Babcock International Group PLC

Annual Report and Accounts 2009

trusted to deliver:

Sharing skills, knowledge and technologies

babcock

Contents

Directors' report

The Directors present the Annual Report and Accounts for the year ended 31 March 2009. This page and pages 1 to 60, inclusive, of this Annual Report and Accounts comprise a Report of the Directors that has been drawn up and presented in accordance with English company law and the liabilities of the Directors in connection with that report shall be subject to the limitations and restrictions provided by such law. In particular, Directors would be liable to the Company (but not to any third party) if the Directors' report contains errors as a result of recklessness or knowing misstatement or dishonest concealment of a material fact, but would not otherwise be liable.

Forward looking statements

Certain statements in this document are forward looking statements. By their nature, forward-looking statements involve a number of risks, uncertainties or assumptions that could cause actual results or events to differ materially from those expressed or implied by the forward-looking statements. These risks, uncertainties or assumptions could adversely affect the outcome and financial effects of the plans and events described herein. Forward-looking statements contained in this document regarding past trends or activities should not be taken as a representation that such trends or activities will continue in the future. You should not place undue reliance on forward-looking statements, which speak only as of the date of this announcement. Except as required by law, Babcock is under no obligation to update or keep current the forward-looking statements contained in this document or to correct any inaccuracies which may become apparent in such forward-looking statements.

Front cover:

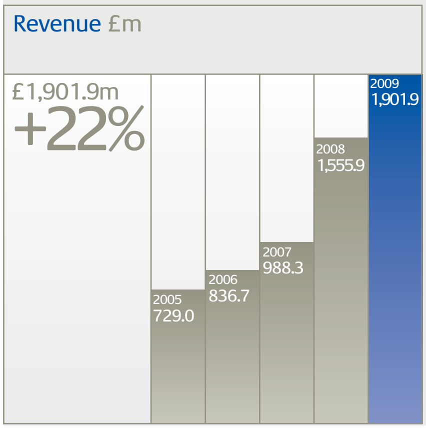
JET, the Joint European Torus, the world's largest nuclear fusion research facility. Babcock was involved in the initial construction phase and continue to provide support to JET.

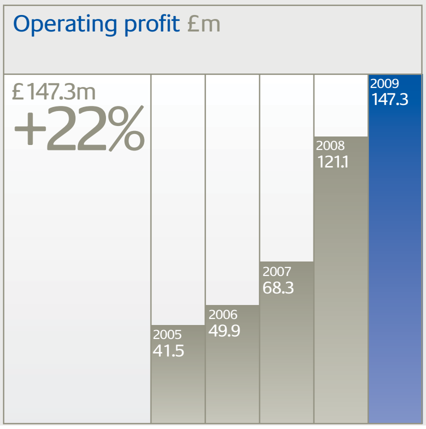
Highlights

- Sixth successive year of revenue and profit growth and continuing attractive growth prospects
- Strong growth trend continues – 22% increase in revenue, 22% increase in underlying operating profit
- Marine and Nuclear divisions build on strength of market positions and reputation for excellence
- Marine revenue +41%, underlying operating profit +30%
- Nuclear revenue +40%, underlying operating profit +128%
- Robust financial position, cash generative business model – cash conversion rate of 115%
- Implementation of liability cap to reduce long-term volatility and risk on pension liabilities nearing completion
- Order book increased by 90% to £5.7 billion, bid pipeline remains strong providing long-term revenue visibility
- Major contract wins including £1.5 billion RSME contract and HMS Vigilant contract worth in excess of £300 million

Underlying financial highlights

(before amortisation of acquired intangibles and exceptional items)





Company profile

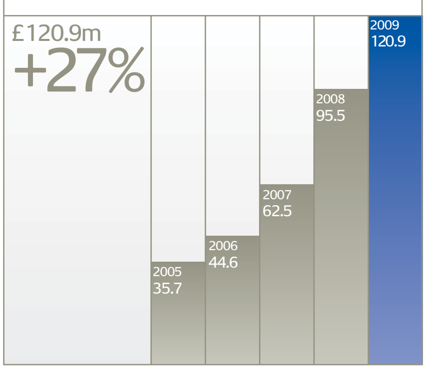
Our objective is to be the leading engineering support services company in the UK and in selected overseas markets.

Statutory results

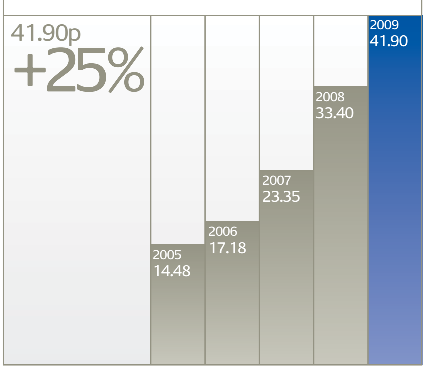
Revenue (2008: £1,555.9m)	£1,901.9m +22%
Operating profit (2008: £110.2m)	£133.1m +21%
Profit before tax (2008: £84.6m)	£106.7m +26%
Basic earnings per share (2008: 29.99p)	37.42p +25%

Throughout the business review, unless otherwise stated, revenue, operating profit, operating margin, profit before tax and earnings per share refer to results from continuing operations, before amortisation of acquired intangibles and exceptional items.

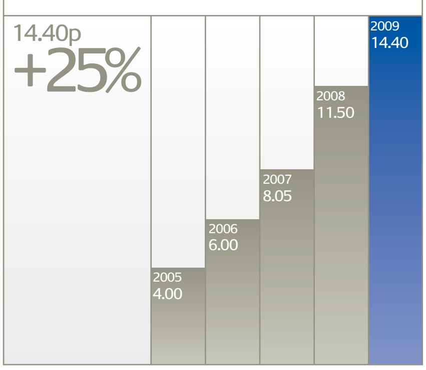
Profit before tax £m



Basic earnings per share p



Full year dividend proposal p



Group overview

Using the breadth and depth of our skills and expertise we work in long-term partnerships with our customers.

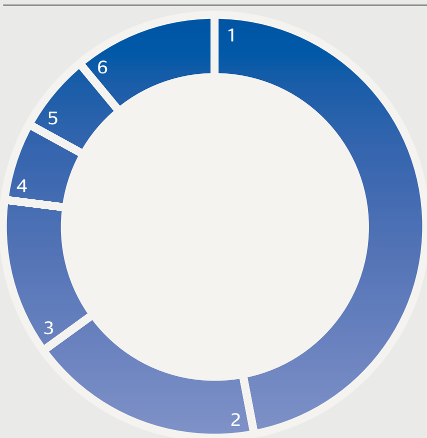









Contribution to Group revenue



1	Marine	£892.9	47%
2	Defence	£338.4	18%
3	Rail	£228.9	12%
4	Nuclear	£106.7	6%
5	Networks	£119.4	6%
6	Engineering and Plant	£215.6	11%

Read more pages 5 to 29

Our Executive team


Kevin Thomas
Group Business Development Director


Archie Bethel
Chief Executive, Babcock Marine


Mike Fellowes
Managing Director, Babcock Infrastructure Services


David Ruff
Managing Director, Babcock Defence Services


Andy Pearson
Chief Executive, Babcock Rail


Martin Austick
Chairman, BNS Nuclear Services


Bob Whiley
Managing Director, Babcock Networks


Roger O'Callaghan
Chief Executive, Babcock Africa


Tony Moore
Managing Director, BNS Nuclear Services

Marine £89.3m operating profit 10.0% operating return on revenue

Profile

We are the UK's leading naval support business and have a unique role supporting the Royal Navy and the Ministry of Defence. We are also expanding our international submarine support operations.

Key activities

- Submarines – base porting, refit, refuelling and decommissioning
- Surface ships – warship refit, member of Aircraft Carrier Alliance
- Naval bases – management of HMNB Devonport and HMNB Clyde
- Integrated Technology – design and technical solutions

Key customers

- MoD
- DE&S Equipment Support
- Canadian Government
- Navantia

Defence £28.9m operating profit 8.5% operating return on revenue

Profile

We provide facilities management, equipment support and training expertise. We are the largest provider of facilities management support to the Ministry of Defence.

Key activities

- Facilities management for MoD through two Regional Prime Contracts
- Technical support for the RAF through multi-activity and IOS contracts
- Training and training support to the Royal School of Military Engineers
- Baggage handling systems at London Heathrow

Key customers

- MoD Defence Estates
- Army
- RAF
- BAA
- BAE Systems

Rail £6.4m operating loss

Profile

We are a major player in the UK rail infrastructure market and the largest track renewal contractor for Network Rail.

Key activities

- High output track renewal
- Traditional track renewal
- Signalling and control system installation
- Provision of rail power solutions

Key customers

- Network Rail
- Transport Scotland
- Regional Passenger Transport Executives

Nuclear £13.0m operating profit 12.2% operating return on revenue

Profile

We have one of the largest specialist nuclear resources in the UK. We provide outage and maintenance support for current power generation and operate in the decommissioning and waste management markets.

Key activities

- Outage support for operational reactors
- Decommissioning activities
- Waste management solutions
- Mechanical system design and engineering
- Safety and risk analysis

Key customers

- Sellafield Ltd
- British Energy (part of EDF Energy)
- Magnox Electric
- Dounreay Site Restoration Ltd

Networks £7.0m operating profit 5.9% operating return on revenue

Profile

We operate in the high voltage power transmission, mobile and fixed telecommunications and digital broadcast infrastructure markets in the UK and Ireland. We are one of three key suppliers to the National Grid.

Key activities

- High voltage power transmission maintenance and upgrade
- Transmission design activities
- Digital switchover antennae design and replacement
- Mobile telecommunications network upgrade
- Fixed line communication networks

Key customers

- National Grid
- EDF Energy Networks
- Scottish and Southern Energy
- Vodafone
- Orange
- Ericsson

Engineering and Plant £19.7m operating profit 9.1% operating return on revenue

Profile

Operating mainly in South Africa the division supports Eskom, the national power supplier, and operates the Volvo franchise for construction equipment. In the US we provide specialist oil pipeline support.

Key activities

- Maintenance and engineering support on power station boilers
- Construction, erection and maintenance of high voltage power lines
- Sole distributor for Volvo equipment to mining and infrastructure construction companies
- Regional dealership for Nissan trucks
- After sales parts and servicing support for Volvo

Key customers

- Eskom
- Volvo customers

Chairman's statement

In my first statement as Chairman, I am delighted to report that in 2008/09 Babcock International has continued to build on the excellent progress of recent years to deliver another set of record results.

Creating value for shareholders

I am fortunate to have rejoined Babcock at such an exciting time in its development. Since I first joined the Board in 1996, I have witnessed an incredible transformation in the fortunes of the Group.

In 2001, my predecessor Gordon Campbell put into action a clear strategy to create a leading engineering support services company, a strategy that has been executed to deliver continuous growth over the intervening period. Through a series of carefully selected strategic acquisitions, major contract wins and strong organic growth, not only has Babcock been able to transform its financial performance but it has significantly strengthened its business base. I would like to thank Gordon personally, and on behalf of the Board, for all that he did as Chairman to create the business we have today.

We have successfully built on the skills and expertise within our business to become a leading player in our key market sectors, all of which the Board believes have good long-term growth prospects. We have established a reputation for working in long-term partnerships with our customers to deliver the efficiencies and cost effective solutions they are seeking.

Gordon and the Executive team created a strong and dynamic company and I strongly believe we can continue to build on this; even in these more challenging economic times.

We are focused on delivering long-term value for our shareholders by establishing leading positions in each of our chosen markets.

The Board

In April I was pleased to welcome Sir David Omand to the Board as an independent Non-Executive Director. David brings to the Board a keen intellect and a wealth of experience in strategic thinking in domestic and international affairs at the highest levels.

At the time of the forthcoming AGM in July, Dipesh Shah will be retiring from the Board, having been a Non-Executive Director since 1999. On 1 April 2009, he stood down from the Remuneration Committee, of which he had been Chairman, the Audit and Risk Committee and Nominations Committee. I would like to thank Dipesh for his dedication and considerable contribution to the Company's success over the past 10 years.

Justin Crookenden has taken over from Dipesh as Chairman of the Remuneration Committee.

On behalf of the Board I would also like to thank all our employees for their efforts and commitment. Without their hard work this year we would not have been able to deliver yet another set of excellent financial results. We acknowledge the vital role our employees play in the continuing success of our business and we will do everything we possibly can to ensure Babcock is a rewarding place to work.

Dividend

The Board of Babcock has always been committed to creating sustainable value for our shareholders and I believe we have a business that will be able to continue this excellent track record. This year we are reporting a 25% increase in continuing earnings per share to 41.90 pence per share (2008: 33.40 pence per share). As a result of this continuing growth in earnings and reflecting our confidence in the Company's future prospects, the Board is recommending a final dividend of 10.40 pence per share (2008: 8.20 pence per share), an increase of 25% giving a total dividend for the year of 14.40 pence per share (2008: 11.50 pence per share).

Subject to shareholder approval at the AGM, the dividend will be paid on 7 August 2009, to shareholders on the register at close of business on 10 July 2009.

The Board believes Babcock has excellent prospects. The £5.7 billion order book gives us excellent visibility and we look forward to another year of progress.

Mike Turner

Mike Turner CBE
Chairman

Operational review

We are confident that all our markets offer significant potential for further growth.

Peter Rogers
Chief Executive

2008/09 has been another strong year for Babcock. We have achieved 22% growth in revenue to £1,901.9 million (2008: £1,555.9 million), operating profit has also increased by 22% to £147.3 million (2008: £121.1 million) and profit before tax has grown by 27% to £120.9 million (2008: £95.5 million). As a result, continuing earnings per share have increased by 25% to 41.90 pence per share (2008: 33.40 pence per share), a clear demonstration of our continuing success in delivering long-term, sustainable growth for our shareholders.

We have a clear strategy of growth in our chosen markets, both organically and through acquisition. During this year we successfully completed the integration of the acquisitions we made during 2007 and early 2008 and our results clearly demonstrate the value we have created from them. The combined businesses give us considerable scale and put us among the leading players in some of our key markets.

Babcock Marine has consolidated its position as the leading support provider to the Royal Navy. We are now working in long-term partnership with the Ministry of Defence (MoD) on a number of major maritime before projects to deliver through-life efficiencies and maximum benefits for both parties.

Building on the strength of our UK submarine support business, we are investigating a number of opportunities where the scale of our knowledge and expertise can be extended into overseas markets, with Canada being our first major step.

BNS Nuclear Services has a significant market presence in all areas of the civil nuclear market and is well placed to benefit further from growth in the decommissioning market and the new build programme.

Elsewhere in our business, our track record of working in partnership with our customers to provide cost effective solutions has helped us achieve growth through extending the length or scope of existing contracts. This has also helped us win new contracts and further strengthen our market positions.

The award of the 30 year, £1.5 billion Royal School of Military Engineering (RSME) contract has established Babcock as a leader in the provision of Army training support. We now have a strong position from which to expand further into the defence training market.

Across many of the markets in which we operate there is a scarcity of appropriately trained or suitably qualified people. Our highly skilled and experienced workforce is vital to our continuing success. We continue to invest heavily in attracting, retaining and developing the talent within our business.

Major emphasis has also been placed on further improving our health and safety record. Whilst our incident rate continues to reduce I am disappointed that we have not been able to make better progress in achieving our goal of an accident-free Babcock. I am committed to ensuring everyone in the Company works in an environment where safety is the first priority.

As well as our leading market positions, the Group's order book, and record bid pipeline give us excellent forward visibility and confidence in the future. Compared to the same time last year, the order book has increased by 90% to £5.7 billion (2008: £3.0 billion).

Objective and strategy

Our objective

Our objective is to be the leading engineering support services company in the UK and in selected overseas markets thus creating superior levels of returns for our shareholders.

Our strategy

In order to achieve this we will develop a balanced portfolio of businesses by focusing on the following strategy:

Leading market positions

Aim	Progress	Key examples
We expect our businesses to be one of the top three in their market sector. If they are not they will have clear plans to achieve this goal.	During the year we have consolidated our leading position in all our divisions through acquisitions and major contract wins.	→ Sole provider of support to the Royal Navy's submarine fleet → Largest Prime contractor for Defence Estates → The sole distributor of Volvo equipment in South Africa

Preferred customers

Aim	Progress	Key examples
We seek to work with customers who own large strategically important assets. These customers tend to be government departments, public bodies or private companies operating in highly regulated markets.	The majority of our revenue is derived from our preferred customer base. This is consistent with previous years.	→ The MoD is our largest customer in both the Marine and Defence divisions → Network Rail, our Rail division's largest customer, owns and operates Britain's rail infrastructure → We provide support to British Energy's fleet of AGR nuclear power stations → Eskom, the South African power utility

Customer focused, long-term relationships

Aim	Progress	Key examples
We seek to work collaboratively with our customers to support the long-term nature of our contracts.	We have been awarded a number of contracts where the emphasis is on long-term partnerships rather than on short-term tasks.	→ Ten year Submarine Engineering Support Contract for Royal Navy's submarine fleet → WSMI contracts to provide naval base and water front support at Devonport and Faslane to 2013 → 30 year RSME training and training support contract → Five year in-service submarine support contract for Canadian government – with option to extend to ten years

Integrated engineering and technical expertise

Aim	Progress	Key examples
We seek to use our skills, integrating engineering and technical expertise to deliver projects and long-term asset management.	The majority of our employees are technically qualified and their skills are used to support our customers' strategically important assets.	→ The refit of HMS Victorious required 2.2 million skilled engineering man hours → Babcock engineers are providing around 50% of the design input in the CVF programme → CARE, developed by Networks, is a system which forecasts degradation of steel structures in the electricity transmission and other markets

Balance risk and reward

Aim	Progress	Key examples
We seek to enter into contracts that fairly balance the risk and reward with our customers, so we can each share the financial effects of success or failure.	The Terms of Business Agreement (ToBA) being negotiated with the MoD will move all naval support contracts away from a cost plus to a pain/gain share basis.	→ Successful delivery of the following contracts will ensure maximum benefits are shared by Babcock and the MoD → HMS Vigilant LOP(R) → WSMI extension at Devonport → East and South West Regional Primes

Maintain an excellent safety record

Aim	Progress	Key examples
We expect all our divisions to deliver a sector-leading safety performance. We believe all our employees and others working on or visiting our operations should be able to return home safe and well at the end of the working day.	During 2008/09 we reduced our RIDDOR frequency rate by 13%. Over two years this has reduced by 49%.	→ British Safety Council Sword of Honour – Marine → RoSPA Gold Award – Nuclear, Airports, Networks → British Safety Council 5 star award – Marine → RoSPA Sector Award (facilities management) – Infrastructure Services → British Safety Council International Award – Infrastructure Services, Networks

Measuring our performance

Since 2001 we have consistently achieved growth in revenue and profits and our objective is to create superior levels of returns for our shareholders.

We have identified a number of Group and divisional level financial and non-financial Key Performance Indicators (KPIs) that reflect the internal benchmarks we use to measure the success of our businesses and will enable investors and other stakeholders to measure our progress.

By focusing on these areas we will ensure continuous sustainable improvement across the company.

Group KPIs are clearly set out and defined and are discussed in detail in the Financial review on pages 30 to 33.

Divisional KPIs

The key KPIs for our divisions featured over the following pages are:

Operating return on revenue (ORR)

Operating return on revenue is defined as operating profit before amortisation of acquired intangibles and exceptional items expressed as a percentage of revenue.

Revenue growth

Revenue growth is defined as the percentage increase in the Company's continuing revenue when compared to that of the previous year.

The reconciliation between divisional statutory operating profit and operating profit before amortisation of acquired intangibles and exceptional items is reflected in note 3 to the financial statements.

Segmental analysis

	Revenue			Operating profit*			Operating return on revenue	
Division	2009 £m	2008 £m	Growth	2009 £m	2008 £m	Growth	2009	2008
Marine	892.9	633.2	41%	89.3	68.7	30%	10.0%	10.8%
Defence	338.4	302.1	12%	28.9	27.5	5%	8.5%	9.1%
Rail	228.9	228.1	–	(6.4)	0.5	–	-2.8%	0.2%
Nuclear	106.7	76.3	40%	13.0	5.7	128%	12.2%	7.5%
Networks	119.4	98.5	21%	7.0	7.2	-3%	5.9%	7.3%
Engineering and Plant	215.6	217.7	-1%	19.7	17.1	15%	9.1%	7.9%
				(4.2)	(5.6)			
Total	1,901.9	1,555.9	22%	147.3	121.1	22%	7.7%	7.8%

*Represents underlying operating profit which is before amortisation of acquired intangibles and exceptional items.

Reconciliation to statutory operating profit

	Revenue		Operating profit		Operating return on revenue		Growth	
	2009 £m	2008 £m	2009 £m	2008 £m	2009	2008	Revenue 2009	Operating profit 2009
Total statutory	1,901.9	1,555.9	133.1	110.2	7.0%	7.1%	22%	21%
Amortisation of acquired intangibles			14.2	10.9				
Total underlying	1,901.9	1,555.9	147.3	121.1	7.7%	7.8%	22%	22%

Marine

Market overview

The UK Naval support sector is the division's most important market. As the Ministry of Defence (MoD), our key customer, continues to seek efficiencies and cost benefits, our focus has been on building long-term partnerships and arrangements with them to ensure the programmes on which we are working deliver maximum benefits.

Throughout the year we have consistently supported the MoD in developing their Maritime Change Programme, as well as with other cost saving initiatives in the submarine and surface ship support areas.

Internationally, as other governments seek similar cost efficiencies for their submarine support activities, we are looking at a number of opportunities where our expertise can be used.

Operational review

The Marine division is our largest business representing 47% of Group revenue. The division has had another excellent year, exceeding all financial and operational targets. This is partly due to the benefit of a full year's contribution from Devonport but is mainly the result of strong organic growth and the considerable scale the division has within the naval support market.

We have made significant synergy cost savings across the division, which has contributed to the growth in profit. By the end of the 2009/10 financial year we expect efficiency and synergy savings to be running at the rate of £14 million per year. At the same time we have maintained our high level of service, confirmed in performance feedback, and have developed the long-term partnering arrangements with our customer.

Negotiations on the Terms of Business Agreement (ToBA) have continued throughout the year without any delay to the award of new contracts. The key principles have been agreed and recent contracts have been awarded under new arrangements, similar to those to be contained in the ToBA. The MoD continues to negotiate other Maritime Change Initiatives with other parties and we do not expect our ToBA to be concluded ahead of these.

Submarines

Babcock Marine is the leading submarine support partner to the Royal Navy. Routine maintenance and support of the submarine fleet has continued at our Devonport facilities and at HM Naval Base Clyde (Faslane). We have also benefited from the continuous programme of scheduled refuelling and refit work.

The long overhaul period and refuelling (LOP(R)) of HMS Victorious was successfully completed as planned in October 2008 and HMS Vigilant started her LOP(R) in November. This programme is expected to conclude in 2012 and the contract, valued in excess of £300 million, was the first to be signed under new contracting arrangements with the MoD.

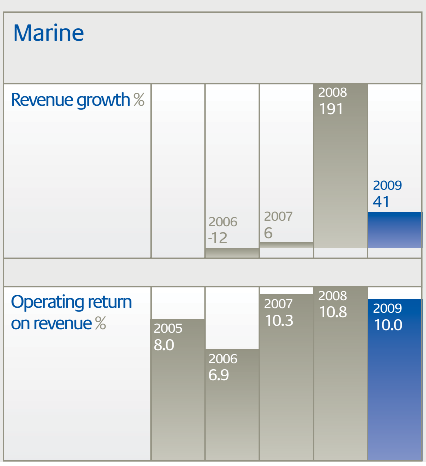
Safety hat-trick for Rosyth
Reflecting our continuing focus on creating a safe working environment, Babcock Marine at Rosyth has won the British Safety Council Sword of Honour for the third year in a row. This is their fifth sword in six years and demonstrates the success of the health and safety management systems that have been established.

The Council only presents 40 swords each year and this, as well as achieving 5 star status earlier in the year is testament to the hard work and commitment shown by all employees.

Training for the future
At HMNB Clyde a modern apprentice programme ensures the future availability of skilled engineers. This year there were over 300 applications for 15 vacancies. After a week-long induction programme at the base, the successful candidates will be spending their first year on block release at Clydebank College. There they will learn electrical and mechanical engineering skills to complete the first year of a National Certificate in Engineering.

Apprentice ship builders at Appledore
To make sure ship building skills don't disappear from Appledore, a new group of apprentices have been taken on. After three months training at North Devon College, 14 apprentices are starting to put their skills to the test working on the bow sections of the two new Queen Elizabeth class Aircraft Carriers. The first ship building apprentices in Appledore for a number of years, the apprentices will be given an experienced mentor with many years' experience; ensuring that skills and knowledge can once again pass from generation to generation.

Trusted to ensure strategic assets perform throughout their life cycle...



The last refuelling of the Trafalgar class submarines will be complete in 2010 when HMS Triumph returns to service. A business improvement project is well underway to reshape our submarine support activity providing a sharper focus on defuelling and decommissioning. At Devonport, the major nuclear licensed site modernisation programme to handle the defuelling of redundant submarines, has continued to progress very well.

Surface ships

In our core warship support activities we have supported the Royal Navy with its continuous programme of refit and upgrade projects at both Devonport and Rosyth. HMS Ocean, the largest warship in the Royal Navy has undergone a major refit and a number of other major upgrade packages have been completed on frigates and mine warfare vessels. During the year we received a commendation from the MoD for the repairs to HMS Grimsby, which included the largest ever structural repair to a vessel of its type.

...by working in long-term partnerships with our customers.

Working in partnership at Faslane

Our contract to manage the Clyde Royal Naval Base (Faslane) is one of the longest and most successful within Babcock. We first took over management of the base in 2002 and are currently half way through a six year extension period. The success of the contract has been a result of the partnership agreements between Babcock and the naval base command. The two organisations now work as one integrated team and in 2009 they introduced their first joint business plan which marks an important milestone in the ongoing success of the partnering arrangement.

Since 2002, targets for reducing costs have been beaten. Chris Hockley, the Clyde Naval Base Commodore said "It made sense to bring our two organisations together as one integrated team. Together we can be more effective and more efficient." The Scottish Government is interested in this business model which could be used to remove cost whilst improving output performance in government agencies where funding is strained. These working practices are a benchmark for partnership within Babcock. Faslane is Scotland's biggest single site employer with a payroll of over 6,000 employees and through Babcock, the site is also a major provider of apprenticeships in the area.

During the coming year, we expect to enter into a MoD/industry alliance for through-life support of all complex Royal Navy warships aimed at reducing costs and delivering greater efficiency and availability. This will increase our role in the technical and planning aspects of warship support and provide a significant opportunity for future development.

Babcock is a key member of the Aircraft Carrier Alliance that will design, build, assemble and support the two new Queen Elizabeth class aircraft carriers, the largest vessels ever operated by the Royal Navy. In March 2009, revisions to the build strategy for the two vessels were announced and this will result in additional activity for the division. Whilst the impact of this is still to be finalised, we anticipate it will be worth an additional 25% to the original £675 million contract awarded in July 2008. The original contract included the build of the bow section, a significant element of the detailed design activity and final assembly of the vessels at our dockyard at Rosyth. In addition Babcock will now be responsible for construction of the sponsons and other elements of the vessels. Construction of the bow section has already started at our Appledore facilities and the upgrade and modification to the facilities at Rosyth is progressing well. To support our commitment to CVF, we have embarked on a substantial apprentice and graduate recruitment programme which will last over the next four years.

In addition we have successfully completed the refurbishment of the third and final vessel for the Estonian Navy. This contract to regenerate ex-Royal Navy vessels for sale has been recognised as the most successful project of its type ever undertaken by the MoD.

Integrated Technology

During the year we formed a new business unit within the division to bring together the engineering, design, systems integration and platform management capabilities across the Group. Integrated Technology is one of the leading organisations of its type in the UK defence sector with over 1,300 staff and a strong range of products and enabling technologies. Our focus on technology will be a key driver in delivering true through-life capability management for our customers in the UK and will enable us to develop our international naval support activities.

In April 2009 we were awarded the £155 million, ten year Submarine Engineering Support Contract (SESC) to provide in-service support to the submarine fleet. We will take the industry lead in the Submarine Support Management Group (SSMG) providing a wide range of design and technical support services, working in partnership with the MoD to transform the provision of through-life submarine support.

Through Integrated Technology we have been able to increase our involvement in the CVF project, which is increasingly reliant on the scale of our design capability. In addition we have growing roles in some of the UK's other major defence projects including both the Astute and future deterrent submarine programmes.

A strong team has been established in Canada to deliver the £125 million, five year support contract for Canada's Victoria class submarines. This provides us with a solid base from which to grow our own local engineering support operation.

We continue to expand our international submarine support activities and good progress has been made in the design and manufacture of the weapons handling and launch system for Spain's new S-80 submarine class. Contracts for the provision of initial designs for weapons handling systems for new submarine programmes in South Korea and Australia have also been secured.

Naval bases

At the Devonport and Clyde Naval Bases we continue to work closely with the Royal Navy and MoD to improve the efficiency of their operations. In April 2009 we were awarded a £560 million Warship Support Modernisation Initiative (WSMI) contract for Devonport, extending the provision of naval base support and management through to 2013.

Equipment support

Our Equipment Support business unit has had a very successful year and continues to deliver improved equipment upgrade and availability services to our land, sea and air customers in the MoD as well as to the wider defence industry.

We are now firmly established as the largest provider of piece-part spares to the MoD with an inventory of 70,000 unique spares. In addition, we are continuously growing our portfolio of maritime equipment support contracts, recently adding a ten year contract for the availability management of electric motors and generators for the Royal Navy.

To date, our Land Systems team has delivered in excess of 200 Jackal off-road armoured patrol vehicles and 32 specialist utility MEP vehicles in support of Urgent Operational Requirements (UOR) for the Army. In addition we supported operations through specialist driver training services and integrated logistic support for spares and repairs to the vehicles. We have started work on the next UOR to deliver around 200 more Jackal type vehicles and expect this contract to be worth in the order of £55 million.

Outlook

We are confident the division will continue to benefit from the strength of the relationship with our major customer and our ability to reduce its operational costs whilst improving the availability of its assets will be of continuing benefit to the division. We have excellent long-term visibility through both existing orders and the scheduled programme of refits and maintenance. In addition there are a number of opportunities in the UK and overseas where we believe we can build on the strength of our reputation and expertise to deliver further growth.

E-learning at Valley

Recognising the need for structured training and development of all employees, Babcock has launched a modern learning suite for employees at RAF Valley in a joint initiative with the union Unite. The suite gives access to over 800 on-line courses including: computer skills, languages and health and safety. The courses allow people to train and develop at their own speed, and from their own structured learning. Improving the skills, knowledge and understanding of our employees is already starting to benefit on-site customers: the RAF; BAE Systems and Rolls-Royce.

2008 Debut Sustainability Conference

Sustainable procurement is a major concern for our key customer, the Ministry of Defence. Working together, Defence Estates and Debut (part of Babcock Infrastructure Services) held a two day conference focusing on and highlighting the key issues of sustainability. On Day 1, various representatives from the MoD's various estates departments and Debut project and site delivery managers met to discuss best practice in delivering sustainable solutions.

On Day 2, Debut and its supply chain partners discussed the practical solutions for those tasked with developing and delivering projects. The programme focused on communicating and training programmes to raise awareness of sustainability and energy saving issues. In addition to key note speeches and presentations, a total of 35 workshops were also held and a number of exhibitions provided examples of new technologies, materials and methods available for use within the MoD's Defence estates and Debut.

Defence

Market overview

Across the division, the Ministry of Defence continues to be our major customer, and their focus throughout the year has been on delivering cost efficiencies. The continuing pressure on MoD expenditure has resulted in greater collaborative working with industry at all levels and across all our contracts we are seeking to add value and increase effectiveness.

Operational review

Revenue growth has been driven mainly by scope expansions within the Regional Prime contracts but has also benefited in the final quarter of the financial year from the start of the 30 year Royal School of Military Engineering (RSME) contract. As a result, the division's overall operating margin decreased slightly as meaningful profit will only be recognised on this contract during 2009/10.

Training

The £1.5 billion, RSME contract has started extremely well and has exceeded our customer's expectations from the outset. The Private Public Partnership contract, the first of its type, is to provide training, training support and facilities management. It establishes Babcock as a major provider in the technical training market sector and the leading provider of Army training support services. This places us in a strong position from which to benefit from a number of defence training opportunities coming up over the next few years.

Infrastructure and technical support

The two Regional Prime contracts continue to perform well with a number of additional projects, services and locations being added. These contracts demonstrate that the MoD can improve cost effectiveness and service delivery through integrated facilities management contracts operated by private companies. The second phase of the SLAM contract to provide a further 5,000 military accommodation units also started successfully during the year.

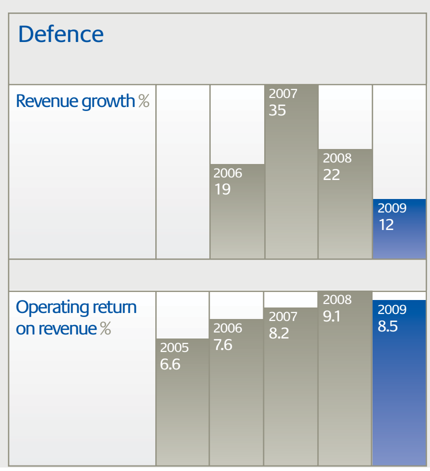
The multi-activity and integrated support contracts for the Hawk T Mk 1 fleet, Ardour engines and Hercules aircraft have all continued to perform well and have provided high levels of service, availability and operational capability.

Airports

Airport operations have had a very strong year continuing to add to the level of support they provide for BAA's integrated baggage handling operations at Heathrow. These now include Terminal 5, where a first class service is being provided. Additional projects at Gatwick and Stansted have also been completed.

Outlook

We believe the markets in which the division operates remain robust. We are confident that the Government and other major customers will continue to seek the most cost effective solutions for their operational needs and that our successful partnering model places us in a strong position from which to benefit.



Rail

Market overview

Over the next five years, in Control Period 4 (from 1 April 2009 to 31 March 2014) Network Rail has £34 billion to spend on the UK's railways. Of this £18 billion will be spent on track renewal and project work which represents a positive outlook for the division.

Network Rail currently faces a number of challenges, set by the Office of the Rail Regulator, to seek alternative delivery mechanisms for Control Period 4. These include a proposed reduction in volume on current track renewals framework contracts but with a potential for tendering additional works through a track enhancement frameworks. Discussions on the detail and implications of these proposals are ongoing with Network Rail.

Operational review

Throughout the year the division has focused on recovery and delivering long-term financial improvements. We continue to manage out a number of underperforming multi-disciplinary projects that have had an adverse impact on our performance.

We have built on our already strong reputation for delivering quality engineering, championing innovation by bringing new technologies to the rail industry and partnering leading companies. Our effort is now on using our core skills and expertise to secure and deliver track renewal, power and signalling led contracts efficiently to ensure the division delivers acceptable levels of return.

Our track, signalling and telecoms framework contracts continue to provide a steady flow of profitable work. In particular, track successfully delivered several works over the Christmas and New Year period including the second successful installation of a modular switches and crossings crossover in North West England and renewal of Dubbs Junction in Ayrshire, Scotland.

Network Rail is seeking to reduce volumes placed through existing track renewal frameworks and increase work placed through track enhancement frameworks. We are one of seven qualified contractors for these enhancement works, valued in excess of £100 million over five years.

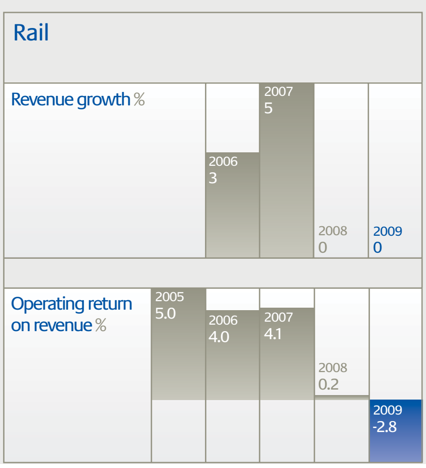
Building on our successful five year partnership with Swietelsky for high output track renewals, the Swietelsky Babcock Rail (SB Rail) joint venture has submitted a tender for the high output track renewals framework contract currently valued in excess of £500 million over five years. We expect the outcome of this tender process to be known in June/July with work expected to start in September 2009. SB Rail has also just been awarded an £11 million, one year extension to the nationwide on-track plant contract.

Additional works are now coming through the Signalling Type C contracts, particularly in Scotland, and should result in increased revenue. The telecommunication business unit has recently been awarded contracts including Driver Only Operated Closed Circuit Television renewal works and Radio Electronic Token Block base station works across Scotland.

We have successfully commissioned the £49 million Trent Valley Four Track project in which the new high speed railway is enabling enhanced journey times and increased capacity.

Outlook

Despite a 30% reduction in Network Rail's track renewal budget we believe there are a number of opportunities for the division to benefit from growth in track enhancement projects and high output track renewal as well as other framework opportunities. We will continue to take the necessary action to create a more efficient business and complete the withdrawal from unprofitable multi-disciplinary project work to build on our reputation for delivering quality engineering.



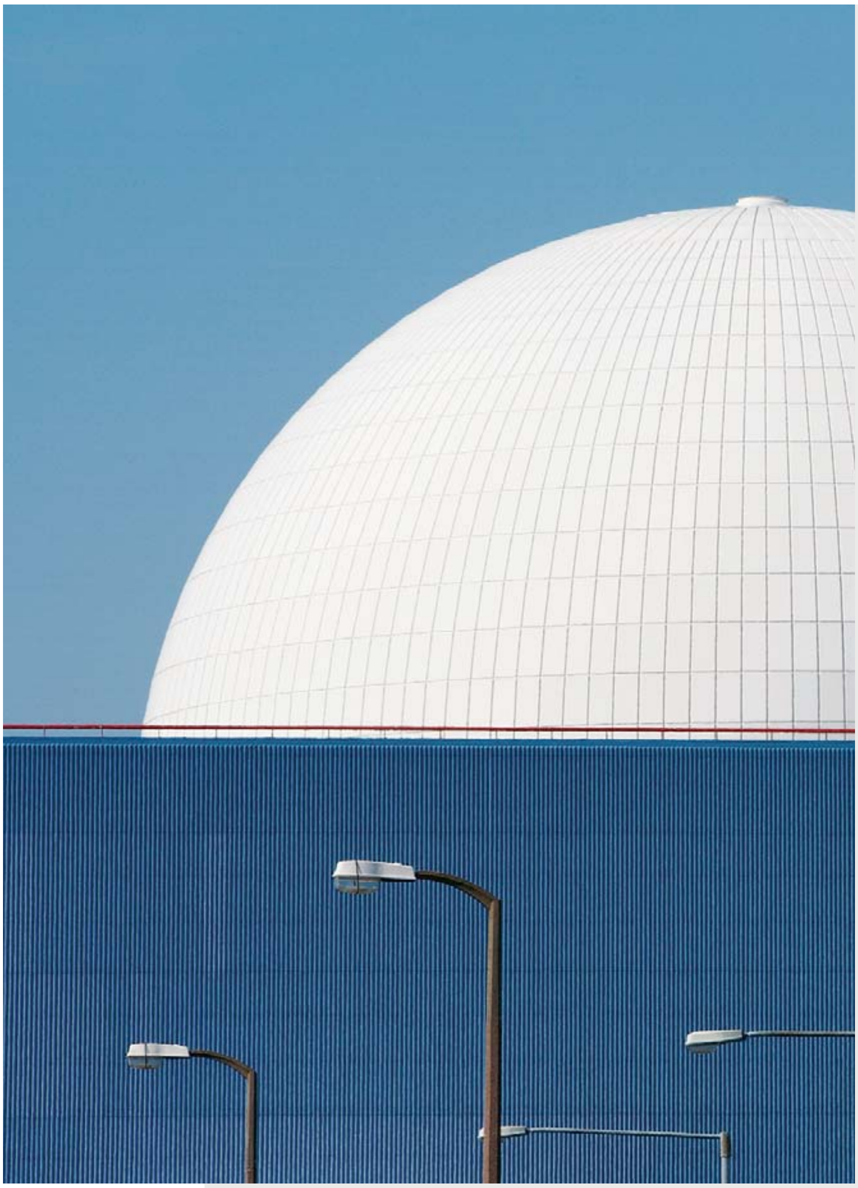
Investing in skills for the Rail industry

Babcock Rail is investing in the skills it will require for the future with new custom built training facilities to open shortly in Glasgow. In addition, this year 17 apprentices across the division have embarked on four years' practical training, study at college and hands-on site experience to achieve NVQ levels 2 and 3 in railway engineering disciplines. The introduction of The Apprentice of the Year Award will recognise and reward those who have achieved exceptional results during their year of training.

