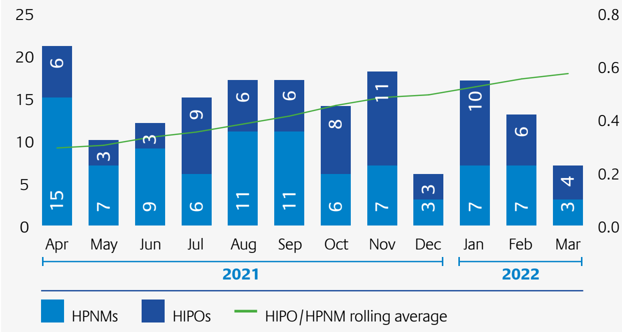

**Recordable injuries**



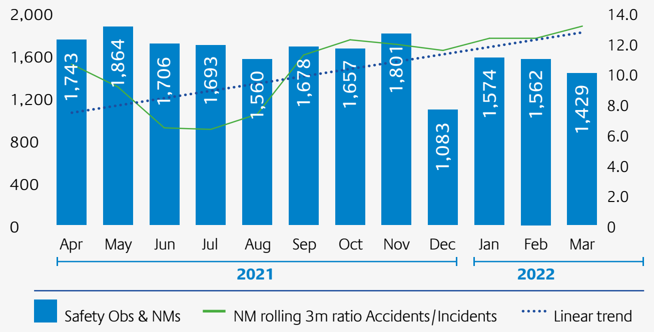

1. Number of recordable work-related injuries and illnesses per 200,000 working hours (200,000 represents 100 employees working 40 hours for 50 weeks per year).
2. Taken from US Bureau of Labor Statistics, the average rates for Repair and Maintenance industry sector was TRIR of 1.8 and DACR of 0.9, whilst the Management Consulting industry sector had average rates of TRIR of 0.4 and DACR of 0.2.

## Proactive reporting – Reporting safety issues before they cause harm continued

### High-Potential Occurrences and High-Potential Near Misses




### Near Misses and Safety Observations




## Employee inclusion and diversity

At Babcock, we are guided by our Purpose – '*creating a safe and secure world, together*' – and a clear set of Principles that are central to everything we do. To deliver on our Purpose, we are committed to creating an agile, people-centred business where everyone is included, supported and empowered to unlock their potential.

We see inclusion as an enabler and the key to creating the right foundations to attract and retain the best, diverse talent. We recently appointed our first Global Head of Inclusion and Diversity (I&D) to develop our approach to I&D and to review, design and implement activities that enable Babcock to become a more inclusive business that values difference.

Our three-pillar approach outlines the:

- insight and data needed to drive an evidence-led approach to I&D
- policies and programmes that drive greater talent engagement
- ways in which we educate and demonstrate the value of an inclusive organisation

We remain firmly committed to embedding this approach and monitoring our progress.

Our gender targets are:

1. 30% women within senior leadership teams by 2025
2. 30% female representation at all levels by 2030
3. 80% disclosure of diversity data by 2025

In the 2021 report we indicated a target of 80% disclosure of diversity data within 18 months. As we analysed the data for our People strategy and revisited all our targets, we realised this target was going to be difficult to achieve. However, we remain focused on our diversity data as it's a key component of our I&D strategy and approach. We have identified a breadth of activity required to help us meet this target by 2025 and drive real and sustainable changes across the workplace. Alongside our continued work on gender balance, LGBTQ+, faith and neurodiversity, we will renew our focus on disability and ethnicity, as well as greater exploration of social mobility as we drive to be a more inclusive company.

## Gender diversity

We are proud of our work on gender diversity which is a key business priority and we know there is still much to do to deliver gender balance through attraction and retention of female talent.

Our global workforce diversity has improved over the past year, moving from 19% in 2021 to 21% in 2022. This is in spite of an overall headcount reduction through 2021 that focused on business functional areas and tend to be female dominated. Female representation declined at the Board level reflecting a snapshot in time after the retirement of one female Board member. As recruitment proceeds to build the Board back to its full complement, maintaining diversity will be an important consideration as covered in the Nominations Committee report (see page 106.)

There has however been an improvement in representation at the senior management levels, that has resulted in a shift from 21% to 23% over the past year. Most notably, at the Executive Committee and management level, good progress has been made around the attraction and promotion of female talent, resulting in a positive move of 5 percentage points since 2021, from 16% to 21%.

Following our overall headcount reductions, our graduate population shrank this year from 258 in 2021 to 135 in 2022, which resulted in a subsequent reduction in our female intake by three percentage points. This is mainly driven by the challenges associated with recruiting in a very competitive graduate market, and in response we have implemented a number of changes that will drive back up our progress and build our pipeline of female talent.

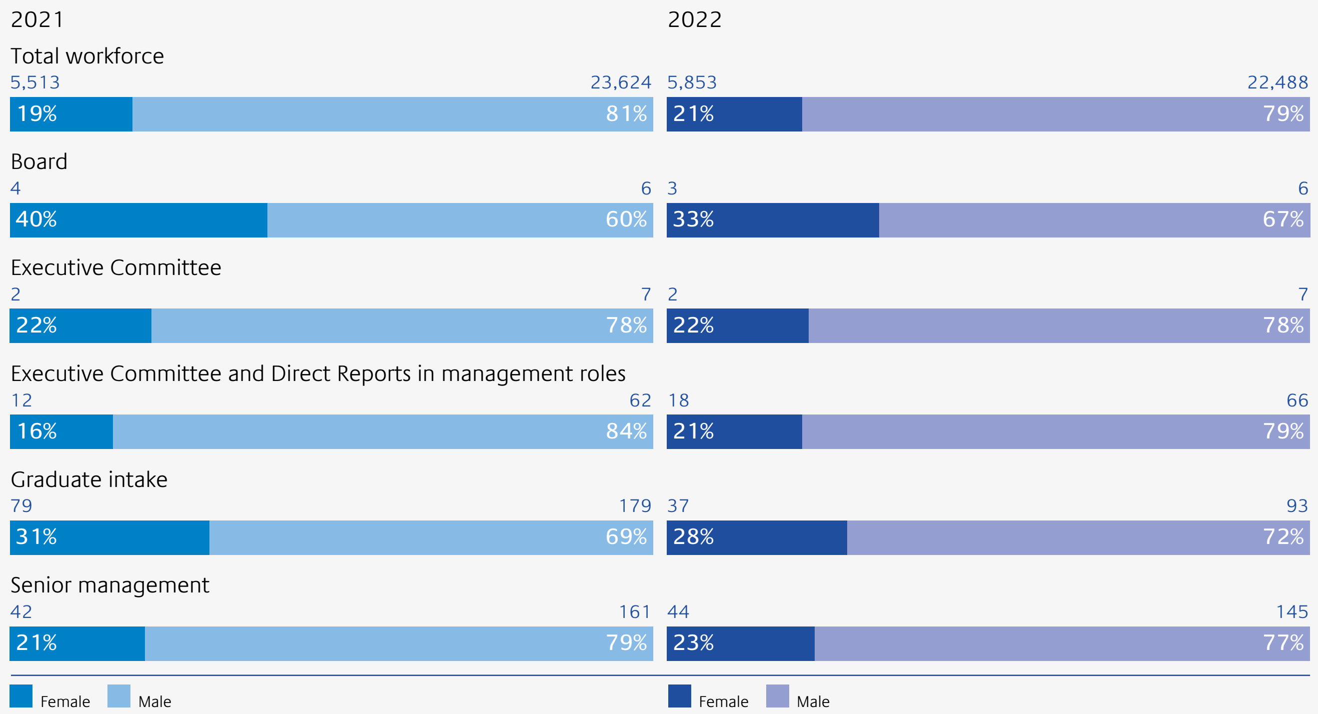
In spite of these challenges, Babcock is on track to fulfil our commitment to our gender targets and be an inclusive and diverse company, a great place to work where people feel part of an integrated, more global business.

Areas we are addressing to accelerate the pace of change:

### 1. Providing a culture in which women can progress their careers

- Redefining our ways of working
- Designing interventions and policies to support women at work, including, for example the introduction of Group-level menopause and gender-neutral leave policies
- Establishing a Returners approach and programme of activity which includes an overarching STEM returners programme. Elements within the programme will support different stages of a woman's life and career

## Gender diversity




1. The total workforce is 28,560 but excludes 2 non-binary, 4 prefer not to say, 151 non specified and 62 unknown in the gender percentages.
2. The gender diversity reflects Board composition at a point in time. We are recruiting for two non-executive directors in FY23 and we would expect this to change.
3. Executive Committee and Direct Reports in management roles total is 86 but excludes 2 non-specified in the gender percentages. Senior managers are defined as employees (excluding Executive Directors) who have responsibility for planning, directing or controlling the activities of the Group (Executive Committee) or a strategically significant part of the Group (sector/functional leadership teams) and/or who are directors of subsidiary business units (BU leadership).
4. Senior management role total is 189.
5. Graduate intake is 135 (119 UK, 12 South Africa, 4 Australasia) but excludes 1 non-binary and 4 unknown in the gender percentages.

- Designing an Early Careers strategy and approach to maximise increase in numbers of female students entering the organisation, to continue to increase the diversity of our pipeline
- Establishing an approach to supporting carers in the workplace – like the Gender-Neutral policy, this will benefit any carers, not just female ones. It is of course also a support tool and mechanism for women to stay in and progress at work

### 2. Establishing a pipeline of women ready to move up through the business

- We continue to engage with our women's networks across the Group to identify gaps in how we support women
- We will create individual leadership development plans to prepare female talent for senior roles
- We have opened our Women in Defence mentoring scheme to a wider range of employees to apply as both mentors and mentees

We are encouraged by our progress and are confident we have put in place a strategy which will provide a roadmap to drive systematic and sustainable change for the better.

### Creating gender balance and closing the gender pay gap

Work to reduce our gender pay gap has seen year-on-year progress. Whilst we are pleased to see the median pay gap decreasing from 12.5% to 11.8%, we know we still have a way to go.

Our challenge is not a pay issue but an issue of representation. The engineering and defence sectors in which we operate in continue to be male-dominated. For us, enabling a more equal gender representation remains key to our long-term strategy.

Our intention is to create an environment which attracts and retains more women into the business and delivers a better gender balance. To make this a reality, we will continue to work with internal and external stakeholders, including our gender networks and organisations such as Women in Defence, Nuclear, Science and Engineering, and review our policies and activities that inspire and support women – such as offering access to new ways of working.

We remain committed to closing the gender pay gap, growing our talent pipeline for the long term, developing our processes to attract female talent, and enabling employees to flourish and shape their own future within Babcock.

*For further information, please see our 2021 Gender Pay Gap Report on our corporate website at https://www.babcockinternational.com/news/uk-gender-pay-gap-report-2021/.*

## Focus for FY23 and beyond

Our vision for the future is to be a strong, safe and unified global business that delivers year-on-year sustainable growth with better outcomes for our culture, customers and communities.

Championed by the Board and our Group Executive Committee, our leaders are encouraged and empowered to act in line with our Principles and to role-model inclusive behaviours. They will be supported by our three pillar approach to deepen inclusion and drive results.

Our focus for the coming year is to:

- Gather data and insight from our employees to enable an evidence-led approach to driving greater inclusion and diversity
- Set clear metrics for disability and ethnicity (in addition to gender) to focus our effort, measure our performance and progress and create accountability across the Group
- Establish and embed I&D governance globally, including the further development of employee networks and peer support groups – to create a more consistent approach and build a better people experience
- Identify processes and interventions that will enable us to realise the targets set and increase I&D
- Further embed our Principles and engage our people in understanding the benefits of inclusion, social mobility and community engagement
- Continue our commitment to the Social Mobility Pledge and reduce inequalities through a thorough review of our recruitment practices and how we support progression once in employment

As we develop our Employee Networks, we will embed a new Peer Support Group model to support their development as they will continue to play a critical role in achieving Babcock's ambition for a more inclusive business. Our current networks include multi-faith, ethnicity, gender, LGBTQ+ and neurodiversity along with wider common interest groups.

We will work with our networks across a three-year programme to develop them to a global level, to drive a consistent employee experience and greater diversity across the Group. We will also identify where networks could be developed to support employee enablement, for example in relation to disability and those with caring responsibilities.

## Ways in which we are changing to meet our inclusion and diversity aspirations

### Growing new talent pipeline for the long term

- STEM support: more than 738 STEM ambassadors within the organisation have engaged over 32,220 students in STEM activities
- STEM returners: by FY23 we aim to increase the pool of female talent by establishing a UK pilot to hire women back into a career in STEM and support returners
- Early careers: more than 1,024 apprentices (14% female) and 335 graduates (30% female) are employed on our early careers' schemes. Our target is to achieve a 50/50 balanced intake in early careers by FY24
- Community engagement: we are extending our community engagement to attract, retain and develop more diverse talent

### Attracting the best diverse candidates from the current talent pool

- Recruitment analytics: we have increased the amount of data collected and reviewed to highlight any bias in our recruitment process
- Charters and memberships: we are proud stakeholders in the Women in Defence Charter, Women in Aviation Charter and Women in Nuclear UK. We are also members of the Armed Forces Covenant and are actively looking to develop further partnerships
- Our networks, supported by our newly introduced Peer Support Groups model, play a key role in championing and supporting colleagues across Babcock to drive the cultural change we seek

### Enabling employees to fulfil their potential within Babcock

- Flexible working: we have introduced the Agile Working Framework to encourage work-life balance, support family commitments, improved health and wellbeing and drive inclusivity
- Culture change: as part of an ongoing cultural change programme, we have reinforced our zero-tolerance position to any form of discrimination

## Employee engagement: (see Culture change section page 18)

Our Purpose and Principles were formally launched this year. Developed with the help of hundreds of employees across the Group, we are continuing to drive engagement in our culture and bring it to life through town halls, vlogs, videos, workshops, meetings, webinars, team discussions and focused weeks.

Our people have embraced our new Principles by sharing stories of where they have seen them in action and when they have 'lived' one of our Principles. We will continue to collect and share these stories and create a cultural guide to working at Babcock.

To support the engagement and cultural immersion of new hires into the UK business, we now have a dedicated onboarding platform, designed to enable new employees to familiarise themselves with the business before they officially start. Information is tailored, based on their start date and business area and we plan for this to be extended to the whole business in due course.

Whilst during the pandemic we facilitated online engagement of current employees, this is being balanced with more face-to-face communication as many of our colleagues return to the workplace. However, we know there is more to do to make sure engagement is happening on an ongoing basis throughout the business.

We want to continue to effectively engage with employees to understand their views and ensure we achieve our people goals. Today, Babcock uses a variety of focus groups and surveys to do this. Last year we committed to moving to a consistent approach to understanding and measuring employee engagement across the Group in 2022.

We are now implementing a global platform to establish a baseline of engagement (through an annual survey) and consistently measure and benchmark ourselves externally and track progress. The platform is designed to empower leaders to own and deliver engagement and take action to increase motivation and performance.

This and other insights will inform much of our people decision-making as well as our understanding of areas for improvement. They will form an important part of the conversations our leaders and managers have about our culture.

Implementing our one Babcock approach will help us to focus our effort, drive meaningful change and enable high performance.

## 4 Making a positive impact on the communities in which we operate

### Oxford Economics assessment

We have engaged Oxford Economics to conduct a comprehensive review of how Babcock delivers social value and contributes to the UK Government's objectives outlined in its Social Value Model, as well as maximising economic value from defence procurement.

### Progressing Group-wide volunteering approach

Volunteering is a rewarding and meaningful experience that supports communities and brings personal reward for our employees, enabling them to develop new skills and personal wellbeing.

We want to make a genuine difference to our communities and help them to thrive. For example, our Driving and Maintenance (D&M) instructors in the TMASS contract at Bovington are registered volunteer 'Blood Bikers' with YFW Blood Bikes. They give up their time to provide emergency courier services for blood, platelets, blood and tissue samples, medication, breast milk, documents, X-rays, CT scans, and equipment.

We have also supported teams across Babcock to take part in group voluntary activities, such as the National Beach Clean in the UK. In South Africa many of our employees worked with the Bokantsho Primary School in Viljoensdrift, Free State, to carry out extensive and much-needed renovations at the school. A play area was also built for the children in a rural area and blankets donated before the winter.

Following COVID-19, the UK businesses also supported the COVID vaccination programme by allowing employees time to train and administer vaccines with St John's Ambulance and a number of employees took up this very worthwhile challenge.

We are currently developing a Group-wide volunteering approach, supporting one of our key Principles, 'be kind', to facilitate every employee to volunteer one day per year.

### Group-wide sponsorship

During the latter part of the year we developed our internal charity and sponsorship guidelines. The current criteria have been broadened and clarified to align to our corporate Purpose '*to create a safe and secure world, together*'. We are committed to the communities in which we operate and the broader interests of the customers we serve. As good corporate citizens, we want to make a genuine difference by supporting our communities and helping them rebuild following COVID-19. Our new criteria are based on supporting military charities and events and also protecting communities around the world by focusing on local charities where we have our sites or attract our employees from.

### Indigenous peoples

In Australia, we partner with Supply Nation to expand our supply chain to include Aboriginal and Torres Strait Islander-owned businesses across Australia. We have an equivalent commitment to Māori and Pasifika-owned businesses in New Zealand through the Amotai initiative.

Babcock continues to actively support Indigenous students to increase their career opportunities, through sponsorship to Engineering Aid and Yalari in Australia, and encouraging curiosity about STEM subjects in younger children in New Zealand through employee volunteering at local schools.

This year, Babcock Canada renewed our commitment to the Phase II stage of the Canadian Council for Aboriginal Business' (CCAB) Progressive Aboriginal Relations (PAR) programme. This phase centres around engagement with Indigenous communities in the areas where Babcock operates, as well as external communications to our customers, partners, and the wider business about our Indigenous engagement activities. Much of this engagement activity is currently ongoing with the First Nations in Victoria and in northern Manitoba.

In support of commitments made through the PAR programme, Babcock selected and implemented an Indigenous Cultural Awareness training programme. This programme has been added as a mandatory training requirement for all employees.

In addition to the activities directly related to the PAR programme, Babcock also continued to strengthen our internal procurement policies to identify and incorporate more Indigenous businesses. A comprehensive review of the supply chain was undertaken to identify Indigenous business opportunities in the short, medium and long term. Through this activity, we also engaged with several potential Indigenous suppliers and partners, such as Cota Aviation in B.C., Tipi Insurance in M.B., and Makivik Corporation in Q.C.

Over the last year, Babcock has engaged in comprehensive engagement of several First Nation and Métis communities, businesses, employment and training and post-secondary institutions. Furthermore, the team continues to participate in Indigenous conferences, trade shows and networking events in order to further existing relationships and foster new engagements.

### STEM

In the last year we improved our STEM recording. Commitments to STEM and the communities in which we operate translates into 160 newly trained STEM ambassadors, bringing our total to over 738 ambassadors across the business and 30,000 students engaged in our STEM activities.

The STEM team continues to deliver virtually whilst returning to in-person events where possible, which have been extremely well received by attendees of all ages. Focus has been on developing our offering to raise awareness and increase engagement, by developing STEM activity booklets for employees' children and external use.

The Clyde STEM Coordination Team launched its first STEM activity catalogue, which is designed to help teachers successfully deliver STEM activities with their students. We have evolved the way we conduct community outreach to encourage more take-up of STEM subjects and to help address diversity disparity and improve social mobility.

Babcock now more accurately represents the communities and countries in which we operate and in so doing delivered our first Virtual Neuro Diverse Work Experience Programme at Devonport with several local schools in attendance along with two virtual work experience weeks across the UK, both focussed on STEM and accredited by the Industrial Cadets.

Our employees volunteer not only their time but write books to inspire the next generation to take small positive action to better the world. The3Engineers gifted 4,000 copies of their set of rhyming children's book to local schools and communities. They have also created a suite of free-to-download STEM resources for schools to use in the future based on the books.

In FY23 Babcock will continue to engage with young people, their parents, and teachers to ignite interest in studying STEM subjects and pursue a rewarding career in the industry by focusing on our Group-wide strategic objectives around raising awareness of STEM, increasing I&D and supporting schools that are located in deprived areas of the UK.

### Support for Armed Forces, veterans, and reserves

Babcock is committed to honouring and supporting the Armed Forces Covenant and the Armed Forces community. We recognise the value serving personnel, both regular and reservists, veterans and military families contribute to our business and country.

As part of our continued commitment to the Armed Forces Covenant, Babcock supports employee and graduate membership of the Reserve Forces and references our support in recruitment activity. We also support the employment of service leavers, veterans, and members of the Volunteer Forces by providing a guaranteed job interview where applicants meet the minimum requirements of a role.

Members of the Armed Forces community and their families can rely on our support. We offer a degree of flexibility in granting leave for service personnel spouses and partners before, during and after a partner's deployment, and will consider special paid leave for employees who have been bereaved or whose spouse or partner has been injured.

We work closely with the Career Transition Partnership, to ensure our employment opportunities are made available to service leavers and veterans, and we participate in careers fairs for those leaving the Armed Forces. We understand that Armed Forces spouses need flexibility when their service partner is posted to a new location, and we do our best to find alternative employment within the business if our employees need to move to accompany their partner to a new posting.

We are proud to currently employ 186 service leavers and 322 veterans in the business. We support the UK's Armed Forces and reservists and continue to actively back our reservist employees. We have approximately 43 volunteer and 12 regular reserves and around 14 uniformed cadet instructors in the business. We provide a minimum of 10 days' special paid leave per year. The reserve service is actively promoted to everyone in the Group, including our new graduates and apprentices.

### Partnership with academia

Innovation is in our people and our partnerships. Last year we announced our strategic partnership with the University of Strathclyde, one of the leading international technology universities. Babcock and Strathclyde have been working together for more than 30 years, and formalising the partnership will strengthen existing educational programmes for degree apprenticeships and industry placements and build on existing innovative research projects in nuclear, advanced manufacturing, space, and security-related technologies.

Our recently opened state-of-the-art Additive Manufacturing Centre is part of an innovative partnership with Plymouth Science Park. The partnership builds on our strong relationship with the academic and technology community across the south west and the local community around our Devonport dockyard.

Last year we also launched an exciting new project management degree apprenticeship programme at our Devonport facility in partnership with the University of Plymouth.