Engineering Training Conference

In November 2008 Babcock Rail held its second annual conference for all its engineering graduates and trainees from all disciplines, including their mentors. The Rail training schemes all have accreditation from the Institution of Engineering and Technology and the Institution of Mechanical Engineers.

Part of the conference was to make sure trainees were clear on how they achieved professional membership and engineering council registration and helped to encourage more employees to take part.



Trusted to operate in highly regulated environments...

... because
of our commitment
to health and safety.

Nuclear

Market overview

The civil nuclear market has received greater attention during the year, with a National Policy Statement expected towards the end of 2009, early 2010 which supports a programme of new build nuclear generating stations. These will replace operational reactors scheduled to close over the next 10–15 years. The acquisition of British Energy by EDF and their drive to have a new plant operational by 2017 has also added impetus across the civil nuclear market.

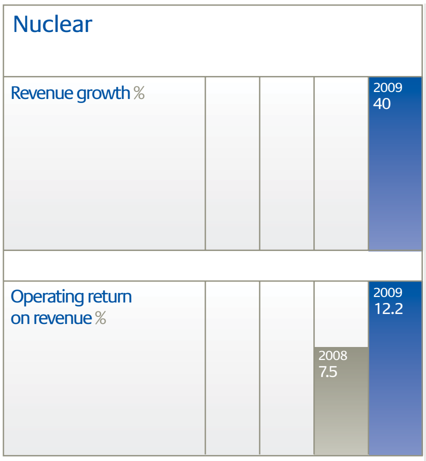
Operational review

The successful consolidation of Alstec, INS and Strachan & Henshaw to create BNS Nuclear Services has created a business with considerable scale and expertise. The financial benefits accruing from the integration and successful contract performance are clearly reflected in the significant improvement in the division's operating margin.

BNS Nuclear Services is now one of the major suppliers of nuclear engineering and support services in the UK civil nuclear market. It has also continued successfully to develop the capability to utilise the nuclear skills existing in Babcock Marine and deploy them in the civil nuclear marketplace, thus providing significantly enhanced capability.

There continues to be a steady programme of investment in the existing operational reactors as plant improvements and work to address key technical issues and support life extensions is undertaken. Supporting the operational AGR fleet continues to be a major focus for the division with the development of Reactor Core Monitoring Equipment for British Energy a major success in reducing AGR outage periods. We expect to conclude discussions with Areva NP for the continuation of the outage and maintenance activities for British Energy's Sizewell B reactor. This follows a successful earlier contract which concluded with the shortest outage period at the station.

The division has continued to support the nuclear scientific sites at both Culham and the Rutherford Appleton Laboratories (RAL). This year saw the successful completion and start of operation of the second Target Station for the ISIS project at RAL where we were the managing contractor and have been successful in winning a follow on support framework.



Meeting the President

Recognising the shortage of professional engineers in the UK, Babcock is working with professional bodies to promote engineering as a profession for young people. In support of this aim, Professor Bill Banks, President of the Royal Institution of Mechanical Engineers, visited BNS Nuclear Services' Whetstone site to meet their current graduate trainees and others in the early stages of their career in engineering.

Professor Banks was keen to gather views on their training and also their expectations of what the Institution had to offer. The visit was organised by two young engineers from BNS Nuclear services who serve on the IMechE young members' panel and board. During the visit Professor Banks and other senior members of the Institution discussed how Babcock could provide continuous professional development, particularly for those working towards professional status.

The decommissioning marketplace remains subdued. Although the Parent Body Organisation (PBO) contract has been let for Sellafield, funding remains constrained. BNS Nuclear Services has successfully completed the installation of the complex equipment for the Sellafield Product and Residue Store project. Earlier this year, as part of the Accord Alliance, we were awarded the next phase of the Box Encapsulation Plant Product Store contract, along with other engineering packages, to support the high hazard work areas on the site. These contracts are strongly supported by our local design and workshop facilities.

At the Dounreay site we successfully won a three year support contract to provide maintenance services for both the PFR and DFR reactors thus consolidating our position as a long-term support services provider for the site. However, decommissioning at Dounreay and Magnox has been delayed until the requirement for funding at Sellafield is established.

This year the first fuel elements were removed from Chapelcross. This was achieved using equipment designed, supplied, installed and commissioned by BNS Nuclear Services as part of the Chaplecross/Calder Hall decommissioning programme.

Our involvement on the AWE sites has continued to grow with a number of contract successes in the decommissioning, facility refurbishment and new facility design areas. The development of our local engineering office at Aldermaston has contributed strongly to this success along with our ability to utilise reachback into the nuclear capability in Babcock Marine.

Outlook

There is growing public acceptance of the need for a new build nuclear power generation programme as well as strong support from Government and an appetite within the industry to make it happen. We are well placed to benefit as this market develops and we are exploring partnering possibilities with a number of parties involved in this programme.

BNS Nuclear Services has one of the largest specialist nuclear resources in the UK. It has a strong position, through its scale and expertise, to serve each market area and deliver further significant growth.

An end-to-end service

To achieve our objective of developing long-term relationships with our customers, our divisions need to properly understand their detailed requirements and long-term goals. Babcock Networks is working hard to ensure EDF Energy Networks meet its goal of improved performance of its electricity distribution networks to meet the future demand for power. During 2009 Babcock will be working on 30 projects throughout East Anglia and the South-East ranging from fittings and foundation replacements to full tower and line refurbishments. There are a number of engineering challenges to be met along the way with crossings over the M1 and a mainline railway.

The 2008/09 programme of works for EDF was all successfully and safely delivered without a single lost time accident. This was the single largest project undertaken for EDF to date and demonstrates our ability to provide a full end-to-end service.

Safety culture

To achieve a complete health and safety culture, we are keen to understand why individuals behave the way they do, the decisions they make and what their underlying beliefs about health and safety are. Babcock Networks is linking up with the University of Nottingham on an Industrial Psychology programme to consider the nature, causes and consequences of accidents in the workforce. We hope the outcomes of this research can be used across the Group.

Networks

Networks

Market overview

Market conditions across the division have seen some volatility during the year. The mobile network operators have continued to outsource to Original Equipment Manufacturers (OEM's), although there has been some increased spending on new infrastructure and upgrading existing networks. In the UK broadcast market, the main focus is on the Digital Switchover (DSO) project which will continue until 2012.

The Digital Britain interim report that was recently presented to Parliament is the Government's plan to secure Britain's place at the forefront of the digital economy. As the Government pushes these plans forward we expect to see our markets benefit significantly.

Operational review

The division has achieved steady growth in revenue following major contract wins in the transmission business and continued growth in the National Grid Electricity Alliance contract (a joint venture with AMEC). Long term alliance partnering has helped insulate the division from some volatility and provide greater visibility and increased work streams, although this is at a slightly reduced operating margin. Margins were also impacted by start up losses in the Irish telecoms business.

Both the National Grid and EDF Energy Networks Alliances have had successful second years, delivering strong volumes with notable improvements in efficiency, innovation and safety performance. In 2009 we expect volumes to remain static ahead of anticipated increases in 2010, when the next regulatory period and Distribution Price Control Review 5 start.

Specialist transmission design activities again increased throughout the year. Whilst finding suitably qualified staff in this area remains difficult, sustained recruitment for both our London and Sofia, Bulgaria, design offices helped the design function respond to the increasing business needs.

Trusted to identify and deliver complex technical solutions...

The division successfully completed its first fixed line communication network contract and there have been consistent and increasing work loads throughout the year. We are now established in this market with a strong pipeline of further opportunities. We have established a dedicated team looking at maximising opportunities from the projected investment in Next Generation networks.

Digital Switchover work has provided a steady revenue stream. Following the acquisition of National Grid Wireless by Arqiva, we now work with a single customer who is responsible for the entire new network being built for the UK Digital Switchover programme.

Outlook

The markets in which we operate remain attractive with significant opportunities resulting from infrastructure upgrade work as well as new technologies. We believe the strong positions we hold in these markets and the long-term relationships we have developed with our key customers will underpin our performance in the future.

Recognising young expertise

In a drive to tackle the world-wide shortage of trained mechanics, Volvo has introduced a scholarship programme for top apprentices from around the world. Four apprentices from the equipment business in South Africa were chosen to travel to Sweden to deepen their knowledge of Volvo construction equipment. Babcock is recognised by Volvo Construction Equipment as a leader in the field of apprentice training and many other distributors have sought advice from Babcock on how to run successful training programmes.

Engineering and Plant

Market overview

In South Africa, whilst the rapid drop in global commodity prices has impacted the economy, the slow down in infrastructure spending, has not been as steep as in some more developed countries. The South African government remains committed to improving and extending the supply of electricity and other civil infrastructures and has allocated additional funds to spend within the power markets that we serve.

Operational review

Despite the sudden decline in the African equipment business during the second half, divisional revenues held up well, ending the year broadly in line with the previous year in Sterling terms. Margins for the division benefited from a very strong performance in the Eagleton pipelines business in the US and improving profitability on Eskom related business in South Africa.

Eskom, the South African power utility, has announced expansion programmes that include new coal fired power stations as well as upgrades and extensions to the transmission line networks. Our power generation support and maintenance business has shown strong growth during the year with continuing benefit from the return to service programme and increased outage and maintenance work on the existing in-service stations.

The Powerlines business has had another good year with successful projects undertaken in South Africa, Namibia and Botswana. Focus on production efficiency has helped to drive margin improvement. Health and safety improvements continue to be a highlight for this area of the business.

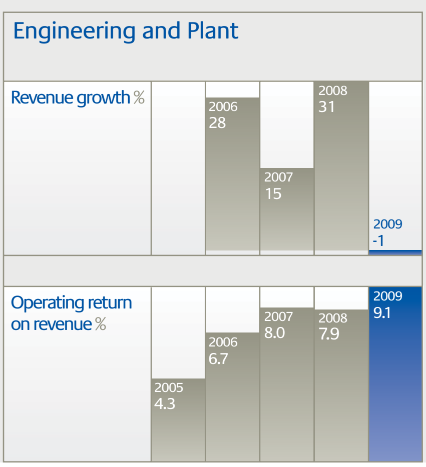
The South African Equipment business has had a challenging year. In the first half we delivered strong results, continuing our track-record of growth. However order intake fell by some 40% in the last quarter compared with the prior year. We started to take action to mitigate the impact of declining orders during October putting plans in place to reduce inventory and cut costs. Our focus on parts and servicing has been beneficial with revenue in this area increasing by 51% with consequent margin enhancement.

Building on our track record of growing market share for Volvo construction equipment, we have taken on a regional dealership for Nissan trucks and are progressing negotiations for the MACK truck franchise for Southern Africa. Whilst we do not expect significant sales in the short-term, the market for smaller commercial vehicles has been relatively resilient and the larger MACK rigid trucks and concrete mixers will complement the current range of construction equipment.

Adding further strength to the business, the Plant Hire business saw good growth in revenues. During the year we made significant investment in new cranes to cope with increased demand that shows no signs of slowing down.

Outlook

With continuing increase in demand for electricity across Southern Africa we anticipate a secure future for our power generation support and Powerlines businesses. In the equipment market we have taken a more cautious approach and in the medium-term we expect the demand in the power markets to off-set only some of the decline in the equipment market. As a result, we expect results for the division for 2009/10, excluding the effects of currency movements, to return to levels similar to those reported in 2007/08.



Corporate responsibility

Our objective is to be the leading engineering support services company in the UK and in selected overseas markets. Our strategic objectives are set out on page 6.

To achieve our strategic goals we must behave as a responsible company and operate with the highest standards of honesty and integrity.

Our continuing financial success is built on long-term customer relationships; technical knowledge and expertise within our business; our commitment to providing a safe working environment as well our ability to work within the regulatory requirements of all our customers' market places, particularly with regard to environmental issues.

In a sector where it is difficult to find enough suitably qualified people, we must focus on recruiting, retaining and developing the best talent we can. We must also play our part in encouraging young people into engineering careers.

This report identifies a range of non-financial issues that need to be addressed to help us reduce business risk. We believe the following areas are key to driving our business success: Corporate Governance; Health and Safety; Employees; Customer Relations; Environment; Procurement and Community.

Corporate governance

We remain committed to achieving the highest standards of corporate governance, so we can retain our 'trusted to deliver' ™ reputation and continue to work in long-term partnerships with our customers. In the current economic climate it is more important than ever to demonstrate excellence in our approach to business ethics and internal control. We address other aspects of corporate governance and internal controls in more detail on pages 36 to 60.

Our approach to and responsibility for matters relating to corporate responsibility is embedded in our management structures and forms part of our approach to the conduct of business in general. Divisional Managing Directors are responsible for such matters at a divisional level, reporting to the Chief Executive who oversees things from a Group perspective and on behalf of the Board. These matters are also addressed in the Executive Committee and through the Safety Leadership Team which are attended by all divisional Managing Directors and the Chief Executive. In addition, we now have or will shortly be appointing senior Group managers, reporting to the Chief Executive, responsible for sustainable procurement, carbon reduction and employee training and development.

Ethical conduct

The Board insists that our business is carried out to the highest standards of honesty and integrity. We have a strict ethical policy in place with guidance on business dealings. This policy defines expected behaviours and is formally re-emphasised to senior management each year who formally confirm compliance. All employees are expected to avoid conflicts of interest, to act lawfully and ethically and report any non-compliance issues of which they become aware. We will be reviewing this policy over the coming year to ensure it continues to meet the Group's requirements as we grow and broaden our activities and to keep abreast of general legal and market developments.

Babcock also subscribes to the Common Industry Standards for European Aerospace and Defence (CIS).

Whistle blowing

At a Group level we have an independently managed 'whistle blower' hot line and every employee has been issued with details of how to contact it. Any reported issues are relayed to Group executives within 24 hours. This ensures all employees can anonymously express any concerns that they have about the way the business is being operated.

Health and safety

babcock HOME SAFE EVERY DAY

During the year we launched our Home Safe Every Day message, to ensure all our employees, contractors and visitors return to their families each day without injury.

We have always regarded the health and safety of our employees and those working alongside them as paramount: this is a key priority at all levels of the business. Due to the large range of activities that we undertake across the Group, some of which are inherently dangerous, our health and safety record is vital to our reputation and our ability to retain and win new contracts. We seek to ensure that best practice, innovative programmes and experiences are shared across the Group in a number of ways;

The Safety Leadership Team consisting of the Executive Committee convenes prior to each Executive Committee meeting to discuss health and safety issues.

The Corporate Safety Steering Group, chaired by the Chief Executive meets several times per year attended by the health and safety managers or directors from each division.

An online best practice forum has been created and is being rolled out across the Group in order to share best practice as widely as possible across the workforce.

Cross–divisional visits by health and safety managers are made during each year.

On-site safety walk rounds are regularly undertaken by divisional directors.

Performance is monitored, reviewed and discussed each month by the Safety Leadership team and the Board reviews performance twice a year.

As part of the ongoing drive for safety improvement, a safety cultural assessment questionnaire is being issued across the Group to employees, customers and on-site contractors. The divisional and Group-wide results from this exercise will assist in pinpointing what can be done to shape attitudes and behaviours and provide a better understanding of the current and desired culture.

Safety culture performance indicators

In the past we have not formally assessed the impact of safety culture initiatives. We have therefore created a structured mechanism to measure safety-related programmes and link them to performance. The divisions will monitor and log good practice events to meet targets that have been set based on injury / incident numbers in 2008/9. Performance will be presented in the monthly health and safety reports.

Over the coming year we will seek to reduce our accident frequency rate by 50% as we strive towards our ultimate goal of zero accidents.

Employees

Babcock operates in highly technical and complex environments and many of our contracts rely on highly skilled, qualified and experienced engineers and project management staff. We need to have one of the best workforces in our sector to deliver the best service for our customers. To achieve this we need to ensure we can recruit, retain and develop sufficient talent within our business.

We want Babcock to be a rewarding and inclusive place to work. We have group-wide policies relating to the strict adherence of equal opportunities. We believe that having a diverse workforce and an inclusive culture is good for our business and should be encouraged. We will not discriminate against employees on grounds of their race, religious belief, gender, marital status, sexual orientation or other considerations that do not affect their ability to carry out their duties.

We believe people with disabilities should have fair consideration for all vacancies and should be supported and encouraged in their application and to achieve progress once employed. We will make reasonable adjustments wherever practicable to accommodate their needs.

Recruitment and training

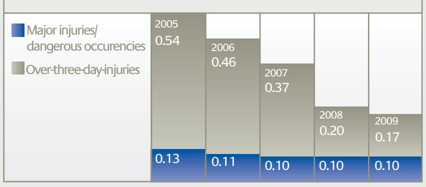
Each of our businesses works with different customers and in different markets. We believe that, in the main, HR issues, including recruitment, training and development and succession planning are best managed locally. Wherever possible, our divisions seek to recruit from the communities in which they operate. Like many other companies who operate in similar highly technical, engineering based markets, we are concerned about the increasing shortage of skilled employees at all levels. Across our divisions we are working with a number of institutions and have a range of initiatives to promote engineering as a career of choice for young people. We are placing increasing emphasis on ensuring opportunities for career development are managed on a Group-wide basis, to ensure our future generations of senior managers and leading specialists are properly identified and developed. A senior Group manager is responsible for this and for ensuring key HR matters affecting the Group's reputation and business development are properly addressed.

Number of incidents
(prior years restated for acquisitions)

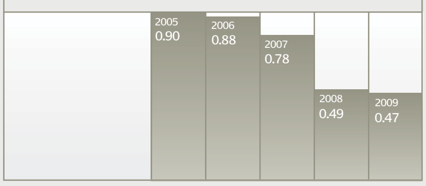
	2005	2006	2007	2008	2009
Fatalities	1	2	2	0	1
Major injuries/ dangerous occurrences	44	40	43	46	50
Over-three-day-injuries	186	159	154	89	83
Other lost time accidents	83	106	128	87	94

The fatality in 08/09 relates to a motor accident in South Africa when our employees stationary vehicle was hit by a third party truck.

Incident rate per 100,000 hours worked
(prior years restated for acquisitions)



Total reported lost time accidents per 100,00 hours worked
(prior years restated for acquisitions)



Apprentices – Apprentice recruitment is undertaken by each division as appropriate for its future requirements. We have 535 apprentices in training within our UK operations, of which 159 were recruited this year. We offer accredited apprenticeships in a wide range of different trades relevant to the operations of each division.

In South Africa we have 50 apprentices working on three or four year schemes. Our goal is to increase this number to 80 this year. To date we have been able to provide full employment to all the apprentices who have completed their training.

Graduates – In 2006 and 2007, 162 graduates joined divisional training programmes, this year we recruited 108 graduates for a Babcock Group graduate programme to provide a wider range of opportunities. We take a range of graduates who have studied engineering, naval architecture, finance, HR, IT and operational management. We provide formal development and training programmes so they can achieve accredited status with the appropriate professional body. We hope to take on a similar number of graduates again this year.

Management development – The Babcock Academy programme, introduced in 2005 and organised in conjunction with Strathclyde University, is designed to enhance the leadership, strategic planning and commercial skills of our managers and senior executives and to introduce the Babcock approach to a number of key operational areas. During last year around 200 directors and senior managers passed through the programme. In 2009 Phase II has been introduced with new modules on Strategic Business Winning and Improving Operational Performance.

Employee communications

We communicate with our employees in a number of ways to keep them informed of strategic developments and the financial performance of the Group as well as promoting best practice initiatives.

Our Group-wide Employee Forum meets twice a year. Each business unit sends their elected representative to be informed of and consulted on all major developments within the Group. Representatives consult within their businesses and bring any issues to the Forum to be discussed.

We produce our Group-wide magazine ‘Big Picture’ several times a year to keep employees and other external stakeholders informed of the Group’s financial performance and strategic developments as well as promote divisional business initiatives and successes.

Most divisions and many operating sites produce their own regular news letters which are distributed by email or are posted on notice boards.

Some divisions have their own intranets for communicating with all employees and for disseminating important information. We are reviewing the possible benefits of establishing a Group-wide intranet.

Customers and customer relations

Strong customer relations are at the heart of any support services business. We pride ourselves on our ability to work in partnership with our customers to deliver jointly agreed objectives. Our financial security is based on a number of key, long-term contracts. It is vital to our ongoing business success that we meet and exceed the different financial and quality KPIs that are used to measure the success of these contracts.

Ultimate responsibility for Group-wide customer relations lies with the Group Business Development Director. Each division has a Business Development director responsible for overall customer relations and each contract has an identified person responsible for liaising directly with the customer and monitoring performance on the agreed KPIs.

For the past five years we have participated in an annual performance review by the Ministry of Defence which measures our performance on all its contracts by quality, value, timeliness and eleven core criteria including responsiveness, management of risk, quality of relationship, flexibility and innovation. We have regular dialogue with our other customers to ensure we identify any potential threats to our relationships and resolve them in a timely manner.

In 2008 we commissioned an independent survey across all our customer groups. In response to this and other survey results we are taking action to improve the quality of service that supports our trusted to deliver reputation.

We have highlighted the following as areas of focus to ensure we achieve maximum success

Partnership – by achieving a real partnership both parties feel the benefits through added confidence that project goals will be met.

Cost efficiency – we are committed, wherever possible, to improve cost efficiency, this is extremely important for many of our customers particularly in today’s economic climate. Our ability to manage and reduce cost is evident in many of our long-term relationships.

Added value – we want our customers to find us easy to do business with – open, approachable and flexible to deliver more than the basic contract requirements

The results of the research have shown us that we need to be more systematic in the delivery of customer service. We will commission regular reviews of our business partnering arrangements to identify areas that are working well and where action is required.

To ensure a consistent approach across the Group, we have seconded a Customer Relations Project Manager from the MoD to work with us in 2009 to try to replicate the MoD's performance review with key civilian customers. Through this we hope to establish Group-wide customer satisfaction benchmarks.

Environment

We recognise that we need to achieve the highest standards of environmental management and that this is a key element of maintaining our business reputation and success.

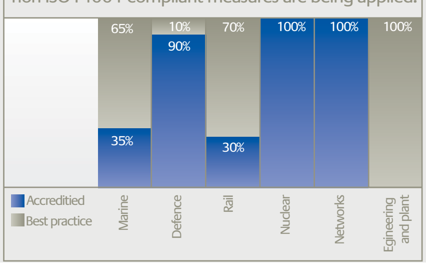
In compliance with the Carbon Reduction Commitment, the Government's carbon emissions trading scheme, Babcock recognises the benefits achievable by both being more energy efficient and reducing our carbon footprint. We are therefore making progress to be fully compliant with the new regulations which will come in to force in April 2010. Additionally, base lines will be set and performance measurements will be introduced.

This regime enhances activities that are already undertaken across the Group, such as participation in the Climate Change Agreement (Gas usage) and the EU Emissions Trading Scheme (Gas and Oil usage) by Babcock Marine (Devonport).

These activities will help us manage the footprint and reduce our emissions over time and allow us to report accurately in the future.

Environment %

KPI:
Although our ability to implement good environmental stewardship practices is on occasion set for us by customer requirements our target is to grow the percentage of revenues in each business segment from contracts which are ISO14001 accredited. 'Best practice' refers to activities where non-ISO14001 compliant measures are being applied.



Procurement

We work mainly with government departments or other regulated industries who often have budgetary as well as regulatory or political constraints that could significantly impact on our contracts. We have a duty to ensure that our customers' money is spent efficiently and contracts are managed effectively.

Our customers rely on us to manage a number of suppliers and sub-contractors on their behalf. We need to ensure that the supply chain for all our contracts adheres to our standards of ethical behaviour, environmental and other working policies.

We are working with the Government on their Sustainable Procurement initiative. As well as seeking to reduce CO_2 emissions part of the initiative is focused on broader sustainable procurement issues. As part of the MoD's performance review process in 2009 we will be required to complete the Sustainable Procurement Flexible Framework.

We have appointed a Group Sustainable Procurement Manager to introduce benchmarks and measure performance on a number of KPIs related to this initiative as well as other supply chain issues. During this year we will be looking to introduce a range of processes and measures to ensure we meet the Government's required standards, as well as those of our other customers, and are in a good position from which to improve them. We will be able to report on progress next year.

Community

In many places our operations are the largest employer in the region. If we are to continue to recruit from our local communities we must maintain our reputation as a responsible employer. We therefore seek to engage with the communities around our sites and operations and to provide opportunities for employees to assist with local initiatives and support local charities that are important to them.

We have Group-wide guidelines in place setting out our approach to charitable donations, our commitment to the communities in which we operate and the broader interests of our customers. As well as ensuring financial donations are appropriately targeted, they also encourage active engagement with the communities in which we operate through local community support programmes.

In South Africa, local management has identified three specific areas of support which will benefit the local communities as well as being key areas of concern for the country. These are education, HIV prevention and training and HIV orphan support.

In support of our major customer we have continued to provide corporate sponsorship for the Soldiers, Sailors, Airmen and Families Association (SSAFA), the forces charity providing support to service families in times of need. Six years ago Babcock was one of the 'founding friends' that helped start a fundraising initiative that now has over 35 companies involved.

Across the Group we have provided support to a number of charitable causes and during the year we donated £129,000 (2008: £105,000).

Principal risks

In the course of our day-to-day operations we face a number of risks and uncertainties. The Board considers the matters described in this section to be those that could adversely affect the business, results of operations, revenue, profit, cash flow, assets and the delivery of our growth strategy. Given the size, complexity and spread of our businesses and the continually changing environment in which the Group operates, this cannot be an exhaustive list of such risks.

Systems and procedures are in place across the Group to identify, assess and mitigate major business risks. The management of risk is an integral part of our operational review process and is supplemented at Group level by independent challenge and review by the Group Risk Manager and the Audit and Risk Committee. Further details on our internal control processes are set out on pages 44 and 45.

Risk

Health, safety and environmental issues

The working environments in which the Group operates are complex and, in some instances, can be inherently dangerous. Some of our activities, if not appropriately managed, could have an adverse effect on the environment which could reasonably be avoided.

Our commitment to our employees and the nature of our business and our customers mean that our ability to manage these issues is a key element of our business reputation and success.

Impact

Damage to our reputation would affect our ability to win and retain contracts and attract and retain our staff and therefore adversely affect the financial performance of the Group.

Action

The Executive Committee and the Board review health, safety and environmental performance regularly and satisfactory performance on these matters is one of the performance criteria included in executive bonus schemes. A Safety Leadership Team comprising the Executive Directors and all divisional Managing Directors meets regularly to set policy and procedures and to monitor performance and agree corrective actions where necessary. For further details of our approach to Health, Safety and Environment see pages 22 and 23 and page 25.

Risk

The Group is dependent on a number of key people

The Group operates in highly technical and complex businesses and is dependent on recruiting, retaining and developing highly skilled, qualified and experienced engineers and project management staff. The marketplace for such staff remains highly competitive.

Impact

The Group's operations could be constrained by a lack of suitably qualified and experienced employees in key areas.

Action

We seek to make our businesses attractive places to work by offering competitive remuneration packages aimed at long-term employee retention as well as appropriate training and development opportunities. In the past few years we have extended both our graduate and apprentice recruitment and development programmes and we continue to improve our management development programmes.

Risk

The Group's ethical reputation could be damaged

We pride ourselves on our 'trusted to deliver' ™ reputation. This is a key factor in our ability to win, complete and retain contracts and is an important element in our ability to build and maintain long-term relationships with our customers.

Impact

Any damage to our reputation could have an adverse effect on the Group's future results and financial position.

Action

We insist on the highest standards of honesty, integrity and performance in all aspects of business. We have an ethical policy in place that defines the level of behaviour we expect. The policy is formally re-emphasised to senior management every year and they formally confirm compliance. We have established a 'whistle blower' hot line so all employees can anonymously express any concerns they have about the way the business is being operated. We maintain regular dialogue with customers and carry out customer surveys to ensure we identify any potential threats to our customer relationships and act on them.

Risk

Information technology

The Group relies on the use of complex software for the management of engineering, commercial and financial data. The Group and its customers are dependent on the resilience of the applications' software, the data processing facilities and the network infrastructure linking the sites where we operate.

Impact

A serious failure in any of these areas would have a significant adverse effect on our businesses.

Action

The Group's businesses have detailed disaster recovery plans in place. We have also established a Group data centre which has in-built high resilience levels with a physically separate disaster recovery facility. This will increasingly form the hub of all shared IT services.

Risk

The Group is reliant on large contracts from a limited number of major customers

A significant proportion of the Group's revenue comes from large contracts placed by a limited number of major customers such as the Ministry of Defence, Network Rail, and National Grid. These customers are affected by budgetary, regulatory or political constraints which could have a significant impact on the size, scope, timing and duration of contracts and orders under them. In addition, because of their size, these customers have considerable bargaining power and the ability to cancel contracts at short notice.

Impact

The loss, expiration, delay, suspension, cancellation or termination of a number of these large contracts, or any damage to the relationship with any of our major customers, could have a material adverse effect on the Group's future results and financial position.

Action

We make it a priority to have a close understanding of our customers and their needs and objectives. Our aim is to develop and maintain long-term co-operative working relationships with them, and to ensure the financial success or failure of contracts is fairly shared. We aim to position our businesses in markets where the risk of adverse changes to the size, scope, timing and duration of contracts is low.

Management regularly reviews contract performance and Executive Committee members are closely involved in ensuring the strength of customer relationships.

Risk

Maintaining growth through continuing bid success

Our ability to achieve growth and deliver value for our shareholders relies on our ability to win new contracts and retain existing contracts on expiry. Our ability to manage the bid process successfully is vital. Bid processes can be long and are often subject to delays, changes or abandonment by the customer, all of which are outside our control. The significant financial and manpower costs of these bids are generally not recoverable if bids are unsuccessful or the tenders are withdrawn or aborted by the customer.

Impact

Failure to win significant new contracts will materially affect the Group's future results and its ability to achieve its strategic growth objectives.

Action

All bids are subject to continuous monitoring and review by senior Group and divisional executives to ensure resources are appropriately focused so the chances of success and the financial returns are acceptable. The final submission of any significant bid or re-bid requires formal approval from one or more Executive Directors.

Principal risks continued

Risk

Poor contract performance

The continuing financial success of the Group depends on our ability to meet or exceed the contractual requirements of our customers. On many contracts we employ sub-contractors or work with other commercial partners and so are reliant on their performance as well as that of our own employees to meet the key performance indicators and financial standards expected.

Impact

Failure to meet contractual performance criteria either directly or through sub-contractors and the resultant damage to our reputation could have an adverse effect on the Group's future results and financial position.

Action

Each division has procedures in place to monitor the ongoing performance of each contract and these are discussed at operational reviews with Group Executive management. The financial performance of all contracts is reviewed quarterly by Group Finance.

Risk

The Group derives a large proportion of its revenues from national and local government activities

Our largest customer is the Ministry of Defence. We also have significant contracts with private sector companies who are strongly influenced by political and regulatory considerations. As such our businesses are susceptible to changes in government policy, budget allocations and the political environment.

Impact

The termination or significant amendment of any of our large contracts arising from changes in the factors noted could have an adverse effect on the Group's future results and financial position.

Action

We seek to maintain a regular dialogue with our customers and others within government departments to ensure we fully understand at both Group and divisional levels the considerations that are affecting budgetary and policy decisions and the changing political environment.

Risk

The Group has experienced growth through acquisitions, the financial and strategic benefits of these acquisitions may not be realised

Since 2001 the Group has grown through a series of acquisitions. This is expected to continue as the Group seeks to meet its strategic objectives. The integration of operations and employees is a complex process and post-acquisition performance may not be at the levels anticipated. The Group may not be able to integrate the operations of acquired businesses with existing operations as rapidly as expected or without encountering other difficulties.

Impact

The diversion of management attention to integration issues and other difficulties encountered could adversely affect the Group's business. Post-acquisition performance may not meet the financial performance expected and could therefore not justify the price paid and could adversely affect the Group's future results and financial position.

Action

We seek to carry out appropriate due diligence as far as we are able and carry out a detailed valuation process based on information available and our knowledge of the marketplace. All acquisition processes are overseen by the Board and no acquisition may be completed without the formal approval of the Board.

Risk

The Group operates large defined benefit pension schemes

The Group's defined benefit pension schemes are currently in overall surplus. However this could be adversely affected by a number of factors including lower than assumed investment returns, changes in mortality or other valuation assumptions and the funds could go into deficit.

Impact

A pension scheme deficit could require the Group to make greater cash contributions to the schemes and reduce the cash available to meet the Group's other obligations or business needs.

Action

We seek to maintain constructive and open relationships with the scheme trustees and to encourage them to follow appropriate investment policies for the profile of their members as well as seek other means of eliminating or mitigating risk. For an example of how we are addressing this see the financial review page 32, where we discuss proposed longevity swaps. We also maintain a suitable ongoing funding rate. We have a Group Pensions Manager reporting to the Group Finance Director whose task is to keep such strategic matters under close review. He regularly reports to the Board. An annual review of the pension schemes is also conducted by the Board and the schemes form part of Board discussions at other times of the year. Further details of the Group's pension schemes are detailed in note 28 to the Group financial statements.

Risk

The material misstatement of financial results

The Group could materially misstate financial results through fraud or error if financial and operational controls are inadequate.

Impact

Misstatement of financial results could adversely damage the Group's reputation, affect its ability to operate and its future results and financial position.

Action

The Group has robust structures to mitigate or manage these risks, including a comprehensive financial policy and accounting standards manual with authority and approval mandates. All material commercial and contractual activities are overseen by Group executives and governed by the Group Policy and Procedures manual which sets out the Group's approach to doing business. These policies and procedures are backed up by a system of regular contract reviews conducted by Group Finance and a regime of internal audit, conducted by Ernst and Young which reports to the Audit and Risk Committee. Further detail of internal controls is given on pages 44-45.

Risk

Default of a significant debtor or counterparty

Impact

The failure of a significant debtor or counterparty could adversely effect the cash flow of the Group.

Action

All significant credit risks are reviewed by Group Finance and an Executive Director and, where appropriate and available, risk limitation actions are taken.

Risk

Liquidity risk

The Group relies on the ongoing provision of lines of credit from its relationship banks. Banking lines of credit could be withdrawn if legally binding covenants are not met.

Impact

The Group's ability to fund current and future obligations and future expansion could be adversely affected.

Action

The Group has committed lines of credit of £600 million through to 2012. Borrowing ratios are comfortably within the banking covenants set out in financing agreements and are monitored on a regular basis. The conversion of profit to cash is a key performance indicator.

Risk

Interest and foreign exchange risk

Historically the Group has financed its operations through equity and bank debt. Some of the Group's debt is denominated in foreign currency. The interest rate charged on bank debt could increase significantly or foreign currency exchange rates could move materially against Sterling, the Group's base currency.

Impact

Adverse movements in interest and foreign exchange rates could impact Group profit and net assets causing a reduction in returns to shareholders.

Action

Interest rate risk is managed by the use of interest rate collars and swaps to ensure an appropriate mix of fixed and floating rate debt is maintained. Foreign exchange translation exposure is managed by restricting foreign borrowing to the value of assets denominated in the same currency or in the case of transactions in foreign currency, by the mandatory use of foreign currency contracts.

Financial review

Financial highlights

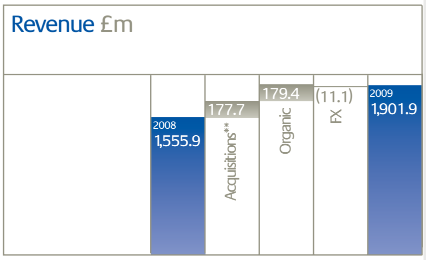
	2009	2008	Growth
Revenue	£1,901.9m	£1,555.9m	+22%
Operating profit	£147.3m	£121.1m	+22%
Profit before tax	£120.9m	£95.5m	+27%
Continuing earnings per share	41.90p	33.40p	+25%
Full year dividend proposal	14.40p	11.50p	+25%
Net debt	£351.5m	£322.2m	

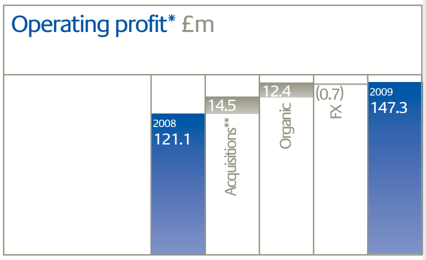
Group income statement

In the year to 31 March 2009 Babcock recorded another strong set of financial results as we continued to pursue our growth strategy both organically and through acquisition. We significantly enhanced our presence in the Marine and Nuclear markets through the acquisition of Strachan & Henshaw Ltd (S&H) in May 2008 which contributed revenue and operating profit of £58.9 million and £7.3 million respectively in the year. Performance in these key strategic markets was excellent with both divisions recording double digit growth in revenue and operating profits with a number of major contracts secured during the year. Excluding the contribution from S&H, organic growth in Group revenue and operating profit was 10% and 9% respectively.

The Group operating margin remained robust at 7.7%, in line with last year despite an adverse performance in Rail. The Group's return on invested capital of 18.5% (2008: 14.4%) remains comfortably ahead of our weighted average cost of capital, a performance driven by focus on operating margins and optimisation of fixed and working capital.

Bridging analysis





* Before amortisation of acquired intangibles and exceptional items.
** Acquisitions both this year and last year.

We have delivered another set of record results, have continued to focus on generating cash and have maintained a secure financing position.

Bill Tame
Finance Director

In Rail, the multi-disciplinary projects business failed to improve during the second half and despite profitable trading from the track and signalling businesses, losses overall increased to £6.4 million from £4.7 million at the half year (2008: profit £0.5 million). Whilst this out-turn was a drag on the Group's result, the strength of performance elsewhere has been more than sufficient to compensate and ensured the Group continued to deliver double digit growth. The anticipated recovery in Rail is expected to add further momentum to bottom line growth in 2009/10.

2008/09 witnessed significant volatility in credit markets with the London Interbank Offered Rate (LIBOR) peaking at a high of 6% in early April 2008 and ending the financial year at approximately 1.2%, still significantly above the Bank of England official rate, or 'base rate', of 0.5% reflecting ongoing credit concerns between banks. We have benefited to some extent from the decline in LIBOR in the rate of interest we have paid to our lending banks during the second half and are likely to benefit further during 2009/10. Approximately 50% of the Group's gross debt is hedged at a fixed rate of interest and that portion of Group debt has not and will not benefit from lower rates in the medium-term. The total net charge for interest in the year was £26.2 million (2008: £25.6 million) covered 6.5 times (2008: 5.5 times) by earnings before interest, depreciation and amortisation (ebitda) and comfortably within banking covenants.