### Talent and development

To enable us to take on the challenges of today and the future, it is important for us to build and maintain the capability and skills of our workforce. In FY22 work was carried out on the kind of leader required to drive the future success of the business and focused on understanding the profiles of the leaders we have today.

We measured drivers, personality traits and competencies through a self-report tool – things that are our natural tendencies and capabilities which we can learn and develop. Seventy of our most senior leaders were assessed by evaluating their technical and behavioural skills and then compared to our future leader profile as well as a FTSE100 leader benchmark.

As a result, we were able to develop our leadership capability by clarifying and resetting the expectation of what it takes to be a successful high-performing leader in Babcock and understanding what is needed to deliver our strategy.

Babcock's leadership group has a wide spread of capabilities and styles and we enable them to inspire, motivate and empower their teams to make sure we deliver on our contractual and operational commitments so together we can build a stronger, more sustainable Babcock.

### Early careers

Last year saw the implementation and introduction of a dedicated one Babcock Early Careers Team responsible for the development of our early careers talent nationally as well as globally.

We recruited 263 apprentices globally during FY22, bringing the total number of apprentices to 1,024 across the business. Previously, most of our new starters have entered on level two and three programmes. However, emphasis has been on expanding the apprenticeship offering with the intent to offer programmes starting from level two all the way to level seven.

One of our very own apprentices was awarded the title of Shipyard Apprentice of the Year and won the Queen's Silver Medal 2021: a prestigious award for final-year apprentices from the maritime sector, which has been running since 1944. Simultaneously, the Devonport Apprentice Team won the Best Apprenticeship Programme in Plymouth in 2021.

One hundred and thirty five graduates entered onto our graduate development programme this year and have been assigned a buddy and formal mentor to accelerate their learning throughout the programme – which in many cases lead to professional registration such as charter-ship.

We will continue to run these successful, comprehensive apprenticeship and graduate development programmes to bring more young people into the business.

# GOVERNANCE

## 5 Being a collaborative, trusted partner across the supply chain

We are committed to conducting business honestly, transparently and with integrity. Diverse and robust supply chains enable us to provide quality and timely delivery of products and services.

External expenditure via third-party suppliers, including original equipment manufacturers (OEMs), continues to account for a significant part of our turnover and we recognise how our ability to deliver performance and margin is affected by our approach and ability to manage these relationships.

Our supply base design is balanced to meet our customer, regulatory and financial performance requirements. It considers supply chain risk and addresses appropriate mitigating actions. We review our business-critical suppliers on an annual basis to address any risks or concerns. To support this process we have invested in an AI risk monitoring solution that will allow us to map our supply chain ecosystem, monitor activities and alert us when hidden risk is exposed in our sub-tier supply chain. This has been rolled out in Q1 FY22.

We buy a wide range of goods and services from over 14,000 suppliers. These range from large multinational OEMs to small and mid-size enterprises (SMEs). Approximately 250 of these suppliers are considered to be key partners supporting our ability to deliver continuous improvement and innovative quality outputs. We combine technology, market intelligence and business process to engage with our supply base and form long-term sustainable relationships.

Our activities ensure that we continue to deliver value through working effectively with our supply chains. By improving upfront supply chain involvement in bid processes, we have been able to engage earlier with potential suppliers. This enables our suppliers to actively support both the design and implementation stages of our work with innovative solutions and deliver enhanced productivity and increased quality.

Over the past year we have undertaken a structural reset of our procurement and supply chain, appointing a new Chief Procurement Officer to lead its transformation. We have made strong progress with the implementation of the Group Procurement and Supply Chain operating model and standardisation of key business processes. The purpose of this strategy is to create a Group procurement and supply chain team with a common purpose and strategy which is fully integrated and aligned with the business. We aim to achieve consistent long-term value creation for our interested parties by continually enhancing our supply chain to deliver best-in-class and sustainable products, goods and services.

### Sustainable sourcing

Babcock aims to maintain strong and sustainable supply chains and we recognise that to be successful we must work collaboratively with our suppliers and sub-contractors to identify and deliver ever more sustainable goods and services. Our intention is to reduce the environmental footprint of our supply chain and provide social benefits to society in parallel with meeting our business goals.

We continue working to align our processes and standards to ISO20400 (Sustainable Procurement) including circular economy principles such as recycling and disposal options. A strategic roadmap has been developed which establishes the framework required to integrate sustainability within procurement and supply chain activities, driven by the need to deliver sustainable outcomes through our supply chain. Our procurement and supply chain business processes will continue to be developed and aligned to ISO20400 guidelines throughout 2022, with a view to full alignment by the end of 2023.

To support this intent we have published a new Supplier Sustainability policy which is being rolled out to our supply chain through planned communication activities and supplier engagement events during FY23.

Supporting guidance has also been produced in the form of our Sustainable Procurement Supplier guide. This document is provided to assist suppliers in meeting the requirements of our Sustainable Procurement policy. It identifies areas for emphasis, reference documents and some regional requirements arising from national policies.

Our suppliers and their extended supply chains are required to share our commitment to respecting, protecting and promoting human rights and to support our efforts to achieve transparency within higher-risk supply chains and take responsibility for the issues we uncover such as hidden labour exploitation.

## Scope 3 carbon emissions mapping

We are currently conducting an assessment of upstream Scope 3 emissions (categories 1 and 2) to establish data for Babcock's upstream value chain emissions.

A spend-based calculation methodology is being adopted for the mapping activity to produce tabular and graphical results for Babcock's upstream value chain emissions and provide a baseline for developing Babcock's carbon strategy further.

See Environmental section page 57

## Working with SMEs

We recognise the value that SMEs play in the wider economy and we actively encourage them to engage with us. We will continue to engage with both smaller and local suppliers, especially those that help inclusion of under-represented groups, which fosters economic prosperity and societal integration.

Working with SMEs also ensures that we have access to innovative new solutions and provides enhanced flexibility and agility. As part of the wider Group procurement and supply chain strategy, we expanded key performance indicators throughout FY22 to measure and monitor our percentage spend with SMEs. This is now a key measure within the procurement and supply chain function and our performance against benchmark targets is subject to ongoing management review, which supports both our decision-making and any actions required to support the growth of our SME supplier population.

## Human rights

Babcock is an international company and we are committed to conducting our dealings with the utmost integrity. We are committed to the protection of human rights and we comply with all national laws in the jurisdictions in which we operate. We welcome the opportunity to contribute positively to global efforts to ensure that human rights are understood and observed. We believe that a culture of respect for, and promotion of, human rights is embedded throughout our business and can be demonstrated by our commitment to ethical conduct in everything we do.

We recognise the United Nations Universal Declaration of Human Rights and the standards established by the International Labour Organization. Our suppliers and their extended supply chain are expected to share this commitment and to meet the following:

### Treat workers equally

- Respect the human rights of all employees and the rights of the communities in which they operate
- Ensure work is performed on a voluntary basis
- Ensure that all employees can make a free choice about their employment – there should be no illegal, forced, bonded, involuntary or exploited labour
- Ensure there is no involvement in human trafficking or involuntary movement of people

### Reasonable working hours

- Ensure employees do not work hours in excess of the limitations set by relevant local and national laws and regulations
- Ensure all overtime work is voluntary
- Other than for extraordinary situations, all workers are entitled to at least one day off in every seven-day period

### Workers are of an appropriate age

- Ensure that no underage workers are employed, either directly or indirectly
- Babcock's suppliers are encouraged to participate in appropriate apprenticeship programmes that comply with applicable laws and regulations

### Workers are paid fair wages

- Pay wages which at least meet national legal standards. Pay industry benchmark standards wherever possible
- Ensure overtime work is used responsibly and compensated fairly
- Ensure that everyone is working in a recognised employment relationship as defined by law, and explain clearly to employees the terms and conditions of their employment and the expected work output to which their wages relate

### Workers' health and safety in the workplace is protected

- Provide a safe and sanitary workplace, taking all necessary actions to educate employees to prevent accidents and injury to health

### Ensure access to fair procedures and remedies

- Allow access to full and confidential remedy/grievance processes
- Freedom of association and collective bargaining
- Allow free association and the opportunity to communicate directly with management without fear of intimidation or reprisal

Core processes to ensure compliance with our expectations include supplier onboarding, audits and assessments, issue management and performance management. The requirements are also incorporated into our Supplier Code of Conduct, Supplier Sustainability policy and Supplier Sustainability Guideline which are subject to routine periodic review.

The human rights risk assessment process is embedded into a number of our due diligence and management processes, where a targeted approach is taken within our questionnaires to understand the maturity levels of controls within our supply chain. Our supplier lifecycle management controls also trigger scheduled reviews within our supplier onboarding solution.

The supplier audit programme is currently being reviewed to ensure human rights issues are being embedded into the standard audit content. The supplier quality and development audit programme is being extended during FY23 to cover a wider section of our supply chain and the audit checklists are being standardised across each of the business units to consistently verify adequate human rights controls are demonstrable by the supplier throughout the audit process. Formal actions are taken when risks are identified during the audit process.

Our strategy for supply chain risk management has also led to the introduction of an AI solution for live monitoring of human rights risk within our extended supply chain. Babcock can now assess our suppliers' policy and performance strength regarding human rights, including information on child or compulsory labour, treatment of people throughout the supply chain and treatment of local populaces. This approach serves as an early warning system. Should events or changes occur in our supply, live alerts are communicated to the procurement and supply chain team.

## Modern slavery

In the UK, we expect our suppliers and extended supply base to adhere to the Modern Slavery Act 2015, as we do ourselves. We expect all our overseas suppliers to understand and comply with the intent of the Act.

Modern slavery considerations are included as part of our risk management and supplier selection processes and we will continue to review our approach to training our employees and ascertaining risks in regards to the prevention of modern slavery.

If it is discovered that there has been a breach of the above, or any other relevant, declarations and legislation, we will take all necessary steps to mitigate any impact.

Our Modern Slavery Transparency Statement is reviewed and approved annually by the Board. The statement remains available on our website.

## Fair operating practices

Our Group-wide Suppliers' Code of Conduct (available on the Group's website) is designed to provide clarity about our expectations of suppliers, including compliance with all applicable laws. While we recognise that many of our suppliers operate in different geographic and economic environments, we expect that products and services are delivered in a way that supports Babcock's high standards and contributes to the reputation of Babcock and our customers.

Suppliers and the extended supply chain are expected to meet these standards at all times and should either be willing to subscribe to our Code, or have equivalent standards and procedures in their own businesses.

Our intention is to be a good partner and to work with suppliers to support necessary improvements, but we will not accept any behaviour which is contrary to either our ethical codes or health, safety and environmental working practices.

Before engaging with suppliers, we assess their ability to demonstrate that they are 'fit for business', with financial, commercial, safety and governance capability. Suppliers also demonstrate they are 'fit for purpose', with technical, health and safety capability and security compliance to meet our contractual requirements.

Our businesses use appropriate processes to qualify, onboard and periodically revalidate sub-contractors to ensure compliance with commercial, regulatory and legal requirements.

Protecting the information and physical assets of our customers is an important part of what we do. We always expect high standards of commercial confidentiality. For certain types of supply we have and continue to develop exacting standards of security compliance.

In the UK, we use the JOSCAR due diligence tool, which is a shared industry-wide management system for defence contractors that collects standardised information about individual suppliers across the UK supply chain.

## Payment to suppliers

We understand the importance of predictable payments when running a business and will ensure good practice across the Group.

17 legal entities submit returns to Companies House according to the Payment Practices and Performance Regulations. 11 of our legal entities are signed up to the Prompt Payment Code and are compliant as of 31 March 2022.

Procurement methodology to calculate average payment days across the group has changed this year from an average to weighted average approach. The average payment over the past six months to March is 24.6 days, versus 23.5 days last year. For reference, using last year's methodology, the equivalent figures would be 30.5 days over the past six months versus 29.6 days last year.

We actively support the Prompt Payment Code and encourage our suppliers to adopt the code themselves and promote its adoption throughout their own supply chains.

## Commercial integrity

We are committed to conducting business honestly, transparently and with integrity. It is the right and proper way to behave, ensuring we uphold high ethical standards across the Group. It also supports our long-term success.

We understand our reputation and good name are amongst our greatest assets and could easily be lost by actual or suspected unprincipled behaviour. To support good governance and ethical behaviour across our Group, our actions and those of our employees, suppliers and partners are guided by a series of Group policies. These are reviewed periodically to ensure that they continue to meet current best practice principles and legislative needs. By establishing transparent policies and procedures we can reduce risk to our business and to our customers.

## Code of Business Conduct and Ethics policy

To protect the Company and reduce risks, we have established a policy on how we should conduct business which is summarised in the form of the Babcock Code of Business Conduct.

Compliance with this policy is compulsory for our employees, business advisors and business partners (or, in the case of business advisors and partners, they must have equivalent standards and procedures in their own businesses). The policy is kept under review by the Group Company Secretary and General Counsel and on an annual basis the Board undertakes an annual ethics review, seeking assurance that the Group's Ethics policy is complied with.

Our Ethics policy comprises a detailed manual, available to employees on the Group's intranet and also available on our website, which contains guidelines, authorisation mechanisms and other procedures aimed at identifying and reducing ethical risks. It supports extensive policies around anti-bribery and competition law that clearly show our zero tolerance for any form of bribery or anti-competitive behaviour.

These controls form an integral part of our risk management arrangements, which also include training our employees and undertaking regular risk assessments throughout the business. We implement appropriate training and procedures designed to ensure that we, and others working for us, understand what our Code of Business Conduct and our Suppliers' Code of Business Conduct (see also page 71) mean for them in practice. This training includes mandatory completion of courses on an annual basis in all our geographies, translated where applicable, such as anti-bribery and corruption, security and data protection. Completion of these courses is monitored.

We treat breaches of our Codes or associated guidance seriously. Employees can raise any concerns that our Code or its associated guidance is not being followed without fear of unfavourable consequences for themselves.

To ensure that anyone with a concern is able to access advice and support, our independent whistleblowing hotline, EthicsPoint, (operated by NAVEX Global) allows for confidential and anonymous reporting and is available 24 hours a day, seven days a week, in all territories where we are based. Employees are encouraged to use it if they feel unable to raise concerns with their local management team and details are available for use by external stakeholders and members of the public.

All reports to the whistleblowing line are sent directly to the Company Secretary who decides the appropriate course of investigation. During the year 83 whistleblowing reports were received (FY21: 83).

More details of our risk management procedures can be found on page 76 whilst our Ethics policy, Code of Business Conduct and Suppliers' Code of Conduct can be found on our website.

### Cyber security

We recognise the very real risk of malicious cyber breach and work hard to ensure both our customers' and our own information assets remain protected. Babcock's Group Security Committee meets quarterly to provide governance covering cyber and other security and informational assurance risks, issues and threats facing the Group.

Babcock is a member of the joint UK Ministry of Defence and industry Defence Cyber Protection Partnership (DCPP) which is an initiative to ensure the defence supply chain understands the cyber threat and is appropriately protected against attack. Babcock is represented on all the working groups and DCPP executive committee, as well as other defence security forums.

Babcock applies all required international and government security standards for installation and secure operation of Information systems.

Babcock's core IT services are certified to ISO27001 (Information Security), ISO22301 (Business Continuity) and Cyber Essentials Plus, which is mandatory for all suppliers of UK Government contracts that involve handling personal information and providing certain products and services.

Babcock continues to invest in cyber resilience and in raising awareness across the workforce.

## Non-financial information statement

Reporting on material yet non-financial measures is important in understanding the performance, opportunities and long-term sustainability of the Company and our ability to generate value for all our stakeholders. We disclose non-financial information in the ESG strategy report and throughout the Strategic report. We are committed to providing greater transparency about our policies, standards and governance approach through the global reporting frameworks and insight in the ESG strategy report.

| Reporting requirement | Policies and standards | Additional information | Page |
|---|---|---|---|
| Environmental matters | Health, Safety and Environmental policy* | Environmental section | 57 |
| | Energy policy* | Environmental section | 57 |
| | Procurement Sustainability policy** | Sustainable sourcing | 69 |
| Employees | Code of Conduct ** | Commercial integrity | 71 |
| | Health, Safety and Environment policy* | Home Safe Every Day | 63 |
| | Agile working framework* | Employee inclusion and diversity | 64 |
| | Charity and Sponsorship High-Level Guidelines* | Group-wide sponsorship | 67 |
| | | Building relationships | 52 |
| Human rights | Code of Conduct** | Code of Business Conduct and Ethics | 71 |
| | Supplier Code of Conduct** | Fair operating practices | 71 |
| | Modern Slavery Transparency Statement** | Commercial integrity | 71 |
| Social matters | Anti-bribery and Corruption/Ethics policy** | Code of Business Conduct and Ethics | 71 |
| | Code of Conduct** | Code of Business Conduct and Ethics | 71 |
| | Respect and Inclusion Charter* | Employee inclusion and diversity | 64 |
| | Canada Indigenous Peoples policy* | Indigenous peoples | 67 |
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| Anti-bribery and corruption | Anti-Bribery and Corruption/Ethics policy** | Code of Business Conduct and Ethics | 71 |
| | Whistleblowing policy** | Principal risks and management controls | 76 |
| | Supplier Code of Conduct** | Fair operating practices | 71 |
| Description of principal risks and impact on business activity | Group Risk Management policy* | Principal risks and management control | 76 |
| Business model | | Our business model | 8 |
| Non-financial KPIs | | Our strategy | 6 |

* Available to employees through the Babcock intranet but not published externally.
** Available on the Babcock website and available to employees through the Babcock intranet.

## Compliance with Global Reporting Initiative (GRI)

We intend to report in accordance with the GRI Standards, Core option. We have indicated the disclosure topics that are relevant to Babcock and the level of disclosure in AR21 and AR22.

| Standards | Disclosures | | AR-21 | AR-22 |
|---|---|---|---|---|
| | GRI 101: Foundation 2016 | GRI 101-01 to 101-10 | ● | ● |
| Universal Standards | GRI 102: General Disclosures 2016 | GRI 102-01 to 102-56 | ● | ● |
| | GRI 103: Management Approach 2016 | GRI 103-01 to 103-03 | ● | ● |
| | GRI 201: Economic Performance 2016 | GRI 201-01 to 201-04 | ◐ | ◐ |
| | GRI 202: Market Presence 2016 | GRI 202-01 to 202-02 | ◔ | ◔ |
| | GRI 203: Indirect Economic Impacts 2016 | GRI 203-01 to 203-02 | ◕ | ◕ |
| Economic Topics | GRI 204: Procurement Practices 2016 | GRI 204-01 | ● | ● |
| | GRI 205: Anti-corruption 2016 | GRI 205-01 to 205-03 | ◐ | ◐ |
| | GRI 206: Anti-competitive Behaviour 2016 | GRI 206-01 | ◐ | ◐ |
| | GRI 207: Tax 2019 | GRI 207-01 to 207-04 | ◐ | ◐ |
| | GRI 301: Materials 2016 | GRI 301-01 to 301-03 | ○ | ◔ |
| | GRI 302: Energy 2016 | GRI 302-01 to 302-05 | ◕ | ◕ |
| | GRI 303: Water and Effluents 2018 | GRI 303-01 to 303-05 | ◔ | ◕ |
| | GRI 304: Biodiversity 2016 | GRI 304-01 to 304-04 | ○ | ◔ |
| Environmental Topics | GRI 305: Emissions 2016 | GRI 305-01 to 305-07 | ◕ | ◕ |
| | GRI 306: Waste 2020 | GRI 306-01 to 306-05 | ◔ | ◐ |
| | GRI 307: Environmental Compliance 2016 | GRI 307-01 | ◕ | ◕ |
| | GRI 308: Supplier Environmental Assessment 2016 | GRI 308-01 to 308-02 | ◐ | ◐ |
| | GRI 401: Employment 2016 | GRI 401-01 to 401-03 | ● | ● |
| | GRI 402: Labour/Management Relations 2016 | GRI 402-01 | ● | ● |
| | GRI 403: Occupational Health and Safety 2018 | GRI 403-01 to 403-10 | ◕ | ◕ |
| | GRI 404: Training and Education 2016 | GRI 404-01 to 404-03 | ◐ | ◐ |
| | GRI 405: Diversity and Equal Opportunity 2016 | GRI 405-01 to 405-02 | ◐ | ◐ |
| | GRI 406: Non-discrimination 2016 | GRI 406-01 | ◐ | ◐ |
| | GRI 407: Freedom of Association and Collective Bargaining 2016 | GRI 407-01 | ● | ● |
| | GRI 408: Child Labour 2016 | GRI 408-01 | ● | ● |
| | GRI 409: Forced or Compulsory Labour 2016 | GRI 409-01 | ● | ● |
| Social Topics | GRI 410: Security Practices 2016 | GRI 410-01 | ⊗ | ⊗ |
| | GRI 411: Rights of Indigenous Peoples 2016 | GRI 411-01 | ● | ● |
| | GRI 412: Human Rights Assessment 2016 | GRI 412-01 to 412-03 | ◔ | ◐ |
| | GRI 413: Local Communities 2016 | GRI 413-01 to 413-02 | ◐ | ◐ |
| | GRI 414: Supplier Social Assessment 2016 | GRI 414-01 to 414-02 | ○ | ○ |
| | GRI 415: Public Policy 2016 | GRI 415-01 | ● | ● |
| | GRI 416: Customer Health and Safety 2016 | GRI 416-01 to 416-02 | ⊗ | ⊗ |
| | GRI 417: Marketing and Labelling 2016 | GRI 417-01 to 417-03 | ⊗ | ⊗ |
| | GRI 418: Customer Privacy 2016 | GRI 418-01 | ○ | ○ |
| | GRI 419: Socioeconomic Compliance 2016 | GRI 419-01 | ● | ● |