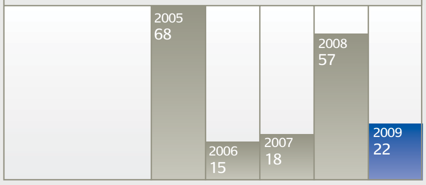
Consequently, with a flat year-on-year interest charge, profit before tax increased by 27% to £120.9 million (2008: £95.5 million). The related charge to corporation tax of £23.1 million (2008: £18.2 million) represented 19% of the underlying (before amortisation of aquired intangibles and exceptionals) pre-tax profit. The Group benefited from tax on income in overseas jurisdictions at rates below that of the UK. UK legislation currently planned to take effect for financial years commencing on or after 1 January 2010 may cause the Group's effective rate to increase from April 2010 onwards but we estimate (based on currently known rates of taxation) a rate of no more than 23% is likely from that date.

Post-tax profit from continuing operations increased by 27% to £97.8 million (2008: £77.3 million). As reported in the first half of the year, following the settlement of a dispute with Tesco Stores Limited, the Group incurred an exceptional post-tax cash charge of £13.3 million against discontinued businesses. As previously disclosed this related to matters arising out of a contract for the design and construction of tunnelling works for the store at Gerrards Cross, for which the Peterhouse Group had provided a Parent Company Guarantee. This contract was originally entered into by the civil engineering division of the Peterhouse Group which was sold, by Peterhouse, prior to Babcock's acquisition of the Peterhouse Group in 2004. After charging this amount shown in the Group's income statement under discontinued operations, profit for the year after charging amortisation of acquired intangibles was £74.3 million (2008: £69.7 million).

Our commitment to delivering value for shareholders has been clearly demonstrated over the past five years during which period we have paid £78 million to shareholders in dividends and have maintained dividend cover of between 2.5 and 3 times. We have achieved this by growing and acquiring businesses with sustainable growth potential and delivering on that potential. Reflecting our confidence in the strength and resilience of our business model the Board is proposing a final dividend for 2008/09 of 10.40 pence per share. If approved by shareholders this will make the total dividend for the year 14.40 pence (2008: 11.50 pence) an increase of 25%.

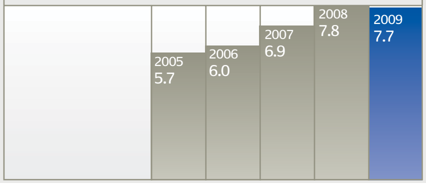
Revenue growth %

KPI:
Revenue growth is defined as the increase in the Company's continuing revenue when compared to that of the previous year.



Operating return on revenue (ORR) %

KPI:
Operating return on revenue (ORR) is defined as operating profit before amortisation of acquired intangibles and exceptional items expressed as a percentage of revenue.



Cash flow and net debt

As our longer term investors will know, we have always considered the most important measure of business health to be cash, both in terms of the absolute value of cash generated from operations and the relative conversion rate of cash from operating profit. Cash conversion in the year was 115% (2008: 108%). We achieve such good conversion through rigorous attention to the negotiation and application of contract terms, being trusted to deliver the services required of us and a thorough understanding of cash payback in both capital expenditure and acquisition projects.

Having increased to £373.9 million at the end of the first half, prinicpally as a aresult of the S&H acquisition, Group net debt reduced to £351.5 million at the year end. During the year we benefited from significant cash inflow on a number of major contracts both at completion and start-up phases resulting in a net inflow of funds from working capital. This profile is not unusual for a long-term contracting organisation such as Babcock and working capital cash flows can be volatile from year to year. Capital expenditure of £19.3 million (including finance leases of £0.2 million) represented 0.8 times depreciation and amortisation of non-acquired intangibles (2008: £14.2 million and 0.7 times) and was predominantly in support of major contracts in Marine, Networks and Engineering and Plant together with Group-wide IT systems. Delays in some expenditure intended for 2008/09 will mean that 2009/10 is likely to see higher levels of capital expenditure.

After cash paid in respect of acquisitions of £66.2 million, the net cost of the Tesco dispute settlement of £13.3 million and interest, tax and dividend payments, the net cash outflow was £29.3 million (2008: £248.5 million).

The Group has in place a £600 million revolving credit facility with its banking group which matures in 2012. With net debt at £351.5 million, financial gearing ratios comfortably within covenanted levels and facilities in place for another three years, the Group's financing position remains secure.

Pensions

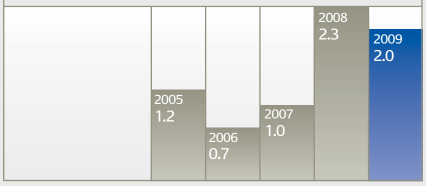
Good progress has been made since the half year on securing a solution to the 'longevity' risk on a significant element of the Group's pension scheme liabilities. We have reached agreement in principle with the trustees of two of our defined benefit pension schemes (the Schemes) for them to enter into contracts with an agreed counterparty to cap their exposure to increasing life expectancy.

The exposure will be capped by the use of longevity swaps which will apply to current pensions in payment whereby the Schemes have agreed to make fixed payments in exchange for receiving the actual value of pensions due to members, irrespective of how long the members and their dependents live. In return for the Schemes' agreement to enter into this arrangement, the Group has agreed to fund the excess of the swap payment over the funding assumptions adopted by the trustees over a 20 year period. Other than the future benefit of capping the liabilities covered by the swaps, there will be no material impact on the Group's income statement, balance sheet or cash flow as a result of this transaction.

This arrangement is designed to ensure for both the Group and the pension schemes that any further financial risk related to improved longevity has been eliminated.

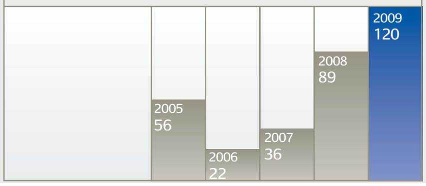
Net debt/EBITDA x

KPI:
Net debt/EBITDA is calculated as net debt divided by earnings before interest, tax, depreciation and amortisation.



Gearing ratio %

KPI:
Gearing ratio measures the extent to which a company is funded by debt. Calculated as net debt divided by shareholders funds.



At 31 March 2009 the Group’s defined benefit pension liabilities and assets each totalled approximately £1.7 billion with a net balance sheet surplus of £50.7 million. Approximately £800 million of the liabilities were in respect of pensions in payment and in this the first stage of the Group’s ongoing liability management programme around £500 million of this amount is planned to be capped by the use of longevity swaps. Approximately £250 million of the remainder of the pensions in payment liabilities are expected to be the subject of a separate arrangement in the near future.

In conjunction with the execution of these swaps, existing inflation and interest rate risk hedging is under review via the schemes’ investment portfolios to ensure that a fully effective hedge is established for all pensions in payment liabilities.

The impact of the defined benefit pensions on the Group income statement was as follows:

	2009 £m	2008 £m
Service cost	£26.7	26.8
Expected return on plan assets	(127.4)	(115.1)
Interest on obligations	116.6	92.1
	(10.8)	(23.0)
Net charge	15.9	3.8

The above is before £1.4 million curtailment gain following reductions in active membership during the year.

Outlook

The major markets in which we operate remain both attractive and resilient.

Our £5.7 billion order book and strong bid pipeline give us excellent long-term visibility. Our financial strength and ability to deliver cost effective solutions give us confidence that the growth prospects for the Group remain strong. We anticipate increasing pressure for improved efficiency in public-sector spend will further increase the opportunities available to us.

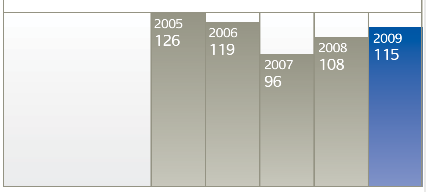
We look forward to another year of excellent progress for Babcock.

Peter Rogers
Chief Executive

Bill Tame
Finance Director

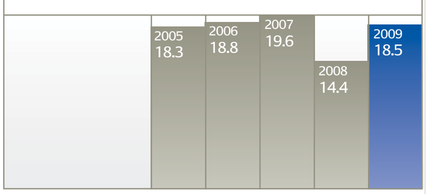
Operating cash flow (OFC) conversion rate %

KPI:
Operating cash flow (OCF) conversion rate is defined as cash generated by operations as a percentage of operating profit (post exceptionals).



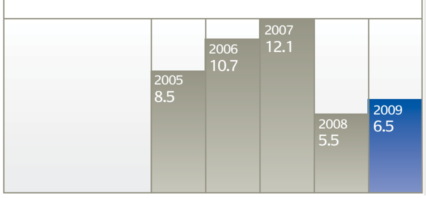
Return on invested capital (ROIC) %

KPI:
Return on invested capital (ROIC) is defined as net income divided by total capital (equity plus net debt).

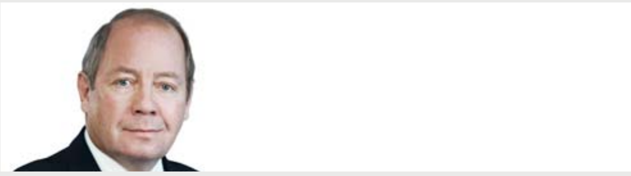


EBITDA interest cover x

KPI:
Interest cover is a measure of the adequacy of the company’s profits relative to interest payments on its debt. Profit before interest, tax, depreciation and amortisation, divided by net interest payable.



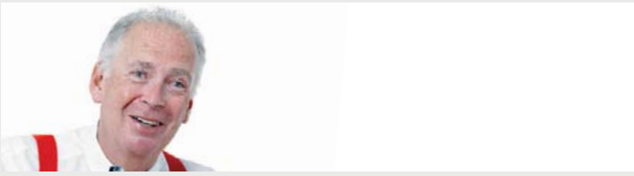
Directors and Company Secretary



Mike Turner CBE (60)
Chairman of the Board (since 1 November 2008)

Chairman of the Nominations Committee

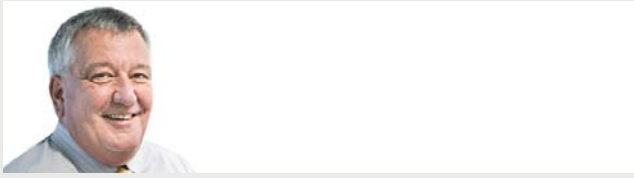
Mike Turner rejoined the Board as a Non-Executive Director on 1 June 2008 and took over from Gordon Campbell as Chairman of the Board on 1 November 2008. From March 2002 until August 2008, Mr Turner was Chief Executive of BAE Systems plc. He is a Non-Executive Director of Lazard Ltd and is currently Chairman of the Defence Industries Council, Joint Chairman of the National Defence Industries Council and is a member of the Government's Apprenticeship Ambassadors Network. He previously served as a Non-Executive Director of the Company, between 1996 and December 2005. He was re-appointed as a Director at the Company's Annual General Meeting in July 2008.



The Rt Hon Lord Alexander Hesketh KBE (58)
Non-Executive Deputy Chairman

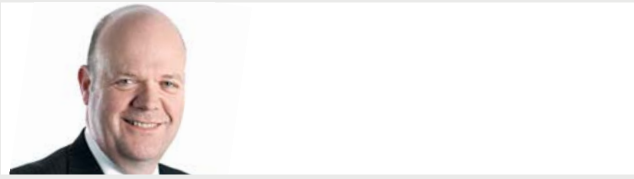
Member of the Nominations Committee

Alexander Hesketh joined the Board in 1993 and has been Non-Executive Deputy Chairman since 1996. He is a former Executive Chairman of British Mediterranean Airways Limited and is a Director of a number of other private companies. Between 1991 and 1993 he was Government Chief Whip in the House of Lords and before that was an Industry Minister at the Department of Trade and Industry. Having served for more than nine years on the Board, Lord Hesketh offers himself for re-appointment annually in accordance with the Combined Code.



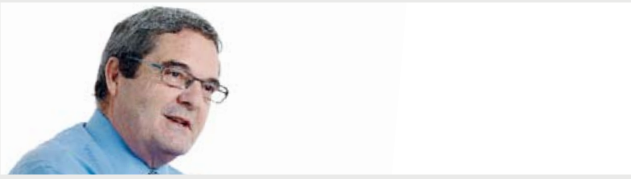
Peter Rogers (61)
Chief Executive

Peter Rogers joined the Board in June 2002 as Chief Operating Officer. He became Chief Executive in August 2003. He is a Non-Executive Director of Galliford Try plc and a former Director of Courtaulds plc and Acordis BV. He was last re-appointed as a Director at the Company's Annual General Meeting in 2008.



William Tame (54)
Finance Director

Bill Tame joined the Board as Group Finance Director in January 2002. He is a Non-Executive Director of Carclo PLC and a former Finance Director of Scapa Group PLC. He was last re-appointed as a Director at the Company's Annual General Meeting in 2008.



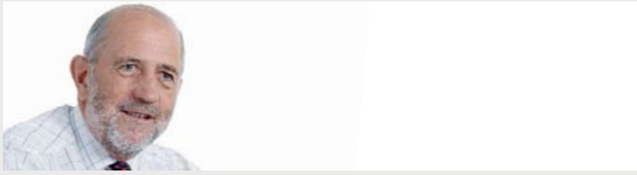
John Rennocks (63)
Senior Independent Non-Executive Director

Chairman of the Audit and Risk Committee
Member of the Remuneration Committee
Member of the Nominations Committee

John Rennocks has been a Non-Executive Director since June 2002. He is a former Finance Director of Corus Group PLC and is Chairman of Diploma Plc, Nestor plc, Intelligent Energy Holdings PLC and Composite Energy Ltd. He is a Non-Executive Director of JP Morgan Overseas Investment Trust PLC and Inmarsat plc. He was last re-appointed as a Director at the Company's Annual General Meeting in July 2008.

Dipesh J Shah OBE (56)
Non-Executive Director

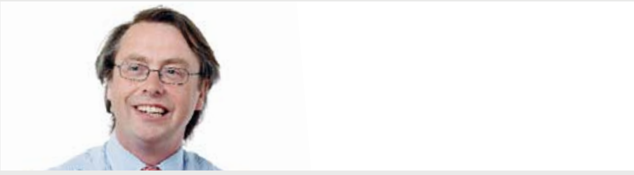
Dipesh Shah has been a Non-Executive Director since June 1999. Until 31 March 2009, he was Chairman of the Remuneration Committee and a member of the Audit and Risk and Nominations Committees. He will be retiring from the Board at the Company's forthcoming Annual General Meeting in July. He is a Director of several other companies, including Thames Water and Kemble Water Group of companies, Lloyd's of London Franchise Board and JKX Oil & Gas plc. Mr Shah was the Chief Executive Officer of the United Kingdom Atomic Energy Authority, Chairman of Viridian Group PLC and Chairman of Hg Capital Renewable Power Partners LLP.



Sir Nigel Essenhigh GCB (64)
Independent Non-Executive Director

Member of the Remuneration Committee
Member of the Audit and Risk Committee
Member of the Nominations Committee

Nigel Essenhigh has been a Non-Executive Director since March 2003. He is a former First Sea Lord and Chief of Naval Staff. He is Chairman of NGC UK Limited, Northrop Grumman Corporation's UK holding company. He was last re-appointed as a Director of the Company in 2006 and will be submitting himself for re-appointment at the Company's forthcoming Annual General Meeting in July.



Justin Crookenden (46)
Independent Non-Executive Director

Chairman of the Remuneration Committee
Member of the Audit and Risk Committee
Member of the Nominations Committee

Justin Crookenden has been a Non-Executive Director since December 2005. He took over the chairmanship of the Remuneration Committee on 1 April 2009, having previously served as a member of the Committee since his appointment to the Board. He is a Chartered Accountant and former investment banker who has worked at UBS, Barclays de Zoete Wedd and Credit Suisse First Boston where he was Managing Director, UK Investment Banking. He was last re-appointed as a Director of the Company in 2006 and will be submitting himself for re-appointment at the Company's forthcoming Annual General Meeting in July.

Sir David Omand (62)
Independent Non-Executive Director

Member of the Remuneration Committee
Member of the Audit and Risk Committee
Member of the Nominations Committee

Sir David joined the Board on 1 April 2009. He was the first UK Security and Intelligence Coordinator, responsible for the professional health of the intelligence community, national counter-terrorism strategy and 'homeland security', and was the UK Government's chief crisis manager for civil contingencies. He served for seven years on the Joint Intelligence Committee. He was previously Permanent Secretary of the Home Office, Director of GCHQ (the UK Signals Intelligence and Information Assurance Agency) and Deputy Under-Secretary of State for Policy in the Ministry of Defence. He was Principal Private Secretary to the Defence Secretary during the Falklands conflict, and was for three years the UK Defence Counsellor in NATO Brussels. He left Government service in 2005. Having been appointed by the Board since the last Annual General Meeting, he will offer himself for re-appointment as a Director at the Company's forthcoming Annual General Meeting in July.

Albert Dungate (52)
Group Company Secretary and General Counsel

Albert Dungate is a Solicitor. He has been Group Company Secretary and General Counsel since February 2002. He was formerly General Counsel and Company Secretary of Arjo Wiggins Appleton PLC. He is Secretary to the Board and to the Audit and Risk, Remuneration and Nominations Committees.

Directors' report

The Directors present their report and the audited financial statements of the Group and the Company for the financial year ended 31 March 2009. The Directors' report is made up of pages 1 to 60 of this Annual Report, including:

- The Business review appearing on pages 1 to 33 – this describes the Group's activities, likely future developments, the principal risks and uncertainties facing the Group, key performance indicators and details of any important events since 31 March 2009;
- The Statement on Corporate Governance on pages 42 to 45 – describing how the Company meets the requirements of the Combined Code and dealing with internal controls;
- The report of the work of the Audit and Risk Committee on pages 46 and 47; and
- The Remuneration report on pages 48 to 60.

each of which is to be treated as part of the Directors' report.

Annual General Meeting

This year's Annual General Meeting will be held at Chandos House, 2 Queen Anne Street, London W1G 9LQ on Thursday, 9 July 2009, at 11 am. The notice of meeting is on pages 108 to 122 and explanatory notes on the resolutions to be proposed at it as special business are set out on page 113. These resolutions relate to the giving of authority to Directors to allot and purchase Company shares, including as to rights issues, renewal of authority to make political donations (as defined by legislation), proposals to introduce a new Performance Share Plan and a Company Share Option Plan applicable to Executive Directors and other employees and the notice period required for the calling of general meetings of the Company (other than Annual General Meetings).

Results and dividends

The profit attributable to shareholders for the financial year was £72.0 million (2008: £67.3 million). An interim dividend of 4.00p per 60p ordinary share was declared in the year (2008: 3.30p). The Directors propose to recommend the payment on 7 August 2009 to those shareholders on the register at the close of business on 10 July 2009 ('the Record Date') of a final dividend of 10.40p (2008: 8.20p) on each of the ordinary shares of 60p entitled thereto and in issue on the Record Date.

Directors

Biographies of the current Directors of the Company are to be found on pages 34 and 35.

During the financial year the Directors who served were as follows:

Director	Service in the year to 31 March 2009
Mike Turner (Chairman)	Joined the Board 1 June 2008; appointed Chairman 1 November 2008
Gordon Campbell (former Chairman)	Retired 31 October 2008
Lord Hesketh (Deputy Chairman)	Served throughout the year
Peter Rogers (Chief Executive Officer)	Served throughout the year
William Tame (Finance Director)	Served throughout the year
John Rennocks (Senior Independent Non-Executive)	Served throughout the year
Dipesh Shah (Non-Executive)	Served throughout the year
Sir Nigel Essenhigh (Non-Executive)	Served throughout the year
Justin Crookenden (Non-Executive)	Served throughout the year

On 1 April 2009, Sir David Omand joined the Board as a Non-Executive Director. Dipesh Shah, who on 9 June 2009 will have served ten years as a Director, will be retiring from the Board at the Company's forthcoming Annual General Meeting in July.

Directors submit themselves for reappointment by shareholders at the first Annual General Meeting following their appointment by the Board and at least every three years thereafter. This is in accordance with the Combined Code.

The Directors submitting themselves for reappointment at this year's Annual General Meeting will be Sir David Omand, Sir Nigel Essenhigh and Justin Crookenden. In addition, Lord Hesketh, who has been a Director since 1993, also submits himself for reappointment on an annual basis as required by the Combined Code. None of these Directors has a service agreement with the Company with an unexpired term, each having letters of appointment that are terminable at will at any time.

Their fellow Board members unanimously recommend members to vote in favour of the Non-Executive Directors standing for reappointment, having rigorously evaluated their performance and the contribution they make to the work and effectiveness of the Board. The Accompanying Notes to the Notice of Annual General Meeting (see page 112) explain why the Board is recommending their reappointment.

Directors' interests in contracts

At the date of this Report, there is no contract or arrangement with the Company or any of its subsidiaries that is significant in relation to the business of the Group as a whole in which a Director of the Company is materially interested.

Significant shareholdings

As at 19 May 2009, the Company had been notified in accordance with Chapter 5 of the Disclosure and Transparency Rules of the following major interests in voting rights attached to its ordinary shares (which represent interests in 3% or more of its issued ordinary share capital).

Name	Number of 60p ordinary shares	%
Schroders plc	20,123,434	8.76
Standard Life Investments Limited	15,502,125	6.75
Lloyds Banking Group plc	13,837,144	6.03
Ameriprise Financial, Inc.	11,483,477	5.00
JP Morgan Chase & Co	11,376,214	4.95
Resolution Investment Services Limited	9,339,302	4.07
Legal & General Group plc	9,095,018	3.96

Employee share schemes

The All Employee Share Ownership Plan

The Company has an All Employee Share Ownership Plan, which is open to all UK employees (including Executive Directors) who meet the necessary service criteria. Under the Plan, employees can buy Company shares in the market out of pre-tax income. The Plan allows the Company to award free and/or matching shares to participants, though the Company has not yet done so. Shares are bought via a tax-approved employee trust which holds them on behalf of the individual participants. The shares must generally be kept in trust for at least three years to obtain any tax advantages, and for five years to obtain maximum tax advantages.

The Babcock 2003 Long-Term Incentive Plan ('the L-TIP')

This is the Plan that has been used since 2003 to make performance-linked share awards to a limited number of Directors and senior employees in the form of options granted at a nominal or nil price. Further details of the Plan are to be found in the Remuneration report. It is proposed, subject to shareholder approval at the forthcoming Annual General Meeting, to introduce a Performance Share Plan ('the PSP') for use in place of the L-TIP. Further details of the PSP can be found in the Remuneration report and in Appendix 1 to the Notice of Meeting on pages 115 to 118.

The Babcock 1999 Approved Executive Share Option Scheme and the Babcock 1999 Unapproved Executive Share Option Scheme ('the 1999 Schemes')

Option grants under these Schemes were performance-linked. No grants under these Schemes have been made to Directors since 2003 or to other employees since 2004. The Schemes expire on 29 July 2009 after which no further grants may be made under them. It is proposed, subject to shareholder approval at the forthcoming Annual General Meeting, by way of replacing the 1999 Approved Share Option Scheme, to introduce a Company Share Option Plan ('the CSOP'), which would be HM Revenue & Customs approved. Further details of the CSOP can be found in Appendix 2 to the Notice of Meeting on pages 119 to 122.

In respect of the L-TIP and the 1999 Schemes mentioned above, shares are held by the trustees of the Babcock Employee Share Trust and the Peterhouse Employee Share Trust. The trustees of these Schemes do not intend to exercise the voting rights attached to the shares held by them. As at 20 May 2009, the total number of ordinary shares in such trusts was 948,095, which represented 0.41% of the Company's issued share capital. Shares are also held by the trustees of the All Employee Share Ownership Plan mentioned above. The trustees only exercise any voting rights attached to those shares in accordance with directions from the employee on whose behalf they are held.

The trustees of the Babcock Employee Share Trust waive dividends on shares held by them – see note 27 on page 92.

Authority to purchase own shares

At the Annual General Meeting in July 2008, members authorised the Company to make market purchases of up to 22.9 million of its own ordinary shares of 60p each. That authority expires at the forthcoming Annual General Meeting in July 2009 when a resolution will be put to renew it so as to allow purchases of up to a maximum of 22.95 million shares (just under 10% of the Company's current issued share capital). No shares in the Company have been purchased by the Company in the period from 10 July 2008 (the date the current authority was granted) to the date of this Report. The Company currently does not hold any treasury shares.

Details of purchases of the Company's shares made in the year to 31 March 2009, or since then to the date of this Report, by the Babcock Employee Share Trust and the Peterhouse Employee Share Trust are to be found in note 27 on page 92.

Research and development

The Group commits resources to research and development to the extent management considers necessary for the evolution and growth of its business.

Charitable and political donations

During the year the Group donated £129,000 (2008: £105,000) to charitable organisations. No donations were made during the year for political purposes.

Supplier payments

The Group's policy is to pay suppliers in accordance with practices or arrangements agreed with them. The Company itself had £703,000 in trade creditors at 31 March 2009 (representing 34 creditor days) and £33,000 in creditors (38 creditor days) at 31 March 2008.

Qualifying third party indemnity provisions

Under their respective Articles of Association, the Directors of the Company and of Group subsidiary companies are, and were during the year to 31 March 2009, entitled to be indemnified by respectively the Company and those UK subsidiaries of which they are or were Directors against liabilities and costs incurred in connection with the execution of their duties or the exercise of their powers, to the extent permitted by the Companies Act 2006. The Directors also disclose qualifying third party indemnity provisions entered into between the Company and two of the former Directors (Mr A Bethel and Mr K Thomas) of International Nuclear Solutions PLC (a subsidiary of the Company) on 6 and 8 November 2007, which were in force at the date of approval of this Report. The Company also entered into deeds with the two former independent Directors of International Nuclear Solutions PLC on 22 January 2008, under which the Company agreed to pre-pay any reasonable costs or expenses incurred by those Directors that are not pre-paid by the Company's directors and officers insurance policy in respect of any claim made against them and which is connected with their positions as Directors of International Nuclear Solutions PLC. If the Director does not successfully defend any such claim, the Director must repay the Company the amount so pre-paid. Qualifying pension scheme indemnity provisions are also in place for the benefit of Directors of the Group companies that act as trustees of Group pension schemes.

Persons with contractual or other arrangements with the Group which are essential to the business of the Group

The majority of the Group's revenue is with the United Kingdom Ministry of Defence through various contracts across different businesses, which contracts together are essential to the business of the Group as a whole. Certain other companies in the Group have contractual or other arrangements with third parties which, though not essential to the Group's business as a whole, are essential to their own respective businesses, namely National Grid (Networks division), Network Rail (Rail division) and, in South Africa, Eskom and Volvo.

Significant agreements that take effect, alter or terminate upon a change of control

The following agreements are those agreements which the Company considers to be significant to the Group as a whole that contain provisions giving the other party a specific right to terminate them if the Company is subject to a change of control following a takeover bid.

Marine

Partnering Agreement dated 29 August 2002 between (1) The Secretary of State for Defence (2) Babcock Marine (Clyde) Limited (formerly Babcock Naval Services Limited) and (3) Babcock International Group PLC

Under the Partnering Agreement (as subsequently amended), Babcock Marine (Clyde) Limited provides services to the Ministry of Defence (MoD) in relation to the operation of HM Naval Base Clyde. In 2005, the period of the Agreement was extended and it will now expire in 2013.

In the event of a change of majority control of Babcock International Group PLC, the MoD may request information regarding the new controlling entity and in certain circumstances, including if it is not satisfied as regards the financial affairs and standing of the new entity, serve a 'Change in Circumstance' notice, and thereafter can elect to terminate the Agreement.

Articles of Association of Devonport Royal Dockyard Limited and Rosyth Royal Dockyard Limited

The Articles of Association of Devonport Royal Dockyard Limited (DRDL) and Rosyth Royal Dockyard Limited (RRDL), both subsidiaries of the Company, grant the MoD as the holder of a special share in each of those companies certain rights in circumstances which are deemed to constitute unacceptable ownership, influence or control over the company concerned and which are contrary to the essential security interest of the UK, including circumstances where any non-UK persons directly or indirectly acquire control over more than 30% of the shares of the Company. Such rights include the right to require the sale of shares in, and the right to remove Directors of, the company concerned. The Company believes that RRDL presently has the right under its Articles of Association to request that the special share held by MoD in RRDL be redeemed.

Networks

Joint Venture Agreement dated 24 November 2006 between (1) Babcock Networks Limited, (2) AMEC Group Limited and (3) Mott MacDonald Limited to form the unincorporated joint venture known as the Energy Alliance

On 16 March 2007, Babcock Networks Limited, AMEC Group Limited and Mott MacDonald Limited, acting jointly and severally as the Energy Alliance, entered into the Area Alliance Agreement with National Grid Electricity Transmission PLC for the provision of services to upgrade National Grid's transmission network as part of its Capital Investment Programme.

Under the terms of the Energy Alliance joint venture agreement, if any party undergoes a change of control, then the other parties may suspend or exclude that party from further participation in the joint venture and by extension the Area Alliance Agreement.

Defence

Joint Venture Agreement dated 16 November 2005 between (1) Babcock Support Services Limited and (2) DynCorp International LLC to form Babcock DynCorp Limited

On 16 November 2005, Babcock DynCorp Limited entered into the Regional Prime Contract (East) with The Secretary of State for Defence acting through the agency of Defence Estates to provide property maintenance and capital works across the MoD Estate in the East of England.

Under the terms of the Babcock DynCorp joint venture agreement, if either party undergoes a change of control, the other party may require that party to sell its shares in the joint venture at a fair value.

Group

Facility agreement

The Group entered into a £600 million credit facility on 9 May 2007 which provides that, in the event of a change of control of the Company, the lenders may within a certain period call for the prepayment of any outstanding loans and cancel the credit facility.

Share plans

The Company's share plans contain provisions as a result of which options and awards may vest and become exercisable on a change of control of the Company in accordance with the rules of the plans.

Contracts with employees or Directors

A description of those agreements with Directors that contain provisions relating to payments in the event of a termination of employment following a change of control of the Company is set out on page 60. One senior employee, not a Director, has a service contract with equivalent provisions to those agreements. One other senior employee, who is not a Director of the Company, has an agreement providing for payment as described on page 60 in the event of a dismissal (including constructive dismissal) by the Company within 12 months following a change of control, but does not have the right voluntarily to resign and claim any payment.

Matters more fully dealt with in other sections of the Annual report and accounts

Some other matters that have to be covered in a Directors' report are dealt with in other sections of this Annual report and accounts (and are to be treated as incorporated into this Report), namely:

Directors' share interests: These are to be found in the table on page 55.

Employees: The Company's approach to employee matters (including employee communication, public interest disclosure, ethical standards and its policy on disabled employees and employee involvement) are dealt with in the Corporate responsibility section on pages 22 to 25. In the year ended 31 March 2009, the Group employed an average of 16,389 staff worldwide, approximately 91% of whom were located in the UK.

Principal subsidiary, joint venture and associated undertakings: These are shown on page 107.

Treasury management, financial risk management and the use of financial instruments: This is covered on page 29 and in Note 2 to the Group financial statements.

Changes in asset values: These are dealt with in the financial statements.

Acquisitions and disposals: Information regarding the Group's acquisitions and disposals during the course of the year is set out in notes 32 and 33 on pages 97 and 98 and they are also referred to in the Business review appearing on pages 1 to 33.

Share capital and rights attaching to the Company's shares

Under the Company's Articles of Association, any share in the Company may be issued with such rights or restrictions, whether in regard to dividend, voting, return of capital or otherwise, as the Company may from time to time by ordinary resolution determine (or, in the absence of any such determination, as the Directors may determine). The Directors' practice is to seek annual authority from shareholders at each year's Annual General Meeting to allot shares (including authority to allot free of statutory pre-emption rights) up to specified amounts and also to buy back the Company's shares, again up to a specified amount.

At a general meeting of the Company, every member has one vote on a show of hands and on a poll one vote for each share held. The notice of general meeting specifies deadlines for exercising voting rights either by proxy or by being present in person in relation to resolutions to be proposed at a general meeting.

No member is, unless the Board decides otherwise, entitled to attend or vote, either personally or by proxy, at a general meeting or to exercise any other right conferred by being a shareholder if they or any person with an interest in their shares has been sent a notice under section 793 of the Companies Act 2006 (which confers upon public companies the power to require the provision of information with respect to interests in their voting shares) and they or any interested person have failed to supply the Company with the information requested within 14 days' after delivery of that notice. The Board may also decide that no dividend is payable in respect of those default shares and that no transfer of any default shares shall be registered. These restrictions end seven days after receipt by the Company of a notice of an approved transfer of the shares or all the information required by the relevant section 793 notice, whichever is the earlier.

The Directors may refuse to register any transfer of any share which is not a fully-paid share, although such discretion may not be exercised in a way which the Financial Services Authority regards as preventing dealings in the shares of the relevant class or classes from taking place on an open or proper basis. The Directors may likewise refuse to register any transfer of a share in favour of more than four persons jointly.

The Company is not aware of any other restrictions on the transfer of shares in the Company other than certain restrictions that may from time to time be imposed by laws and regulations (for example, insider trading laws).

The Company is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities or voting rights in the Company.

At the date of this report, 229,574,959 ordinary shares of 60p each have been issued and are fully paid up and are quoted on the London Stock Exchange. During the year ended 31 March 2009, options were exercised pursuant to the Company's share option schemes, resulting in the allotment of 218,590 new ordinary shares. No new ordinary shares have been allotted under these schemes since the end of the financial year to the date of this report. 0.41% of the issued share capital is currently held within employee benefit trusts for the use of satisfying employee share options or share awards. There are no securities in issue which carry special rights with regard to control of the Company.

Appointment and powers of Directors

A Director is appointed by ordinary resolution at a general meeting of ordinary shareholders. The Directors acting as a Board also have the power to appoint a Director, but any person so appointed must be put up for reappointment by shareholders at the first Annual General Meeting following his or her appointment by the Board.

Subject to its Articles of Association and relevant statutory law and to any directions as may be given by the Company in general meeting by special resolution, the business of the Company is managed by the Directors, who may exercise all powers of the Company that are not required to be exercised by the Company in general meeting.

Articles of Association

The Company's Articles of Association may only be amended by a special resolution at a general meeting of shareholders. They are available for inspection online at www.babcock.co.uk and can also be seen at the Company's registered office.

Directors' duty to avoid conflicts of interest

The Company has adopted a formal procedure for the disclosure, review, authorisation and management of Directors' conflicts of interest and potential conflicts of interest in accordance with the provisions of the Companies Act 2006. The procedure requires Directors formally to notify the Board (via the Company Secretary) as soon as they become aware of any actual or potential conflict of interest with their duties to the Company or of any material change in existing actual or potential conflicts that may have been authorised by the Board. Notified actual or potential conflicts will be reviewed by the Board as soon as possible. The Board will consider whether a conflict or potential conflict does, in fact, exist and, if so, whether it is in the interest of the Company that it be authorised and, if so, on what terms. In making their judgement on this, the other Directors must have regard to their general duties to the Company. A register is maintained for the Board of all such disclosures and the terms of any such authorisation. Authorisations may be revoked, or the terms on which they were given varied, at any time. Cleared conflicts will in any event be reviewed annually by the Board. In the event of any actual conflict arising in respect of any matter, mitigating action would also be considered (for example, non-attendance of the Director concerned at all or part of Board meetings and non-circulation to him of relevant papers). To launch the formal process, a baseline assessment was carried out of all existing actual or potential conflicts of Board members as of 1 October 2008.

Auditors

PricewaterhouseCoopers LLP are willing to continue in office as independent auditors of the Company, and a resolution to reappoint it will be proposed at the forthcoming Annual General Meeting.

Disclosure of relevant audit information

So far as the Directors who are in office at the time of the approval of this Report are aware, there is no relevant audit information (namely, information needed by the Company's auditors in connection with the preparation of their auditors' report) of which the auditors are unaware. Each such Director has taken all steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the auditors are aware of that information.

Directors' responsibility statement

The Directors are responsible for preparing the Annual Report, the Remuneration report and the Group's and the Company's financial statements in accordance with applicable law.

Company law requires the Directors to prepare financial statements for each financial year. In accordance with that law the Directors have prepared the Group's financial statements in accordance with International Financial Reporting Standards (IFRS) (as adopted in the European Union), and the Company's financial statements and the Directors' Remuneration report in accordance with applicable law and UK Generally Accepted Accounting Practice (UK GAAP). The Group's and the Company's financial statements are required by law to give a true and fair view of the state of affairs of the Group and the Company and of the profit and loss of the Group for that year. In preparing those financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state that the Group's financial statements comply with IFRS and that with regard to the Company's financial statements that applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Company will continue in business.

Each of the Directors (whose names and functions are set out on pages 34 and 35) confirms that to the best of his knowledge:

- the Group financial statements (set out on pages 62 to 100), which have been prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group taken as a whole; and
- the Business review contained on pages 1 to 33 includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and the Company and enable them to ensure that the Group's financial statements comply with the Companies Act 2006 and Article 4 of the IAS Regulation and that the Company's financial statements and the Directors' Remuneration report comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and the Company, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Going concern basis

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements.

Internal control

The Board, through the Audit and Risk Committee, has reviewed the assessment of risks and the internal control framework that operates in the Group and has considered the effectiveness of the system of internal control in operation in the Group for the year covered by this report and up to the date of its approval by the Board of Directors.

The Combined Code

The Board's statement as to compliance with the principles and provisions of the Combined Code on Corporate Governance of the Financial Reporting Council ('the Combined Code') is set out on pages 42 to 45. As required by the Listing Rules of the Financial Services Authority, the auditors have considered the Directors' statement of compliance in relation to those points of the Combined Code which are specified for their review.

Approval of report

The Directors' Report for the year ended 31 March 2009, from pages 1 to 47 of this Annual report document, has been approved by the Board of Directors on 20 May 2009 and signed on its behalf by:

A N Dungate
Company Secretary

20 May 2009

Statement on Corporate Governance

Compliance Statement

The Company considers that it complied with the provisions of section 1 of The Combined Code on Corporate Governance 2006, as updated, (the 'Combined Code') during the year under review and continues to do so.

On 1 June 2008, Mike Turner was appointed as a Non-Executive Director of the Company and on 1 November 2008 he took over as Non-Executive Chairman from Gordon Campbell. He previously served as a Non-Executive Director of the Company from 1996 to December 2005 and was a Director of a trading partner of the Group (BAE Systems PLC). The Board is, however, of the view that after a period of nearly three years out of office at Babcock and in light of his strength of character, robust and challenging approach and firm independence of view they can reasonably regard, and do so regard, Mr Turner as having been independent for Combined Code purposes when he was appointed Chairman.

On 9 June 2008, Dipesh Shah completed nine years' service as a Non-Executive Director (though none of the Executive Directors has been in post with him throughout the period since his appointment in June 1999). He served on the Remuneration Committee (as Chairman), the Audit and Risk Committee and the Nominations Committee throughout the year under review, but stood down from those committees on 31 March 2009. He will be retiring from the Board at the forthcoming Annual General Meeting in July. Although for some of the year under review he had served a little over nine years as a Director the Board continued to consider him as independent especially given the relatively short period involved.

For those who may differ from the Board in its view as to the independence of Mr Shah by virtue of his length of service, the provisions of the Code requiring a balance between independent Non-Executive Directors and non-independent Directors (excluding the Chairman) was not, if he is so viewed, complied with. However, even on this view, this balance was restored on 1 April 2009 with the appointment of Sir David Omand as an additional independent Non-Executive Director. Also, on this alternative view, the Remuneration and Audit and Risk Committees would not have consisted throughout the year under review solely of independent Non-Executive Directors. However, the three other members of those committees were, on any view, independent throughout the year and Mr Crookenden (who was appointed Chairman of the Committee on 1 April 2009) led the 2008/9 review of executive remuneration described in the Remuneration report for the year.