## Response to Sustainable Accounting Standards Board (SASB)

| Dimension | General issue category | Disclosure topic | Accounting metric(s) | AR-21 | AR-22 |
|---|---|---|---|---|---|
| Environment | Energy Management | Energy Management | • RT-AE-130a.1: (1) Total energy consumed, (2) percentage grid electricity, (3) percentage renewable | ◕ | ◕ |
| | Hazardous Waste Management | Waste & Hazardous Materials Management | • RTA-AE-150a.1: Amount of hazardous waste generated, percentage recycled<br>• RTA-AE-150a.2: Number and aggregate quantity of reportable spills, quantity recovered | ◑ | ◑ |
| Social Capital | Data Security | Data Security | • RT-AE-230a.1: (1) Number of data breaches, (2) percentage involving confidential information<br>• RT-AE-230a.2: Description of approach to identifying and addressing data security risks in (1) company operations and (2) products | ◕ | ◕ |
| | Product Quality & Safety | Product Safety | • RT-AE-250a.1: Number of recalls issued, total units recalled<br>• RT-AE-250a.2: Number of counterfeit parts detected, percentage avoided<br>• RT-AE-250a.3: Number of Airworthiness Directives received, total units affected<br>• RT-AE-250a.4: Total amount of monetary losses as a result of legal proceedings associated with product safety | ⊗ | ⊗ |
| Business Model & Innovation | Product Design & Lifecycle Management | Fuel Economy & Emission in Use-phase | • RT-AE-410a.1: Revenue from alternative energy-related products<br>• RT-AE-410a.2: Description of approach and discussion of strategy to address fuel economy and greenhouse gas (GHG) emissions of products | ◔ | ◔ |
| | Materials Sourcing & Efficiency | Materials Sourcing | • RT-AE-440a.1: Description of the management of risks associated with the use of critical materials | ◔ | ◔ |
| Leadership & Governance | Business Ethics | Business Ethics | • RT-AE-p510a.1: Total amount of monetary losses as a result of legal proceedings associated with incidents of corruption, bribery, and/or illicit international trade<br>• RT-AE-p510a.2: Revenue from countries ranked in the 'E' or 'F' Band of Transparency International's Government Defence Anti-Corruption Index<br>• RT-AE-p510a.3: Discussion of processes to manage business ethics risks throughout the value chain | ◕ | ◕ |

### Status key

| | Indicative disclosure | | Indicative disclosure |
|---|---|---|---|
| ● Full Disclosure | 100% | ◔ Partial Disclosure | 25% |
| ◕ Partial Disclosure | 75% | ○ No Disclosure | 0% |
| ◑ Partial Disclosure | 50% | ⊗ Not Relevant | N/A |

# Our principal risks and how we manage them

We have a risk management framework and internal control environment to manage the risks that may undermine our ability to execute our strategy or more generally our business model. The Board has had increasing confidence in the risk management processes as a result of improvements made in FY21 and FY22, enabling the Board to have assurance around the overall risk management together with the determination of the nature and extent of the Group's principal risks. Processes will be subject to ongoing continuous improvement.

As part of the Group's turnaround plan, we have reviewed and improved the risk management framework so that it aligns with our new operating model. As a result, the framework, which we describe below, is now standardised across the Group and consistent, with clear risk ownership. In order to assist the Board and the Group in its understanding of its principal risks, we have increased the granularity and quantification of each risk. The framework also now includes the identification and assessment of climate risks, thereby meeting the Task Force on Climate-related Financial Disclosures reporting requirements. In early FY23 we have launched an updated Risk Management policy, which will enhance the guidance and requirements around our risk assessment and reporting process.

## Our risk management framework

The Board sets the Group's strategy, which we describe on page 6. To help deliver this strategy, the Board has now in place procedures for identifying, evaluating and managing the risks inherent in our strategy. As part of those procedures, the Board reviews and approves the Group's risk register on a semi-annual basis to ensure alignment with the Group's strategy. It makes this determination using a risk-rating matrix, which assesses the probability and the impact of each risk occurring. The Board makes this assessment after taking into consideration the controls and mitigations that the Group has in place.

We build our risk-rating matrix by bringing together the risk registers of our sectors. These risk registers include both principal and emerging risks. The sectors compile their risk registers by using a common Group risk management framework. The framework requires the sectors to describe their risks along with the measures in place to control or manage each risk. The Group risk function consolidates the sector risk registers and then produces the risk-rating matrix, which sets out the Group's principal and emerging risks.

The risk-rating matrix is split into two separate five-by-five matrices: one showing the current rating of each risk; and the other showing the target rating. Each matrix measures each risk for probability and impact, with each box on the five-by-five matrix representing a combination of a particular level of probability and impact. We rank probability across very unlikely, unlikely, possible, likely and very likely. We measure impact across insignificant, minor, moderate, major and severe. We give guidance so the sectors have a common approach as to how to measure probability and impact. We have included the current rating for each principal risk alongside its description, which follows.

On a semi-annual basis, the Group Executive Committee reviews the matrix. Following the Group Executive Committee reviews, the Board, on an annual basis, considers the matrix and, in particular, reviews the Group's principal and emerging risks. The review includes a consideration of risk description, as well as our controls and mitigations. In addition to the review of the risk-rating matrix, the Board also undertakes 'deep dives' on specific risks at regular intervals in the year.

## Our internal control environment

During the year, we made significant improvement to our internal control environment which aims to protect the Group's assets and to check the reliability and integrity of the Group's information, thereby providing assurance that the Group appropriately manages the risks to our business model and the delivery of our strategy.

Written policies set the framework for the Group's internal controls. These policies cover a range of matters intended to mitigate risk, such as health and safety, information security, trade controls, contracting requirements and accounting policies. The policies include a new scheme of delegated authorities that was launched in the period. This Group-wide process amalgamates all previous Group, sector and business unit delegation of authorities into one consolidated and standardised document, which imposes strict controls across the Group and details authority levels for any given act. For example under the scheme, which it approves annually, the Board reserves to itself the authority to approve all material acquisitions and disposals, all material capital expenditure, all material non-ordinary-course tenders (the CEO and the CFO may approve material ordinary-course tenders) and all financing arrangements not delegated to the Board's Finance Committee.

The Group's internal controls also include comprehensive financial reporting processes. The Group reports on a monthly basis up through its business units and sectors to the Group Executive Committee. The CEO and CFO report to each Board meeting on matters of significance to the Group, including its operating performance. In addition to backward-looking reports, the Group prepares an annual budget and medium-term financial plans, which the Board reviews, challenges and approves. The Group prepares updated forecasts for the year on a quarterly basis. The Board receives details of monthly actual financial performance compared to budget, forecasts and the prior year.

## Our risk assurance

We use the 'three lines of defence' model to assure ourselves about the management of the risks that we face. The first line of defence is management control, policies and procedures, together with management oversight. The second line is internal assurance activities, which include the review of the sector risks and functional oversight. The third line is external (ie independent) assurance activities, such as internal audits.

## Our risk management framework and our internal control environment

### External audit

Provides external assurance: its aim is to detect material errors and material irregularities in our financial statements.

*Please see page 142 for the independent auditor's report.*

### Board

Overall responsibility for the Group's strategy and risk management

Reviews the Group's risk-rating matrix and determines the Group's principal risks

Reviews and approves the Group's risk register

Reviews the Group's financial reports, including annual budget and five-year plan, to monitor financial performance and identify potential issues/emerging risks

### Audit Committee

Reviews aspects of the Group's risk management and internal control environment

Reviews and monitors the adequacy and effectiveness of the Group's risk management framework and internal control environment

Approves the annual audit plan for the external and internal audits

### Group Executive Committee

Reviews quarterly a consolidated report prepared by the Group risk function, which summarises the Group's principal and emerging risks. Committee members sponsor and own the principal risks

### Internal audit

Provides independent and objective assurance on governance, risk management and internal control to the Board and the Group. For more information, please see page 111

### Sectors

Identify the risks, including emerging risks, along with the controls and assurance to mitigate those risks

### Functions

Provide oversight and management of certain specialised risk areas that benefit from central coordination (for example, tax, treasury, IT, procurement etc)

### Our risk assurance

#### First line of defence – management

We have written policies covering a range of matters to mitigate risk, such as health and safety, information security, contracting requirements and accounting policies. We underpin these policies with a comprehensive scheme of delegated authorities, which the Board annually reviews and approves. Twice a year, the sectors complete a letter of representation to provide confirmation of compliance with the Group's policies.

Management reports up from our business units through the sectors to the Board on operational and financial performance.

#### Second line of defence – internal assurance

The Board and the Group Executive Committee review the Group's financial and operational performance on a regular basis through the monthly reporting packs, which include monthly management accounts, and can compare that performance against the Group's budget, which the Board approves on an annual basis.

Group reviews the sector letters of representation to identify any control weaknesses.

Group functions and specific committees monitor certain risks, such as health and safety, finance, tax and treasury.

The Group maintains an insurance programme. The Group Risk and Insurance Manager reports to the Board annually on the strategic approach to that programme.

#### Third line of defence – external assurance

The internal audit, which reports to the Audit Committee, provides assurance of the effectiveness of the Group's control environment.

The Audit Committee agrees both the external and internal audit plans on an annual basis.

A number of external regulators and other bodies, such as national civil aviation authorities, the UK Office of Nuclear Regulation and the International Office for Standardisation, regularly inspect parts of the Group.

All employees have access to a whistleblowing line to allow them to report any concerns that they may have. The Board receives all the reports to the line along with an explanation of how the Group is investigating them and the outcome of the investigation.

## Risk management and internal control annual review

To provide assurance, the Audit Committee performs an annual review of the Risk Management policy to assess its effectiveness. After last year's review, the Committee concluded that the internal control environment was not operating effectively in certain parts of the Group, particularly in Aviation, Land and Group Head Office. In response, the Committee agreed with management improvement plans for the relevant areas. Throughout the year, the Committee has monitored the implementation of these plans and, following this year's review, is satisfied with the delivery of the improvement plans agreed last year, whilst recognising that there remains ongoing scope for further improvements in FY23, including lessons learnt from FY22 closing.

## Our principal and emerging risks

We have described above our risk management framework. Working through that framework, this year the Board has identified on pages 76 to 87 those risks that it currently believes to be of greatest significance to the Group, as they have the potential to have a material impact on the Group's business or the delivery of its strategy or financial results if they were to occur.

However, our risk management is a dynamic and ongoing process. Therefore, the Group might identify new risks or better understand the significance of existing risks or identify a change in a risk. This means that the risks identified on pages 76 to 87 are not and cannot be an exhaustive list of all the principal risks that could affect the Group. In addition, as part of its risk work, the Board has also identified two emerging risks. Both these risks are not standalone risks, but affect several of our principal risks. Where they do affect one of our principal risks, we have included that effect in the principal risk. The two emerging risks are:

| Emerging risk | Description |
|---|---|
| **Inflation** | As the global economy recovers from the pandemic, it is experiencing increasing inflationary pressure, both in terms of supplier costs, such as products, commodities, energy and freight, and labour rates. This inflationary environment may be exacerbated by the conflict in Ukraine. As a Group, we have a number of long-term contracts, which may include fixed price elements or saving commitments. We also have collective bargaining agreements with our workforce at certain sites. If we have increased costs which we are not able to pass on, this will affect the profitability of the contracts concerned and could mean that they become loss-making or that we are unable to meet our contractual commitments, leading to an adverse financial impact and a longer-term reputational impact.<br><br>We have established a programme watchlist covering our most significant programmes as part of our monthly reviews and are in discussion with customers where inflation is diverging from contract terms. In respect of new contracts, we have put in place controls to ensure that the terms of the new contracts adequately cover the inflation risk. |
| **Supplier resilience** | Our supply chain is subject to the same global inflationary pressures. Furthermore the global supply of raw materials and parts has not fully recovered from the COVID-19 pandemic, leading to supply interruptions. As with inflation, this could be exacerbated by the conflict in Ukraine. As a result, there is a risk that our suppliers may suffer financial distress and/or not be able to fulfil their contracted supply agreements with us. This would add additional cost and time to our programmes, which we may not be able to pass on to our end customer.<br><br>To mitigate the risk, we have increased the level of monitoring of our supply chain's financial distress and operational performance to allow us to intervene if any concerns arise. |

# Principal risks, their impact and mitigation

| Probability | | Impact | | Change from last year |
|---|---|---|---|---|
| 1 | Very unlikely | 1 | Insignificant | Up from last year |
| 2 | Unlikely | 2 | Minor | Same as last year |
| 3 | Possible | 3 | Moderate | Down from last year |
| 4 | Likely | 4 | Major | |
| 5 | Very likely | 5 | Severe | |

## EXISTING MARKETS

We rely on winning and retaining large contracts with a relatively limited number of major customers, whether in the UK or overseas, many of whom national or local governments (directly or indirectly) own, control or fund.