The rest of this statement sets out how the principles of good governance in the Combined Code have been implemented.

Chairman and Chief Executive functions

There is a clear division of responsibilities between the Chairman and Chief Executive which is set out in a statement of their respective roles and responsibilities approved by the Board. A copy of this is available on the Company's website (www.babcock.co.uk).

Senior Independent Director

Mr Rennocks is, and was throughout the year, recognised by the Board as the Senior Independent Director to whom concerns can be conveyed by shareholders if they have concerns which have not been resolved through the normal channels of Chairman, Chief Executive or Finance Director.

The Board and Board balance

The Company has a Non-Executive Chairman, a non-independent Non-Executive Deputy Chairman and, two full-time Executive Directors. In addition, throughout the year there were four Non-Executive Directors and since 1 April 2009, with the appointment of Sir David Omand, there have been five. Of the current Non-Executive Directors (other than the Deputy Chairman), at least four (that is, half the Board excluding the Chairman) are considered by the Board to be independent: Sir Nigel Essenhigh, Mr Rennocks, Mr Crookenden (each of whom served throughout the year under review) and Sir David Omand. The position as regards Mr Shah, whom the Board also regarded as independent, and who is retiring from the Board at the forthcoming Annual General Meeting, is explained above.

Refreshing of the Board

Since the last report, the Chairmanship of the Company has changed, a new independent Non-Executive Director has been appointed, and a long-serving Non-Executive has announced his intention to retire from the Board at the forthcoming Annual General Meeting in July. The other three continuing independent Non-Executive Directors have served between three and half years and seven years in office.

Directors are normally reappointed at the first Annual General Meeting following their appointment by the Board and subsequently have to offer themselves for reappointment at least every three years. It is the Company's policy to review rigorously the reappointment of Non-Executive Directors who have served more than six years.

As required by the Combined Code, the Board explains, in notes accompanying the notice of meeting on page 112, why it recommends the reappointment of the Non-Executive Directors proposed for reappointment at the forthcoming Annual General Meeting (Sir Nigel Essenhigh, Justin Crookenden, Lord Hesketh and Sir David Omand). The Chairman confirms in those notes, as required by the Combined Code, that, having formally evaluated their performance, the Board is of the view that they continue to be effective and to demonstrate commitment to their roles, including commitment of time for Board and, where applicable, committee meetings and other duties.

Board procedures and attendance

During the year to 31 March 2009, there were nine scheduled meetings and one short notice meeting of the full Board. Attendance was as follows:

Director	Scheduled Board meetings attended	Short notice Board meetings attended
Mike Turner (from 1 June 2008)	8 out of 8	1 of 1
Lord Hesketh	6 out of 9	–
Peter Rogers	9 out of 9	1 of 1
William Tame	9 out of 9	1 of 1
John Rennocks	9 out of 9	1 of 1
Dipesh Shah	8 out of 9	1 of 1
Sir Nigel Essenhigh	9 out of 9	1 of 1
Justin Crookenden	9 out of 9	1 of 1
Gordon Campbell (up to 31 October 2008)	5 out of 5	1 of 1

The Board has also given authority for the holding of ad hoc meetings of any two Directors to deal with matters generally in accordance with delegated authorities approved by the Board, including a Finance Committee. It also from time to time establishes special committees for specific purposes, for example in connection with specific acquisitions.

The Chairman regularly meets Non-Executive Directors without Executive Directors or other managers present.

During the year, a review of the performance of the Board as a whole, its committees and individual Directors was carried out. The Company Secretary, using as a starting point the results of an evaluation process carried out in the preceding financial year using an independent facilitator, conducted a series of individual confidential interviews with each Board member in February 2009. The results of those interviews were reported to the Chairman and made available to and discussed by the Board. The review concluded that the Board and its committees, and individual Directors, continued to work well and effectively. It was agreed that strategy and succession planning should continue to be areas of particular Board focus.

The Chairman's performance was evaluated by the Remuneration Committee and was within the scope of the confidential interview process described above.

All Directors have full and timely access to information.

Change in Chairman's significant external commitments

Between 1 April 2008 and his retirement from the Board on 31 October 2008 there were no changes to (former Chairman) Gordon Campbell's significant external commitments. Since his appointment as Chairman on 1 November 2008, there have been no changes to Mike Turner's significant external commitments.

Board Committees

Details of the membership and operation of the Audit and Risk Committee and its work can be found on pages 46 and 47 and of the Remuneration Committee in the Remuneration report.

Nominations Committee

In the year to 31 March 2009, the Nominations Committee consisted (unless otherwise stated, throughout the year) of:

M Turner (Committee Chairman) from 1 November 2008
G Campbell (Committee Chairman) until 31 October 2008
D J Shah
J Rennocks
Sir Nigel Essenhigh
The Rt Hon Lord Hesketh
J Crookenden

On 1 April 2009, Sir David Omand became a member of the Committee.

Membership of this Committee is open to all the Non-Executive Directors provided that at its meetings there is a majority of independent Non-Executive Directors. Its terms of reference are available on the Company's website. During the year, the Committee selected a new independent Non-Executive Director, Sir David Omand, who took office on 1 April 2009. In recruiting Sir David the services of a leading executive search firm were used, the selection process being led on behalf of the Nominations Committee by the Chairman and the Senior Independent Director.

Discussions relating to management succession planning were held in the course of Board meetings or in meetings between the Group Chairman and the Non-Executive Directors (as informal meetings of members of the Nominations Committee) in the absence of executive management.

Whistle-blowing arrangements
These arrangements are dealt with in the Corporate responsibility section on page 22.

Non-audit fees
The Audit and Risk Committee Chairman must authorise any engagement of auditors on non-audit work that would entail their being paid fees in excess of 20% of the audit fee in any year. Before giving that authority, he considers potential conflicts and the possibility of actual or perceived threats to the independence of the external auditors. Authority is given only when he considers it is in the Company's interest to do so.

Contact with shareholders
The Group has a full-time Head of Investor Relations whose role it is to ensure that there is regular dialogue between the Company, its principal shareholders and the wider market so that there is a clear understanding of their respective views and that investors have a good understanding of the Company and its management. The Chief Executive and the Finance Director regularly meet institutional shareholders and analysts. Reports of these meetings are sent to the Board, which also receives at each of its meetings an Investor Relations Report from the Head of Investor Relations. In addition, during the year the Company commissioned from Makinson Cowell a survey of a selection of the Company's major shareholders as to their perceptions of the Group, its management and its future direction, the results of which were formally presented to the Board. The Remuneration Committee also sought the views of leading shareholders on the changes to annual bonus and long-term incentive arrangements described in the Remuneration report.

The Annual General Meeting is also used as an opportunity for communication with shareholders. All of the Company's Directors attended the 2008 Annual General Meeting.

The Company's website keeps shareholders abreast of developments. It is regularly updated with press releases and analyst presentations. Shareholders can register on the website to be sent news releases automatically.

Information and training for Directors
The Company makes arrangements for new Non-Executive Directors to receive detailed business briefings as regards the Group's operations and arranges induction visits to the Group's principal sites. Director training for new directors, when appropriate, is arranged with external providers.

Non-Executive Directors may at any time make visits to Group businesses or operational sites and Board visits are also made to sites. Presentations on the Group's businesses and specialist functions are made to the Group Board from time to time.

Non-Executive Directors receive copies of all minutes of meetings of the Group Executive Committee and regularly receive the operating reports sent to the Group head office by the business operations. General Director training that might be of potential interest or relevance to established Directors can be arranged on request, for which the Company is willing to pay. The Company Secretary briefs Board members about significant changes in the law affecting their duties as Directors.

Internal controls, control environment, procedures and monitoring
The Board acknowledges its overall responsibility for the Group's system of internal controls, and for monitoring its effectiveness.

There is a written delegation of matters from the Board to committees of one or more Directors. The Board retains responsibility for:

- setting overall strategy;
- approving annual budgets;
- authorising business acquisitions and disposals;
- approving significant contracts outside the ordinary course of business; and
- setting treasury and borrowing policy.

There has been a process for identifying, evaluating and managing significant risks throughout the year to 31 March 2009 and up to the date of the approval of the financial statements for that year. The Board considers the system to be effective and in accordance with Internal Controls: Guidance for Directors on the Combined Code ('the Turnbull Guidance').

The internal control system is monitored through review visits by Group management and the internal audit service provided by Ernst & Young LLP, which acts under the overall control and direction of the Audit and Risk Committee. The system covers any material joint ventures or associates.

The Board through its Audit and Risk Committee reviews the effectiveness of the process formally at least once a year. The Committee also reviews aspects of the system on an ongoing basis at its meetings as part of its review of internal audit reports and of risk management reports and against operational outcomes. It seeks the views of internal and external auditors upon the control system and how it compares with processes in other companies.

The system comprises principally:

- a risk identification, evaluation and management process;
- clear delegations and limits of authority;
- clear authorisation and review procedures;
- independent internal audits;
- regular review by the Audit and Risk Committee of risk registers, internal and external audit reports and fraud management reports;
- an independent whistle-blowing hotline available to employees;
- regular divisional operating reviews attended by Group executive management;
- regular contract review meetings;
- monthly reporting of results against budget and forecast, with variances explained;
- an annual presentation on tax matters to the Board;
- regular reports to the Board on the Group's pension scheme exposures and risks;
- an annual report to the Board of the Group's insurance programme;
- monthly reports on disputes and litigation;
- a succession planning process;
- monthly reports to a Safety Leadership Team comprised of the Chief Executive and divisional Managing Directors on health, safety and environmental matters; and
- bi-annual reports to the Board on health, safety and environmental matters.

The Group's systems can, however, only seek to manage, rather than eliminate, the risk of failure to achieve business objectives, as any system can only provide reasonable, not absolute, assurance against material misstatement or loss.

Identification and evaluation of risks and control objectives

The identification and evaluation of risks and control objectives is also addressed on pages 26 to 29.

Budgets

Comprehensive systems are in place to develop annual budgets and medium-term financial plans. The budgets are reviewed by central management before being submitted to the Board for approval. Updated forecasts for the year are prepared at least quarterly. The Board is provided with details of actual performance each month compared with budgets, forecasts and the prior year, and is given a written commentary on significant variances from approved plans.

Audit and Risk Committee

The members

The members of the Committee, who each served throughout the year to 31 March 2009 and who were considered by the Board to be independent (as explained on page 42), are:

J Rennocks (Committee Chairman)
Sir Nigel Essenhigh
J Crookenden
D Shah (retired from the Committee on 31 March 2009)

Sir David Omand (joined the Committee on 1 April 2009)

Biographical details of the members are set out on pages 34 and 35.

Mr Rennocks is a former Finance Director of Corus Group PLC and is considered by the Board to have the necessary recent and relevant financial experience for his role as Committee Chairman.

Attendance at Meetings in the year to 31 March 2009:

Director	Committee meetings attended
John Rennocks	4 out of 4
Dipesh Shah	3 out of 4
Sir Nigel Essenhigh	4 out of 4
Justin Crookenden	4 out of 4

How it operates

The Committee's formal terms of reference are available on the Company's website at www.babcock.co.uk.
Its responsibilities include:

- appointing internal and external auditors and assessing their independence;
- deciding audit fees and approving fees in respect of non-audit services provided by the external auditor (or by any firm providing internal audit services);
- ensuring the provision of non-audit services does not impair auditors' independence or objectivity;
- agreeing the nature and scope of internal and external audits;
- reviewing the external auditor's management letter and management's response;
- ensuring that the internal audit function is adequately resourced and has appropriate standing within the Company;
- considering management's response to any major external or internal audit recommendations;
- reviewing the Company's procedures for handling allegations from whistle-blowers;
- reviewing the effectiveness of systems for internal financial control, financial reporting and risk management; and
- reviewing, and challenging where necessary, the actions and judgements of management, in relation to the interim and annual financial statements.

The Company Secretary is secretary to the Committee. The Committee invites the Group Chairman, Chief Executive, Finance Director and Group Financial Controller to attend its meetings. Non-Executive Directors not sitting on the Committee are also welcome to attend.

The Group Risk Manager attends Committee meetings for discussion of Group risk reports and related items.

Ernst & Young LLP provides internal audit services to the Company. PricewaterhouseCoopers LLP is the Group's external auditor.

Both auditors usually attend all or part of the Committee's meetings.

The Committee Chairman meets PricewaterhouseCoopers LLP and Ernst & Young in the absence of executive management, and other Committee members have the opportunity to do so.

What it did in the year
The Committee met formally four times in the year to 31 March 2009.

In the year, the Committee:

- reviewed the preliminary and interim statements of results, having considered any matters calling for judgement in their preparation;
- reviewed proposed announcements relating to preliminary and interim results;
- reviewed the financial statements for the year ended 31 March 2008 and the half year ended 30 September 2008 and internal and external auditors' comments in connection with them;
- evaluated the effectiveness of internal controls;
- considered reports specifically evaluating the scope for fraud in the Group's operations and misreporting of results by business units;
- reviewed internal audit reports from Ernst & Young LLP and external audit reports from PricewaterhouseCoopers LLP and duly considered any matters raised in them;
- considered the levels of audit fees and non-audit fees paid to auditors;
- agreed internal and external audit plans;
- reviewed the arrangements for confidential whistle-blowing;
- reviewed the Group risk standard and its implementation, together with Group risk reports; and
- conducted a going concern review.

Remuneration report

This Remuneration report has been prepared on behalf of the Board by the Remuneration Committee. The Board considers that in all its activities the Remuneration Committee has adopted the principles of good governance as set out in the Combined Code and complies with the Listing Rules of the Financial Services Authority, the relevant schedules of the Companies Act and the Directors' Remuneration Report Regulations, 2002 ('the Regulations'). The Board's view as to the independence of the members of the Committee is discussed further in the Corporate Governance section of the Directors' report on page 42.

The report is divided into audited and unaudited information. The Regulations require the Company's auditors to report that the 'Audited information' in this report has been properly prepared in accordance with the Regulations.

The Remuneration report will be submitted for shareholder approval at the Annual General Meeting on 9 July 2009.

Overview

During the year to 31 March 2009, Babcock continued the strong performance seen now for several years, maintaining strong cash flow and reducing net debt.

Management is tasked with continuing this performance in the coming year and over the longer term. This will be against the backdrop of a general environment which, at least in the medium term, looks set to remain uncertain and difficult. Management will seek to meet the challenge by, amongst other things:

- continued development and implementation of appropriate strategic plans that address the short and longer term risks, needs and changing environment for Babcock as it continues to increase in size;
- preserving, improving and building upon Babcock's existing strengths and customer relationships;
- positioning Babcock for expansion into new business and customer markets where the Group's core skills can be exploited;
- building strategic alliances that will further those expansion plans;
- addressing decisively any areas of business weakness;
- ensuring that good management succession planning for the medium and longer term is in place and that Group-wide management training meets the needs of Babcock's increasing size and the challenges it faces; and
- securing continued order book growth by building on Babcock's performance record, improving bidding processes and enhancing customer satisfaction.

The Committee's approach to setting the structure of remuneration packages for executives, including the proposals for changes, described in this Report is designed to underpin the effective and proper management of these risks and challenges and to reward executive management fairly if it is successful in continuing the track record of strong performance and long-term growth prospects enjoyed by Babcock and its shareholders over recent years. The Committee believes that this is achieved by:

- increasing the emphasis on performance-related rewards, particularly in the form of share-based incentives that align management interests more closely with shareholders and ensure that they are exposed to the longer term impact (both risks and benefits) of their decisions;
- greater use of non-financial measures in bonus plans; and
- ensuring that total remuneration for superior performance is adequately competitive.

The following sections of this Report explain the implementation of this approach more fully.

Committee members

The Committee members who served at any time during the year were as follows (each of them having served throughout the year):

J Crookenden (Chairman since 1 April 2009)

D Shah (Chairman until 31 March 2009 when he retired from the Committee)

J Rennocks

Sir Nigel Essenhigh

(Sir David Omand joined the Committee from 1 April 2009).

The Committee members are all considered by the Company to be independent Non-Executive Directors.

Biographical details of the members are set out on pages 34 and 35.

Attendance at meetings in the year to 31 March 2009

Director	Meetings attended
D Shah	7 out of 7
J Rennocks	7 out of 7
Sir N Essenhigh	6 out of 7
J Crookenden	7 out of 7

What the Committee has done during or in respect of the year to 31 March 2009

The Committee:

- conducted the normal annual review of the basic salaries of Executive Directors and senior managers effective 1 April 2008;
- set the terms of annual bonus schemes for the financial year;
- decided on the level of bonus payments to be made;
- made share awards under the Company's Long-Term Incentive Plan and determined the comparator group for comparative TSR purposes;
- considered the level of vesting of prior year share awards;
- reviewed the level of bonus payable to the Chief Executive and Finance Director;
- considered the impact of exceptional items on annual bonuses;
- decided the terms for former Chairman, Mr Campbell, leaving the Company;
- determined the terms of appointment of the new Chairman;
- carried out a process to select and appoint new remuneration consultants; and
- conducted a full review of the remuneration for Executive Directors and certain senior managers (as explained further in this Report).

What is the Company's remuneration policy?

The Committee strongly believes that the remuneration of executives should dovetail with the key strategic objectives of the business and be aligned with the long-term interests of shareholders. The link between remuneration policy and strategy is made through the performance criteria used in both the annual bonus and long-term incentive schemes. The Committee's intention is that executives have remuneration packages overall that are fair and allow enhanced and fair rewards for the delivery of superior performance. It is the policy of the Committee not to fix high base salaries. Given this, the other components of the remuneration package need to provide significant competitive upside opportunity.

2008/09 review

During the year, the Committee reviewed the Company's executive remuneration practices to ensure they are achieving the objectives of the Company's remuneration policy. The outcome of that review as it affects annual bonus and longer term incentives is described more fully in the following sections of this Report.

In formulating its proposals for remuneration structure from 2009, the Committee was conscious of the economic backdrop and the need to link pay to both the short- and long-term success of the Company. Despite recent economic circumstances, Babcock has continued to deliver strong EPS growth and TSR performance. It is clear to the Committee that the reward opportunities for Babcock executives have lagged behind the Company's growth. The Company is seeking to provide a more competitive upside opportunity for stretching levels of performance consistent with the objectives of the remuneration policy.

A key objective of the revised incentives is to align the Directors' interests more closely with shareholders' long-term interests. To this end the Committee proposes to increase the emphasis on performance-related pay and long-term incentive opportunities by increasing the reward opportunities for superior performance, but without increasing rewards for 'average' or 'median' performance. For example, under the proposed TSR performance target for awards to be made in 2009 under the proposed new Performance Share Plan ('PSP'), vesting at threshold for the element of the award to which it applies would be reduced from 25% (as currently applies under existing L-TIP awards) to 16.7% so that, despite the increased incentive opportunity under that plan for superior performance, the same percentage of salary would be paid for around median performance as would have been paid under the L-TIP. At the same time, the proposed longer term EPS target for 2009 PSP awards will be made more stretching. Similarly, whilst increasing the scope for performance-related annual bonus, the Committee is imposing in the current financial year a requirement on Executive Directors and certain senior managers for mandatory deferral of a significant part (40%) of any future annual bonus earned into shares (no such deferral was previously required). The new bonus arrangements will also include a significant element attributable to non-financial performance metrics to ensure better linkage to Babcock's strategic objectives and management of longer term risks.

How the Committee operates

The Committee meets formally at least three times a year. The Committee also meets on an ad hoc basis as may be necessary.

The Company Secretary attends meetings as secretary to the Committee. The Group Chairman and the Chief Executive attend formal meetings by invitation of the Committee, except when their own remuneration is being discussed. The Deputy Chairman attends some meetings as an observer.

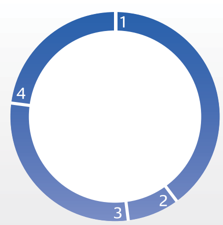
During the year, the Committee received advice from Kepler Associates ('Kepler'), who succeeded the Inbucon Group Limited ('Inbucon') as the independent executive remuneration advisers to the Committee in December 2008. The choice of Kepler to advise it was made solely by the Committee (after a formal selection process conducted by the Committee that involved several potential advisers). Kepler is formally retained, with the Committee's approval, by the Company (acting through the Company Secretary). Neither Kepler nor Inbucon provide or provided other services to Group companies (except in connection with remuneration advice).

Balance of remuneration

The balance of remuneration for Executive Directors is such that the major part of overall remuneration is subject to achieving performance conditions over both the short and long term. The reward mix for the Chief Executive and the Finance Director is shown in the charts below, with long-term incentive awards being valued on a fair value basis. The charts assume that the proposals for a new Performance Share Plan (PSP) are approved by shareholders at the Company's forthcoming Annual General Meeting in July and that PSP awards over shares have a value on grant equal to 150% of the Director's basic salary. The charts are based on fair values of 72% of salary for the annual bonus (including the mandatorily deferred share element now being introduced as described below) and 59% of salary for the proposed Performance Share Plan.

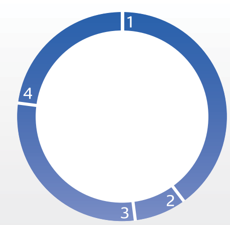
Chief Executive

1	Base Pay	40%
2	Pension	8%
3	Annual Bonus	29%
4	Performance Share Plan	23%



Finance Director

1	Base Pay	40%
2	Pension	8%
3	Annual Bonus	29%
4	Performance Share Plan	23%



Note: Based on remuneration proposals for 2009.

Internal relativity

The Committee is sensitive to the need to set Directors' remuneration having regard to pay and conditions in the Group as a whole and is satisfied that the approach taken by the Company is fair and reasonable in light of current market practice and the best interests of shareholders.

Basic pay

Basic pay is considered in the context of total remuneration at companies that are comparable in terms of size, market capitalisation, revenues and number of employees and other companies in the support services sector. Against these data sources taken as a whole, the Company's total remuneration fair value is around the median and basic pay is below median. Basic pay is normally reviewed annually.

The normal annual review of Executive Director's pay for the year commencing 1 April 2008 resulted in an increase of 4%. For the current year commencing 1 April 2009, the Committee has limited the annual increase to approximately 2% as follows:

Director	Basic pay at 1 April 2009 £'000	Basic pay at 1 April 2008 £'000
P L Rogers (Chief Executive)	479.5	470.0
W Tame (Finance Director)	312.0	305.5

Performance-related rewards

Annual bonus schemes

Annual bonuses for 2008/09 were based on profit, cash flow performance and earnings per share growth, and were up to a maximum of 100% of base salary for Executive Directors. (The Committee decided to bring Mr Tame's bonus potential into line with Mr Rogers', by increasing it from 80% to 100%, effective from 1 April 2008.)

The annual bonuses payable to Mr Rogers and Mr Tame were structured as follows: a bonus of up to 20% of salary was dependent on hitting budgets for profit before tax and operating cash flow. The balance of 80% of salary depended on growth in earnings per share, which was calculated before amortisation of acquired intangibles and exceptional items, with maximum pay-out for this element being achieved at 20% year-on-year growth.

Mr Rogers and Mr Tame earned maximum annual bonus for the financial year 2008/09 and, in accordance with past practice, this is to be paid in full in cash.

Following its remuneration review and to meet its framework for remuneration as described above, the Committee has increased the maximum bonus opportunity for 2009/10 for Executive Directors from 100% to 150% of base salary. However, at the same time, the Executives will be required to defer 40% of any annual bonus earned (i.e. worth up to 60% of salary if the maximum bonus is awarded) into Babcock shares for two years. For the financial year 2009/10 the Committee will set annual bonuses for Mr Rogers and Mr Tame principally by reference to achieving budgets (20% of bonus opportunity), growth in earnings per share (before amortisation of acquired intangibles, but, unless the Committee otherwise decides, after exceptional items) (60% of the bonus opportunity), with maximum bonus only for year-on-year growth of 20% or more. In addition, the bonus for 2009/10 will include within the performance requirements (accounting for up to 20% of the total bonus opportunity) key non-financial metrics that are directly related to the Group's key strategic objectives, risk factors and management challenges described in the 'Overview' section on page 48 above.

It is the Committee's intention to provide rewards that are fair to both executives and shareholders. In light of this, and consistent with current investor sentiment the Committee will commit to review the ongoing financial impact of any prior year activities, and the role of individual executives in such activities, and may make appropriate adjustments to future individual bonus awards to reflect material new information or circumstances that might later have emerged from or about those activities.

Annual bonus schemes for divisional managing directors and certain senior Group executives will in future also provide for increased maximum bonus potential also with a requirement for deferral of 40% of any bonus earned into Babcock shares for two years. For divisional Managing Directors the schemes for 2009/10 will include performance measures dependent on growth in divisional profits and/or achievement of budgeted divisional profits and cash flow according to the objectives for the division concerned and will have non-financial metrics forming a significant part (20%) of the bonus opportunity.

The Committee has discretion to reduce or extinguish bonuses in light of health, safety or environmental performance.

Annual bonuses are not pensionable.

Long-term incentives

Since 2003, qualifying Directors and certain senior Group employees have been granted performance-related long-term incentives in the form of annual awards of nil-price options under the Babcock 2003 Long-Term Incentive Plan ('L-TIP'). Before 2003 they were granted performance-related market-priced share options under the Babcock 1999 Approved and Unapproved Executive Share Option Schemes. Following the 2008/09 remuneration review, the Committee is proposing, subject to shareholder approval at the forthcoming Annual General Meeting in July, to make share-based long-term incentive awards from 2009 onwards under a new Babcock Performance Share Plan 2009 ('PSP') – see further below.

It is the intention of the Company that shares needed to satisfy executive options for Directors and awards under the L-TIP and PSP will be purchased in the market to the extent not already held in the Group's employee share trusts at the date the options or awards are granted or are exercised, unless it is in the interests of the Company to do otherwise. PSP awards may be granted in the form of nil-cost options. PSP Awards may also be combined with an award of HMRC approved options under the proposed Company Share Option Plan ('CSOP') (see page 37 above), in which case the PSP award would be adjusted to take account of the CSOP award; it is not intended that Executive Directors will receive CSOP options this year, but may do so in future years.

Details of options and L-TIP Awards already held by Directors are set out on pages 56 and 57.

During the financial year to 31 March 2009, L-TIP awards were made to each of Mr Rogers and Mr Tame over shares having a market value on award of 100% of their qualifying basic salaries. Awards were also made to a small number of other senior managers. The vesting of the L-TIP awards depends on company performance. Half of each award vests according to comparative Total Shareholder Return performance (against a comparator group selected by the Committee) and half on earnings per share (EPS) growth. The performance criteria are set out in more detail on page 58.

For certain divisional senior managers, but not the Company's Directors, there has been a cash-based long-term incentive scheme focused on divisional performance and with particular features to aid retention. The performance targets under that scheme were set by reference to divisional profit targets and return on capital employed or operating cash flow, as appropriate to the division's business. A similar scheme is in place for senior Group employees (but not the Company's Directors) based on EPS growth over the performance period. Target awards under these cash-based schemes varied between participants but did not normally exceed 100% of salary for on-target performance, with maximum payout for out-performance capped at 150% of salary. Awards under the scheme are not pensionable. It is proposed that from 2009 this scheme will be replaced with future awards being made in the form of share-based incentives under the proposed PSP.

Remuneration report continued

Proposed PSP from 2009

A summary of the principal features of the proposed PSP can be found in Appendix 1 to the Notice of Annual General Meeting (pages 115 to 118 in this document). Under the PSP, the Committee proposes to increase the maximum annual long-term incentive award for Executive Directors (and certain other senior executives) to 150% of salary, but with full vesting accompanied by a commensurate increase in the stretch in EPS performance. In exceptional circumstances (for example, on the recruitment of a new senior executive), awards may be made up to 200% of salary, but the Committee currently has no intention to grant awards of more than 150% of salary. The proposed performance metrics for 2009 PSP awards would be broadly the same as for recent awards under the L-TIP (subject to the increase in EPS growth requirement for full vesting mentioned above), with half of each award vesting according to comparative TSR performance and half according to EPS growth. The Committee also proposes that the peer group for TSR comparison purposes for 2009 awards be the broader FTSE 350 group (excluding financial services companies and investment trusts) and to calibrate performance on a percentage out-performance basis rather than on a ranking basis. Further, in the proposed targets for 2009 PSP awards, the Committee is proposing to reduce the percentage vesting at threshold for both the EPS and TSR elements from 25% to 16.7% so that the same percentage of salary is 'paid' for achieving threshold performance as would be payable for existing L-TIP awards. The increase in opportunity will be fully realised only for achievement of stretch performance, for which the Committee proposes to increase the EPS target. The detailed proposed performance criteria for 2009 are set out on page 58.

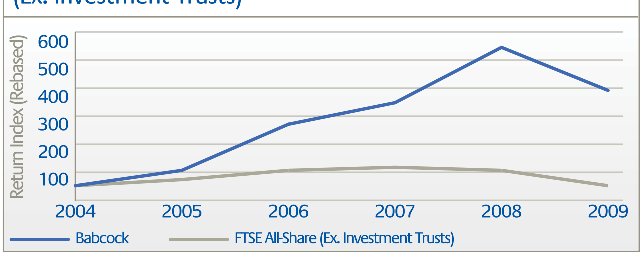
For certain senior Group managers and divisional senior managers, it is proposed, as mentioned above, that the cash-based awards under the long-term incentive schemes for them will be replaced in the future by share-based awards under the PSP. For divisional managers vesting would normally be determined according to divisional performance targets. For senior Group managers the performance targets would be as for PSP awards made to Executive Directors or other targets appropriate to them.

Performance graph

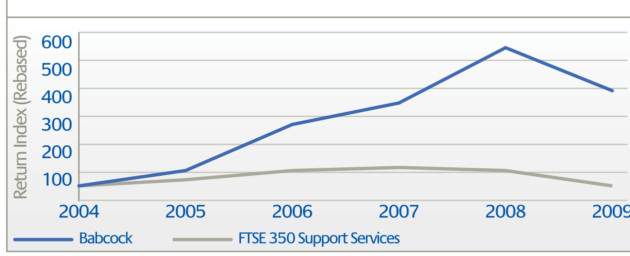
The graphs below were prepared by Kepler Associates. They show the total shareholder return for a holding in the Company's shares for the period from 1 April 2004 to 31 March 2009 relative to a holding of shares representing respectively the FTSE All-Share Index (excluding investment trusts) and the FTSE 350 Support Services Sector. The calculation of the return assumes dividends are reinvested to purchase additional equity. This FTSE All-Share Index (excluding investment trusts) is the same index as has been used for this purpose in earlier Remuneration reports, as it is a broad index that allows comparison of the Company's performance against the performance of the stock market as a whole. Support Services is the sector in which the Company's share price is reported.

Over the five-year period, the Company has substantially out-performed both indexes. An investment of £100 in the Company on 1 April 2004 would have been worth (assuming the dividends were reinvested in further Company shares) £417 at 31 March 2009.

Babcock International vs. FTSE All-Share (Ex. Investment Trusts)



Babcock International vs. FTSE 350 Support Services



Directors' emoluments and compensation (audited)

Director	Salary or fee Year ending 31 March 2009[1] £'000	Other[2] £'000	Cash allowances[3] £'000	Annual bonus £'000	Benefits in kind[4] £'000	Total year ended 31 March 2009 £'000	Total year ended 31 March 2008 £'000
Chairman and Executive Directors							
M Turner (Appointed as a Director on 1 June 2008 and Chairman from 1 November 2008)	119	–	–	–	–	119	–
G A Campbell (former Director, Chairman to 31 October 2008)	151	130	–	–	–	281	250
P L Rogers (Chief Executive)	470	–	64	470	1	1,005	939
W Tame (Finance Director)	306	–	36	306	22	670	578
Non-Executive Directors							
The Rt Hon Lord Hesketh	60	–	–	–	–	60	60
J L Rennocks	43	–	–	–	–	43	42
D J Shah	40	–	–	–	–	40	40
Sir Nigel Essenhigh	35	–	–	–	2	37	36
J N A Crookenden	35	–	–	–	–	35	35
Total	1,259	130	100	776	25	2,290	1,980

(The emoluments disclosed above do not include any amounts for the value of options or other share-based rewards. Details of share-based awards held by the Directors are to be found on pages 56 and 57.)

Notes:

1. Mr Turner's remuneration includes fees at the rate of £35,000 per annum from 1 June to 31 October 2008 and thereafter at the rate of £250,000.

   The comparative remunerations for Mr Rogers and Mr Tame for the year to 31 March 2008 include part paid at the rate before the in-year remuneration reviews referred to in last year's remuneration report (and also for Mr Rogers an amount in lieu of pensions that predated the increase, in October 2007, of the pension supplement referred to under 'Directors' pensions' below). That remuneration review resulted in an increase in basic salary of 6% with effect from 1 October 2007 for Mr Rogers and 7% with effect from 25 June 2007 for Mr Tame. In addition, in the year to 31 March 2008, Mr Tame's bonus was 80% as compared to 100% for the year to 31 March 2009.

2. Amount paid to Mr Campbell on loss of office pursuant to a Compromise Agreement entered into in connection with his leaving the Company.

3. For Mr Rogers, the allowance is pay in lieu of all pension benefits. For Mr Tame, the payment includes £25,000 in lieu of pension benefits on that part of his basic salary as exceeds the earnings cap for the pension scheme (see detailed explanation under Directors' pensions below) and £11,000 in respect of expenses connected with accommodation.

4. For Mr Tame, benefits comprised medical insurance, home to work travel expenses and accommodation benefits. For Mr Rogers, they comprised medical insurance. For Sir Nigel Essenhigh, they comprised home to work travel expenses.

The fees for Lord Hesketh reflected his additional duties as Deputy Chairman. Mr Rennocks' and Mr Shah's fees reflected their additional duties as Chairmen of, respectively, the Audit and Risk Committee and the Remuneration Committee.

Bonus payments and benefits in kind paid to Directors are not pensionable.

Directors' pensions (audited)

Of the Directors, only Mr Tame currently participates in a Group pension scheme. He receives a salary supplement for his earnings in excess of the scheme earnings cap (see the table below).

Mr Rogers receives a supplement in lieu of any pension benefits, which is not taken into account for the purpose of bonus or share awards. It is separately identified in the table on page 53 under 'Cash allowances'. In the year to 31 March 2008 a first step was made towards bringing the supplement up to a level closer to market practice for equivalent executives by increasing it from 8% to 14% of salary but which still left it significantly below market levels. As part of its 2008/09 review of total remuneration, the Committee has completed the move and increased the supplement with effect from 1 April 2009 to 20% to bring it into line with market practice for senior executive directors.

The Company's policy is to remain competitive in the marketplace to attract and retain the calibre of employee it needs. Subject to that, it is not the Company's policy to compensate Directors for changes to the taxation of pensions.

Babcock International Group Pension Scheme ('the Scheme')

Mr Tame is a member of the senior executive tier of the Babcock International Group Pension Scheme. No other Directors are members of the Scheme or receive pension benefits from the Group.

The accrual rate for Mr Tame under the Scheme is one-thirtieth for each year of service, with pension being calculated on his base salary (up to the Scheme's 'earnings cap') in the 12 months prior to retirement at age 60 or above. Membership of the Scheme also entitles him to life assurance cover of four times base salary up to the earnings cap. The earnings cap adopted by the Scheme is the same as the former statutory earnings cap, index-linked in the same way. The Company takes out additional life assurance cover in respect of four times his salary in excess of the earnings cap.

Mr Tame's pension entitlements under the Scheme (defined benefit) are set out in the following table:

Director	Accrued pension at 31 March 2009 £ pa	Increase in accrued benefits excluding inflation during the year ended 31 March 2009	Change in accrued benefits after allowing for inflation £	Transfer value at 1 April 2008 £	Transfer value at 31 March 2009 £	Transfer value of increase in accrued benefits less Director's contributions £	Increase in transfer value less Director's contribution £
W Tame	28,578	4,926	3,743	405,486	467,680	43,665	56,314

1. Inflation has been taken as 5% for the purposes of calculating increases in transfer values and pension earned.
2. The transfer value of the increase in pension accrued is calculated in accordance with Actuarial Guidance Note GN11, and is stated after deducting members' contributions.
3. The figures in the above table make no allowance for the cost of death in service benefits under the Scheme.
4. The figures in the above table make no allowance for any benefits in respect of earnings in excess of the Inland Revenue earnings cap.
5. In calculating the above figures for Mr Tame no account has been taken of any retained benefits which he may have from previous employments.
6. No payments have been made to retired Directors in excess of the retirement benefit to which they were entitled on the date the benefits first became payable or, if later, 31 March 1997.

Other pension arrangements (audited)

Before 1 April 2006, the Company provided a Funded Unapproved Retirement Benefit Scheme (FURBS) for Mr Tame in respect of his salary in excess of the earnings cap. The Company contributed to the FURBS an amount equal to 20% of the excess (including employer's national insurance contributions), with Mr Tame making contributions into the Company's pension scheme on his full uncapped salary. As from April 2006, this was replaced with a salary supplement of 15% of the excess (including employer's national insurance contributions), with Mr Tame contributing into the Company's pension scheme only on capped salary. The value of this supplement in the year to 31 March 2009 was £25,000.

The cost of providing additional life assurance cover was:

Director	2009 £'000	2008 £'000
W Tame	2	2

Non-Executive Directors

The Non-Executive Directors receive only fixed fees. These fees are reviewed against market practice from time to time by the Chairman and the Executive Directors, to whom the task has been delegated by the Board. Fees payable to Non-Executive Directors (other than the Chairman) were last reviewed in October 2006. With effect from 1 April 2009, the fees have been reviewed, in light of market practice at companies of a similar size and in the support services sector, and are now as follows:

Chairman	£255,000
Deputy Chairman	£60,000
Senior Independent Director	£60,000
Chairmanship of Audit and Risk Committee	£12,500
Chairmanship of Remuneration Committee	£7,500
Basic Non-Executive Director's Fee	£47,500

No additional fees are paid for membership of committees.

Directors' interests in shares

The table below shows the holdings of fully paid ordinary shares of 60p each of the Directors (including family interests) in the issued share capital of the Company. The interests were beneficial interests.

Hitherto, the Board has encouraged Executive Directors to build and maintain, over time, a personal holding of shares equivalent in value to around a year's basic pay. Following implementation of the proposed changes to remuneration described elsewhere in this report, this will be increased to at least one and a half times salary.

Director	At 31 March 2009[1]	At 1 April 2008[2]
Chairman and Executive Directors		
M J Turner (Director since 1 June 2008)	20,000	–
G A Campbell (ceased to be a Director on 31 October 2008)	150,000	250,000
P L Rogers	597,064	100,000
W Tame	304,035	26,189
Non-Executive Directors		
Lord Hesketh	1,667	1,667
D J Shah	8,333	8,333
Sir Nigel Essenhigh	–	–
J L Rennocks	–	–
J N A Crookenden	6,961	–
Sir David Omand	–	–

1. The figure for Mr Campbell shows the position as at the date he ceased to hold office as a Director (31 October 2008).

2. The figure for Mr Turner shows the position as at 1 June 2008, the date on which he became a Director.

There were no changes in the continuing Directors' interests in shares between 31 March 2009 and 20 May 2009.

Directors' share-based rewards and options (audited)

Options

Details of the Directors' share options are set out in the table below and the notes beneath it. All of the outstanding options are vested and exercisable.

Director	Option scheme	Number of shares subject to options at 1 April 2008	Granted during the year	Exercised during the year*	Lapsed during the year	Number of shares subject to options at 31 March 2009	Exercise price (pence)	Exercisable from	Expiry date
P L Rogers	a	401,606	–	401,606	–	–	124.50	Jun 2005	Jun 2012
W Tame	b	21,278	–	–	–	21,278	104.33	Jan 2005	Jan 2012

*Details of the options exercised during the year are as follows:

Director	Option scheme	Exercise date	Number of shares acquired on exercise	Number of acquired shares sold on exercise	Market value per share on exercise (pence)	Exercise price per share (pence)	Total gain* on date of exercise £
P Rogers	a	20/03/09	401,606	231,103	447.09	124.50	1,295,541

a = Share Option Agreement (agreed as part of the terms of recruitment).

b = Babcock 1999 Approved Executive Share Option Scheme.

* The amount by which the market value of all shares acquired on exercise exceeded the aggregate exercise price.

Options vested according to comparative TSR performance over three-year performance periods. They were not subject to re-testing. The comparator group was the companies in the FTSE Engineering and Machinery Sector when the options were granted (which was the sector in which the Company's shares were then listed). There was no vesting unless the Company ranked above median performance, in which case 25% of the options vested. Full vesting was for top quartile ranking with proportionate vesting on a straight-line basis for a ranking between those points.

The exercise price was set at the average of the mid-market closing price of the Company's shares for the three business days preceding the date of the grant. This price was not discounted.

Directors must exercise vested options before the tenth anniversaries of the grant dates, or earlier if there is a change of control, they leave or die, failing which they will lapse.

There were no changes in the Directors' share options between 31 March 2009 and 20 May 2009.

Share awards under the L-TIP

Details of share awards under the L-TIP ('L-TIP awards') in the form of nil-cost options made to Directors are set out in the table below:

Director and year of award	Number of shares subject to award at 1 April 2008	Granted during the year to 31 March 2009 (19.06.08)	Exercised during the year to 31 March 2009[1,2]	Lapsed during the year to 31 March 2009[2]	Number of shares subject to award at 31 March 2009[2]	Market value (in pence) of each share at date of award	Exercisable (subject to vesting and plan rules) from[3]	Expiry date
G A Campbell (former Director)								
2003	166,395	–	166,395	–	–	113.50	Jun 2006	Jul 2013
2004	158,730	–	–	–	158,730	126.00	May 2007	Jul 2014
2005	117,994	–	–	–	117,994	169.50	May 2008	Jul 2015
2006	66,469	–	–	–	66,469	338.50	May 2009	Jul 2016
2007	42,202	–	–	14,067	28,135	556.80	May 2010	Jun 2017
P L Rogers								
2004	281,746	–	281,746	–	–	126.00	May 2007	Jul 2014
2005	230,088	–	230,088	–	–	169.50	May 2008	Jul 2015
2006	118,168	–	–	–	118,168	338.50	May 2009	Jul 2016
2007	74,528	–	–	–	74,528	556.80	May 2010	Jun 2017
2008		79,080	–	–	79,080	594.33	May 2011	Jun 2018
W Tame								
2003	170,775	–	170,775	–	–	113.50	Jun 2006	Jul 2013
2004	162,698	–	162,698	–	–	126.00	May 2007	Jul 2014
2005	132,743	–	132,743	–	–	169.50	May 2008	Jul 2015
2006	69,423	–	–	–	69,423	338.50	May 2009	Jul 2016
2007	51,182	–	–	–	51,182	556.80	May 2010	Jun 2017
2008		51,402	–	–	51,402	594.33	May 2011	Jun 2018

1. Exercise details in the table below.
2. For Mr Campbell, who ceased to hold office on 31 October 2008, the number shown is the number as at that date.
3. The 2005 L-TIP award was fully vested and exercisable as at 31 March 2009. Vesting date depends on the date of notification of the vesting, but will be after the announcement of results for the final year of the applicable performance period. The above table assumes that the announcement is made in May and notification of vesting given in the same month.

Details of exercises of L-TIP awards: (note: as the awards were in the form of nil-cost options, no exercise price applies)

Director	Year(s) of award	Date of exercise (and, if applicable, sale)	Total number of award shares exercised	Number of award shares sold on exercise	Market price on exercise (pence per share)	Total value of shares on exercise £
P L Rogers	2004 and 2005	20/03/09	511,834	210,273	447.09	2,288,359
W Tame	2003, 2004, and 2005	20/03/09	466,216	191,532	447.09	2,084,405
G A Campbell (includes exercises after cessation of employment on 31 October 2008)	2003 2004, 2005, 2006 and 2007	2/09/08 11/11/08	166,395 371,328	166,395 78,268	589.89 412.01	981,547 1,529,908

The number of shares sold on exercise of the LTIP awards by Mr Rogers and Mr Tame were in each case just sufficient to cover income tax and employee national insurance charges arising on exercise, and dealing costs.

The Remuneration Committee exercised its powers under the rules of the L-TIP to treat all of the L-TIP award made to him in 2006 and two-thirds of the L-TIP award made to him in 2007 as having vested on Mr Campbell's ceasing to be employed on 31 October 2008.

The Company's mid-market share price at close of business on 31 March 2009 was 429.50p. The highest and lowest mid-market share prices in the year ended 31 March 2009 were 647.50p and 348.50p respectively.

The L-TIP awards that vested during the year to 31 March 2009 were those granted in July 2005. The market value of those shares on award was 169.50p per share. On the date of vesting, 22 May 2008, they had a market value of 597.50p per share, being the mid-market closing price on that day. The performance conditions attached to the awards are described below.

All the L-TIP awards made to Directors to date have been made by the trustee of the Babcock Employee Share Trust as nil cost options. The number of shares awarded had a value equal to the Director's qualifying annual salary at the date of the award (using the average of the mid-market closing price of the Company's shares for the three business days' preceding that date).

Subject to satisfaction of the performance criteria attached to LTIP awards (see below), the Directors may call for the release to them of the award shares during the respective exercise periods. Subject to the rules of the plan, an earlier release of shares under unvested awards may be allowed by the Remuneration Committee (for example, in the event of a cessation of employment or a change in control), but (unless the Committee otherwise decides) of not more than a time-apportioned proportion and then only having regard to the Company's performance, though the Committee has discretion to allow a greater proportion to be released.

Performance measures attached to L-TIP awards and proposed PSP

Performance under the L-TIP is (and would under the PSP also be) judged over the period of three financial years from the start of the financial year in which the award is made. Performance is measured at the end of the period and is not re-tested.

Awards not vested as at 31 March 2009

2005–2008 awards

For L-TIP awards made between 2005 and 2008, half of the shares vest based on comparative TSR performance and half according to growth in earnings per share (EPS). For the TSR element, a ranking immediately above median results in 25% of those shares vesting. There is no vesting for ranking below that level. A ranking in the upper quartile results in 100% vesting. Rankings between these threshold levels result in proportionate vesting calculated on a straight-line basis between 25% and 100%.

The comparator group of listed companies for the 2005 and 2006 awards comprised AEA Technology, W.S. Atkins, Aggreko, Amec, Bodycote, Capita, Carillion, Cobham, Interserve, Laing (John), Mitie, Mouchel-Parkman, PHS Group (dropped in 2006), Rentokil Initial, Serco, VT Group and WSP Group.

The comparator group for the awards made in 2007 comprised AEA Technology, W.S. Atkins, Aggreko, Amec, Bodycote, Capita, Carillion, Cobham, Interserve, Mitie, Mouchel-Parkman, Rentokil Initial, Serco, VT Group, WSP Group, Weir Group, Ashtead Group, Alfred McAlpine and Davis Service Group.

For L-TIP awards made in 2008, the comparator group comprises the constituents of the FTSE 350 Support Services Index as at the date of grant – this was a peer group in the same FTSE sector as the Company and was chosen pending the fuller review of longer term incentives described above.

The TSR calculation normally uses a 12-month average for share prices adjusted for dividends paid during the period. The Company feels that this is the most appropriate period because a 12-month average ensures both that the short-term market volatility is excluded and that for each company a 12-month period will capture the impact of the announcement of results and payment of dividends. A shorter period would not capture all these events and would not necessarily put all companies on an equal footing. For the half of the 2005–2008 L-TIP awards where vesting depends on EPS growth, 25% of the shares vest if growth in EPS (adjusted to exclude exceptional items and acquired intangible amortisation) over the performance period is equivalent to a real (i.e. growth in excess of the increase in the consumer prices index) compound annual growth rate of 4%, with full vesting if this reaches 8%. Vesting is on a straight-line basis for growth between those two points. There is no vesting for compound annual earnings per share growth of below 4% (real).

2009 awards (subject to shareholder approval of the PSP)

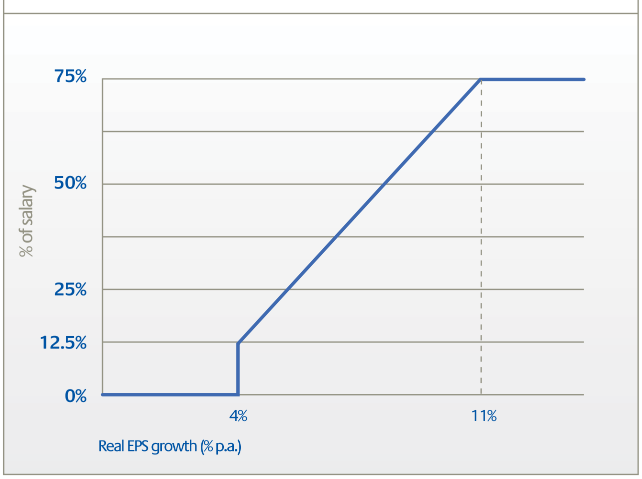
For awards to be made in 2009 under the proposed PSP, it is proposed that half should vest according to comparative TSR performance ('the TSR element') and half according to growth in earnings per share ('the EPS element'). The Committee considers the use of two measures, in these proportions, to be appropriate. The TSR performance measure is dependent on the Company's relative long-term share price performance and so provides strong alignment with shareholders' interests. This is used in conjunction with EPS growth, which is the primary internal benchmark of financial performance and ties in with the Company's strategic goals. For the TSR element, it is proposed that the TSR sector peer group would be the broader FTSE 350 (excluding investment trusts and financial services) due to the fact that Babcock's closest peers straddle multiple sectors, not just support services, and to make the calibration more robust. The Company intends to use TSR percentage out-performance as a measure of performance rather than a ranking. As with previous L-TIP awards, the TSR calculation would normally use a 12-month average for opening and closing share prices adjusted for dividends paid during the period. For both the TSR and EPS elements, the Committee proposes to leave threshold vesting as a percentage of salary unchanged (at what it was for the existing L-TIP Awards), i.e. 12.5% of salary for each element, which implies a reduced percentage of the award vesting at threshold. For TSR performance at median, 16.7% of the TSR element of the award would vest. There would be no vesting for TSR performance below median. Out-performance of the median by at least 9% p.a. would result in 100% vesting of the TSR element. For out-performance of the median between 0% and 9% p.a. vesting would increase on a straight-line basis between 16.7% and 100%. Participants will only be entitled to a vesting of shares under the TSR element if the Remuneration Committee is satisfied that the recorded TSR is a genuine reflection of the underlying performance of the Company over the performance period.

For the other half of the 2009 PSP awards, the EPS element, 16.7% of this element would vest if earnings per share growth (adjusted to exclude acquired intangible amortisation, but, unless the Committee decides otherwise, after inclusion of exceptional items) over the performance period is equivalent to a real compound annual growth rate of 4%. Real growth would be measured as growth in excess of the growth in the retail price index, rather than the consumer price index as used for previous L-TIP awards, thus bringing the Company in line with common practice. The proposed real growth target required for full vesting will be increased from 8% (as applied under the existing L-TIP Awards) to 11% real growth p.a. Vesting would be on a straight-line basis for growth between those two points. There would be no vesting for compound annual earnings per share growth of below 4% real.

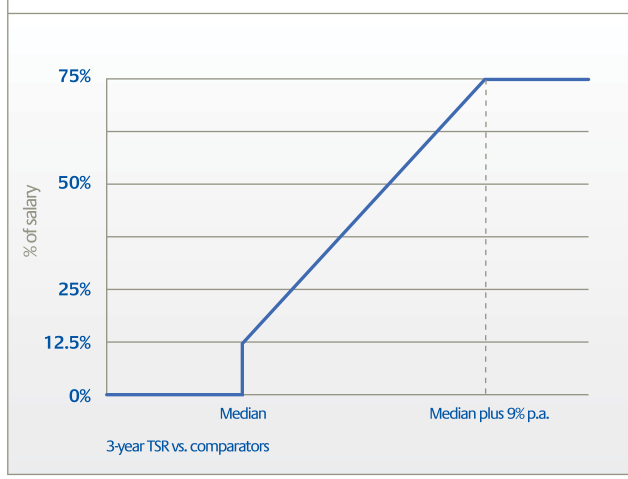
The Remuneration Committee will have the discretion to review the performance conditions attached to future PSP awards prior to the start of each cycle to ensure they remain appropriate. However, no material reduction in targets would be made without prior consultation with shareholders.

The charts below illustrate the proposed vesting schedules for each element of the proposed 2009 PSP award:

EPS element



TSR element



It is also proposed that, in common with recent market practice, the share awards would carry the right to receive on vesting any dividends (or, if the Committee so decides, a number of shares having a market value equivalent to the amount of the dividends when the dividend was paid) that would have been paid in the period between grant and vesting, but only on the shares that actually vest.

Service contracts

The following table summarises the key terms (apart from as to remuneration, on which see above) of the Directors' service contracts or terms of appointment:

Executive Directors

Name	Date of service contract	Notice period	Contractual retirement age
P L Rogers (Chief Executive)	31 July 2003 (amended by letters dated 5 May 2004 and 3 April 2006)	12 months from Company, 6 months from Director	65
W Tame (Finance Director)	1 October 2001 (amended by letters dated 5 May 2004 and 3 April 2006)	12 months from Company, 6 months from Director	65

(Mr G Campbell, former Chairman, who left the Board on 31 October 2008 also had a service agreement with the Company (dated 31 July 2003 as amended by letters dated 5 May 2004 and 3 April 2006) which provided for termination by the Company on giving 12 months' notice or by Mr Campbell by giving six months' notice. It also contained similar provisions relating to termination following a change of control as are described below for Mr Rogers and Mr Tame, though there was no right to any payment in lieu of bonus. The agreement terminated on 31 October 2008 pursuant to a Compromise Agreement.)

The Company's policy is that Executive Directors' service contracts should be capable of being terminated by the Company on not more than 12 months' notice.

If the Company terminates a Director's service contract (other than following a change of control (see below) or by the exercise of the Company's option to pay salary in lieu of notice) the Company will have regard to all the circumstances in determining the amount of compensation, if any, payable to him in connection with that termination.

The agreements for Mr Rogers and Mr Tame contain provisions relating to termination following a change of control. Each contract provides that within 90 days of the occurrence of the change of control, Mr Rogers or Mr Tame (as the case may be) may terminate his employment forthwith. If he exercises this right, he is entitled, for a 12-month period, to be paid (on a monthly basis) his basic salary plus 40% (compared to a maximum entitlement under the annual bonus scheme of 150%) in lieu of bonus and all other contractual entitlements. From this there is to be deducted any amount that the Director receives by way of income, if it exceeds 10% of his Babcock salary, from other sources that he would not have been able to earn had he continued in employment with the Company. If the Company terminates his appointment within 12 months of a change of control, he would be entitled to a termination payment equal to 100% of his annual salary (plus 40% in lieu of bonus and all other benefits).

Chairman and Non-Executive Directors

Name	Date of appointment as a Director	Date of current appointment letters	Expiry of present term of appointment (subject to re-election as required either under the Articles or the Combined Code)*
M J Turner (Chairman)	1 June 2008	28 May 2008	AGM for 2011
Lord Hesketh	6 October 1993	8 May 2009	AGM for 2010
D J Shah	15 June 1999	15 May 2008	AGM for 2009
J L Rennocks	13 June 2002	15 May 2008	AGM for 2012
Sir Nigel Essenhigh	4 March 2003	15 May 2008	AGM for 2012
J N A Crookenden	1 December 2005	15 May 2008	AGM for 2011
Sir David Omand	1 April 2009	19 March 2009	AGM for 2012

* The Company's policy is for Non-Executive Directors to have written terms of appointment normally for no more than three-year terms at a time; however, in all cases appointments are terminable at will at any time by the Company or the Director.

The latest written terms of appointment are available for inspection at the Company's registered office and at the Company's Annual General Meeting. The expected time commitment of Non-Executive Directors is set out in their current written terms of appointment.

Outside directorships

Before taking up any new outside appointment, an Executive Director must first seek the approval of the Chairman. Any fees for outside appointments are retained by the Director. Mr Rogers is a Non-Executive Director of Galliford Try plc, having joined its board on 1 July 2008. During the year to 31 March 2009 he received £25,700 by way of fees for that role. Mr Tame is a Non-Executive Director of Carclo PLC. During the period 1 April 2008 to 31 March 2009 his fees for that role were £26,500.

This Remuneration report has been approved by the Board on 20 May 2009 and signed on its behalf by:

J N A Crookenden
Chairman of the Remuneration Committee

20 May 2009

Independent auditors' report to the members of Babcock International Group PLC

We have audited the Group financial statements of Babcock International Group PLC for the year ended 31 March 2009 which comprise the Group income statement, the Group balance sheet, the Group cash flow statement, the Group statement of recognised income and expense and the related notes. These Group financial statements have been prepared under the accounting policies set out therein.

We have reported separately on the parent Company financial statements of Babcock International Group PLC for the year ended 31 March 2009 and on the information in the Directors' Remuneration report that is described as having been audited.

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the Annual Report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union are set out in the Statement of Directors' responsibilities.

Our responsibility is to audit the Group financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This Report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this Report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the Group financial statements give a true and fair view and whether the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Directors' report is consistent with the Group financial statements. The information given in the Directors' report includes that specific information presented in the Business review that is cross referred from the Business review section of the Directors' report.

In addition we report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We review whether the Corporate Governance statement reflects the Company's compliance with the nine provisions of the Combined Code (2006) specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited Group financial statements. The other information comprises only the Directors' report, the unaudited part of the Directors' Remuneration report, the Chairman's statement, the Business review, the Statement on Corporate Governance and the other information listed on the contents page. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Group financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Group financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Group financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Group financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Group financial statements.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's affairs as at 31 March 2009 and of its profit and cash flows for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation; and
- the information given in the Directors' report is consistent with the Group financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

20 May 2009

Group income statement

For the year ended 31 March 2009

	Note	2009 Before acquired intangible amortisation and exceptional items £m	2009 Acquired intangible amortisation and exceptional items £m	2009 Total £m	2008 Before acquired intangible amortisation and exceptional items £m	2008 Acquired intangible amortisation and exceptional items £m	2008 Total £m
Revenue	3	1,901.9	–	1,901.9	1,555.9	–	1,555.9
Operating profit	3, 4, 5, 6	147.3	(14.2)	133.1	121.1	(10.9)	110.2
Share of loss from joint ventures	3	(0.2)	–	(0.2)	–	–	–
Finance costs	7	(32.1)	–	(32.1)	(32.0)	–	(32.0)
Finance income	7	5.9	–	5.9	6.4	–	6.4
Profit before tax		120.9	(14.2)	106.7	95.5	(10.9)	84.6
Income tax expense	9	(23.1)	4.0	(19.1)	(18.2)	3.3	(14.9)
Profit for the year from continuing operations		97.8	(10.2)	87.6	77.3	(7.6)	69.7
Discontinued operations							
Loss for the year from discontinued operations	10	–	(13.3)	(13.3)	–	–	–
Profit for the year	5	97.8	(23.5)	74.3	77.3	(7.6)	69.7
Attributable to:							
Equity holders of the parent				72.0			67.3
Minority interest				2.3			2.4
				74.3			69.7
Earnings per share from continuing operations	12						
– Basic				37.42p			29.99p
– Diluted				37.16p			29.43p
Earnings per share from continuing and discontinued operations	12						
– Basic				31.59p			29.99p
– Diluted				31.38p			29.43p

Group balance sheet

As at 31 March 2009

	Note	2009 £m	2008 £m
Assets			
Non-current assets			
Goodwill	13	535.2	479.6
Other intangible assets	14	68.7	62.9
Property, plant and equipment	15	147.1	145.9
Investment in joint ventures	16	1.5	0.4
Loan to joint venture	16	12.0	–
Retirement benefits	28	90.9	142.6
Trade and other receivables	19	0.2	1.7
Deferred tax	17	2.8	3.0
		858.4	836.1
Current assets			
Inventories	18	94.4	76.7
Trade and other receivables	19	335.7	340.9
Income tax recoverable		4.6	2.3
Other financial assets	23	1.0	1.7
Cash and cash equivalents	20	123.6	199.6
		559.3	621.2
Total assets		1,417.7	1,457.3
Equity and liabilities			
Equity attributable to equity holders of the parent			
Share capital	25	137.7	137.6
Share premium		148.2	148.1
Capital redemption and other reserves		18.5	20.9
Retained earnings		(16.0)	50.6
		288.4	357.2
Minority interest		4.4	3.6
Total equity	27	292.8	360.8
Non-current liabilities			
Bank and other borrowings	22	356.5	377.5
Trade and other payables	21	16.0	15.3
Deferred tax	17	0.2	31.2
Retirement liabilities	28	40.2	0.4
Provisions for other liabilities	24	35.4	32.3
		448.3	456.7
Current liabilities			
Bank and other borrowings	22	118.6	144.3
Trade and other payables	21	518.0	466.7
Income tax payable		15.2	11.6
Other financial liabilities	23	15.1	4.2
Provisions for other liabilities	24	9.7	13.0
		676.6	639.8
Total liabilities		1,124.9	1,096.5
Total equity and liabilities		1,417.7	1,457.3

The notes on pages 65 to 100 are an integral part of the consolidated financial statements.

The Group financial statements were approved by the Board of Directors on 20 May 2009 and are signed on its behalf by:

P L Rogers
Director

W Tame
Director

Group cash flow statement

For the year ended 31 March 2009

	Note	2009 £m	2008 £m
Cash flows from operating activities			
Cash generated from operations	29	153.6	119.2
Income tax paid		(7.7)	(9.5)
Interest paid		(34.2)	(26.7)
Interest received		5.4	6.4
Net cash flows from operating activities		117.1	89.4
Cash flows from investing activities			
Disposal of subsidiaries and joint ventures	33	(16.9)	0.3
Proceeds on disposal of property, plant and equipment		4.9	5.4
Proceeds on disposal of intangible assets		–	0.2
Dividend received from joint ventures		–	0.2
Purchases of property, plant and equipment		(17.0)	(13.1)
Purchases of intangible assets		(2.1)	(1.1)
Acquisition of minority interests		–	(12.5)
Investment in and loans to joint venture		(13.3)	–
Acquisition of subsidiaries net of cash acquired	32	(66.2)	(372.3)
Net cash flows from investing activities		(110.6)	(392.9)
Cash flows from financing activities			
Dividends paid	11	(27.9)	(20.3)
Finance lease principal payments		(0.5)	(0.5)
Bank loans (repaid)/raised		(20.7)	276.5
Dividends paid to minority interests	27	(1.8)	(1.1)
Net proceeds on issue of shares	27	0.2	89.8
Movement on own shares	27	(7.5)	(5.0)
Net cash flows from financing activities		(58.2)	339.4
Net (decrease)/increase in cash, cash equivalents and bank overdrafts		(51.7)	35.9
Cash, cash equivalents and bank overdrafts at beginning of year		56.5	22.1
Effects of exchange rate fluctuations		1.5	(1.5)
Cash, cash equivalents and bank overdrafts at end of year	31	6.3	56.5

Group statement of recognised income and expense

For the year ended 31 March 2009

	Note	2009 £m	2008 £m
Profit for the year (including discontinued operations)		74.3	69.7
Currency translation differences		6.3	(3.2)
Fair value adjustment of interest rate and foreign exchange hedges		(11.6)	(2.7)
Net actuarial (losses)/gains in respect of pensions	28	(145.6)	43.0
Tax on net actuarial (losses)/gains in respect of pensions and hedges		44.0	(9.7)
Total recognised income and expense		(32.6)	97.1
Attributable to:			
Equity holders of the parent		(35.2)	94.9
Minority interest		2.6	2.2
		(32.6)	97.1

Notes to the Group financial statements

1. Basis of preparation and significant accounting policies

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and International Financial Reporting Interpretations Committee (IFRIC) interpretations as adopted by the European Union and with those parts of the Companies Act 1985/2006 applicable to companies reporting under IFRS. The consolidated financial statements have been prepared under the historic cost convention as modified by the revaluation of certain financial instruments.

Principal accounting policies

The principal accounting policies adopted by the Group are disclosed below:

Basis of consolidation

The Group financial statements comprise the Company and all of its subsidiary undertakings made up to 31 March.

(a) Subsidiaries
Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. Acquisitions are included from the date of acquisition and the results of the businesses disposed of or terminated are included in the results for the year up to the date of relinquishing control or closure and analysed as continuing or discontinued operations.

(b) Joint ventures
The Group's interest in jointly controlled entities are accounted for by the equity method of accounting and are initially recorded at cost. The Group's investment in jointly controlled entities includes goodwill (net of any accumulated impairment loss) identified on acquisition.

The Group's share of its jointly controlled entities' post-acquisition profits or losses after tax is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment.

Unrealised gains and losses on transactions between the Group and its jointly controlled entity are eliminated to the extent of the Group's interest in the joint controlled entity.

Revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

(a) Sale of goods
Revenue is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer and can be reliably measured and recovery of consideration is considered probable.

(b) Rendering of services
Revenue from services rendered is recognised by reference to the stage of completion of the transaction. The provision of services over a long-term period are accounted for under the principles of construction contracts, and the revenue recognised as set out below.

(c) Long-term service contracts
Revenue from long-term service contracts, is recognised by reference to the stage of completion of the contract. The stage of completion is determined according to the nature of the specific contract concerned. Methods used to assess the stage of completion include incurred costs as a proportion of total costs, labour hours incurred or earned value of work performed. Profit attributable to the contract activity is recognised if the final outcome of such contracts can be reliably assessed. An expected loss on a contract is recognised immediately in the income statement.

Exceptional items

Items that are exceptional in size or nature, are presented as exceptional items within the consolidated income statement. The separate reporting of exceptional items helps provide a better indication of the Group's underlying business performance. Events which may give rise to the classification of items as exceptional include gains or losses on the disposal of properties and businesses along with the restructuring of businesses and asset impairments.

Transactions with minorities

The Group policy is to treat transactions with minorities as transactions with equity holders and therefore result in movements in reserves.

1. Basis of preparation and significant accounting policies (continued)

Goodwill and intangible assets

(a) Goodwill

When the fair value of the consideration for an acquired undertaking exceeds the fair value of its separable net assets, the difference is treated as purchased goodwill and is capitalised. When the fair value of the consideration for an acquired undertaking is less than the fair value of its separable net assets, the difference is taken directly to the income statement.

Goodwill relating to acquisitions prior to 1 April 2004 is maintained at its net book value on the date of transition to IFRS. From that date goodwill is not amortised but is reviewed at least annually for impairment.

(b) Acquired intangibles

Intangible assets, which are capable of being recognised separately and measured reliably on acquisition of a business, are capitalised at fair value on acquisition. These intangibles will include contracts and customer relationships. Where these assets have a finite life, they are amortised over the period which they are expected to generate benefits, but generally not exceeding ten years. Customer contracts and relationships valued on acquisition are expected to generate higher benefits in the early years following such acquisition as the existing contracts unwind.

(c) Research and development

Research expenditure is recognised as an expense as incurred. Costs incurred on development projects are recognised as intangible assets when it is probable that the project will be a success considering its commercial and technological feasibility, and only if the cost can be measured reliably. Other development expenditure is recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs that have been capitalised are amortised from the date the product is available for use on a straight-line basis over the period of its expected benefit but not exceeding seven years.

(d) Computer software

Computer software costs are amortised over their expected useful lives of between three and five years.

Property, plant and equipment (PPE)

Property, plant and equipment is shown at cost less subsequent depreciation and impairment, except for land, which is shown at cost less impairment. Cost includes expenditure that is directly attributable to the acquisition of the items. Depreciation is provided on a straight-line basis to write off the cost of PPE over the estimated useful lives to their estimated residual value (reassessed at each balance sheet date) at the following annual rates:

Freehold land	Nil
Freehold property	2% to 8%
Short leasehold property	lease term
Plant, machinery and motor vehicles	6.6% to 33.3%

PPE are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the fixed asset may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount exceeds the higher of an asset's fair value less cost to sell or value in use.

Leases

Assets under finance leases are capitalised and the outstanding capital element of instalments is included in borrowings. The interest element is charged against profits so as to produce a constant periodic rate of charge on the outstanding obligations. Depreciation is calculated to write the assets off over their expected useful lives or over the lease terms where these are shorter.

Operating lease payments are recognised as an expense in the income statement. A provision is made where the operating leases are deemed to be onerous.

Inventory and work in progress

Inventory is valued at the lower of cost and net realisable value. Cost is determined on a first-in first-out method. In the case of finished goods and work in progress, cost comprises direct material and labour and an appropriate proportion of overheads.

Contract accounting

The Group presents as an asset the gross amount due from customers for contract work for all contracts in progress for which costs incurred plus recognised profits (less recognised losses) exceed progress billings.

The Group presents as a liability the gross amount due to customers for contract work for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses).

Pre-contract costs are recognised as expenses as incurred, except that directly attributable costs are recognised as an asset when it can be reliably expected that a contract will be obtained and the contract is expected to result in future net cash inflows.

1. Basis of preparation and significant accounting policies (continued)

Taxation

(a) Current income tax

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

(b) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction, other than a business combination, that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not accounted for. Deferred income tax is determined using tax rates (and laws) that have been enacted, or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group, and it is probable that the temporary difference will not reverse in the foreseeable future.

Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Foreign currencies

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Sterling, which is the Company's functional and presentation currency.

(b) Transactions and balances.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the local currency at the year end exchange rates.

Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at exchange rates ruling at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement except when deferred in equity as part of the net investment of a foreign operation.

Exchange differences arising from the translation of the balance sheets and income statements of foreign operations into Sterling are recognised as a separate component of equity on consolidation. Results of foreign subsidiary undertakings are translated using the average exchange rate for the month of the applicable results. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at period end exchange rates.

Finance costs

Finance costs are recognised as an expense in the period in which they are incurred.

1. Basis of preparation and significant accounting policies (continued)

Employee benefits

(a) Pension obligations

The Group operates a number of pension schemes. The schemes are generally funded through payments to trustee-administered funds, determined by periodic actuarial calculations. The Group has both defined benefit and defined contribution plans. A defined benefit plan is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity.

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

For defined benefit pension schemes, the cost of providing benefits is determined using the projected unit credit actuarial valuation method. The Group's current and past service cost and imputed interest on the defined benefit schemes' obligations, net of the expected return on the scheme's assets, are charged to operating profit within the income statement. Actuarial gains and losses are recognised directly in equity through the Statement of recognised income and expense so that the Group's balance sheet reflects the fair value of the scheme's surpluses or deficits at the balance sheet date.

(b) Share-based compensation

The Group operates equity-settled, share-based compensation plans. The economic cost of awarding shares and share options to employees is recognised as an expense in the income statement equivalent to the fair value of the benefit awarded. The fair value is determined by reference to option pricing models. The charge is recognised in the income statement over the vesting period of the award.

The share's purchased by the Group's ESOP trusts are recognised as a deduction to equity.

(c) Holiday pay

Paid holidays are regarded as an employee benefit and as such are charged to the income statement as the benefits are earned.

Investments

The accounting for investments is decided on a case by case basis depending on whether the investment is held for resale or other strategic reasons.

Derivative financial instruments

Derivatives are initially recognised at fair value on the date a derivative is entered into and are subsequently remeasured at their fair value. The Group designates certain of the derivative instruments within its portfolio to be hedges of the fair value of recognised assets or liabilities or unrecognised firm commitments.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

For foreign exchange contracts that qualify as cash flow hedges, gains and losses are deferred in equity until such time as the firm commitment is recognised, at which point any deferred gain or loss is included in the assets carrying amount. These gains or losses are then realised through the income statement as the asset is sold.

Certain derivatives do not qualify or are not designated as hedging instruments and any movement in their fair values is recognised in the income statement immediately.

Dividends

Dividends are recognised as a liability in the Group's financial statements in the period in which they are approved.

Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The key areas of estimates and judgements for the Group are contract accounting (see above), the accounting for defined benefit pension schemes (see note 28), impairment of goodwill (see note 13) and income tax recognition.

Profit recognition on contracts is a key judgement exercised by management on a contract by contract basis. In order to make such a judgement an estimate of contract outturn is made and for all significant contracts both local management and Group review and challenge estimates made.

Fair value adjustments on acquisitions are by nature subject to critical judgements. The size of recent acquisitions make them significant in Group terms.

The Group has disposed of a number of businesses in recent years. There are a number of disputes arising from these disposals, which results in a provision for settlement, the quantum of which is a judgemental issue.

1. Basis of preparation and significant accounting policies (continued)

Standards, amendments and interpretations to published standards that are not yet effective

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 April 2008 or later periods but which the Group has not early adopted.

a) Standards, amendments and interpretations effective in 2008 with minimal or no impact on the Group:

- IFRIC11, 'Group and Treasury Share Transactions'.
- IFRIC 14, 'IAS19 – The limit on a defined benefit asset, minimum funding requirements and their interaction'.

b) New standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Group. The impact on the Group's operations is currently being assessed:

- IFRS 1 (amendment), 'First time adoption of IFRS', and IAS 27 'Consolidated and separate financial statements', effective from 1 January 2009.
- IFRS 2 (amendment), 'Share based payments', effective from 1 January 2009.
- IFRS 3 (revised), 'Business combinations: revised', effective from 1 July 2009.
- IFRS 5 (amendment), 'Non-current assets held-for-sale and discontinued operations', (and consequential amendment to IFRS 1 'First time adoption'), effective from 1 July 2009.
- IFRS 8, 'Operating Segments'. This standard is effective for annual periods beginning on or after 1 January 2009. IFRS 8 replaces IAS 14 'Segmental reporting', and requires a 'management approach' under which segmental information is presented on the same basis as that used for internal reporting purposes.
- IAS 1 (revised), 'Presentation of Financial Statements', effective from 1 January 2009.
- IAS 16 (amendment), 'Property, plant and equipment' (and consequential amendment to IAS 7, 'Statement of cash flows'), effective from 1 January 2009.
- IAS 19 (amendment), 'Employee Benefits', effective from 1 January 2009.
- IAS 20 (amendment), 'Accounting for government grants and disclosure of government assistance', effective from 1 January 2009.
- IAS 23 (amendment), 'Borrowing costs', effective from 1 January 2009.
- IAS 27 (revised), 'Consolidated and separate financial statements', effective from 1 July 2009.
- IAS 28 (amendment), 'Investments in associates', (and consequential amendment to IAS 32 'Financial instruments: presentation', and IFRS 7 "Financial instruments: disclosure"), effective from 1 January 2009.
- IAS 29 (amendment), 'Financial reporting in hyperinflationary economies', effective from 1 January 2009.
- IAS 31 (amendment), 'Interests in joint ventures', (and consequential amendments to IAS 32 and IFRS 7), effective from 1 January 2009.
- IAS 32 (amendment), 'Financial instruments: presentation' and IAS 1 (amendment), 'Presentation of financial statements' – 'Puttable financial instruments and obligations arising on liquidation', effective from 1 January 2009.
- IAS 36 (amendment), 'Impairment of assets', effective from 1 January 2009.
- IAS 38 (amendment), 'Intangible assets', effective from 1 January 2009.
- IAS 39, Financial instruments: 'Recognition and measurement – Amendments for eligible hedged items' 1 July 2009.
- IFRIC 16 (amendment), 'Hedges of a net investment in a foreign operation', effective from 1 October 2008.

c) Interpretations to existing standards that are not yet effective and are not anticipated to be relevant for the Group's operations:

- IFRIC13 'Customer loyalty programmes', effective from 1 July 2008
- IFRIC 15, 'Agreements for construction of real estates', effective from 1 January 2009.
- IFRIC 17, 'Distributions of Non-cash assets to Owners', effective from 1 July 2009.
- IFRIC 18, 'Transfers of assets from customers', effective from 1 July 2009.
- IAS 40 (amendment), 'Investment property' (and consequential amendments to IAS 16), effective from 1 January 2009.
- IAS 41 (amendment), 'Agriculture', effective from 1 January 2009.

2. Financial risk management

Financial risk management

Financial instruments, in particular, forward currency contracts and interest rate swaps, are used to manage the financial risks arising from the business activities of the Group and the financing of those activities.

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

Gearing and liquidity are managed to external and internal benchmarks.

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

All treasury transactions are carried out only with prime rated counterparties as are investments of cash and cash equivalents. The Group's customers are mainly from government, government backed institutions or blue chip corporations and as such credit risk is considered small.

Foreign exchange risk

The foreign exchange exposure of Group entities on the net monetary position against their respective functional currencies expressed in the Group's presentation currency is insignificant with the largest exposure being less than £0.2 million (2008: Sterling to Euro £1.6 million).

Consequently, the pre tax effect on profit and equity, increase or (decrease), if the rates moved up or down by an appropriate percentage volatility, assuming all other variables remained constant would in total be less than £0.1 million (2008: £0.2 million). The reasonable shifts in exchange rates are based on historic volatility and range from 15% for Sterling to Euro to 30% for South African Rand to Euro and 30% Sterling to US Dollars.

Interest rate risk

The fair values of debt, and related hedging instruments are affected by movements in interest rates. The following table illustrates the sensitivity in cash flow of interest rate-sensitive instruments to a hypothetical parallel shift of the forward interest rate curves of ±50bp (2008: ±50bp), with pre tax effect from the beginning of the year. All other variables are held constant.

	2009		2008	
	£m +50bp	£m –50bp	£m +50bp	£m –50bp
Net results for the year	(0.9)	0.9	(0.6)	1.2
Equity	2.7	(2.7)	2.3	(3.2)

2. Financial risk management (continued)

Liquidity risk

Liquidity risk management includes maintaining sufficient cash and the availability of funding from an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, Group treasury maintains flexibility in funding by maintaining availability under committed credit lines.

The table below analyses the Group's liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contract maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances, as the impact of interest is not significant.