**Probability** 4 ↔ **Impact** 4 ↔

### Potential impact

Major customers, such as our single biggest customer the UK Ministry of Defence (MOD), have significant bargaining power and can exert pressure to change, amend or even cancel programmes and contracts. As governments, whether in the UK or overseas, own or fund many of our major customers, political and public spending decisions may have a significant impact on our customers.

For example, the UK Government's national security and international policy objectives control the budget of the MOD. Another example may be the UK's exit from the EU, the consequences of which remain difficult to predict, as UK companies may not be able to bid on EU programmes, or may have to trade on different terms to a non-EU member, or may experience difficulties holding operating licences or recruiting qualified personnel.

Whilst customer policy changes or budgets can potentially offer more opportunities for us to pursue, they can also be a risk in that they could lead to changes in customer strategy and spend, which could include:

- reductions in the number, frequency, size, scope, profitability and/or duration of future contract opportunities
- in the case of existing contracts, early termination, non-extension or non-renewal or lower contract spend than anticipated and pressure to renegotiate contract terms in the customer's favour
- favouring the retention of, or return to, in-house service provision, either generally or in the sectors in which we operate
- favouring small or medium-sized suppliers or adopting a more transactional rather than a cooperative, partnering approach to customer/supplier relationships
- imposing new or extra eligibility requirements as a condition of doing business with the customer that we may not be able readily to comply with, or that might involve significant extra costs, thereby affecting the profitability of doing business with them.

A significant number of our contracts with the MOD are subject to the Single Source Contract Regulations (SSCR), which the Single Source Regulations Office (SSRO) administers. The SSRO sets the baseline profit rate for single source contracts let by the MOD on an annual basis. These regulations and their implementation are subject to review by the UK Government, which could lead to lower returns for industry.

In certain jurisdictions, we bid on programmes that may include offset arrangements. Such arrangements are designed to generate work in the customer's country and may constrain how we deliver and benefit from those programmes.

### Mitigation

Our focus on the aerospace, defence and security markets, together with our geographical spread, provides a degree of portfolio diversification. We are in ongoing dialogue with our key customers in order to understand their requirements, objectives and constraints, so that we can remain as aligned with them as possible. We monitor expenditure changes in our markets in order to allow us to make the appropriate adjustments. We maintain a public listing, as we believe it is an important factor in winning contracts and retaining our business position, particularly with government customers.

We have a clear business strategy to target a large bid pipeline, both in the UK and internationally. We bid for contracts we consider have an alignment with the Group strategy and where we believe we stand a realistic chance of success due to, for example, customer understanding, domain knowledge or technical expertise, both in the UK and overseas. We maintain a dialogue with our customers to understand their intentions regarding their pipeline.

During the pandemic, we worked closely with our customers in order to understand their priorities in response to the pandemic. All our businesses have implemented the necessary plans in consultation with our key customers to continue to deliver on our contracts where possible.

The Group remains in dialogue with the SSRO, the MOD and wider industry regarding future planned changes to the SSCR.

## NEW MARKETS

We seek new markets and contracts for our services both with existing and new customers, whether in territories where we are already established or in territories where we are not.

**Probability** 3 ↔ **Impact** 5 ↔

### Potential impact

We may fail to secure and/or deliver new opportunities for a number of reasons. These reasons may include customer funding constraints, our services not being relevant due to the non-acceptance of our business model by customers, our failure to anticipate future market requirements or future changes in technology, our failure to find the appropriate quantity and quality of resource, our failure to align our bid strategy to a customer's strategy, or increased competition in our markets.

In addition, COVID-19 or the UK's departure from the EU or other geopolitical developments may give rise to economic nationalism and a reluctance from international customers to award contracts to a non-domestic company. A lack of success in exporting the Group's business model outside the UK and our current core markets could adversely affect the growth prospects and strategic development of the Group. Failure to convert our bidding pipeline into contracts may put pricing pressure on the remaining pipeline.

### Mitigation

We aim to target our resources in those new markets where we believe our services are relevant and where we believe we have a good chance of success. As appropriate, we aim to invest in innovation and people to prepare for new ways of working or delivering our services. We maintain ongoing dialogue with our customers in order to understand their requirements and their budgets.

## FINANCIAL RESILIENCE

The Group is exposed to a number of financial risks, some of which are of a macroeconomic nature (for example, foreign currency, interest rates) and some of which are more specific to the Group (for example, liquidity and credit risks).

**Probability** 3 ↓ **Impact** 4 ↔

### Potential impact

A lack of financial resilience may hinder us in raising debt funding to invest in existing or future business. The weakness also may cause our existing banks to increase the cost of our funding. If our debt is denominated in a currency other than Sterling, movements in exchange rates may make that debt more costly when we repay it.

Customers and/or suppliers may question our long-term sustainability if we have a weak balance sheet. This may tighten the terms of business on which they are prepared to contract with us or, in the extreme, cause them to not award work to Babcock due to their perception of risk.

Credit rating agencies may downgrade our rating, which could increase our cost of borrowing.

The lack of financial resilience may trigger certain pension scheme financial thresholds, requiring us to allocate further resource to the schemes.

We could face capital allocation constraints and consequently have reduced capital to invest in the business to meet all our obligations or to pay a dividend.

In addition, if companies working in the defence or nuclear sectors were deemed to be not suitable for investment by certain investment funds (eg due to extremely strict ESG policies) the cost and/or availability of capital to the Group could be adversely affected.

### Mitigation

We have undertaken a rationalisation of the Group portfolio and raised in excess of the £400 million proceeds target we set ourselves last year from disposals. This has strengthened our balance sheet during FY22.

Last year, we also secured an additional debt facility of £300 million to provide additional liquidity, along with a temporary relaxing of financial covenants.

We are proactive in our dealings with credit rating agencies and lenders. The Board reviews the financial position of the Group on a monthly basis against the Board-approved three-year plan.

The Group has a very proactive ESG agenda (see page 54) and regularly communicates Group activities to assist in more informed investment decisions by providers of capital.

| Probability | | Impact | | Change from last year | |
|---|---|---|---|---|---|
| 1 | Very unlikely | 1 | Insignificant | ↑ | Up from last year |
| 2 | Unlikely | 2 | Minor | ↔ | Same as last year |
| 3 | Possible | 3 | Moderate | ↓ | Down from last year |
| 4 | Likely | 4 | Major | | |
| 5 | Very likely | 5 | Severe | | |

## CONTRACT AND PROJECT PERFORMANCE

We operate large contracts, which often require us to price for the long term and for risk transfer. Our contracts can include fixed prices.

**Probability** 4 ↔ **Impact** 4 ↔

### Potential impact

We seek to win and operate long-term high-value contracts for the provision of complex and integrated services to our customers. This has a number of key risks.

There are usually only a relatively limited number of customers in each of our market sectors. In addition, our market sectors can be highly competitive. This means that our customers have significant market power and can require bidders to accept a substantial transfer of risk from the customer to the supplier. For example, it is common in our markets that the contracts that we tender for may impose strict conditions and clauses, including unlimited liabilities, termination without cause and strict performance conditions, which, if not complied with, may trigger compensation for the customer.

If we (or our supply chain) underestimate or under-price actual risk exposure or the cost of performance, or if, during the contract, cost inflation diverges from revenue inflation, or if unforeseen or additional costs are incurred, for example, due to the UK's exit from the EU or COVID-19 or rates of inflation, this could increase our cost to deliver the contract. For example, we operate fixed-price contracts. Actual costs may exceed projected costs, including assumptions on future rates of inflation on which the fixed prices are agreed. Since these contracts can extended over many years, it can be difficult to predict the ultimate outturn of costs.

Our contracts tend to involve significant supply chains. Failure by our supply chain partners to deliver on their contractual obligations may cause us increased costs or missed schedules, or put us in breach of our contractual obligations.

Long-term contracts often have changes, or updates, to their scope. If we do not properly manage contract changes, we may incur additional costs or fail to deliver contractual requirements, which may reduce overall profitability or lead to penalties or contract termination.

If any of these key risks materialise, they may increase our costs to deliver on our contractual obligations or may result in the imposition of penalties or the early termination of the contract with the imposition of damages, or reputational damage, which may cause strain on our customer relationship. This may undermine not only our current contract, but also our ability to win future contracts.

COVID-19 may increase the likelihood of each of these key risks arising as it makes our operations less efficient or effective. Any of these outcomes may adversely affect our future profitability, cash generation and growth.

### Mitigation

We have formal reviews and gating processes at key stages of each material bid to reduce the risk of underestimating risks and costs and to ensure that we target limited bid resources at opportunities where we consider that we have the best prospects of winning or retaining business. Group policies and procedures continue to set a commercial, financial and legal framework for all bids.

Contractual performance is continuously under review (at a business unit, sector and/or senior Group executive level as appropriate) with a view to highlighting at an early stage risks to delivery and profitability. Where we identify poor performance, the business will implement a remediation plan.

These reviews also consider the performance of our supply chain. In the current circumstances, the reviews consider the impact of COVID-19. We also regularly review project costs to complete to ensure accuracy of the financial profile of the contract.

## BUSINESS INTERRUPTION

Failure to withstand the impact of an event or a combination of events may significantly disrupt all or a substantial part of the Group's business.

**Probability** 3 ↔ **Impact** 4 ↔

### Potential impact

A range of events – for example, extreme weather, natural hazards (such as floods or earthquakes), political events, financial insolvency of a critical supplier, scarcity of materials, loss of data or corruption of our IT estate, fire or infectious disease – could cause business interruption. The consequences of these events could have an adverse impact on our people, our facilities, our supply chains, or our ability to meet our contractual obligations.

The COVID-19 pandemic is an example of such an event. The pandemic has had a significant impact on our business and the markets that we served over the last two financial years. For our customers, the pandemic may reduce their current or future budgets or cause them to deploy their budgets in different ways, changing our markets. For our employees, the pandemic has changed the ways that we work. These measures may create inefficiencies in some of our businesses, adding time and cost to our programmes or even leading to loss of contracts due to KPI default. The pandemic may also affect our suppliers and lead to failures in the supply chain, which may adversely affect our ability to deliver our programmes.

An outbreak of another contagious disease or a new variant of COVID-19 may have an adverse effect on the Company's business, financial condition and prospects.