	Less than 1 year £m	Between 1 and 2 years £m	Between 2 and 5 years £m	Over 5 years £m
At 31 March 2009				
Bank and other borrowings	118.6	0.6	355.9	–
Derivative financial instruments	4.7	5.3	4.4	–
Trade and other payables	518.0	5.9	3.9	8.2
At 31 March 2008				
Bank and other borrowings	144.3	1.1	376.4	–
Derivative financial instruments	(0.5)	1.4	1.6	–
Trade and other payables	466.7	11.1	2.3	2.8

The table below analyses the Group's derivative financial instruments that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

	Less than 1 year £m	Between 1 and 2 years £m	Between 2 and 5 years £m	Over 5 years £m
At 31 March 2009				
Forward foreign exchange contracts – cash flow hedges:				
– outflow	6.3	–	–	–
– inflow	6.6	–	–	–
Forward foreign exchange contracts – held for trading:				
– outflow	1.9	–	–	–
– inflow	2.4	–	–	–
At 31 March 2008				
Forward foreign exchange contracts – cash flow hedges:				
– outflow	8.3	–	–	–
– inflow	7.4	–	–	–
Forward foreign exchange contracts – held for trading:				
– outflow	2.9	–	–	–
– inflow	3.1	–	–	–

Group accounts
61 – 100

3. Segmental information

(a) Primary reporting format – business segments

	2009 Group revenue £m	2009 Operating profit before acquired intangible amortisation, exceptional items £m	2009 Acquired intangible amortisation and exceptional items £m	2009 Group operating profit £m	2008 Group revenue £m	2008 Operating profit before acquired intangible amortisation, exceptional items £m	2008 Acquired intangible amortisation and exceptional items £m	2008 Group operating profit £m
Continuing operations								
Marine	892.9	89.3	(9.3)	80.0	633.2	68.7	(5.4)	63.3
Defence	338.4	28.9	(1.3)	27.6	302.1	27.5	(1.4)	26.1
Rail	228.9	(6.4)	(1.0)	(7.4)	228.1	0.5	(1.8)	(1.3)
Nuclear	106.7	13.0	(2.2)	10.8	76.3	5.7	(1.8)	3.9
Networks	119.4	7.0	(0.4)	6.6	98.5	7.2	(0.5)	6.7
Engineering and Plant	215.6	19.7	–	19.7	217.7	17.1	–	17.1
Unallocated	–	(4.2)	–	(4.2)	–	(5.6)	–	(5.6)
Total continuing operations	1,901.9	147.3	(14.2)	133.1	1,555.9	121.1	(10.9)	110.2
Finance cost		(32.1)	–	(32.1)		(32.0)	–	(32.0)
Finance income		5.9	–	5.9		6.4	–	6.4
Share of post-tax profit from joint ventures (net of tax)		(0.2)	–	(0.2)		–	–	–
Profit before tax		120.9	(14.2)	106.7		95.5	(10.9)	84.6
Income tax		(23.1)	4.0	(19.1)		(18.2)	3.3	(14.9)
Profit for the year from continuing operations		97.8	(10.2)	87.6		77.3	(7.6)	69.7
Discontinued operations								
Exceptional item		–	(18.4)	(18.4)		–	–	–
Income tax		–	5.1	5.1		–	–	–
Total for the year from discontinued operations		–	(13.3)	(13.3)		–	–	–
Total for the year	1,901.9	97.8	(23.5)	74.3	1,555.9	77.3	(7.6)	69.7

Inter divisional sales are immaterial.

The share of joint venture results not separately disclosed above are:

	2009				2008			
	Revenue £m	Operating profit £m	Tax and interest £m	Net JV results £m	Revenue £m	Operating profit £m	Tax and interest £m	Net JV results £m
Continuing operations								
Defence	12.5	0.4	(0.5)	(0.1)	0.6	0.1	–	0.1
Rail	0.7	0.2	(0.3)	(0.1)	0.7	0.3	(0.3)	–
Engineering and Plant	0.1	–	–	–	3.6	(0.1)	–	(0.1)
Total continuing operations	13.3	0.6	(0.8)	(0.2)	4.9	0.3	(0.3)	–

3. Segmental information (continued)

The segment assets and liabilities at 31 March 2009 and 31 March 2008 and capital expenditure for the years then ended are as follows:

	Assets		Liabilities		Capital expenditure	
	2009 £m	2008 £m	2009 £m	2008 £m	2009 £m	2008 £m
Marine	659.2	667.2	307.8	263.4	8.0	5.8
Defence	184.0	175.9	90.4	70.3	0.5	0.7
Rail	120.2	144.0	40.1	47.9	0.8	0.6
Nuclear	86.9	89.2	27.0	21.8	0.3	0.3
Networks	90.4	88.1	20.2	22.1	2.1	3.0
Engineering and Plant	119.7	93.7	77.6	79.1	4.5	3.5
Unallocated	157.3	199.2	561.8	591.9	3.1	0.3
Group total	1,417.7	1,457.3	1,124.9	1,096.5	19.3	14.2

Capital expenditure represents additions to property, plant and equipment and intangible assets.

All assets and liabilities are allocated to their appropriate segments except for cash, cash equivalents, borrowings and income and deferred tax which are included in the unallocated segment.

The segmental depreciation and amortisation of intangible assets for the years ended 31 March 2009 and 31 March 2008 are as follows:

	Depreciation		Amortisation of intangible assets	
	2009 £m	2008 £m	2009 £m	2008 £m
Marine	15.4	12.1	10.4	6.4
Defence	0.4	0.4	1.3	1.4
Rail	0.9	0.9	1.8	2.7
Nuclear	0.3	0.3	2.3	2.0
Networks	1.6	1.0	1.0	1.0
Engineering and Plant	2.5	2.2	0.1	–
Unallocated	0.6	0.5	–	–
Group total	21.7	17.4	16.9	13.5

(b) Secondary reporting format – geographical segments

	Revenue		Assets		Capital expenditure	
	2009 £m	2008 £m	2009 £m	2008 £m	2009 £m	2008 £m
United Kingdom	1,658.6	1,335.4	1,273.4	1,361.3	13.1	10.8
Africa	204.3	210.4	120.3	91.3	4.2	3.2
North America	29.6	7.2	18.9	2.6	2.0	0.2
Rest of World	9.4	2.9	5.1	2.1	–	–
Group total	1,901.9	1,555.9	1,417.7	1,457.3	19.3	14.2

	2009 £m	2008 £m
Analysis of revenue by category		
Sales of goods	249.1	252.9
Sales of services	1,651.5	1,301.7
Rental income	1.3	1.3
	1,901.9	1,555.9

4. Operating expenses

	2009 £m	2008 £m
Continuing operations		
Cost of sales	1,685.1	1,375.5
Distribution expenses	6.4	5.9
Administrative expenses	77.3	64.3
	1,768.8	1,445.7

5. Operating profit for the year

The following items have been included in arriving at operating profit for the year.

	Continuing operations	
	2009 £m	2008 £m
Employee costs (note 8)	615.1	487.9
Inventories		
– cost of inventories recognised as an expense	273.3	214.7
– (decrease)/increase in inventory provisions	(0.7)	1.0
Depreciation of property, plant and equipment (PPE)		
– owned assets	21.2	16.8
– under finance leases	0.5	0.6
	21.7	17.4
Amortisation of intangible assets		
– acquired intangibles	14.2	10.9
– software and development costs	2.7	2.6
	16.9	13.5
Impairment of other investments (note 16)	–	(0.3)
Profit on disposal of PPE	3.4	2.5
Operating lease rentals payable		
– property	13.4	10.6
– vehicles, plant and equipment	12.7	9.4
Research and development	0.7	0.3
Trade receivables impairment	1.1	1.7
Net foreign exchange (gains)/losses	0.6	(0.2)

There were no expenses in discontinued operations apart from the exceptional item disclosed in note 10.

5. Operating profit for the year (continued)

Services provided by the Group's auditor and network firms

During the year the Group (including its overseas subsidiaries) obtained the following services from the Group's auditor as detailed below:

	Total	
	2009 £m	2008 £m
Audit fees:		
Fees payable to the Group's auditor for the audit of the parent entity and the consolidated financial statements	0.4	0.5
Fees for other services:		
The auditing of accounts of subsidiaries of the company pursuant to legislation (including that of countries and territories outside Great Britain)	0.6	0.6
Tax	0.1	0.2
All other services	0.1	0.6
Total fees paid to the Group's auditor and network firms	1.2	1.9

Other services, last year, were in the main related to statutory requirements in relation to the DML acquisition.

6. Operating exceptional items and acquired intangible amortisation

In 2009 there were no operating exceptional items (2008: nil).

In 2009 acquired intangible amortisation was £14.2 million (2008: £10.9 million). The acquisition of Strachan & Henshaw (S&H) resulted in acquired intangible amortisation of £4.8 million of which £4.3 million is included in the Marine segment and £0.5 million in the Nuclear segment.

	2009 Acquired intangible amortisation £m	2008 Acquired intangible amortisation £m
Marine	(9.3)	(5.4)
Defence	(1.3)	(1.4)
Rail	(1.0)	(1.8)
Nuclear	(2.2)	(1.8)
Networks	(0.4)	(0.5)
	(14.2)	(10.9)

7. Net finance costs

	2009 £m	2008 £m
Finance costs		
Bank loans and overdrafts	25.2	25.0
Finance leases	0.1	0.2
Interest rate hedge	1.2	2.8
Amortisation of issue costs of bank loan	1.3	1.4
Other	4.3	2.6
Total finance costs	32.1	32.0
Finance income		
Bank deposits	4.7	6.4
Interest rate hedge	1.2	–
Total finance income	5.9	6.4
Net finance costs	26.2	25.6

8. Employee costs

	2009 £m	2008 £m
Wages and salaries	536.8	432.6
Social security costs	46.6	38.9
Share-based payments (note 26)	1.9	1.4
Pension costs – defined contribution plans (note 28)	13.9	11.2
Pensions charge – defined benefit plans (note 28)	15.9	3.8
	615.1	487.9

Pension costs on defined benefit schemes are before curtailment and settlement gains (see note 28).

The average number of people employed by the Group during the year were:

	2009 Number	2008 Number
Operations	14,200	13,231
Administration and management	2,189	1,771
	16,389	15,002

Emoluments of Executive Directors are included in employee costs above.

Key management compensation
Key management is defined as those employees who are directly responsible for the operational management of the key cash generating units. The employees would typically report to the Chief Executive.

	2009 £m	2008 £m
Salaries	7.7	7.2
Post-employment benefits	0.4	0.2
Share-based payments	1.7	1.4
	9.8	8.8

The key management figures given above include Directors.

9. Income tax expense

	2009 £m	2008 £m
Analysis of tax charge in the year		
Current tax		
– UK current year charge	19.1	12.6
– Overseas current year charge	5.7	7.8
– UK prior year charge/(credit)	0.6	(0.3)
– Overseas prior year credit	–	(1.3)
	25.4	18.8
Deferred tax		
– UK current year credit	(7.2)	(4.2)
– Overseas current year charge/(credit)	1.5	(1.3)
– Overseas prior year (credit)/charge	(0.6)	0.9
– Impact of change in UK tax rate	–	0.7
	(6.3)	(3.9)
Total income tax expense – continuing operations	19.1	14.9

The tax for the year is lower than the standard rate of corporation tax in the UK (28%). The differences are explained below:

	2009 £m	2008 £m
Profit before tax – continuing operations	106.7	84.6
Profit on ordinary activities multiplied by rate of corporation tax in the UK of 28% (2008: 30%)	29.9	25.4
Effects of:		
Expenses not deductible for tax purposes	1.5	1.0
Adjustments in respect of foreign tax rates	(8.1)	(6.5)
Utilisation of brought forward tax assets not previously recognised	–	(0.5)
Other	(4.2)	(5.2)
Remeasurement of deferred tax change in UK tax rate	–	0.7
Total income tax expense – continuing operations	19.1	14.9

10. Discontinued operations

The discontinued post tax exceptional item of £13.3 million arises from settlement being agreed between Babcock and other parties with Tesco Stores Limited (Tesco). As previously disclosed Babcock was in dispute with Tesco in relation to matters arising out of tunnelling works for the store at Gerrards Cross. This contract was originally entered into by the civil engineering division of Peterhouse Group plc, which was sold by Peterhouse Group plc, prior to Babcock's acquisition of the Peterhouse Group plc in 2004.

	2009 £m	2008 £m
Financial performance of discontinued operations		
Costs on previously disposed of businesses	(18.4)	–
	(18.4)	–
Taxation	5.1	–
Total discontinued operations	(13.3)	–

11. Dividends

	2009 £m	2008 £m
Final dividend for the year ended 31 March 2008 of 8.20p (2007: 5.65p) per 60p share	18.7	12.8
Interim dividend for the year ended 31 March 2009 of 4.00p (2008: 3.30p) per 60p share	9.2	7.5
	27.9	20.3

In addition, the Directors are proposing a final dividend in respect of the financial year ending 31 March 2009 of 10.40p (2008: 8.20p) per share which will absorb an estimated £23.8 million (2008: £18.7 million) of shareholders' equity. It will be paid on 7 August 2009 to shareholders who are on the register of members on 10 July 2009. These financial statements do not reflect this dividend payable.

12. Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year excluding those held in the Babcock Employee Share Trust and the Peterhouse Employee Share Trust. The calculation of the basic and diluted EPS is based on the following data:

Number of shares

	2009 Number	2008 Number
Weighted average number of ordinary shares for the purpose of basic EPS	228,037,214	224,459,855
Effect of dilutive potential ordinary shares: share options	1,550,512	4,264,409
Weighted average number of ordinary shares for the purpose of diluted EPS	229,587,726	228,724,264

Earnings

	2009 Earnings £m	2009 Basic per share Pence	2009 Diluted per share Pence	2008 Earnings £m	2008 Basic per share Pence	2008 Diluted per share Pence
Continuing operations						
Earnings from continuing operations	85.3	37.42	37.16	67.3	29.99	29.43
Add back:						
Amortisation of acquired intangible assets, net of tax	10.2	4.48	4.45	7.6	3.41	3.34
Exceptional items, net of tax	–	–	–	–	–	–
Earnings before discontinued operations, amortisation and exceptionals	95.5	41.90	41.61	74.9	33.40	32.77
Continuing and discontinued operations						
Earnings from continuing and discontinued operations	72.0	31.59	31.38	67.3	29.99	29.43
Add back:						
Amortisation of acquired intangible assets, net of tax	10.2	4.48	4.45	7.6	3.41	3.34
Exceptional items, net of tax	13.3	5.83	5.78	–	–	–
Earnings before amortisation and exceptionals	95.5	41.90	41.61	74.9	33.40	32.77

13. Goodwill

	2009 £m	2008 £m
Cost		
At 1 April	484.4	203.0
On acquisition of subsidiaries (note 32)	55.0	281.4
Exchange adjustments	0.6	–
At 31 March	540.0	484.4
Accumulated impairment		
At 1 April	4.8	4.8
Impairment charge	–	–
At 31 March	4.8	4.8
Net book value at 31 March	535.2	479.6

During the year, the goodwill was tested for impairment in accordance with IAS36. The recoverable amount for all the cash-generating units has been measured based on a value in use calculation derived from Board approved three year budgeted cash flows and extrapolated cash flows thereafter based on an estimated growth rate of 2% (effectively zero real growth allowing for inflation). A post-tax discount rate in the range 8% to 9% was grossed up for tax and used in the pre tax value in use calculation for the cash-generating units within each segment. The Group's weighted average cost of capital is approximately 8.6% (2008: 8.5%). The business with the least headroom (£12.8 million) in terms of impairment under the above assumptions is Rail where a 9.7% WACC or a 20% reduction in third year budgeted profits could result in an impairment.

Goodwill is allocated to the Group's cash-generating units (CGUs) identified according to the business segment and country of operation. A segment level summary of goodwill allocation is presented below:

	2009 £m	2008 £m
Marine	294.9	264.1
Defence	95.1	95.1
Rail	30.6	30.6
Nuclear	60.6	36.1
Networks	52.6	52.6
Engineering and Plant	1.4	1.1
	535.2	479.6
United Kingdom	533.8	478.5
Africa	0.1	0.2
North America	1.3	0.9
	535.2	479.6

Notes to the Group financial statements continued

14. Other intangible assets

	Acquired intangibles £m	Software £m	Development costs £m	Total £m
Cost				
At 1 April 2008	87.2	13.5	3.2	103.9
On acquisition of subsidiaries (note 32)	20.0	0.6	–	20.6
Additions	–	2.1	–	2.1
At 31 March 2009	107.2	16.2	3.2	126.6
Accumulated amortisation and impairment				
At 1 April 2008	33.3	4.6	3.1	41.0
Amortisation charge	14.2	2.7	–	16.9
At 31 March 2009	47.5	7.3	3.1	57.9
Net book value at 31 March 2009	59.7	8.9	0.1	68.7
Cost				
At 1 April 2007	40.5	7.2	3.2	50.9
On acquisition of subsidiaries	46.7	5.8	–	52.5
Additions	–	1.1	–	1.1
Disposals	–	(0.6)	–	(0.6)
At 31 March 2008	87.2	13.5	3.2	103.9
Accumulated amortisation and impairment				
At 1 April 2007	22.4	2.4	3.1	27.9
Amortisation charge	10.9	2.6	–	13.5
Amortisation on disposals	–	(0.4)	–	(0.4)
At 31 March 2008	33.3	4.6	3.1	41.0
Net book value at 31 March 2008	53.9	8.9	0.1	62.9

All amortisation charges for the year have been charged through cost of sales.

Acquired intangibles are the fair value of contracts and customer relationships of acquired entities.

15. Property, plant and equipment

	Freehold property £m	Leasehold property £m	Plant and equipment £m	Total £m
Cost				
At 1 April 2008	55.2	3.1	150.5	208.8
Exchange adjustments	0.1	–	3.7	3.8
On acquisition of subsidiaries (note 32)	2.0	–	2.8	4.8
Additions	0.6	1.7	14.9	17.2
Disposals	(1.3)	(0.9)	(17.7)	(19.9)
At 31 March 2009	56.6	3.9	154.2	214.7
Accumulated depreciation and impairment				
At 1 April 2008	13.3	1.1	48.5	62.9
Exchange adjustments	–	–	1.4	1.4
Charge for the year	3.7	0.2	17.8	21.7
Disposals	(0.5)	(0.7)	(17.2)	(18.4)
At 31 March 2009	16.5	0.6	50.5	67.6
Net book value at 31 March 2009	40.1	3.3	103.7	147.1
Cost				
At 1 April 2007	14.8	2.9	58.3	76.0
Exchange adjustments	–	–	(2.0)	(2.0)
On acquisition of subsidiaries	40.8	0.6	84.6	126.0
Additions	1.6	0.3	11.2	13.1
Disposals	(2.2)	(0.5)	(1.6)	(4.3)
Reclassification	0.2	(0.2)	–	–
At 31 March 2008	55.2	3.1	150.5	208.8
Accumulated depreciation and impairment				
At 1 April 2007	10.5	1.1	36.2	47.8
Exchange adjustments	–	–	(0.9)	(0.9)
Charge for the year	3.0	0.2	14.2	17.4
Disposals	(0.2)	(0.2)	(1.0)	(1.4)
At 31 March 2008	13.3	1.1	48.5	62.9
Net book value at 31 March 2008	41.9	2.0	102.0	145.9

Assets held under finance leases have the following net book value within plant and equipment:

	2009 £m	2008 £m
Cost	5.5	5.3
Aggregate depreciation and impairment	(3.3)	(2.7)
Net book value	2.2	2.6

Notes to the Group financial statements continued

16. Investment in and loan to joint ventures and other investments

	Joint ventures		Other investments		Total	
	2009 £m	2008 £m	2009 £m	2008 £m	2009 £m	2008 £m
At 1 April						
– Net assets excluding goodwill	0.2	0.7	–	9.4	0.2	10.1
– Goodwill	0.2	0.2	–	–	0.2	0.2
	0.4	0.9	–	9.4	0.4	10.3
Loans to joint ventures	12.1	–	–	–	12.1	–
Investment in joint venture	1.2	–	–	–	1.2	–
Reclassified as investment in subsidiary	–	–	–	(9.7)	–	(9.7)
Disposals	–	(0.3)	–	–	–	(0.3)
Dividends received	–	(0.2)	–	–	–	(0.2)
Share of profits	(0.2)	–	–	–	(0.2)	–
Impairment of investment	–	–	–	0.3	–	0.3
At 31 March						
– Net assets excluding goodwill	0.1	0.2	–	–	0.1	0.2
– Goodwill	1.4	0.2	–	–	1.4	0.2
– Loan to joint venture	12.0	–	–	–	12.0	–
	13.5	0.4	–	–	13.5	0.4

Following the signing of the RSME contract the Group loaned the joint venture company Holdfast Training Services Limited the sum of £12.0 million. It also acquired an additional interest of 26% in the joint venture company from WS Atkins plc for a net cash consideration of £1.2 million. The resultant shareholding is 74% but due to the sharing of control with our partners it will be accounted for as a joint venture.

On 25 January 2007 the Group acquired a 24.5% holding in International Nuclear Solutions PLC for £9.7 million, including costs. On 4 April 2007 the Group made an offer for the balance of the shares at 63p per share and on 9 July 2007 the Group had acquired 50.9% of the share capital and therefore reclassified the investment as an investment in subsidiary.

Included within joint ventures are:

	Country of incorporation	Assets £m	Liabilities £m	Revenue £m	Operating profit £m	Retained profit £m	% interest held
2009							
Holdfast Training Services Limited	United Kingdom	23.2	(10.2)	7.4	0.3	(0.2)	74%
FSP (2004) Limited	United Kingdom	3.6	(3.7)	0.7	0.3	–	50%
Mouchel Babcock Education Services Limited	United Kingdom	2.6	(2.4)	5.1	0.1	0.1	50%
Other		0.5	(0.1)	0.1	(0.1)	(0.1)	
		29.9	(16.4)	13.3	0.6	(0.2)	

	Country of incorporation	Assets £m	Liabilities £m	Revenue £m	Operating profit £m	Retained profit £m	% interest held
2008							
DynCorp-Hiberna Limited	United Kingdom	–	–	0.6	0.1	0.1	50%
FSP (2004) Limited	United Kingdom	4.0	(4.0)	0.7	0.3	–	50%
Babjeh Joint Venture	South Africa	0.3	(0.2)	3.6	(0.1)	(0.1)	50%
Other		0.4	(0.1)	–	–	–	
		4.7	(4.3)	4.9	0.3	–	

The joint ventures have no significant contingent liabilities to which the Group is exposed.

17. Deferred tax

	2009 £m	2008 £m
Deferred tax asset	2.8	3.0
Deferred tax liability	(0.2)	(31.2)
	2.6	(28.2)

The movements in deferred tax assets and liabilities (prior to offsetting of balances within the same tax jurisdiction as permitted by IAS12) during the period are shown below:

	Accelerated tax depreciation £m	ACT £m	Retirement benefit obligations £m	Tax losses £m	Other £m	Total £m
At 1 April 2008	(8.9)	3.1	(39.8)	3.3	14.1	(28.2)
Income statement credit/(charge)	(0.9)	–	4.1	–	3.1	6.3
Tax charge to equity	–	–	40.7	–	3.3	44.0
Transfer to corporation tax	–	–	(19.2)	6.0	(0.7)	(13.9)
Acquisition of subsidiaries (note 32)	–	–	–	–	(5.5)	(5.5)
Exchange differences	–	–	–	–	(0.1)	(0.1)
At 31 March 2009	(9.8)	3.1	(14.2)	9.3	14.2	2.6
At 1 April 2007	4.9	3.3	(16.0)	0.1	7.7	–
Income statement credit	0.4	–	0.4	–	3.8	4.6
Tax charge to equity	–	–	(12.9)	–	3.5	(9.4)
Transfer to corporation tax	–	–	(9.1)	3.2	(0.3)	(6.2)
Acquisition of subsidiaries	(13.8)	–	(4.6)	–	–	(18.4)
Effect of change in tax rate						
– income statement	(0.4)	(0.2)	–	–	(0.1)	(0.7)
– equity	–	–	2.4	–	(0.4)	2.0
Exchange differences	–	–	–	–	(0.1)	(0.1)
At 31 March 2008	(8.9)	3.1	(39.8)	3.3	14.1	(28.2)

The deferred tax asset in respect of 'other' includes an asset of £2.8 million (2008: £3.0 million) in respect of the Group's non-UK operations. This is disclosed separately in the Group's balance sheet, as it cannot be offset against the net overall UK deferred tax liability of £0.2 million (2008: £31.2 million).

Deferred tax assets have been recognised in respect of tax losses and other temporary differences giving rise to deferred tax assets because it is probable that these assets will be recovered.

Certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2009 £m	2008 £m
Deferred tax asset	(23.8)	(17.5)
Deferred tax liability	24.0	48.7
	0.2	31.2

At the balance sheet date, the Group has unused tax losses (excluding UK capital losses and advance corporation tax) of £82.4 million (2008: £61.3 million) available for offset against future profits. A deferred tax asset has been recognised in respect of £33.0 million (2008: £11.0 million) of such losses, which may be carried forward indefinitely. No deferred tax has been recognised in respect of the remaining £49.4 million (2008: £50.3 million) due to the unpredictability of future profit streams.

At the balance sheet date, the aggregate amount of temporary differences associated with undistributed earnings of subsidiaries for which deferred tax liabilities have not been recognised was £95 million (2008: £50 million). No liability has been recognised in respect of these differences because the Group is in a position to control the timing of the reversal of the temporary differences and it is probable that such differences will not reverse in the foreseeable future.

18. Inventories

	2009 £m	2008 £m
Raw materials	24.1	24.1
Work in progress and long-term contracts	11.2	10.3
Finished goods and goods for resale	59.1	42.3
Total	94.4	76.7

19. Trade and other receivables

	2009 £m	2008 £m
Current assets		
Trade receivables	111.7	108.2
Less: provision for impairment of receivables	(5.7)	(4.4)
Trade receivables – net	106.0	103.8
Amounts due from customers for contract work	182.4	204.7
Retentions	9.7	6.9
Amounts owed by related parties (note 37)	12.8	7.2
Other debtors	7.5	3.9
Prepayments and accrued income	17.3	14.4
	335.7	340.9
Non-current assets		
Other debtors	0.2	1.7

Trade and other receivables are classified as loans and receivables and are stated at amortised cost.

As of 31 March 2009, trade receivables of £5.8 million (2008: £5.0 million) were impaired. Impairment arises in the main, through contract disputes rather than credit disputes. The amount of the provision was £5.7 million (2008: £4.4 million). The individually impaired receivables mainly relate to debtors in Engineering and Plant. It was assessed that a portion of these receivables is expected to be recovered.

The ageing of the impaired receivables is as follows:

	2009 £m	2008 £m
Less than three months	–	–
Three to six months	–	–
Over six months	0.1	0.6
	0.1	0.6

As of 31 March 2009, trade receivables of £22.8 million (2008: £26.7 million) were past due but not impaired. These relate to a number of independent customers for whom there is no recent history of default. The ageing analysis of these trade receivables is as follows:

	2009 £m	2008 £m
Less than three months	13.2	21.0
Three to six months	8.9	4.2
Over six months	0.7	1.5
	22.8	26.7

The carrying amounts of the Group's trade and other receivables are, in the main, denominated in Sterling.

19. Trade and other receivables (continued)

Movements on the provision for impairment of trade receivables are as follows:

	2009 £m	2008 £m
Balance at 1 April	(4.4)	(2.2)
Acquisition of subsidiaries	–	(0.8)
Provision for receivables impairment	(2.5)	(2.3)
Receivables written off during the year as uncollectable	0.2	0.1
Unused amounts reversed	1.4	0.6
Exchange differences	(0.4)	0.2
Balance at 31 March	(5.7)	(4.4)

The creation and release of provisions for impairment of receivables have been included in cost of sales in the income statement (note 5). Amounts charged to the impairment provision are generally written off when there is no expectation of recovering additional cash.

The other classes within trade and other receivables do not contain impaired assets.

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivables mentioned above. The Group does not hold any collateral as security other than retention of title clauses issued as part of the ordinary course of business.

20. Cash and cash equivalents

	2009 £m	2008 £m
Cash at bank and in hand	116.3	193.7
Short-term bank deposits (overnight)	7.3	5.9
	123.6	199.6

The carrying amount of the Group's cash and cash equivalents are denominated in the following currencies:

	2009		2008	
	Total £m	Floating rate £m	Total £m	Floating rate £m
Currency				
Sterling	105.8	105.8	178.7	178.7
Euro	5.6	5.6	2.2	2.2
US Dollar	5.6	5.6	2.0	2.0
South African Rand	1.1	1.1	15.1	15.1
Canadian Dollar	3.5	3.5	–	–
Swedish Krona	–	–	0.2	0.2
Other currencies	2.0	2.0	1.4	1.4
	123.6	123.6	199.6	199.6

The above balances are invested at short term, floating rates linked to LIBOR in the case of Sterling, the prime rate in the case of South African Rand and the local prime rate for other currencies.

21. Trade and other payables

	2009 £m	2008 £m
Current liabilities		
Contract cost accruals	178.4	162.7
Amounts due to customers for contract work	52.2	29.8
Trade creditors	138.5	146.1
Amounts owed to related parties (note 37)	0.6	2.6
Other creditors	16.7	20.6
Other taxes and social security	25.7	27.7
Accruals and deferred income	105.9	77.2
	518.0	466.7
Non-current liabilities		
Other creditors	16.0	15.3

22. Bank and other borrowings

	2009 £m	2008 £m
Current liabilities		
Bank loans and overdrafts due within one year or on demand		
Unsecured	117.9	143.7
	117.9	143.7
Finance lease obligations (a)	0.7	0.6
	118.6	144.3
Non-current liabilities		
Bank loans		
Unsecured	355.0	375.5
	355.0	375.5
Finance lease obligations (a)	1.5	2.0
	356.5	377.5

(a) Finance leases are secured against the assets to which they relate

Bank loans are denominated in a number of currencies and bear interest based on LIBOR or foreign equivalents appropriate to the country in which the borrowing is incurred. The Group has entered into interest rate swaps and collars, details of which are included in note 23.

The carrying amount of the Group's borrowings are denominated in the following currencies:

	2009		
	Total £m	Floating rate £m	Fixed rate £m
Currency			
Sterling	462.9	461.2	1.7
South African Rand	11.5	11.5	–
Other	0.7	0.7	–
	475.1	473.4	1.7

22. Bank and other borrowings (continued)

	2008		
	Total £m	Floating rate £m	Fixed rate £m
Currency			
Sterling	520.7	518.6	2.1
South African Rand	–	–	–
Other	1.1	1.1	–
	521.8	519.7	2.1

The weighted average interest rates of Sterling fixed rate borrowings, which comprise finance lease obligations, are 5.0%. The weighted average period for which these interest rates are fixed is four years.

The floating rate for borrowings is linked to LIBOR in the case of Sterling, the prime rate in the case of South African Rand and the local prime rate for other currencies.

The exposure of the Group to interest rate changes when borrowings re-price is as follows:

Total borrowings	1 year £m	1–5 years £m	5 years £m	Total £m
As at 31 March 2009	313.6	161.5	–	475.1
As at 31 March 2008	319.3	202.5	–	521.8

The effective interest rates at the balance sheet dates were as follows:

	2009 %	2008 %
UK bank overdraft	1.5	6.8
UK bank borrowings	2.2	6.2
Other borrowings	14.7	14.2
Finance leases	2.0–15.0	5.0–6.0

Repayment details
The total borrowings of the Group at 31 March are repayable as follows:

	2009		2008	
	Bank loans and overdrafts £m	Finance lease obligations £m	Bank loans and overdrafts £m	Finance lease obligations £m
Within one year	117.9	0.7	143.7	0.6
Between one and two years	–	0.6	0.5	0.6
Between two and five years	355.0	0.9	375.0	1.4
Greater than five years	–	–	–	–
	472.9	2.2	519.2	2.6

22. Bank and other borrowings (continued)

Borrowing facilities

The Group has the following undrawn committed borrowing facilities available at 31 March in respect of which all conditions precedent had been met at that date.

	2009 £m	2008 £m
Expiring in less than one year	24.0	45.0
Expiring in more than one year but not more than five years	245.0	225.0
	269.0	270.0

The minimum lease payments under finance leases fall due as follows:

	2009 £m	2008 £m
Not later than one year	0.6	0.6
Later than one year but not more than five years	1.7	2.2
More than five years	–	–
	2.3	2.8
Future finance charges on finance leases	(0.1)	(0.2)
Present value of finance lease liabilities	2.2	2.6

23. Financial instruments

Other financial assets and liabilities

	Fair value			
	Assets		Liabilities	
	2009 £m	2008 £m	2009 £m	2008 £m
Financial derivatives	1.0	1.7	0.1	0.5
Interest rate hedges	–	–	15.0	3.7
Total other financial assets and liabilities	1.0	1.7	15.1	4.2

The Group enters into forward foreign currency contracts to hedge the currency exposures that arise on sales and purchases denominated in foreign currencies, as the transaction occurs.

The Group enters into interest rate hedges to hedge interest rate exposure.

Interest rate hedges

The notional principal amount of the outstanding interest rate swap and collar contracts at 31 March 2009 was £200 million (2008: £200 million).

The Group held the following interest rate hedges at 31 March 2009:

	Amount £m	Fixed %	Maturity
Hedged			
SWAPS	40.0	5.27	20/10/2009
Collar	10.0	Cap 6.25 and floor 5.25	20/07/2011
Collars	150.0	Cap 6.25 and floor 5.25	20/07/2012
Total interest rate hedges	200.0		

23. Financial instruments (continued)

Fair value of financial assets and financial liabilities

The fair values of financial assets and liabilities at the balance sheet date were:

	2009		2008	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Fair value of non-current borrowings and loans				
Long-term borrowings	(356.5)	(356.4)	(377.5)	(377.2)
Loan to joint venture	12.0	6.2	–	–
	(344.5)	(350.2)	(377.5)	(377.2)
Fair value of other financial assets and financial liabilities				
Short-term borrowings	(118.6)	(118.6)	(144.3)	(144.3)
Trade and other payables	(549.2)	(547.2)	(493.6)	(493.6)
Trade and other receivables	340.5	340.5	344.9	344.9
Short-term deposits	7.3	7.3	5.9	5.9
Cash at bank and in hand	116.3	116.3	193.7	193.7
Other financial assets and liabilities	(14.1)	(14.1)	(2.5)	(2.5)
	(217.8)	(215.8)	(95.9)	(95.9)

Fair values of long-term borrowings are based on cash flows discounted using a rate of 4.0% (2008: 5.5%).

24. Provisions for other liabilities

	Acquisition/ deferred consideration £m	Insurance provisions (a) £m	Reorganisation or disposal of businesses (b) £m	Property and other (c) £m	Total provisions £m
At 1 April 2008	0.7	3.6	3.9	37.1	45.3
On acquisition of subsidiaries	–	–	–	1.9	1.9
Charged/(released) to income statement	(0.4)	1.3	1.5	1.8	4.2
Utilised in year	(0.3)	(0.1)	(1.1)	(4.8)	(6.3)
Exchange differences	–	–	–	–	–
At 31 March 2009	–	4.8	4.3	36.0	45.1

Provisions have been analysed between current and non-current as follows:

	2009 £m	2008 £m
Current	9.7	13.0
Non-current	35.4	32.3
	45.1	45.3

(a) The insurance provisions arise in the Group's captive insurance companies, Chepstow Insurance Limited and Peterhouse Insurance Limited. They relate to specific claims assessed in accordance with the advice of independent actuaries.

(b) Provisions for costs, claims and litigation relating to the reorganisation or disposal of businesses.

(c) Property and other in the main relate to provisions for onerous leases, dilapidation costs and contractual obligations in respect of infrastructure.

Included within property and other provisions is £21.8 million expected to be utilised in approximately ten years. Other than this provision the Group's non-current provisions are expected to be utilised within two to five years.

25. Share capital

	Ordinary shares of 60p Number	Unclassified shares of 30p Number	Ordinary shares of 60p £m	Unclassified shares of 30p £m
Authorised:				
At 1 April 2008	306,219,012	1	183.7	–
Authorised during the year	–	–	–	–
At 31 March 2009	306,219,012	1	183.7	–
At 1 April 2007	306,219,012	1	183.7	–
Authorised during the year	–	–	–	–
At 31 March 2008	306,219,012	1	183.7	–

	Ordinary shares of 60p Number	Total £m
Allotted, issued and fully paid		
At 1 April 2008	229,356,369	137.6
Shares issued	218,590	0.1
At 31 March 2009	229,574,959	137.7
At 1 April 2007	209,741,819	125.8
Shares issued	19,614,550	11.8
At 31 March 2008	229,356,369	137.6

Potential issues of ordinary shares

The table below shows options existing over the Company's shares as at 31 March 2009. They represent outstanding options granted under all the Company's Executive Share Option Schemes. Of the total number of shares shown, 175,258 are in respect of options granted by the trustee of the Babcock Employee Share Trust and 51,782 are in respect of options granted by the trustee of the Peterhouse Employee Share Trust, both are options to acquire shares already purchased or intended to be purchased in the market by the respective trustees. The balance of 559,501 shares is in respect of options granted by the Company to subscribe for newly issued shares.

Grant date	Exercise price Pence	Exercise period	2009 Number	2008 Number
08 July1999	122.50	08/07/2002 – 07/07/2009	11,604	86,604
09 September 1999	118.00	09/09/2002 – 08/09/2009	11,800	11,800
25 June 2001	99.33	25/06/2004 – 24/06/2011	28,096	64,600
31 January 2002	104.33	31/01/2005 – 30/01/2012	21,278	21,278
24 June 2002	124.50	24/06/2005 – 23/06/2012	224,291	625,897
27 November 2002	106.33	27/11/2005 – 26/11/2012	31,480	35,082
30 June 2003	115.60	30/06/2006 – 29/06/2013	153,049	222,449
06 July 2004	126.00	06/07/2007 – 05/07/2014	304,943	501,962
			786,541	1,569,672

Options granted to Directors are summarised in the Remuneration report on pages 48 to 60 and are included in the outstanding options set out above.

25. Share capital (continued)

A reconciliation of option movements is shown below:

	2009		2008	
	Number '000	Weighted average exercise price	Number '000	Weighted average exercise price
Outstanding at 1 April	1,570	£1.22	4,220	£1.21
Forfeited/lapsed	(37)	£1.16	(35)	£1.26
Exercised	(746)	£1.23	(2,615)	£1.20
Outstanding at 31 March	787	£1.21	1,570	£1.22
Exercisable at 31 March	787	£1.21	1,570	£1.22

Weighted average share price for options exercised during the year was 489.3p per share (2008: 547.1p per share).

26. Share-based payments

The charge to the income statement has been based on the assumptions below and is based on the binomial model as adjusted, allowing for a closed form numerical-integrated solution, which makes it analogous to the Monte Carlo simulations, including performance conditions. The detailed description of the plans below is included within the Remuneration report.

During the year the total charge relating to employee share-based payment plans was £1.9 million (2008: £1.4 million) all of which related to equity settled share-based payment transactions.

After tax, the income statement charge was £1.4 million (2008: £1.0 million).

The fair value per option granted and the assumptions used in the calculation are as follows:

L-TIPS

Grant or modification date	2008 TSR 19/6/08	2008 EPS 19/6/08	2007 TSR 26/6/07	2007 EPS 26/6/07	2006 TSR 24/7/06	2006 EPS 24/7/06
Share price at grant or modification date (pence)	594.3	594.3	556.8	556.8	338.5	338.5
Vesting period (years)	3.0	3.0	3.0	3.0	3.0	3.0
Expected volatility	25%	25%	25%	25%	25%	25%
Option life (years)	10.0	10.0	10.0	10.0	10.0	10.0
Expected life (years)	3.0	3.0	3.0	3.0	3.0	3.0
Expected dividends expressed as dividend yield	2.8%	2.8%	2.8%	2.8%	2.8%	2.8%
Expectations of meeting performance criteria	n/a	40%	n/a	100%	n/a	100%
Fair value per option (pence)	448	546	370	512	276	311
Correlation	32%	n/a	18%	n/a	15%	n/a

The number of L-TIP's awarded in 2008 were 427,218, in 2007 were 396,227 and in 2006 were 551,405.

The expected volatility is based on historical volatility over the last one to three years. The expected life is the average expected period to exercise. The risk free rate of return is the yield on zero-coupon government bonds of a term consistent with the assumed option life.

Notes to the Group financial statements continued

27. Statement of changes in equity

	Share capital	Share premium	Capital redemption £m	Retained earnings £m	Other reserves £m	Total £m	Minority interests £m	Year ended 31 March £m
At 1 April 2007	125.8	70.1	30.6	(17.1)	(3.8)	205.6	1.6	207.2
Shares issued in the period	11.8	78.0	–	–	–	89.8	–	89.8
Recognised income and expense	–	–	–	100.8	(5.9)	94.9	2.2	97.1
Dividends	–	–	–	(20.3)	–	(20.3)	(1.1)	(21.4)
Share-based payments	–	–	–	1.4	–	1.4	–	1.4
Tax on share-based payments	–	–	–	2.3	–	2.3	–	2.3
INS acquisition	–	–	–	–	–	–	1.9	1.9
Transactions with minority interests	–	–	–	(11.5)	–	(11.5)	(1.0)	(12.5)
Own shares	–	–	–	(5.0)	–	(5.0)	–	(5.0)
Net movement in equity	11.8	78.0	–	67.7	(5.9)	151.6	2.0	153.6
At 31 March 2008	137.6	148.1	30.6	50.6	(9.7)	357.2	3.6	360.8
At 1 April 2008	137.6	148.1	30.6	50.6	(9.7)	357.2	3.6	360.8
Shares issued in the period	0.1	0.1	–	–	–	0.2	–	0.2
Recognised income and expense	–	–	–	(32.8)	(2.4)	(35.2)	2.6	(32.6)
Dividends	–	–	–	(27.9)	–	(27.9)	(1.8)	(29.7)
Share-based payments	–	–	–	1.9	–	1.9	–	1.9
Tax on shared-based payments	–	–	–	(0.3)	–	(0.3)	–	(0.3)
Own shares	–	–	–	(7.5)	–	(7.5)	–	(7.5)
Net movement in equity	0.1	0.1	–	(66.6)	(2.4)	(68.8)	0.8	(68.0)
Equity at 31 March 2009	137.7	148.2	30.6	(16.0)	(12.1)	288.4	4.4	292.8

Other reserves include a translation reserve of £1.4 million debit (2008: £7.4 million debit) and a hedging reserve of £10.7 million debit (2008: £2.3 million debit).

During the year the Company acquired 1,749,925 ordinary shares (2008: 1,342,845) through either the Babcock Employee Share Trust or the Peterhouse Employee Share Trust (together 'the Trusts') in respect of obligations under the Babcock 1999 Executive Share Option Schemes or the Babcock 2003 L-TIP. During the year ended 31 March 2009 2,517,578 shares (2008: 3,179,286 shares) were disposed by the Trusts resulting from options exercised. At 31 March 2009, the Trusts held between them a total of 948,095 (2008: 1,715,748) ordinary shares at a total market value of £4,072,068 (2008: £9,805,500) representing 0.41% (2008: 0.75%) of the issued share capital at that date. The Company elected to pay dividends to the Babcock Employee Share Trust at the rate of 0.001p per share during the year, though full dividends were paid in respect of shares held by the Peterhouse Employee Share Trust. All the Trusts' shares are under option, the subject of L-TIP share awards to employees or represent a provision for future L-TIP vesting. The Company meets the operating expenses of the Trusts.

The Trusts enable shares in the Company to be held or purchased and made available to employees through the grant and exercise of rights or awards under the Babcock 1999 Executive Share Option Schemes and the Babcock 2003 L-TIP. The Trusts are discretionary settlements for the benefit of employees within the Group. The Company is excluded from benefiting under them. They are controlled and managed outside the UK and each has a single corporate trustee which is an independent trustee services organisation. The right to remove and appoint the trustees rests ultimately with the Company. The trustee of the Babcock Employee Share Trust is required to waive both voting rights and dividends payable on any share in the Company in excess of 0.001p, unless otherwise directed by the Company, but the trustee of the Peterhouse Employee Share Trust does not have the power to waive dividends due on Babcock ordinary shares and therefore receives the full amount of any dividends declared.

28. Retirement benefits and liabilities

The Group has established a number of pension schemes around the world covering many of its employees. The principal funds are those in the UK.

Defined contributions schemes

Pension costs for defined contribution schemes are as follows:

	2009 £m	2008 £m
Defined contribution schemes	13.9	11.2

Defined benefit schemes

Balance sheet assets and liabilities recognised are as follows:

	2009 £m	2008 £m
Retirement benefits – funds in surplus	90.9	142.6
Retirement benefits – funds in deficit	(40.2)	(0.4)
	50.7	142.2

The Group operates four principal defined benefit schemes for employees in the United Kingdom; the Devonport Royal Dockyard Pension Scheme, the Babcock International Group Pension Scheme, the Rosyth Royal Dockyard Pension Scheme and the First Engineering Shared Cost Section of the Railways Pensions Scheme. The Alstec Pension Scheme merged into the Babcock International Group Pension Scheme with effect from 1 July 2008. All four schemes are funded by payments to separate trustee-administered funds and the level of the Group's contributions to the schemes is assessed in accordance with the advice of independent, qualified actuaries. The details of the latest formal actuarial valuations of these four schemes are as follows:

	Devonport Royal Dockyard Scheme	Babcock International Group Scheme	Rosyth Royal Dockland Scheme	First Engineering Scheme
Date of last formal actuarial valuation	31/03/08	01/04/07	31/03/06	31/12/04
Number of active members at 31 March 2009	3,655	757	1,037	667
Actuarial valuation method	Projected unit	Projected unit	Projected unit	Attained age
Results of formal actuarial valuation:				
Value of assets	£850.0m	£468.9m	£448.3m	£121.4m
Level of funding	95%	103%	98%	96%
Principal valuation assumptions:				
Excess of investment returns over earnings increases	2.0%	1.65%–2.4%	1.75%	(0.5%)–1.75%
Excess of investment returns over pension increases	3.0%	1.6%–3.25%	2.75%	1.75%–1.95%

As a result of the level of surplus the Group's required contribution to the Babcock International Group Pension Scheme is currently suspended in respect of the majority of active members until at least the results of the next formal valuation are available. The Group does however make voluntary payments to the Scheme.

The contribution rate for the Devonport Royal Dockyard Pension Scheme is 20.5% of pensionable pay with additional payments of £5 million per annum to meet the funding deficit. The contribution rate for the Rosyth Royal Dockyard Pension Scheme is 16.4% and the First Engineering Scheme is 20.1%. The cash contributions forecast for next year are: the Devonport Royal Dockyard Pension Scheme £23.8 million, the Babcock International Group Pension Scheme £4.4 million, the Rosyth Royal Dockyard Pension Scheme £7.0 million and the First Engineering Scheme £3.2 million.

The Babcock Holdings (USA) Inc Pension Plan is for employees of US subsidiaries of Babcock Holdings (USA) Inc. A full actuarial valuation of the Scheme was carried out as at 31 December 2007. The Company made a contribution of £0.1 million during the year to 31 March 2009. The plan was frozen as of 31 January 2003 and therefore, no active members existed as at 31 March 2009.

The HMNB Clyde contract includes a contract specific defined benefit pension scheme where all funding risk is borne by the customer and hence the costs are included within the defined contribution analysis above.

28. Retirement benefits and liabilities (continued)

The latest full actuarial valuation of the Group's defined benefit pension schemes have been updated to 31 March by qualified independent actuaries for IAS19 purposes using the following assumptions:

	2009 (weighted average) %	2008 (weighted average) %
Rate of increase in pensionable salaries	3.20	4.36
Rate of increase in pensions	2.65	3.26
Discount rate	7.10	6.90
Inflation rate	2.70	3.50
Expected return on plan assets	7.39	6.97
Total life expectancy – future pensioners (years)	84.5	83.4

The fair value of the assets, the present value of the liabilities and the expected rates of return of the Group pensions schemes at 31 March were as follows:

	2009		2008	
	Expected rate of return %	Fair value £m	Expected rate of return %	Fair value £m
Equities	9.0	608.8	8.0	803.0
Property	8.0	117.9	7.5	149.3
Bonds – corporate	7.1	181.6	6.9	297.3
Bonds – government	4.0	81.0	4.6	147.7
Liability matching bonds	6.1	661.1	6.0	541.2
Cash plus infrastructure	8.0	14.2	8.0	28.1
Cash	–	–	5.3	17.2
Funds awaiting investment	7.3	38.3	–	–
Fair value of assets		1,702.9		1,983.8
Present value of funded obligation		(1,652.2)		(1,841.6)
Net assets recognised in the balance sheet		50.7		142.2

The amounts recognised in the income statement are as follows:

	2009 £m	2008 £m
Current service cost	(26.7)	(26.8)
Interest on obligation	(116.6)	(92.1)
Expected return on plan assets	127.4	115.1
Charge before settlements and curtailments	(15.9)	(3.8)
Settlement gains	–	2.4
Curtailment gain	1.4	0.1
Total included within operating profit	(14.5)	(1.3)

28. Retirement benefits and liabilities (continued)

Amounts recorded in statement of recognised income and expense

	2009 £m	2008 £m
Actual return less expected return on pension scheme assets	(383.0)	(158.0)
Experience gains/(losses) arising on scheme liabilities	6.1	(15.7)
Change in assumptions relating to present value of scheme liabilities	231.3	216.7
At 31 March	(145.6)	43.0
Cumulative recognised income and expense at 31 March	(86.5)	59.1

Analysis of movement in the balance sheet

	2009 £m	2008 £m
Fair value of plan assets		
At 1 April	1,983.8	1,200.9
Acquisition of subsidiaries	–	883.6
Expected return	127.4	115.1
Actuarial loss	(383.0)	(158.0)
Assets acquired on settlements	–	(14.7)
Employer contributions	68.6	30.8
Employee contributions	5.8	5.3
Benefits paid	(100.5)	(79.2)
Exchange differences	0.8	–
At 31 March	1,702.9	1,983.8
Present value of benefit obligations		
At 1 April	1,841.6	1,147.8
Acquisition of subsidiaries	–	867.0
Service cost	26.7	26.8
Interest cost	116.6	92.1
Employee contributions	5.8	5.3
Actuarial gain	(237.4)	(201.0)
Settlement gains	–	(17.1)
Curtailment gain	(1.4)	(0.1)
Benefits paid	(100.5)	(79.2)
Exchange differences	0.8	–
At 31 March	1,652.2	1,841.6
Net surplus at 31 March	50.7	142.2
Actual return on plan assets		
Year ending 31 March	(255.6)	(42.9)

The expected return on plan assets is based on long-term market expectations at the beginning of the year. In the case of equities there is a premium over the risk free rate.

Notes to the Group financial statements continued

28. Retirement benefits and liabilities (continued)

History of experience gains and losses

	2009 £m	2008 £m	2007 £m	2006 £m	2005 £m
Difference between the expected and actual return on scheme assets	(383.0)	(158.0)	(9.5)	121.3	32.8
Percentage of scheme assets at 31 March	(22%)	(8%)	(1%)	11%	3%
Experience gains/(losses) of scheme liabilities	6.1	(15.7)	(13.1)	(22.1)	(11.4)
Percentage of present value of scheme liabilities at 31 March	0%	1%	1%	2%	1%
Total amount recognised in Statement of recognised income and expense	(145.6)	43.0	8.7	42.2	(34.8)
Percentage of present value of scheme liabilities at 31 March	(9%)	2%	1%	4%	3%

The changes to the balance sheet at March 2009 and the charges to the income statement for the year to March 2010, if the assumptions were sensitised by the amounts below, would be:

	Balance sheet 2009 £m	Income statement 2010 £m
Initial assumptions	50.7	19.0
Discount rate moves up or down by 0.1%	±21.9	±0.7
Inflation rate moves up or down by 0.1%	±19.3	±1.8
Equity return moves up or down by 0.1%	–	±0.4
Total life expectancy changes by half a year up or down	±19.3	±1.7
Real salaries move up or down by 0.25%	±16.2	±1.9

29. Reconciliation of operating profit to cash generated from operations

	2009 £m	2008 £m
Cash flows from operating activities		
Operating profit	133.1	110.2
Depreciation of property, plant and equipment	21.7	17.4
Amortisation of intangible assets	16.9	13.5
Equity share-based payments	1.9	1.4
Impairment of investments	–	(0.3)
Profit on disposal of property, plant and equipment	(3.4)	(2.5)
Operating cash flows before movement in working capital	170.2	139.7
Increase in inventories	(7.0)	(16.3)
Increase in receivables	(9.9)	(95.4)
Increase in payables	2.1	97.2
Decrease in provisions	(1.8)	(6.0)
Cash generated from operations	153.6	119.2

30. Movement in net debt

	2009 £m	2008 £m
(Decrease)/increase in cash in the year	(51.7)	35.9
Cash flow from the decrease/(increase) in debt and lease financing	21.2	(276.0)
Change in net funds resulting from cash flows	(30.5)	(240.1)
Loans acquired with subsidiaries	–	(7.0)
New finance leases	(0.2)	–
Foreign currency translation differences	1.4	(1.4)
Movement in net debt in the year	(29.3)	(248.5)
Net debt at the beginning of the year	(322.2)	(73.7)
Net debt at the end of the year	(351.5)	(322.2)

31. Changes in net debt

	At 1 April 2008 £m	Cash flow £m	Acquisitions and disposals £m	New finance leases £m	Exchange movement £m	At 31 March 2009 £m
Cash and bank balances	199.6	(84.5)	6.9	–	1.6	123.6
Bank overdrafts	(143.1)	25.9	–	–	(0.1)	(117.3)
Cash, cash equivalents and bank overdrafts at end of year	56.5	(58.6)	6.9	–	1.5	6.3
Debt	(376.1)	20.7	–	–	(0.2)	(355.6)
Finance leases	(2.6)	0.5	–	(0.2)	0.1	(2.2)
	(378.7)	21.2	–	(0.2)	(0.1)	(357.8)
Total	(322.2)	(37.4)	6.9	(0.2)	1.4	(351.5)

32. Acquisitions

On 21 April 2008 the Group acquired 100% of the share capital of S&H for a consideration of £72.1 million, inclusive of costs. S&H is a specialist engineering design, project manager and provider of through-life support for the defence and nuclear industries.

The goodwill arises from the experience, knowledge and location of the workforce along with the market position of the entities involved.

Details of the assets acquired and the goodwill are as follows:

	S&H £m	Other £m	Total £m
Cost of acquisition			
Purchase consideration	70.6	1.0	71.6
Direct costs	1.5	–	1.5
Total purchase consideration and costs	72.1	1.0	73.1
Fair value of assets acquired (see below)	17.1	1.0	18.1
Goodwill	55.0	–	55.0

Notes to the Group financial statements continued

32. Acquisitions (continued)
Net assets and liabilities arising from the acquisition are as follows:

	S&H		Other	Total	
	Book value of assets acquired £m	Fair value acquired £m	Book value/ fair value acquired £m	Book value of assets acquired £m	Fair value acquired £m
Goodwill	1.9	–	–	1.9	–
Intangible assets	0.9	0.6	–	0.9	0.6
Acquired intangibles*	–	19.1	0.9	0.9	20.0
Property plant and equipment	5.1	4.8	–	5.1	4.8
Deferred tax	0.2	(5.3)	(0.2)	–	(5.5)
Cash, cash equivalents and bank overdraft	6.9	6.9	–	6.9	6.9
Inventory	0.1	0.1	–	0.1	0.1
Current assets	15.1	15.1	–	15.1	15.1
Current and non-current liabilities	(22.3)	(22.3)	0.3	(22.0)	(22.0)
Provisions	(1.9)	(1.9)	–	(1.9)	(1.9)
Net assets acquired	6.0	17.1	1.0	7.0	18.1

*Acquired intangibles are: customer relationships and order book.

Cash outflow to acquire businesses net of cash acquired:

	S&H £m	Other £m	Total £m
Total purchase consideration plus costs	72.1	1.0	73.1
Cash, cash equivalents and bank overdrafts	(6.9)	–	(6.9)
Cash outflow this period	65.2	1.0	66.2

The revenue and operating profit of acquired businesses since the date of acquisition and as if they had been acquired on 1 April 2008 are:

	Since date of acquisition £m	For full year £m
Revenue		
S&H	58.9	62.3
Other	–	–
	58.9	62.3
Operating profit (before amortisation of acquired intangibles)		
S&H	7.3	7.7
Other	–	–
	7.3	7.7

33. Disposals
The cash outflow on disposals represents £18.4 million gross costs (£13.3 million net of tax) on the discontinued business offset by deferred consideration received on a previously disposed of business.

34. Operating lease commitments – minimum lease payments

	2009		2008	
	Property £m	Vehicles, plant and equipment £m	Property £m	Vehicles, plant and equipment £m
Commitments under non-cancellable operating leases payable:				
Within one year	13.0	7.7	12.0	6.5
Later than one year and less than five years	40.7	8.6	36.7	8.2
After five years	40.3	–	43.7	–
	94.0	16.3	92.4	14.7

The Group leases various offices and warehouses under non-cancellable operating lease agreements. The leases have various terms, escalation clauses and renewal rights. The Group also leases plant and machinery under non-cancellable operating leases.

35. Contingent liabilities

a. Pursuant to the Rosyth Dockyard privatisation agreement, the MoD will share in the net proceeds of sale or development of the Dockyard following planning enhancement, on terms set out in the asset purchase agreement between the RRDL and the MoD dated 30 January 1997. By way of security for the MoD's rights to such share, the Company has granted a fixed charge (standard security) over the Dockyard in favour of the Authority.

b. The Group has given certain indemnities and warranties in the course of disposing of businesses and companies. The Group believes that any liability in respect of these is unlikely to have a material effect on the Group's financial position.

c. The Group is involved in disputes and litigation which have arisen in the course of normal trading. The Directors do not believe that the outcome of these matters will result in any material adverse change in the Group's financial position.

36. Capital and other financial commitments

	2009 £m	2008 £m
Contracts placed for future capital expenditure not provided in the financial statements	1.6	0.7

37. Related party transactions

(a) The following related parties either sell to or receive services from the Group. In addition British Nuclear Fuels PLC and United Kingdom Atomic Energy Authority have had a common director, with Babcock International Group PLC during the year. For details regarding loans to joint ventures see note 16.

	2009 Sales to £	2009 Purchases from £	2009 Year end debtors' balance £	2009 Year end creditor balance £
Joint venture and alliances				
Debut Services (South West) Ltd	121,120,000	–	81,000	–
DynCorp-Hiberna Limited	14,761,000	–	35,000	–
Holdfast Training Services Limited	21,470,000	–	4,820,000	–
Mouchel Babcock Education Services Limited	1,402,000	–	355,000	–
First Swietelsky Operation and Maintenance	6,235,000	–	1,846,000	–
First Swietelsky Joint Venture High Output	34,573,000	–	2,939,000	–
Related by common directorships				
BAE Systems PLC	21,473,000	2,478,000	2,705,000	625,000
BVT Surface Fleet Limited	71,219,000	–	–	–
British Nuclear Fuels PLC	9,804,000	–	–	–
			12,781,000	625,000

	2008 Sales to £	2008 Purchases from £	2008 Year end debtors' balance £	2008 Year end creditor balance £
Joint venture and alliances				
Debut Services (South West) Ltd	100,622,000	–	–	–
First Swietelsky Operation and Maintenance	6,638,000	–	1,521,000	–
First Swietelsky Joint Venture High Output	36,046,000	–	3,878,000	2,625,000
Related by common directorships				
British Nuclear Fuels PLC	7,036,000	–	193,000	–
United Kingdom Atomic Energy Authority	15,422,000	526,000	1,598,000	–
			7,190,000	2,625,000

All transactions noted above arise in the normal course of business.

(b) Babcock Employee Share Trust and Peterhouse Employee Share Trust
During the year the Company sold ordinary shares through the Babcock Employee Share Trust and the Peterhouse Employee Share Trust. Further information is given in note 27 on page 92.

(c) Defined benefit pension schemes
Please refer to note 28 for transactions with the Group defined benefit pension schemes.

38. Post balance sheet events

(a) Dividend
Details on dividends are given in note 11. There are no further material events subsequent to 31 March 2009 that require disclosure.

Independent auditors' report to the members of Babcock International Group PLC

We have audited the parent Company financial statements of Babcock International Group PLC for the year ended 31 March 2009 which comprise the Company balance sheet and the related notes. These parent Company financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration report that is described as having been audited.

We have reported separately on the Group financial statements of Babcock International Group PLC for the year ended 31 March 2009.

Respective responsibilities of Directors and auditors

The Directors' responsibilities for preparing the Annual Report, the Directors' Remuneration report and the parent Company financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' responsibilities.

Our responsibility is to audit the parent Company financial statements and the part of the Directors' Remuneration report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This Report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this Report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the parent Company financial statements give a true and fair view and whether the parent Company financial statements and the part of the Directors' Remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' report is consistent with the parent Company financial statements. The information given in the Directors' report includes that specific information presented in the Business review that is cross referred from the Business review section of the Directors' report.

In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited parent Company financial statements. The other information comprises only the Directors' report, the unaudited part of the Directors' Remuneration report, the Chairman's statement, the Business review, the Statement on Corporate Governance and the other information listed on the contents page. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the parent Company financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the parent Company financial statements and the part of the Directors' Remuneration report to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the parent Company financial statements, and of whether the accounting policies are appropriate to the Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the parent Company financial statements and the part of the Directors' Remuneration report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the parent Company financial statements and the part of the Directors' Remuneration report to be audited.

Opinion

In our opinion:

- the parent Company financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Company's affairs as at 31 March 2009;
- the parent Company financial statements and the part of the Directors' Remuneration report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' report is consistent with the parent Company financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

20 May 2009

Company balance sheet

As at 31 March 2009

	Note	2009 £m	2008 £m
Fixed assets			
Investment in subsidiary undertakings	3	359.1	359.3
Tangible fixed assets	4	0.3	0.3
		359.4	359.6
Current assets			
Debtors	5	527.6	440.9
Cash and bank balances		48.9	53.8
		576.5	494.7
Creditors – amounts due within one year	6	104.0	62.6
Net current assets		472.5	432.1
Total assets less current liabilities		831.9	791.7
Creditors – amounts due after one year	6	355.0	380.0
Net assets		476.9	411.7
Capital and reserves			
Called up share capital	7	137.7	137.6
Share premium account	8	148.2	148.1
Capital redemption reserve	8	30.6	30.6
Profit and loss account	8	160.4	95.4
Shareholders' funds – equity interests		476.9	411.7

The accompanying notes are an integral part of this Company balance sheet.

The financial statements were approved by the Board of Directors on 20 May 2009 and are signed on its behalf by:

P L Rogers
Director

W Tame
Director

Notes to the Company financial statements

1. Significant accounting policies

The principal accounting policies adopted by the Company are disclosed below:

Basis of accounting

The Company's financial statements have been prepared under the historical cost convention and in accordance with applicable United Kingdom Accounting Standards and in compliance with the Companies Act 1985.

Investments

Fixed asset investments are stated at cost less provision for impairment in value.

Leases

Operating lease payments are recognised as an expense in the income statement.

Taxation

Current UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Timing differences are differences between the Company's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

A deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

Deferred tax is recognised in respect of the retained earnings of overseas subsidiaries and associates only to the extent that, at the balance sheet date, dividends have been accrued as receivable or a binding agreement to distribute past earnings in future has been entered into by the subsidiary or associate.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on a non-discounted basis.

Bank and Borrowings

Having reassessed the substance of the company's borrowing arrangements, the long term loan facility terminating in June 2012 has been classed in creditors due after one year. The 2008 balance has been changed to reflect the move from creditors due within one year.

Finance costs

Finance costs are recognised as an expense in the period in which they are incurred.

Employee benefits

(a) Share-based compensation

The Company operates equity-settled, share-based compensation plans. The economic cost of awarding shares and share options to employees is recognised as an expense in the income statement equivalent to the fair value of the benefit awarded. The fair value is determined by reference to option pricing models. The charge is recognised in the income statement over the vesting period of the award and recharged to subsidiaries. Full details of the share-based compensation plans are disclosed in note 26 of the Group financial statements.

(b) Treasury shares

The shares purchased by the Company's ESOP trusts are recognised as a deduction to equity. Refer to the Group financial statements note 27 for further details.

(c) Pension arrangement

The Company operates a multi-employer defined benefit pension scheme. The scheme is accounted for on a defined contribution basis as the Company is unable to identify its share of the underlying assets and liabilities.

There is no material difference between the FRS17 (as amended): 'Retirement Benefits' and IAS19: 'Employee Benefits' valuation. Refer to the Group financial statements note 28 for further details.

As a result of the level of surplus the Company's compulsory contribution to the Babcock International Group Pension Scheme is currently suspended until at least the results of the next formal valuation are available although voluntary contributions have been made.

Notes to the Company financial statements continued

1. Significant accounting policies

Derivative financial instruments

Derivatives are initially recognised at fair value on the date a derivative is entered into and are subsequently remeasured at their fair value. The Company designates certain of the derivative instruments within its portfolio to be hedges of the fair value of recognised assets or liabilities or unrecognised firm commitments.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

Certain derivatives do not qualify or are not designated as hedging instruments and any movement in their fair values is recognised in the income statement immediately.

Financial risk management

All treasury transactions are carried out only with prime rated counterparties as are investments of cash and cash equivalents.

Dividends

Dividends are recognised in the Company's financial statements in the period in which they are approved and in the case of interims, when paid.

2. Company profit

The Company has taken advantage of the exemption granted by section 230 of the Companies Act 1985 whereby no individual profit and loss account of the Company is disclosed. The Company's profit for the financial year is £107.6 million (2008: £104.3 million).

Audit fees and expenses paid to the Company's auditors was £0.1 million (2008: £0.1 million).

3. Investment in subsidiary undertakings

	2009 £m	2008 £m
Investment in shares	359.1	359.3

The value of the Company's investments include an impairment in the year of £0.2 million (2008: £nil million). The cumulative impairment is £0.2 million (2008: £nil).

4. Tangible fixed assets

	Leasehold property £m
Cost	
At 1 April 2008	0.5
Additions	–
At 31 March 2009	0.5
Accumulated depreciation	
At 1 April 2008	0.2
Charge for the year	–
At 31 March 2009	0.2
Net book value at 31 March 2009	0.3
Net book value at 31 March 2008	0.3

5. Debtors

	2009 £m	2008 £m
Trade debtors	0.4	0.3
Amounts owed by subsidiary undertakings	522.5	439.5
Deferred tax	4.3	0.8
Prepayments and accrued income	0.4	0.3
	527.6	440.9

6. Creditors

	2009 £m	2008 £m
Amounts due within one year		
Trade creditors	0.7	–
Amounts owed to subsidiary undertakings	85.9	55.2
Derivative financial instruments	15.0	3.6
Accruals and deferred income	2.4	3.8
	104.0	62.6
Amounts due after one year		
Bank loans	355.0	375.0
Amounts owed to subsidiary undertakings	–	5.0
	355.0	380.0

The Company has £624 million (2008: £645 million) of Sterling bank facilities of which £355 million (2008: £375 million) was drawn at the year end. The interest rate applying is 2.2% (2008: 6.2%) and is linked to LIBOR.

7. Share capital

	Ordinary shares of 60p Number	Unclassified shares of 30p £m	Ordinary shares of 60p £m	Unclassified shares of 30p £m
Authorised:				
At 1 April 2008 and at 31 March 2009	306,219,012	1	183.7	–

	Ordinary shares of 60p Number	Total £m
Allotted, issued and fully paid		
At 1 April 2008	229,356,369	137.6
Shares issued	218,590	0.1
At 31 March 2009	229,574,959	137.7

Notes to the Company financial statements continued

8. Reserves

	Share premium account £m	Capital redemption reserve £m	Profit and loss account £m
At 1 April 2008	148.1	30.6	95.4
Shares issue in the period	0.1	–	–
Share-based payments	–	–	1.9
Movement on ESOP	–	–	(7.5)
Fair value adjustments to interest rate hedges (net of tax)	–	–	(9.1)
Retained profit for the year – profit for the year	–	–	107.6
– dividends	–	–	(27.9)
At 31 March 2009	148.2	30.6	160.4

9. Operating lease commitments

The Company has an operating lease commitment for land and buildings as at 31 March 2009 with an annual commitment expiring after more than five years of £2.2 million (2008: £2.2 million).

10. Contingent liabilities

a. The Company has guaranteed or has joint and several liability for bank facilities of £370.1 million (2008: £375.0 million) provided to certain Group companies.

b. Throughout the Group, guarantees exist in respect of performance bonds and indemnities issued on behalf of Group companies by banks and insurance companies in the ordinary course of business. At 31 March 2009 these amounted to £53.7 million (2008: £32.3 million), of which the Company had counter-indemnified £47.6million (2008: £22.0 million).

c. The Company has given guarantees on behalf of Group Companies in connection with the completion of contracts within specification.

11. Post balance sheet events

(a) Disclosure

There are no further material events subsequent to 31 March 2009 that require disclosure.

(b) Dividends

A dividend of 10.40p per 60p ordinary share (2008: 8.20p per 60p ordinary share) was declared after the balance sheet date and will be paid on 7 August 2009 to shareholders registered on 10 July 2009.

Principal subsidiaries, joint ventures and associated undertakings

Marine
Babcock Design & Technology Limited

Babcock Marine Holdings Limited

Babcock Marine (Rosyth) Limited

Rosyth Royal Dockyard Limited

Devonport Royal Dockyard Limited

Babcock Marine (Clyde) Limited

LSC Group Limited

Frazer-Nash Consultancy Limited

Appledore (2004) Limited

Strachan & Henshaw Australia (PTY) Limited (Australia)

Strachan & Henshaw Canada Inc (Canada)

Babcock Integrated Technology Limited

Defence Services
Air Power International Limited

Babcock Support Services Limited

Acetech Personnel Limited

Babcock Airports Limited

Nuclear
BNS Nuclear Services Limited

Engineering and Plant Services
Babcock Africa (Pty) Limited (South Africa)

Babcock Africa Services (Pty) Limited (South Africa)

Babcock Ntuthuko Engineering (Pty) Limited (75% owned) (South Africa)

Babcock Eagleton Inc. (USA)

Rail
Babcock Rail Limited

Networks
Babcock Networks Limited

Others
Babcock UK Holdings Limited

Babcock Holdings Limited

Babcock International Holdings BV (Netherlands)

Babcock International Limited

Babcock Investments Limited

Babcock Management Limited

Babcock Overseas Investments Limited

Babcock Support Services (Investments) Limited

Chepstow Insurance Limited (Guernsey)

PHG Insurance Limited (Guernsey)

Joint Ventures
FSP (2004) Limited

Mouchel Babcock Education Services Limited

Holdfast Training Services Limited (74%)

All undertakings are wholly-owned unless otherwise stated. With the exception of Babcock UK Holdings Limited, which is owned by the Company, all Group undertakings are owned by subsidiary undertakings.

All undertakings are incorporated and operated in Great Britain unless otherwise stated. Undertakings located overseas operate principally in the country of incorporation.

Notice of meeting

THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION. If you are in any doubt as to what action to take, you should consult your stockbroker, solicitor, accountant or other appropriate independent professional adviser authorised under the Financial Services and Markets Act 2000. If you have sold or otherwise transferred all your shares in Babcock International Group PLC, please forward this document and the accompanying Form of Proxy to the person through whom the sale or transfer was effected, for transmission to the purchaser or transferee.

A Form of Proxy for the Annual General Meeting is enclosed and should be completed and returned so as to reach the Company's registrar no later than 11.00 am on Tuesday 7 July 2009. Completion and return of the Form of Proxy will not prevent you from attending and voting at the Meeting in person, should you so wish.

BABCOCK INTERNATIONAL GROUP PLC

NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the 2009 Annual General Meeting of the members of Babcock International Group PLC ('the Company') will be held at Chandos House, 2 Queen Anne Street, London W1G 9LQ on Thursday 9 July 2009, at 11.00 am for the transaction of the following business:

As Ordinary Business:

1. To receive the Directors' and Auditors' reports and the audited financial statements of the Group and the Company for the year ended 31 March 2009.
2. To declare a final dividend for the year ended 31 March 2009.
3. To reappoint Sir Nigel Essenhigh as a Director of the Company.
4. To reappoint Mr Justin Crookenden as a Director of the Company.
5. To reappoint Lord Hesketh as a Director of the Company.
6. To reappoint Sir David Omand as a Director of the Company.
7. To approve the Remuneration Report of the Directors for the year ended 31 March 2009.
8. To reappoint PricewaterhouseCoopers LLP as independent auditors.
9. To authorise the Directors to set the remuneration of the independent auditors, as they shall in their discretion see fit.

As Special Business, to consider and, if thought fit, to pass the following resolutions:

Ordinary Resolutions

10. That the rules of the Babcock International Group PLC Performance Share Plan 2009 ('PSP'), as produced in draft to the meeting and initialled by the Chairman for purposes of identification, and of which a summary is found in Appendix 1 to this notice of meeting, are hereby approved and adopted and the Directors are hereby authorised to do all acts and things necessary to carry the PSP into effect.
11. That the rules of the Babcock International Group PLC Company Share Option Plan 2009 ('CSOP'), as produced in draft to the meeting and initialled by the Chairman for purposes of identification, and of which a summary is found in Appendix 2 to this notice of meeting, are hereby approved and adopted and the Directors are hereby authorised to do all acts and things necessary to carry the CSOP into effect.
12. That in accordance with sections 366 and 367 of the Companies Act 2006 (the '2006 Act'), the Company and all companies that are its subsidiaries at any time during the period for which this resolution is effective are authorised to:

    (a) make political donations to a political party or to an independent election candidate;

    (b) make political donations to political organisations other than political parties; and

    (c) incur any political expenditure,

    up to an aggregate amount of £100,000, and the amount authorised under each of paragraphs (a) to (c) shall also be limited to such amount, during the period beginning with the date of the passing of this resolution and ending on 30 September 2010 or, if sooner, the conclusion of the Annual General Meeting of the Company in 2010. For the purpose of this resolution 'political donation', 'political party', 'political organisation', 'independent election candidate' and 'political expenditure' are to be construed in accordance with sections 363, 364 and 365 of the 2006 Act.

13. That the Directors be and are hereby generally and unconditionally authorised for the purposes of section 80 of the Companies Act 1985 (the '1985 Act'), to exercise all the powers of the Company to allot relevant securities (within the meaning of section 80(2) of the 1985 Act):

(a) up to an aggregate nominal amount of £45,869,076; and

(b) comprising equity securities (as defined in section 94 of the 1985 Act) up to an aggregate nominal amount (when added to any allotments made under (a) above) of £91,738,153 in connection with or pursuant to an offer or invitation by way of a rights issue in favour of holders of ordinary shares in proportion (as nearly as practicable) to the respective number of ordinary shares held by them on the record date for such allotment (and holders of any other class of equity securities entitled to participate therein or if the Directors consider it necessary, as permitted by the rights of those securities), but subject to such exclusions or other arrangements as the Directors may consider necessary or appropriate to deal with fractional entitlements, treasury shares, record dates or legal, regulatory or practical difficulties which may arise under the laws of, or the requirements of any regulatory body or stock exchange in, any territory or any other matter whatsoever,

these authorities to expire at the conclusion of the next Annual General Meeting of the Company (save that the Company may before such expiry make any offer or agreement which would or might require relevant securities to be allotted after such expiry and the Directors may allot relevant securities in pursuance of any such offer or agreement as if the authorities conferred hereby had not expired).

Special Resolutions

14. That, subject to the passing of resolution 13 above, the Directors be and are hereby empowered pursuant to section 95(1) of the Companies Act 1985 (the '1985 Act') to:

(a) allot equity securities (within the meaning of section 94 of the 1985 Act) of the Company for cash pursuant to the authority conferred by resolution 13; and

(b) sell relevant shares (as defined in section 94(5) of the 1985 Act) held by the Company as treasury shares (as provided for in section 94(3) of the 1985 Act) ('treasury shares') for cash (as defined in section 162D(2) of the 1985 Act),

as if section 89(1) of the 1985 Act did not apply to any such allotment or sale, provided that this power shall be limited to the allotment of equity securities for cash and the sale of treasury shares:

(i) in connection with or pursuant to an offer or invitation (but in the case of the authority granted under resolution 13(b), by way of a rights issue only) in favour of holders of ordinary shares in proportion (as nearly as practicable) to the respective number of equity securities held by them on the record date for such allotment but subject to such exclusions or other arrangements as the Directors may deem necessary or expedient to deal with fractional entitlements, treasury shares, record dates or legal or practical problems arising under the laws of any overseas territory or the requirements of any regulatory body or stock exchange in any territory or any other matter whatsoever; or

(ii) in the case of the authority granted under resolution 13(a) above, and otherwise than pursuant to paragraph (i) of this resolution, up to an aggregate nominal amount of £6,887,248,

and shall expire at the conclusion of the next Annual General Meeting of the Company, save that the Company may before such expiry make any offer or enter into any agreement which would or might require equity securities to be allotted, or treasury shares to be sold, after such expiry and the Directors may allot equity securities, or sell treasury shares in pursuance of any such offer or agreement as if the power conferred hereby had not expired.

15. That the Company is hereby authorised for the purposes of section 166 of the Companies Act 1985 (the '1985 Act') to make market purchases (within the meaning of section 163 of the 1985 Act) of ordinary shares of 60p each ('ordinary shares') in the capital of the Company on such terms and in such manner as the Directors may from time to time determine provided that:

    (a) the maximum number of ordinary shares hereby authorised to be purchased shall be 22,950,000 shares;

    (b) the minimum price which may be paid for each ordinary share is not less than the nominal value thereof exclusive of the expenses of purchase;

    (c) the maximum price which may be paid for each ordinary share (exclusive of the expenses of purchase) shall not exceed 105% of the average middle market quotation for an ordinary share as derived from the London Stock Exchange Daily Official List for the five business days preceding the day of purchase;

    (d) the authority hereby conferred shall expire on the date falling 12 months from the date of this resolution or at the conclusion of the Annual General Meeting of the Company to be held in 2010, whichever shall be the earlier, unless such authority is renewed prior to such time; and

    (e) the Company may make a contract to purchase ordinary shares under the authority hereby conferred prior to the expiry of such authority which will or may be executed wholly or partly after the expiry of such authority and may make purchases of ordinary shares in pursuance of any such contract.

16. That a general meeting of the Company (other than an annual general meeting) may be called on not less than 14 clear days' notice.

By order of the Board.

A N Dungate
Company Secretary

8 June 2009

Registered Office: 33 Wigmore Street, London W1U 1QX.