### Mitigation

Throughout the pandemic, we have looked to prioritise the key programmes of our customers and to demonstrate the mission-critical nature of our services.

For employees, our priority has been their wellbeing and safety. We have adapted working practices and facilities, including introducing social distancing, PPE requirements, improved cleaning regimes and increased remote working, to seek to keep our people safe and well throughout this crisis.

We continue to manage the situation closely and follow government and health authority advice to help prevent the spread of the virus. For general business continuity, we have in place IT disaster recovery and business continuity processes. We also maintain relevant and appropriate insurance.

## OPERATIONAL RESILIENCE

We are undertaking multiple change programmes with the introduction of a new strategy, a new operating model to restructure the shape of the Group, and a new People strategy, as well as undertaking the alignment of both the business portfolio and our property portfolio. Additionally there are several new material opportunities that the Group may pursue – some in new geographies – that may further stretch management bandwidth.

**Probability** 3 ↔ **Impact** 4 ↔

### Potential impact

All these programmes are underway concurrently, in addition to the delivery of the Group's services to its customers. This may put pressure on management bandwidth to oversee all the change programmes, as well as the regular running of the business. This could lead to an elevated risk of mistakes or missed opportunities.

If we fail to deliver the change programmes, we will not be able to achieve our strategic goals. Failure to deliver the change programmes may also undermine the confidence of key stakeholders in our future growth and plans.

### Mitigation

Management is experienced in delivering programmes of this nature. There is regular monitoring of progress across all the programmes to ensure that they remain on track, along with regular dialogue with customers at a senior level to ensure that delivery of our contracts is in no way compromised. The Board receives a monthly report with a status update on the key change programmes and major new opportunities.

| Probability | | Impact | | Change from last year | |
|---|---|---|---|---|---|
| 1 | Very unlikely | 1 | Insignificant | ↑ | Up from last year |
| 2 | Unlikely | 2 | Minor | ↔ | Same as last year |
| 3 | Possible | 3 | Moderate | ↓ | Down from last year |
| 4 | Likely | 4 | Major | | |
| 5 | Very likely | 5 | Severe | | |

## HEALTH, SAFETY AND ENVIRONMENT

Our operations entail the potential risk of significant harm to people, property or the environment, wherever we operate across the world.

**Probability** 2 ↓ **Impact** 5 ↑

### Potential impact

Parts of our business (for example, our nuclear operations) involve working in potentially hazardous operations or environments, which we must manage and control to minimise the risk of injury or damage. Others, for example our aerial emergency services operations, involve an inherent degree of risk that is compounded by the nature of the services provided (firefighting, search and rescue, air ambulance and emergency services) or the environments in which they operate (low-altitude flying in adverse weather, terrain or operational conditions).

Serious accidents have a major impact on the lives of those directly involved and on their families, friends, colleagues and community, as can serious environmental incidents. These accidents may arise from: inadequate hazard control or training or management supervision; the failure to implement changes or learning from previous accidents; poor safety leadership and culture; equipment failure; or human or organisational factors.

If we cause or contribute to an incident because of failings on our part, or because as a matter of law we are strictly liable without fault, we may have to pay substantial damages, not all of which may be insured, as well as potentially being subject to criminal proceedings, which could result in substantial penalties. We could also suffer contract penalties due to an inability to deliver the contract or a loss of productivity.

Such incidents (which may have a high public profile given the nature of our operations) may also seriously damage our reputation (whether justifiably or not), which could lead to a significant loss of business or future business opportunities.

An incident may also disrupt our business if it prevents our employees from working.

### Mitigation

Our goal is for everyone to go ‘Home Safe Every Day’. Accordingly, health, safety and environmental performance receives close and continuous attention and oversight from the senior management team.

We have specific health, safety and environmental governance structures in place as well as education and training programmes for staff. Safety leadership teams in each sector and the Corporate Safety Leadership Team oversee the implementation of policy, strategy and initiatives across all our businesses.

The Board receives reviews of health and safety performance.

Nuclear risks: We hold indemnities given to us by the UK Nuclear Decommissioning Authority and the UK MOD, to protect against risk of liability for injury or damage caused by nuclear contamination or incidents, but a reputational risk because of any serious incident would remain.

In respect of the current COVID-19 pandemic, we have taken a number of measures across the Group. Our first priority is the safety of our employees. Our employees deliver essential services on which our customers and the wider community rely. The continuation of these services is key. We have reviewed our methods of working across the Group to institute the appropriate protective measures, including issuing new work guidelines, asking employees to work from home where they can, changing shift schedules, instituting infection control at work sites and ordering the wearing of protective equipment.

We believe we have appropriate insurance cover against civil liability exposures.

## REGULATORY AND COMPLIANCE

Our businesses are subject to the laws, regulations and restrictions of the many jurisdictions in which they operate.

**Probability** 2 ↔ **Impact** 4 ↔

### Potential impact

The laws and regulations that we are subject to include anti-bribery laws, import and export controls, tax, procurement rules, human rights laws and data protection regulations.

Failure to maintain compliance with applicable requirements could result in: fines and criminal prosecution; the removal of a licence to operate; reputational damage; cost of rectification; debarment from bidding; loss of access to markets; and the loss of substantial business streams (and possible damages claims) and opportunities for future business.

If an applicable law or regulation changes, it may cause us substantial expenditure in order to comply, which may not be recoverable (either fully or at all) under customer contracts.

Compliance with some regulatory requirements is a precondition for being able to carry on a business activity at all. For example, our Aviation business is subject to a high degree of regulation relating to aircraft airworthiness and certification, as well as regulations relating to ownership and control. Regulation (EC) No.1008/2008 (the Regulation) requires all air operators in the EU to be majority-owned and controlled by European Economic Area nationals.

Given the nature of our customers and the markets in which we operate, as well as the services that we provide, we believe that our reputation, not only in terms of delivery but also in terms of behaviour, is a fundamental business asset. Failings or misconduct (perceived or real) in dealing with a customer or in providing services to them or on their behalf could substantially damage our reputation with that customer or more generally.

### Mitigation

We maintain internal policies and procedures in order to ensure that the Group complies with all applicable laws and regulations. We also have suitably qualified and experienced employees and expert external advisors to advise and assist on regulatory compliance. We have management systems involving competent personnel with clear accountabilities for operational regulatory compliance.

In order to address the requirements of the Regulation, we have restructured the operations of the relevant operations so that a new sub-group, which is majority-owned and -controlled by an EU-based holding company, holds those parts of the business that fall under the Regulation. The Board believes that this structure satisfies the nationality requirements of the Regulation. However, as the ultimate decision to grant or revoke a licence rests with the EU aviation authorities, there can be no guarantee that this continues to be the case.

Senior management at Group and sector level are keenly aware of reputational risks, which can come from many sources. Our Code of Conduct, together with our Ethics policy, sets out the clear expectations that we have of our employees. We seek to reinforce these values with all employees through a number of different processes, for example our training. We encourage all our employees to use our whistleblowing reporting lines if they see evidence of behaviour which is not in keeping with our values. The Board monitors and reviews all reports and their investigations.

| Probability | | Impact | | Change from last year | |
|---|---|---|---|---|---|
| 1 | Very unlikely | 1 | Insignificant | ↑ | Up from last year |
| 2 | Unlikely | 2 | Minor | ↔ | Same as last year |
| 3 | Possible | 3 | Moderate | ↓ | Down from last year |
| 4 | Likely | 4 | Major | | |
| 5 | Very likely | 5 | Severe | | |

## PEOPLE

We operate in many specialised engineering and technical domains, which require appropriate skills and experience.

**Probability** 2 ↓ **Impact** 4 ↑

### Potential impact

Our business delivery and future growth depend on our ability to recruit, develop and retain experienced, highly skilled employees (including suitably qualified and experienced engineers, technicians, pilots and staff from other specialist skill groups).

Competition for the personnel we need is intense and is likely to remain so for the future. This may be exacerbated by nationality restrictions, which may prevent us from accessing talent from the EU or worldwide. This poses risks in both recruiting and retaining such staff.

If we have insufficient qualified and experienced employees, this could impair our service delivery to customers or our ability to pursue new business, with consequent risks to our financial results, growth, strategy and reputation and the risk of contract claims.

The cost of recruiting or retaining the suitably qualified and experienced employees we need might increase significantly depending on market conditions including inflation. This could affect our contract profitability.

### Mitigation

We undertake workforce and succession planning to identify skill gaps and to form plans to address them. We have programmes to develop our employees so that they have the right skills and experience.

We have developed a new People strategy, led by the Group's Chief Human Resources Officer. This strategy will establish a common approach across the Group. The new approach includes a new 'agile' way of working, a review of the rewards and remuneration structure and improved people management.

## PENSIONS

The Group has significant defined benefit pension schemes in the UK, which provide for a specified level of pension benefits to scheme members.

**Probability** 4 ↔ **Impact** 4 ↔

### Potential impact

Member and employer contributions paid into pension scheme funds and the investment returns made in those funds over time have to meet the cost of the defined benefit obligations.

Various assumptions underpin the level of our contributions. These assumptions are subject to change, such as life expectancy of members, gilt yields, investment returns, inflation and regulatory changes. Based on the assumptions used at any time, there is always a risk of a significant shortfall in the schemes' assets below the calculated cost of the pension obligations. For example, pension liabilities can increase due to rising life expectancy, higher-than-expected inflation rates in the future and lower interest rates.

If the pension trustees believe that the assets in the pension schemes are insufficient to meet pension liabilities or if our balance sheet strength does not meet the pension trustees' expectations, they may require us to make increased contributions and/or lump sum cash payments into the schemes or provide additional security from the Group. The toughening stance of the UK Pensions Regulator may influence our pension trustees' perspectives. Increased contributions or lump sum cash payments may reduce the cash available to meet our other obligations or business needs and may restrict our future growth.

Accounting standard rules governing the measurement of pension liabilities can lead to significant accounting volatility from year to year due to the need to take account of macroeconomic circumstances beyond the control of the Company. Companies, including Babcock, do not calculate actuarial valuations used for funding on the same basis as IFRS accounting standards. This means the future cash contributions are difficult to derive from the Group's IFRS balance sheet.

When accounting for our defined benefit schemes, we have to use corporate bond-related discount rates to value the pension liabilities. Variations in bond yields and inflationary expectations can materially affect the pensions charge in our income statement from year to year as well as the value of the net difference between the pension assets and liabilities shown on our balance sheet.

There is a risk that future accounting, regulatory and legislative changes may also adversely impact pension valuations, both accounting and funding, and, hence, costs and cash for the Group.

### Mitigation

Group senior management undertakes continuous strategic monitoring and evaluation of the assets and liabilities of the pension scheme. Management aims to increase its engagement with the scheme trustee chairs and with the UK Pensions Regulator.

The pension scheme mitigates the risk of liability increases by having investment strategies that hedge against interest rate and inflation risk and using longevity swaps to limit exposure to increasing life expectancy. Trustees use professional advisors to assist in the hedging of risks.

| Probability | | Impact | | Change from last year | |
|---|---|---|---|---|---|
| 1 | Very unlikely | 1 | Insignificant | ↑ | Up from last year |
| 2 | Unlikely | 2 | Minor | ↔ | Same as last year |
| 3 | Possible | 3 | Moderate | ↓ | Down from last year |
| 4 | Likely | 4 | Major | | |
| 5 | Very likely | 5 | Severe | | |

## IT AND SECURITY

A key factor for our customers is our ability to deliver secure IT and other information assurance systems to maintain the confidentiality of sensitive information.