Notes:

1. As required by the Combined Code, the reasons why the Board of the Company believes that the Non-Executive Directors standing for reappointment should be reappointed are set out in the Accompanying Notes on page 112.
2. An explanation of the special business resolutions is given in the Explanatory Notes on pages 113 and 114.
3. Only holders of shares are entitled to attend and vote at this meeting. A member is entitled to appoint another person as their proxy to exercise all or any of their rights to attend, to speak and to vote at the meeting. A member may appoint more than one proxy in relation to the meeting, provided that each proxy is appointed to exercise the rights attached to a different share or shares held by the member. A proxy need not be a member of the Company.
4. A holder of ordinary shares must be entered on the relevant register of securities in respect of such shareholding not later than 48 hours before the time appointed for the meeting in order to have the right to attend and vote at the meeting.
5. A form of proxy is available and, to be effective, must be completed in accordance with the instructions printed thereon and returned so as to be received by the Registrars of the Company not less than 48 hours before the time appointed for the meeting. Completion of a form of proxy will not affect the right of a member to attend and vote in person at the meeting.
6. Copies of the terms of appointment under which the Non-Executive Directors of the Company are engaged, Executive Directors' service agreements and a copy of the proposed PSP (resolution10) and CSOP (resolution11) are available for inspection at the Company's registered office during normal business hours until the date of the Annual General Meeting and will be available for inspection at the place of the Annual General Meeting for at least 15 minutes prior to and during the meeting.
7. Pursuant to regulation 41 of the Uncertificated Securities Regulations 2001, the Company specifies that in order to have the right to attend and vote at the meeting (and also for the purpose of determining how many votes a person entitled to attend and vote may cast), a person must be entered on the register of members of the Company by close of business on 7 July 2009 or, in the event of any adjournment, by close of business on the date which is two days before the day of the adjourned meeting. Changes to entries on the register of members after this time shall be disregarded in determining the rights of any person to attend or vote at the meeting.
8. In order to facilitate voting by corporate representatives at the meeting, arrangements will be put in place at the meeting so that (i) if a corporate shareholder has appointed the Chairman of the meeting as its corporate representative with instructions to vote on a poll in accordance with the directions of all of the other corporate representatives for that shareholder at the meeting then on a poll those corporate representatives will give voting directions to the Chairman and the Chairman will vote (or withhold a vote) as corporate representative in accordance with those directions; and (ii) if more than one corporate representative for the same corporate shareholder attends the meeting but the corporate shareholder has not appointed the Chairman of the meeting as its corporate representative, a designated corporate representative will be nominated, from those corporate representatives who attend, who will vote on a poll and the other corporate representatives will give voting directions to that designated corporate representative. Corporate shareholders are referred to the guidance issued by the Institute of Chartered Secretaries and Administrators on proxies and corporate representatives – http://www.icsa.org.uk – for further details of this procedure. The guidance includes a sample form of representation letter if the Chairman is being appointed as described in (i) above.
9. Any person to whom this notice is sent who is a person nominated under section 146 of the Companies Act 2006 to enjoy information rights (a 'Nominated Person') may have a right, under an agreement between them and the member by whom they were nominated, to be appointed (or to have someone else appointed) as a proxy for the meeting. If a Nominated Person has no such proxy appointment right or does not wish to exercise it, they may have a right, under such an agreement, to give instructions to the member as to the exercise of voting rights. The statement of the above rights of the members in relation to the appointment of proxies does not apply to Nominated Persons. Those rights can only be exercised by shareholders of the Company.

10. Shareholders should note that it is possible that, pursuant to requests made by members of the Company under section 527 of the Companies Act 2006 (the '2006 Act'), the Company may be required to publish on a website a statement setting out any matter relating to: (i) the audit of the Company's accounts (including the auditor's report and the conduct of the audit) that are to be laid before the Annual General Meeting; or (ii) any circumstance connected with an auditor of the Company ceasing to hold office since the previous meeting at which Annual Report and Accounts were laid (in each case) that the members propose to raise at the Annual General Meeting. The Company may not require the members requesting any such website publication to pay its expenses in complying with sections 527 or 528 of the 2006 Act. Where the Company is required to place a statement on a website under section 527 of the 2006 Act, it must forward the statement to the Company's auditor not later than the time when it makes the statement available on the website. The business which may be dealt with at the Annual General Meeting includes any statement that the Company has been required under section 527 of the 2006 Act to publish on a website.
11. As at 20 May 2009 (being the last practicable day prior to the publication of this notice) the Company's issued share capital consisted of 229,574,959 ordinary shares, carrying one vote each. Therefore, the total voting rights in the Company as at that date were 229,574,959.
12. Any electronic address (within the meaning of section 333(4) of the Companies Act 2006) provided in this Notice of Meeting (or in any related documents including the proxy form) may not be used to communicate with the Company for any purpose other than those expressly stated.

Accompanying Notes

The Combined Code requires the Board to set out the reasons why it believes that the Non-Executive Directors standing for reappointment should be reappointed. These are as follows:

Lord Hesketh

The Board continues to value highly the contribution that Lord Hesketh brings to its meetings, with his longer term experience of the Group's activities and the markets in which it operates, together with his wide experience in a variety of commercial and political spheres.

Sir Nigel Essenhigh

Sir Nigel has served on the Board and its Committees since 2003, playing a full part in their deliberations. His perspective on defence matters generally, especially naval affairs (both key markets for the Group), is particularly valuable. The Board believes his continuation as a Director will be of significant benefit to the Company.

Justin Crookenden

Mr Crookenden has served on the Board and its Committees since December 2005 and was appointed Remuneration Committee Chairman with effect from 1 April 2009. The Company benefits greatly from the broad perspective and astute intellectual and business insight he brings from his wide experience in his former role as a financial adviser to a range of leading companies, especially in the field of mergers and acquisitions.

Sir David Omand

Sir David was appointed as a Director by the Board with effect from 1 April 2009. The Board believes that his wide experience at the highest levels in both domestic and international affairs and in strategic thinking will be a great asset to the Company.

Note from the Chairman:

"I can confirm, as required by the Combined Code, that having fully evaluated their performances, the Board is of the view that each of Lord Hesketh, Sir Nigel Essenhigh, Justin Crookenden and Sir David Omand continues to be effective and to demonstrate commitment to his role."

Mike Turner

Explanatory notes

The ordinary business of the meeting and the resolutions under special business to be proposed as ordinary resolutions can be passed if the votes cast for the resolutions are more than those cast against. The resolutions to be proposed as special resolutions can be passed if at least 75% of the votes cast for or against the resolutions are in favour.

Resolutions 3 and 4: Each of Sir Nigel Essenhigh and Justin Crookenden was last reappointed as a Director in 2006 and is therefore offering himself for reappointment as required by the Company's Articles of Association and in accordance with the Combined Code.

Resolution 5: Lord Hesketh offers himself for reappointment annually as required by the Combined Code, having served more than nine years as a Director.

Resolution 6: Sir David Omand, having been appointed by the Board as a Director with effect from 1 April 2009, is submitting himself for reappointment as required by the Company's Articles of Association, this being the first Annual General Meeting following his appointment.

Resolution 7: This is to approve the Directors' Remuneration report for the financial year ended on 31 March 2009. The Report can be found on pages 48 to 60 of the Annual Report and Accounts for the year ended 31 March 2009.

Resolution 10: The effect of this resolution is to give the Directors authority to adopt the PSP and operate it in accordance with its rules. A detailed summary of the principal terms of the PSP is set out in Appendix 1 to the Notice of the Annual General Meeting and forms part of that Notice.

Resolution 11: The effect of this resolution is to give the Directors authority to adopt the CSOP and operate it in accordance with its rules. A detailed summary of the principal terms of the CSOP is set out in Appendix 2 to the Notice of the Annual General Meeting and forms part of that Notice. The CSOP would be an HM Revenue & Customs approved option plan, which means that there will potentially be income tax benefits for participants and savings of National Insurance contributions for both participants and the Company provided certain conditions are satisfied. As an HM Revenue & Customs approved option plan, the CSOP is subject to certain statutory limitations, including being limited to UK-based employees and a limit on the maximum value of options available.

Resolution 12: It is the Company's policy not to make political donations or incur political expenditure as those expressions are normally understood. However, certain activities undertaken in the usual course of business may fall within the legal definition of political donation or political expenditure. The authority is sought annually to ensure that all the activities of the Company fully comply with the law.

Resolution 13: The Directors may only allot shares or grant rights over shares if authorised to do so by shareholders. Resolution No. 13 will be proposed as an ordinary resolution to grant a new authority to allot (a) unissued share capital up to an aggregate nominal value of £45,869,076, and (b) equity securities up to an aggregate nominal amount (when added to allotments under part (a) of the resolution) of £91,738,153 where the allotment is in connection with a rights issue. These amounts represent approximately 33.3% and approximately 66.7% respectively of the total issued ordinary share capital of the Company as at 20 May 2009. As at the date of the notice of this meeting the Company held no treasury shares. If given, this authority will expire at the Annual General Meeting in 2010.

Resolution 14: The Directors also require additional authority from shareholders to allot shares or grant rights over shares or sell treasury shares where they propose to do so for cash and otherwise than to existing shareholders pro rata to their holdings. Resolution 14 will be proposed as a special resolution to grant such authority. Apart from offers or invitations in proportion to the respective number of shares held, the authority will be limited to the issue of shares and sales of treasury shares for cash up to an aggregate nominal value of £6,887,248 (being 5% of the Company's issued ordinary share capital at 20 May 2009). If given, this authority will expire at the Annual General Meeting in 2010. The Directors will have due regard to institutional guidelines in relation to any exercise of this authority, in particular the requirement for advance consultation and explanation before making any such issue which exceeds 7.5% of the Company's issued share capital in any rolling three-year period. With the exception of issues, if necessary, of further shares under the Company's executive or employee share schemes, the Directors do not have any present intention of exercising this authority, but consider it desirable to have the flexibility to use it should opportunities arise.

Notice of meeting continued

Resolution 15: This will be proposed as a Special Resolution and will renew the general authority for the Company to make market purchases of its own ordinary shares. The renewed authority, in respect of a little under 10% of the Company's issued share capital as at 20 May 2009, would be exercisable with a minimum purchase price of 60p per share and a maximum price of not more than 105% of the average middle market quotation for an ordinary share as derived from the London Stock Exchange Daily Official List for the five business days preceding the day of purchase. If granted, the authority would expire at the conclusion of the Annual General Meeting of the Company to be held in 2010 or, if earlier, 12 months from the date of the resolution. Shares purchased under the authority would either be cancelled or held by the Company as treasury shares. The Directors have no present intention of using this power, and would only exercise the power if they were satisfied at any time that it was in the best interests of shareholders generally to do so, and that (except in the case of a purchase of own shares to be held as treasury shares to fulfil obligations under the Company's executive or employee share schemes) any purchase would be likely to result in an increase in earnings per share. The Company has no warrants outstanding and the total number of options to subscribe for equity shares outstanding on 20 May 2009 (being the latest practicable date before publication of the notice of meeting) was 559,501 representing 0.24% of issued share capital as at 20 May 2009. If the full authority to buy back shares were to be used, and the shares cancelled, these outstanding options would represent 0.27% of issued share capital.

Resolution 16: This is required to reflect the proposed implementation in August 2009 of the Shareholder Rights Directive. The regulation implementing this Directive will increase the notice period for general meetings of the Company to 21 days. The Company is currently able to call general meetings (other than an Annual General Meeting) on 14 clear days' notice and would like to preserve this ability. In order to be able to do so after August 2009, shareholders must have approved the calling of meetings on 14 days' notice. Resolution 16 seeks such approval. The approval will be effective until the Company's next Annual General Meeting, when it is intended that a similar resolution will be proposed. The Company will also need to meet the requirements for electronic voting under the Shareholder Rights Directive before it can call a general meeting on 14 days' notice.

Appendix 1 to the Notice of Annual General Meeting
Summary of Proposed Performance Share Plan (Resolution No. 10)

The Babcock International Group PLC Performance Share Plan 2009 ('Plan')

Status of the Plan

Awards granted under the Plan ('Awards') will have no beneficial tax status.

Eligibility

All employees (including Executive Directors) of Babcock International Group PLC ('Company') or any of its subsidiaries (together with the Company, the 'Group') will be eligible to be granted Awards.

Grant

The remuneration committee of the board ('Remuneration Committee') will have absolute discretion to select the persons to whom Awards are to be granted and, subject to the limits set out below, in determining the number of ordinary shares in the capital of the Company ('Ordinary Shares') to be subject to each Award.

Each Award will take the form of an option to acquire Ordinary Shares for nil consideration. As an alternative, the Remuneration Committee will have discretion to make Awards in the form of a conditional right to acquire Ordinary Shares for no consideration, in which case it may make such amendments to the rules of the Plan as may be required to give effect to this. If this arrangement is adopted, Ordinary Shares will be transferred to an Award holder immediately following vesting of an Award.

The Plan will be operated in conjunction with the existing employee benefit trusts operated by the Group (each an 'EBT').

Awards may be granted during the period of 42 days commencing on: (a) the date on which the Plan is adopted by the Company; (b) the dealing day immediately following the date of the preliminary announcement of the Company's annual results or the announcement of its half-yearly results in any year; or (c) any other date fixed by the Remuneration Committee where, in its discretion, it considers circumstances to be exceptional so as to justify the grant of Awards on that date.

If the grant of an Award on any of the above days would be prohibited by virtue of the Model Code or any statute or regulation or any order made pursuant to such statute (a 'Restriction'), then such Award may be granted during the period of 40 days commencing immediately after the second dealing day following the time that such Restriction ceases to have effect.

No consideration is payable for the grant of an Award.

Dividends

If a dividend or other cash distribution is paid by the Company in respect of Ordinary Shares during the period prior to the vesting of an Award, Award holders will not immediately be entitled to receive the distribution in respect of the Ordinary Shares which are the subject of their Awards. Instead, an amount equal to the aggregate value of such distributions will be payable to the Award holder when the Award is exercised ('Dividend Equivalent Cash').

Alternatively, the Remuneration Committee will have the discretion to increase the number of Ordinary Shares which are subject to an Award by an amount equal to the aggregate value of such distributions (calculated as if the distribution had been invested in Ordinary Shares as at the date of payment of such distribution to shareholders) ('Dividend Equivalent Shares').

To the extent that an Award does not become exercisable, any right to Dividend Equivalent Cash or Dividend Equivalent Shares will fall away.

Plan limits

No Award may be granted under the Plan if, as a result, the aggregate nominal value of Ordinary Shares issued or intended to be issuable by the Company pursuant to that Award and any Awards granted during the previous ten years under the Plan or any other employees' share plan, profit sharing plan or employee share ownership plan adopted by the Company would exceed 10% of the nominal value of the share capital of the Company in issue on the date of that Award were it to be made.

In addition, no Award may be granted under the Plan if, as a result, the aggregate nominal value of Ordinary Shares issued or intended to be issuable by the Company pursuant to that Award and Awards granted during the previous ten years under the Plan or any other discretionary share plan (as opposed to an all-employee plan) adopted by the Company would exceed 5% of the nominal value of the share capital of the Company in issue on the date of that Award were it to be made.

For the avoidance of doubt, Dividend Equivalent Shares already acquired would count for the above purposes, but potential future Dividend Equivalent Shares would not. Any Ordinary Shares which are already in issue when made subject to an Award or which are subject to an Award which has lapsed will be disregarded for the purpose of the above limits.

If it is intended that an Award is to be settled with Ordinary Shares which have been or are intended to be acquired in the market by an EBT, those Ordinary Shares will be disregarded for the purposes of the above limits.

Notice of meeting continued

Individual limit

In general, no Award may be granted under the Plan to an employee if the aggregate Market Value (on the date of the proposed grant) of the Ordinary Shares which are to be subject to that Award, when aggregated with the Market Value (on the date such other Award was granted) of the Ordinary Shares which the employee may acquire in relation to other Awards already granted to the employee under the Plan in the same financial year of the Company as the proposed grant, would exceed 150% of the employee's salary as at the date of the proposed grant. All references to 'Market Value' on a particular date are to the average of the middle market prices for an Ordinary Share for the three dealing days immediately preceding that date.

The limit referred to above may be increased to up to 200% of an employee's salary in circumstances which the Remuneration Committee considers to be exceptional, for example, for the purposes of recruitment. The Remuneration Committee currently has no intention of making an Award over Ordinary Shares of a Market Value which would exceed 150% of salary.

Performance targets

The exercise of Awards under the Plan will, in normal circumstances, be made conditional upon the achievement of performance targets set at the time of grant. Performance targets will be measured over a three-year performance period, which will not begin before the start of the financial year in which the Award is granted, as determined by the Remuneration Committee at the time of grant ('Performance Period').

The Remuneration Report set out in the Company's 2009 Annual Report describes on page 58 the performance targets which it is intended will apply to Awards made under the Plan to Executive Directors in 2009, subject to approval of the Plan by shareholders at the Annual General Meeting. Different performance targets, for example, Divisional performance targets, may be applied to Awards made to other Award holders as also described in that Report.

If events occur which cause the Remuneration Committee reasonably to consider that a different or amended target would be a fairer measure of performance, the Remuneration Committee will be able to modify the original performance target in such manner as it deems fit.

It should also be noted that a performance target may be measured over a period shorter than the normal Performance Period in circumstances where an employee ceases to be a Group employee, or certain corporate events occur (such as a change of control of the Company), before the end of the relevant Performance Period. In these circumstances the Remuneration Committee will have the discretion to modify the performance target as it thinks fit.

Exercise of Awards

Awards will become capable of exercise following a date ('Vesting Date'), specified at the time of grant, which occurs on or after the expiry of the relevant Performance Period. In the event that there has been a material delay in the grant of an Award beyond the date on or about which the Remuneration Committee would otherwise, but for the existence of a Restriction, have granted the Award, the Remuneration Committee would be able, but not obliged, to stipulate a 'Notional Award Date' for that Award being the date which it reasonably considers would have been the date on or about which it would have made such Award had the Restriction not existed (or such later date after that date as it may choose). The Vesting Date will not be before the expiry of the Performance Period or earlier than the expiry of a period of three years from and including the Award Date or, if applicable, the Notional Award Date for that Award.

Normally, an Award may only be exercised following the occurrence of the Vesting Date to the extent that the performance target has been satisfied and if the Award holder is still an employee within the Group.

Awards may not be exercised during any prohibited period specified by the Model Code.

An Award will ordinarily only be exercisable during a period commencing immediately after its Vesting Date and ending on a date specified at grant ('End Date') and will lapse on the expiry of such period. However, if an Award holder is prevented from exercising such Award before the end of such period by virtue of a restriction imposed by the Model Code, the Award will be exercisable within the period of 30 days after the Company notifies him in writing that Model Code restrictions no longer exist to prevent the exercise. The Remuneration Committee will also have a discretion to permit exercise of an Award after the specified period, although no Award may be exercised after the date immediately prior to the tenth anniversary of the date of grant.

The Remuneration Committee may (subject to the approval of the trustee of the relevant EBT) determine that, in substitution for the Award holder's right to acquire the Ordinary Shares which are subject to an Award, the Award holder shall instead be paid a cash sum which is equal to the market value of such Ordinary Shares (including any Dividend Equivalent Shares) on the date on which the Award is exercised.

Cessation of employment

If an Award holder dies, any Awards held by him or her may be exercised (subject to any reduction in the number of Ordinary Shares which are subject to such Award which is applied by the Remuneration Committee as described below) at any time during the 12-month period (or such shorter period as is determined by the Remuneration Committee) following the date of death. If an Award holder ceases to be employed within the Group by reason of injury, ill health or disability (evidenced to the satisfaction of the Remuneration Committee), redundancy, retirement, or upon the sale or transfer out of the Group of the company or undertaking employing the Award holder (each 'a Good Reason' and such an Award holder, a 'Good Leaver'), then:

- as regards Awards for which the Vesting Date has not by then occurred, he or she must normally wait until the normal Vesting Date in respect of the Award before being permitted to exercise it (save that the Remuneration Committee will have the discretion instead to allow the Award holder to exercise some or all of such unvested Awards within the period of 12 months, or such shorter period as is determined by the Remuneration Committee, following the date of cessation of employment); and
- as regards Awards for which the Vesting Date has by then occurred (but which have not yet been exercised), he or she will be able to exercise those Awards within 12 months (or such shorter period as the Remuneration Committee may decide) of the cessation of employment,

provided that the number of Ordinary Shares which are subject to such Award may be reduced as described below and no Award may be exercised after the End Date for the Award (unless the Remuneration Committee exercises its discretion to extend the End Date).

Ordinarily, where an Award holder ceases to be employed within the Group (or gives notice to terminate his or her employment) for any reason other than a Good Reason, any Awards held by him or her (whether vested or not) will lapse and cease to be exercisable. However, the Remuneration Committee will have the discretion, subject to such additional conditions as it determines (including a power to reduce the number of shares under Award whether such Award has vested or not), to permit the Award holder to exercise some or all of his or her Awards on the same basis as a Good Leaver.

The Committee will be able to exercise its discretions mentioned above differently, as it thinks appropriate, as regards different Awards held by the same Award holder.

Any exercise of an Award where the Award holder has ceased to be an employee prior to the Vesting Date for the Award will be subject to:

- the prior satisfaction of the performance target (subject to such adjustments as the Remuneration Committee considers to be appropriate in the circumstances); and
- in the case of a Good Leaver, the reduction of the maximum number of Ordinary Shares over which the Award is capable of being exercised. This reduction will normally be on a time apportioned basis based on how much of the period between the Award Date (or, if applicable, the Notional Award Date) and the normal Vesting Date for the Award is left to run as at the date of the cessation of employment. The Remuneration Committee will, though, have discretion, having regard to all the circumstances, not to apply pro-rating or to allow the Award to be exercised over more than a strictly time-apportioned number of shares.

In the case of an Award holder who leaves with unexercised Awards (whether before or after the Vesting Date of an Award) who is not a Good Leaver but whom the Remuneration Committee has exercised its discretion to treat as a Good Leaver, the reduction can be more than a time-apportioned reduction whether the Award held by such deemed Good Leaver has vested or not.

Takeover and other corporate events

Exercise of Awards is also possible earlier than the Vesting Date if the Company is the subject of a takeover or a scheme of arrangement under Part 26 of the Companies Act 2006 sanctioned by the court, or if the Company is voluntarily wound up. In the case of a takeover of the Company or the transfer out of the Group of the undertaking employing the Award holder concerned, the Remuneration Committee may allow the Award to be exercised immediately before, but with effect from, the takeover or the transfer of the undertaking concerned.

Any exercise of an Award in such circumstances will be subject to:

- the prior satisfaction of the performance target (subject to such adjustments as the Remuneration Committee considers to be appropriate in the circumstances); and
- the reduction of the maximum number of Ordinary Shares over which the Award is capable of being exercised. This reduction will normally be on a time apportioned basis based on how much of the period between the Award Date (or, if applicable, the Notional Award Date) and the normal Vesting Date for the Award is left to run as at the date of the relevant event. The Remuneration Committee will, though, have discretion, having regard to all the circumstances, not to apply pro-rating or to allow the Award to be exercised over more than a strictly time-apportioned number of shares.

Other Award terms

Awards will not be capable of transfer or assignment.

Until Awards are exercised, Award holders will have no voting or other rights (subject to the rights relating to dividends as set out above) in relation to the Ordinary Shares subject to those Awards.

Ordinary Shares acquired on the exercise of an Award will rank *pari passu* in all respects with the Ordinary Shares already in issue but will not rank for any dividends or other distributions payable by reference to a record date preceding the date of acquisition. Ordinary Shares acquired on the exercise of an Award will be acquired without the benefit of any rights attaching to the Ordinary Shares by reference to a record date preceding the date of that exercise.

Benefits obtained under the Plan will not be pensionable.

Administration and amendment

The Plan will be administered by the Remuneration Committee. The Board of the Company will be able to amend the provisions of the Plan. However, the rules of the Plan which relate to:

- the persons to whom Ordinary Shares are provided under the Plan;
- the limits on the number of Ordinary Shares which may be issued under the Plan;
- the maximum entitlement of any Award holder;
- the basis for determining an Award holder's entitlement to Ordinary Shares or Awards; and
- the basis for determining the adjustment of any Award granted under the Plan following any increase or variation in the share capital of the Company

will not be capable of being amended by the Board to the advantage of any Award holder or potential Award holder without the prior approval of the Company in general meeting except for minor amendments to benefit the administration of the Plan, to take account of any change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for Award holders or any Group company.

The Remuneration Committee will have the discretion, in respect of employees of the Group who are resident for tax purposes outside the UK, to amend or alter the provisions of any Award to take account of overseas taxation or securities law. However, the Remuneration Committee will not be able to make any such amendment or alteration if this would result in an Award being made upon terms commercially more favourable than the terms upon which an Award could have been granted if such person was tax resident in the UK.

Adjustment of Awards

In the event of any increase or variation in the share capital of the Company, the Remuneration Committee may, with the consent of the relevant EBT trustee, make such adjustment as it deems appropriate to the number of Ordinary Shares comprised in each Award and/or the nominal value of the Ordinary Shares subject to Awards.

Termination

The Plan may be terminated at any time by resolution of the Board of the Company and will in any event terminate on the tenth anniversary of its adoption so that no further Awards can be granted under the Plan after termination. Termination will not affect the outstanding rights of existing Award holders.

Appendix 2 to the Notice of Annual General Meeting
Summary of Proposed Approved Executive Share Option Plan (Resolution No. 11)

The Babcock International Group PLC Company Share Option Plan 2009 (the "CSOP")

Status of the CSOP
The CSOP is designed to be capable of approval by HM Revenue & Customs ("HMRC") under Schedule 4 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA"). The terms of the CSOP summarised below are subject to any amendment required by HMRC in order to achieve approved status.

Eligibility
All employees (including full time executive directors) of Babcock International Group PLC ("Company") or any of its subsidiaries (together with the Company, the "Group") will be eligible to be granted options over ordinary shares in the capital of the Company ("Ordinary Shares") under the CSOP provided that they are not prohibited under the relevant legislation relating to HMRC approved company share option plans from being granted an option by virtue of having, or having had, a material interest in the Company.

Grant
The remuneration committee of the board ("Remuneration Committee") will have absolute discretion to select the persons to whom options are to be granted and, subject to the limits set out below, in determining the number of Ordinary Shares to be subject to each option.

No options may be granted unless and until the CSOP has been formally approved by HMRC under Schedule 4 to ITEPA.

The CSOP may be operated in conjunction with the existing employee benefit trusts operated by the Group (each an "EBT").

Options may be granted during the period of 42 days commencing on: (a) the date on which the CSOP is adopted by the Company; (b) the dealing day immediately following the date of the preliminary announcement of the Company's annual results or the announcement of its half-yearly results in any year (provided that if the Ordinary Shares continue to be admitted to the Official List of the UK Listing Authority at the time in question, no option shall be granted during the first two dealing days following the date of any such announcement); or (c) any other date fixed by the Remuneration Committee where, in its discretion, it considers circumstances to be exceptional so as to justify the grant of options on that date.

If the grant of an option on any of the above days would be prohibited by virtue of the Model Code or any statute or regulation or any order made pursuant to such statute, then such option may be granted during the period of 40 days commencing immediately after the second dealing day following the time that such prohibition shall cease to have effect.

No consideration is payable for the grant of an option.

CSOP limits
No option may be granted under the CSOP if, as a result, the aggregate nominal value of Ordinary Shares issued or intended to be issuable by the Company pursuant to that option and any options granted during the previous ten years under the CSOP or any other employees' share scheme, profit sharing scheme or employee share ownership plan adopted by the Company would exceed 10 per cent of the nominal value of the share capital of the Company in issue on that date.

No option may be granted under the CSOP if, as a result, the aggregate nominal value of Ordinary Shares issued or issuable pursuant to options granted during the previous ten years under the CSOP or any other discretionary employees' share scheme (which excludes any Save As You Earn Scheme approved by HMRC, a share incentive plan approved by HMRC under Schedule 2 to ITEPA or any other share option scheme of the Company which is linked to a contractual savings scheme) adopted by the Company would exceed five per cent of the nominal value of the share capital of the Company in issue on that date.

For the avoidance of doubt, any Ordinary Shares which are already in issue when placed under option or subject to an option which has lapsed will be disregarded for the purpose of the above limits. If it is intended that an option is to be settled with Ordinary Shares which have been or are intended to be acquired in the market by an EBT, those Ordinary Shares will be disregarded for the purposes of the above limits.

Individual limit
Each individual's participation is limited so that the aggregate market value of Ordinary Shares subject to all options (calculated as at the date of grant of each option) held by that individual and granted under the CSOP or any other HMRC approved company share option plan operated by the Company or any associated company, shall not exceed £30,000 (or such other amount as may be permitted by HMRC from time to time).

Exercise price

The exercise price per Ordinary Share under an option is determined by the Remuneration Committee at the time of grant but may not be less than the greater of (i) the market value of an Ordinary Share as at the date of grant and (ii) in the case of an option to subscribe for Ordinary Shares, the nominal value of an Ordinary Share.

The exercise price (as well as the number of Ordinary Shares under option and their nominal value) may be adjusted by the Remuneration Committee in the event of any capitalisation issue or rights issue (other than an issue of Ordinary Shares pursuant to the exercise of an option given to the shareholders of the Company to receive shares in lieu of a dividend) or rights offer or any other variation in the share capital of the Company including (without limitation) any consolidation, subdivision or reduction of capital. Any such adjustment will require the prior approval of HMRC.

Performance targets

The exercise of options granted under the CSOP will, in normal circumstances, be made conditional upon the achievement of objective performance targets set at the time of grant. Performance targets will be measured over a performance period, which will not begin before the start of the financial year in which the option is granted, as determined by the Remuneration Committee at the time of grant ("Performance Period").

If events occur which cause the Remuneration Committee reasonably to consider that a different or amended target would be a fairer measure of performance, the Remuneration Committee will be able to modify the original performance target in such manner as it reasonably deems fit provided that any such amended target is not materially more difficult to achieve than the original performance target.

It should also be noted that in circumstances where an employee ceases to be a Group employee, or certain corporate events occur (such as a change of control of the Company), before the end of the relevant Performance Period, the Remuneration Committee will have the discretion to assess the performance target on a modified basis having regard to the abbreviated Performance Period, provided that any such amended target is not materially more difficult to achieve than the original performance target.

Exercise of options

Options will become capable of exercise following a date ("Vesting Date"), specified at the time of grant, which occurs after the expiry of the relevant Performance Period. The Vesting Date for an option may not occur before the third anniversary of the date on which the option is granted.

Normally, an option may only be exercised following the occurrence of the Vesting Date to the extent that the performance target has been satisfied and if the option holder is still an employee within the Group. An option may not be exercised later than the day immediately prior to the tenth anniversary of its date of grant and, unless exercised, will lapse on the tenth anniversary of its date of grant.

Options may not be exercised during any prohibited period specified by the Model Code.

Cessation of Employment

If an option holder dies, any options held by him or her may be exercised (subject to any reduction in the number of Ordinary Shares which are subject to such options which is applied by the Remuneration Committee as described below) at any time during the twelve month period following the date of death.

If an option holder ceases to be employed within the Group by reason of injury, ill health or disability (evidenced to the satisfaction of the Remuneration Committee), redundancy, or retirement on or after reaching the age of 55, or upon the sale or transfer out of the Group of the company or undertaking employing the option holder (each "a Good Reason" and such an option holder, a "Good Leaver"), then:

- as regards options for which the Vesting Date has not by then occurred, he or she must normally wait until the normal Vesting Date in respect of the option before being permitted to exercise it (save that the Remuneration Committee will have the discretion instead to allow the option holder to exercise some or all of such unvested options within the period of six months following the date of cessation of employment); and
- as regards options for which the Vesting Date has by then occurred (but which have not yet been exercised), he or she will be able to exercise those options within six months of the cessation of employment,

provided that the number of Ordinary Shares which are subject to such option may be reduced as described below and no option may be exercised later than the day immediately prior to the tenth anniversary of its date of grant.

Ordinarily, where an option holder ceases to be employed within the Group (or gives notice to terminate his or her employment) for any reason other than a Good Reason, any options held by him or her (whether vested or not) will lapse and cease to be exercisable. However, the Remuneration Committee will have the discretion, subject to such additional conditions as it determines (including a power to reduce the number of shares under option whether such option has vested or not), to permit the option holder to exercise some or all of his or her options on the same basis as a Good Leaver.

Any exercise of an option where the option holder has ceased to be an employee prior to the Vesting Date for the option will be subject to:

- the prior satisfaction of the performance target (subject to any adjustment of the performance target made by the Remuneration Committee in accordance with the rules of the CSOP); and
- in the case of a Good Leaver, the reduction of the maximum number of Ordinary Shares over which the option is capable of being exercised. This will normally be based on how much of the period between the date of grant of the option and the normal Vesting Date for the option is left to run as at the date of the cessation of employment. The Remuneration Committee will, though, have discretion, having regard to all the circumstances, not to apply pro-rating or to allow the option to be exercised over more than a strictly time-apportioned number of shares.

In the case of an option holder who leaves with unexercised options (whether before or after the Vesting Date of an option) who is not a Good Leaver but whom the Remuneration Committee has exercised its discretion to treat as a Good Leaver, the reduction can be more than a time-apportioned reduction whether the option held by such deemed Good Leaver has vested or not.

Takeover and other corporate events

Exercise of options is also possible earlier than the Vesting Date if the Company is the subject of a takeover or a scheme of arrangement under Part 26 of the Companies Act 2006 sanctioned by the court, or if the Company is voluntarily wound up. In the case of a takeover of the Company or the transfer out of the Group of the undertaking employing the option holder concerned, the Remuneration Committee may allow the option to be exercised immediately before, but with effect from, the takeover or the transfer of the undertaking concerned.

Any exercise of an option in such circumstances will be subject to:

- the prior satisfaction of the performance target (subject to any modification or waiver of the performance target in accordance with the rules of the CSOP); and
- the reduction of the maximum number of Ordinary Shares over which the option is capable of being exercised. This reduction will normally be based on how much of the period between the date of grant of the option and the normal Vesting Date for the option is left to run as at the date of the cessation of employment. The Remuneration Committee will, though, have discretion, having regard to all the circumstances, not to apply pro-rating or to allow the option to be exercised over more than a strictly time-apportioned number of shares.

In the event of a takeover of the Company, an option holder may be allowed to exchange his option for a new option over shares in the acquiring company, provided that the acquiring company agrees to such exchange and the rights under the new option are equivalent to those under the old option.

Other option terms & Issues of Ordinary Shares

The CSOP provides the facility for the exercise of an option to be satisfied by either the issue of Ordinary Shares, the transfer of Ordinary Shares held by an existing shareholder who has agreed to satisfy the exercise of the option or by the transfer of Ordinary Shares held in treasury.

Options will not be capable of transfer or assignment.

Until options are exercised, option holders will have no voting or other rights in relation to the Ordinary Shares subject to those options.

Ordinary Shares allotted on the exercise of an option will rank *pari passu* in all respects with the Ordinary Shares already in issue but will not rank for any dividends or other distributions payable by reference to a record date preceding the date of such allotment. Ordinary Shares transferred on the exercise of an option will be transferred without the benefit of any rights attaching to the Ordinary Shares by reference to a record date preceding the date of that exercise. For so long as the Company's Ordinary Shares are listed on the Official List the Company will use its best endeavours to procure that the Ordinary Shares issued following exercise of any options are admitted to the Official List as soon as practicable after allotment.

Benefits obtained under the CSOP will not be pensionable.

Administration & amendment

The CSOP will be administered by the Remuneration Committee. The Remuneration Committee will be able to amend the provisions of the CSOP. However, no amendment to a key feature of the CSOP shall have effect until HMRC has approved such amendment. Furthermore, the rules of the CSOP which relate to:

- the persons to whom Ordinary Shares are provided under the CSOP;
- the limits on the number of Ordinary Shares which may be issued under the CSOP;
- the maximum entitlement of any option holder;
- the basis for determining an option holder's entitlement to Ordinary Shares or options; and
- the basis for determining the adjustment of any option granted under the CSOP following any increase or variation in the share capital of the Company

will not be capable of being amended by the board to the advantage of any option holder or potential option holder without the prior approval of the Company in general meeting except for minor amendments to benefit the administration of the CSOP, to take account of any change in legislation or to obtain or maintain favourable tax, exchange control or regulatory treatment for option holders or any Group company.

The Remuneration Committee will have the discretion, in respect of employees of the Group who are resident for tax purposes outside the UK, to amend or alter the provisions of any option to take account of overseas taxation or securities law. However, the Remuneration Committee will not be able to make any such amendment or alteration without the consent of HMRC (if required) and/or if this would result in an option being made upon terms commercially more favourable than the terms upon which an option could have been granted if such person was tax resident in the UK.

Adjustment of options

In the event of any increase or variation in the share capital of the Company, the Remuneration Committee may, with the consent of any EBT trustee (if applicable), make such adjustment as it deems appropriate to the number of Ordinary Shares subject to each option and/or the nominal value of the Ordinary Shares subject to options.

Termination

The CSOP may be terminated at any time by resolution of the board of the Company and will in any event terminate on the tenth anniversary of its adoption so that no further options can be granted under the CSOP after termination. Termination will not affect the outstanding rights of existing option holders.

Shareholder information

Financial calendar

Financial year end	31 March 2009
2008/09 preliminary results announced	12 May 2009
Annual General Meeting	9 July 2009
Final dividend payment date (record date 10 July 2009)*	7 August 2009

*See also 'Results and dividends' on page 36.

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Share dealing services
Capita Share Dealing Services provide Babcock shareholders with a quick and easy way to buy or sell Babcock International Group PLC ordinary shares. Commission starts from £20 if you deal online and £25 if you deal by phone. In addition, stamp duty, currently 0.5%, is payable on purchases.

There is no need to open an account in order to deal and you can trade at live market prices during stock market hours. You also have the added convenience of placing 'limit' orders which are valid for up to 90 days. This means that you decide the price at which you wish to sell and your shares will only be sold if the price reaches this pre-set limit during the 90-day period.

To use the service, either log on to www.capitadeal.com or call 0871 664 0448 (calls cost 10p per minute plus network extras). Please have your share certificate(s) to hand when you log on or call. If you are planning to purchase shares, you will need to have your debit card at hand with cleared funds available at your bank.

These services are offered on an execution-only basis and are subject to terms and conditions which are available on request or at www.capitadeal.com. Capita Share Dealing Services is a trading name of Capita IRG Trustees Limited, which is authorised and regulated by the Financial Services Authority.

This is not a recommendation to buy, sell or hold shares in Babcock International Group PLC. Shareholders who are unsure of what action to take should obtain independent financial advice. Share values may go down as well as up, which may result in a shareholder receiving less than he/she originally invested.

ShareGift
If you have only a small number of shares which would cost more for you to sell than they are worth, you may wish to consider donating them to the charity ShareGift (Registered Charity 1052686) which specialises in accepting such shares as donations. The relevant stock transfer form can be obtained from Capita Registrars. There are no implications for Capital Gains Tax purposes (no gain or loss) on gifts of shares to charity and it is also possible to obtain income tax relief. Further information about ShareGift may be obtained on 020 7930 3737 or from www.ShareGift.org.

Five-year financial record

	2009 £m	2008 £m	2007 £m	2006 £m	2005 £m
Continuing revenue	1,901.9	1,555.9	988.3	836.7	729.0
Operating profit	133.1	110.2	62.8	46.6	35.3
Share of profit/(loss) from joint ventures	(0.2)	–	0.4	(0.1)	0.2
Profit before interest	132.9	110.2	63.2	46.5	35.5
Net interest and similar charges	(26.2)	(25.6)	(6.2)	(5.2)	(6.0)
Profit before taxation	106.7	84.6	57.0	41.3	29.5
Income tax expense	(19.1)	(14.9)	(11.0)	(8.2)	(8.2)
Profit from continuing operations	87.6	69.7	46.0	33.1	21.3
Discontinued operations	(13.3)	–	(0.8)	(3.2)	(2.1)
Profit for the year	74.3	69.7	45.2	29.9	19.2
Minority interest	(2.3)	(2.4)	(1.8)	(0.2)	(0.1)
Profit attributable to shareholders	72.0	67.3	43.4	29.7	19.1
Non-current assets	858.4	836.1	327.2	273.4	266.5
Net current assets/(liabilities)	(117.3)	(18.6)	(96.0)	(48.0)	(60.6)
Non-current liabilities and provisions	(448.3)	(456.7)	(24.0)	(54.8)	(93.5)
Total net assets	292.8	360.8	207.2	170.6	112.4
Shareholders' funds	288.4	357.2	205.6	170.2	112.3
Minority interest	4.4	3.6	1.6	0.4	0.1
	292.8	360.8	207.2	170.6	112.4
Earnings per share – basic	37.42p	29.99p	21.10p	14.49p	10.08p
Dividend per share (proposed)	14.40p	11.50p	8.05p	6.00p	4.00p

Radley Yeldar
Design and production

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