**Probability** 4 ↑ **Impact** 4 ↔

### Potential impact

We hold data that is confidential and needs protection, in an environment of increasing cyber threat. Despite controls designed to protect such information, there can be no guarantee that security measures will be sufficient to prevent security breaches or cyber attacks being successful in their attempts to penetrate our network security and misappropriate confidential information or otherwise cause harm to the Group, for example through denial of service. The Group may be seen as a target for attack by 'state actors' from overseas countries because of the nature of the Group's activities for its government customers.

In addition, failure to invest in our IT infrastructure, for example in legacy systems, may create a weakness that may lead to a breach. The risk of loss of information or data by other means (such as physical loss) is also a risk that we cannot entirely eliminate.

A breach or compromise of IT system security or physical security at a physical site could lead to loss of reputation, loss of business advantage, disruptions in business operations and inability to meet contractual obligations. Significant data breaches or losses could lead to litigation and fines for breach of applicable regulations such as data protection laws. This could have an adverse effect on the Group's operations and its ability to win future contracts, which may affect our overall financial condition.

### Mitigation

We have made and will continue to make significant investment in enhancing IT security and security awareness generally. We seek to assure our data security through a multi-layered approach that provides a hardened environment, including robust physical security arrangements and data resilience strategies. We have formal security and information-assurance governance structures in place to oversee and manage cyber security and similar risks. We conduct comprehensive internal and external testing of potential vulnerabilities.

The Group maintains business continuity plans that cover a range of scenarios (including loss of access to IT). We regularly test the plans that relate to IT.

## ACQUISITIONS AND DISPOSALS

We have built our core strengths organically and through acquisition. Decisions to acquire companies, as well as the process of their acquisition and integration, are complex, time-consuming and expensive. If we believe that a business is not 'core', we may decide to sell that business.

**Probability** 1 ↓ **Impact** 4 ↔

### Potential impact

If we acquire companies, we may not realise the financial benefits of the acquisition as expected, due to poor integration or to acquisition business cases relying on market conditions or other business assumptions that subsequently do not materialise, challenging the logic of the acquisition decision.

Those companies that we consider to be non-core, and therefore disposal candidates, may become distracted or demotivated or lose key employees, which may lead to poor performance whilst also undermining their value to their customers and a potential buyer.

### Mitigation

Our focus is currently on operational execution, rather than acquisitions, with the possible exception of 'bolt-on' acquisitions.

We will work to enhance our acquisition and integration capability so that we are ready at the appropriate time in the future.

We will clearly communicate our disposal strategy and put in place the appropriate transaction resource to prioritise the disposals.

# Going concern and viability statement

## Overview

The Directors have undertaken reviews of the business financial forecasts, in order to assess whether the Group has adequate resources to continue in operational existence for the foreseeable future and as such can continue to adopt the going concern basis of accounting.

The Directors have also looked further out to consider the viability of the business to test whether they have a reasonable expectation that the Group will continue in operation and meet its liabilities as they fall due.

For assessing going concern, the Board considered the 12 month period from the date of signing the Group's financial statements for the year ended 31 March 2022. For viability, the Board looked at a five-year view as this is the period over which the Group prepares its strategic plan forecasts.

That five-year view is an update from the previous three-year plan, now that we have completed the first year of turnaround and made initial steps to reshape our portfolio of businesses.

The use of a five-year period provides a planning tool against which long-term decisions can be made concerning strategic priorities, addressing the Group's stated net zero target and climate-related risks and opportunities, funding requirements (including commitments to Group pension schemes), returns made to shareholders, capital expenditure and resource planning.

The annually prepared budgets and forecasts are compiled using a bottom-up process, aggregating those from the individual business units into sector level budgets and forecasts. Those sector submissions and the consolidated Group budget and forecasts are then reviewed by the Board and used to monitor business performance.

The Board considered the budgets alongside the Group's available finances, strategy, business model, market outlook and principal risks. The process for identifying and managing the principal risks of the Group is set out in our Annual Report. The Board also considered the mitigation measures being put in place and potential for further mitigation.

The Board considers the long-term prospects of the Group underpin its conclusions on viability. As outlined in our strategy, business model and markets summaries on pages 6 to 11 of this report, our prospects are supported by:

- a diverse portfolio of businesses based on well-established market positions, focussed on naval engineering, support and systems, and on critical services in our core defence and civil markets. In FY22 55% of Group sales were defence related and 45% civil;
- a geographically diverse business with a high proportion of sales to governments and other major prime defence contractors. In FY22, 63% of sales were to defence and civil customers in the UK, and 37% were international;
- long-term visibility of sales and future sale prospects through an order backlog of £9.9 billion as at 31 March 2022, including incumbent positions on major defence programmes; and
- market positions underpinned by a highly skilled workforce, intellectual property assets and proprietary know-how, which are safeguarded and developed for the future by customer- and Group-funded investment.

## Available financing

As at 31 March 2022, net debt excluding operating leases was £556.7 million and the Group therefore had liquidity headroom of £1.7 billion, including net cash and cash equivalents of £0.8 billion and undrawn facilities of £1.0 billion. These facilities are considered more than adequate to meet current and other liabilities as they fall due, and supports the Group's negative working capital position largely arising from securing customer advances ahead of contract work starting.

As of June 2022, the Group's committed facilities and bonds totalling £2.4 billion were as follows:

- €550 million bond, hedged at £482 million, maturing 6 October 2022
- £300 million three-year RCF maturing 20 May 2024
- Existing £775 million revolving credit facility (RCF) maturing 28 August 2025; of which £730 million now matures 28 August 2026.
- £300 million bond maturing 5 October 2026
- €550 million bond, hedged at £493 million, maturing 13 September 2027
- A committed overdraft facility of £50 million

The RCFs are the only facilities with covenants attached. The key covenant ratios are (i) net debt to EBITDA (gearing ratio) (ii) and EBITDA to net interest (interest cover).

These are measured twice per year – on 30 September and 31 March. In May 2021 our lending banks agreed to raise the covenant limit for the gearing ratio from 3.5x to 4.5x for the measurement periods ending 30 September 2021 and 31 March 2022 in order to provide sufficient downside protection for the Group as the turnaround in performance took place.

As we have now successfully delivered over £400 million from the divestment programme, amongst other turnaround dependencies in the prior 12 months, we have not considered it necessary to seek any extension to the period of time covered by those raised covenant limits. Hence for all periods in this going concern review, the gearing ratio covenant returns to 3.5x at September 2022 and remains so thereafter.

The RCF lenders are fully committed to advance funds under the RCF to the Group, provided that the Group has satisfied the usual ongoing undertakings, and the creditworthiness of the Group's relationship banks is closely monitored. Based on their credit ratings we have no credit concerns with our relationship banks. Given the importance of the RCFs to the Group's liquidity position, our assessments of going concern and viability have tested the Group's gearing ratio, interest cover and liquidity headroom throughout the period under review up to their current maturity dates.

## Base case scenario

The base case budget shows significant levels of headroom against both financial covenants and liquidity headroom based on the current committed facilities outlined above (without assuming any refinancing of the €550 million bond in October 2022). That base case largely assumes we maintain our incumbent programme positions if re-let during the five year period, with margin recovery if they are currently below the Group average. Many opportunities available to the Group, where we do not yet have high conviction of securing the work, have been excluded from the Base Case to seek to maintain a degree of caution.

That base case assumes no further recurrence of business disruption from the COVID-19 pandemic, which is consistent to our trading in FY22.

It also assumes that the impact of current inflationary pressures can be managed within contract estimates assumed in our planning. The base case assumes no further reshaping of the business portfolio, so it is not dependent upon any future cash proceeds from divestments. It also maintains pension deficit contributions in excess of income statement charges of around £130 million relating to FY23 and around £75 million relating to FY24.

## Reverse stress testing of the base case

To assess the level of headroom within the available facilities, a reverse stress test was performed to see what level of performance deterioration against the base case budgets and forecasts (in both EBITDA and net debt) was required to challenge covenant levels.

Of the remaining measurement points within the available facility period, the lowest required reduction in forecast EBITDA to hit the covenant level was 46% and the lowest net debt increase was 50%. Given the mitigating actions that are available and within management's control, such movements are not considered plausible.

## Severe but plausible downside scenarios

The Directors also considered a series of severe but plausible downside scenarios which are sensitivities run against the base case budget and forecasts for the duration of the assessment period. These sensitivities include – separately – a reduction in bid pipeline closure (business winning), an erosion of operating model savings, a deterioration in large programme performance across the Group (including further inflation cost increases, or related failures in supplier resilience, as per our principal risks), a deterioration in the Group's working capital position and a regulator-imposed cessation in flying two of the largest aircraft fleets in the Group.

As stated above, a key contributor to the strengthening of the balance sheet in FY22 was the divestment programme which generated in excess of the original target of £400 million of proceeds. No sensitivities were therefore considered necessary to be tested in relation to further potential divestments.

All of these separate scenarios showed compliance with the financial covenants throughout the period, and with sufficient headroom given the strengthened balance sheet, no extensions have been sought to the temporary increase in the covenant level gearing ratio previously granted by our lending; it has therefore now reverted to the usual 3.5x at September 2022 and for all future measurement periods.

As with any company or group, it would be possible, however unlikely, to model individual risks or combinations of risks that would threaten the financial viability of the Group. The Board has not sought to model events where it considers the likelihood of such events not to be plausible. In preparing a combined severe but plausible (SBP) downside case, the Board considered the feed of individual risks from the sectors covering the above sensitivities. Overall there were c.80 profit and cash flow risks identified.

A simple aggregation of all of these risks is not considered plausible as the Group operates businesses and contracts which run largely independently of each other, albeit with a relatively small number of customers within each geography.

The majority of these identified risks were seen as 'sector independent' (ie there is no direct read across from one sector to another). A small number are deemed 'non independent' eg inflation, FX etc. The Board decided to include in its combined SBP downside all the 'non independent' risks without reduction, but reduced the aggregation of the 'sector independent' risks by 25% to reflect the implausibility of all such risks fully crystallising within the same period.

If such a severe downturn were to occur in the Group's performance, the Board would take mitigation measures to protect the Group in the short term.

Such profit and cash mitigation measures that are deemed entirely within the control of the Group and identified as part of the sector budgeting exercise have been included in the SBP scenario (eg cancelling pay rises and bonus awards, curtailing uncommitted capital expenditure and operational spend including R&D and other investment).

Despite the severity of the above combined SBP scenario, the Group maintained a sufficient amount of headroom against the financial covenants within its borrowing facilities, and sufficient liquidity when compared against existing facilities.

## Going concern assessment and viability conclusion

Based on our review, the Directors have a reasonable expectation that the Group has adequate resources to continue as a going concern for at least 12 months from the date of these financial statements.

As such, these financial statements have been prepared on the going concern basis. The Directors do not believe there are any material uncertainties to disclose in relation to the Group's ability to continue as a going concern.

In concluding on the financial viability of the Group, having considered the scenarios outlined above, the Directors have a reasonable expectation that the Company and the Group will be able to continue in operation and meet all its liabilities as they fall due up to March 2027.