Babcock International Group PLC
2 Cavendish Square
London W1G 0PX
Telephone +44 (0)20 7291 5000
Fax +44 (0)20 7291 5055
www.babcock.co.uk

2004

Babcock International Group PLC

Interim report 2004

Completing the transformation

Financial highlights

	First half 2004/05	First half 2003/04	Percentage change
Sales – existing	£243m	£215m	+13%
Sales – acquisitions	£96m	–	
Sales continuing (1)	£339m	£215m	+58%
Operating profit – existing	£15.4m	£12.3m	+25%
Operating profit – acquisitions	£4.9m	–	
Operating profit – continuing (2)	£20.3m	£12.3m	+65%
Profit before tax	£16.6m	£9.4m	+77%
Adjusted profit before tax (3)	£17.8m	£11.1m	+60%
Earnings per share	7.72p	5.50p	+40%
Adjusted earnings per share (3)	7.73p	6.69p	+16%
Dividend	1.35p	1.25p	+8%

(1) Before discontinued operations (2005: £nil, 2004: £10.2 million), (2) Before goodwill amortisation (2005: £2.7 million, 2004: £1.6 million), discontinued operations losses (2005: £nil, 2004: £0.2 million), and operating exceptional profit (2005: £3.1 million, 2004 £nil), (3) Before total exceptional items (2005: £1.5 million profit, 2004: £(0.1) million) and goodwill amortisation.

Business highlights

- Continuing sales – growth of 58% including acquisitions (13% excluding acquisitions)
- Adjusted profit before tax, goodwill and exceptional items up 60% to £17.8 million
- Adjusted earnings per share up 16% to 7.73p per share
- Interim dividend up by 8% to 1.35p per share
- Peterhouse acquisition completed and integration going well
- Turner and Partners acquisition strengthens position in telecoms
- Networks to benefit from 3G launch
- Good start to South West Prime and to RAF Valley
- Rail volumes increasing

Operating and financial review

Existing operations

£243.4m
Turnover
(2003: £214.9 million)

£15.4m
Operating profit
(before goodwill
and exceptionals)
(2003: £12.3 million)

Acquisitions

£95.8m
Turnover

£4.9m
Operating profit
(before goodwill
and exceptionals)

Introduction

Clearly the most significant event in the half-year has been the acquisition of Peterhouse and the consequent integration effort. I am pleased to report that the progress made so far has been excellent helped by the considerable contribution of Alan Robertson and Janette Anderson, two Directors of the Peterhouse Group.

The synergy benefits we identified at the time of the acquisition are on course to be achieved or exceeded; in particular the Peterhouse head office has been exited some six months earlier than originally forecast, the financial synergies are in place and the other synergy streams are progressing satisfactorily. Some additional areas of benefit have been identified and are being pursued. An assessment of the opportunities for the disposal of some of the smaller non-core businesses is underway. The successful start to the South West Prime and RAF Valley contracts, increasing rail replacement volumes, the launch of 3G cellular telephone technology and increasing spend on reinforcement of the high voltage power transmission system are all positive developments for Babcock.

The Group has adopted a new segmental reporting structure, which is explained in detail later in this report. The performance of these segments is outlined in the Operational Review.

Financial review

Acquisition of Peterhouse Group PLC

The Group declared the offer for Peterhouse Group PLC unconditional in all respects on 14 June 2004 and subsequently acquired 100% of the ordinary share capital for a total consideration of £99.1 million. The results of the Peterhouse subsidiaries have therefore been fully consolidated from that date. The consideration for the share capital was met from the issue of 56.3 million new ordinary shares in Babcock International Group PLC and cash consideration of £31.7 million. The Group agreed a new £140 million acquisition and working capital revolving credit facility with its banking partners in order to finance the offer. The value of net assets acquired after making provisional fair value adjustments was £32.8 million. Goodwill arising on acquisition was £66.3 million.

New segmental structure

As a consequence of the acquisition of the Peterhouse businesses and in order to prepare for the implementation of International Financial Reporting Standards, the Group’s segmental reporting structure has been refined.

Training and Support has been replaced by two new segments; Defence Services combines the services supplied to the UK Ministry of Defence by Babcock Infrastructure Services, Babcock Naval Services and Babcock Defence Services. Engineering and Plant Services combines the Group’s civil operations in Africa with the pipeline installation activity, Babcock Eagleton, based in Texas.

The Technical Services segment has been retained and now represents all the activities undertaken at Rosyth and, until its cessation in May 2004, the dockyard operation based in New Zealand.

Three new segments have been created for the businesses acquired with Peterhouse; Networks combines the activities of the power transmission, telecommunications and site access businesses operating under the Eve brand. Rail covers both the track renewals and rail projects activities of First Engineering whilst the IETG environmental services operations and ESS, the safety training organisation are combined within Health, Safety and Environmental (H,S&E).

Financial performance

At the operating level, Group operating profit pre-exceptional items and goodwill was £20.3 million, up from £12.1 million last time. Acquisitions contributed £4.9 million leaving like-for-like operating profit pre-goodwill and exceptional items from existing operations of £15.4 million against £12.3 million last year, an increase of 25%. The underlying margin on existing operations increased to 6.3% from 5.7%.

The core Peterhouse businesses acquired in mid-June made a strong start. Networks turnover of £28.7 million generated operating profits of £3.0 million whilst Rail turnover was £62.4 million in the same period with operating profit of £2.9 million. Prospects for both sectors remain strong. The remaining H,S&E businesses, which are non-core to Babcock, turned over £4.7 million, losing £0.6 million at the operating level.

Group profit before tax after goodwill and exceptional items for the six months to 30 September 2004 was £16.6 million, up from £9.4 million in the same period last year. Turnover, before discontinued businesses, was £339.2 million, an increase of 58% from £214.9 million in 2003, of which £95.8 million came from the former Peterhouse businesses acquired in June 2004. Net debt increased to £71.1 million through a combination of additional bank borrowings taken on to fund the acquisition of Peterhouse (£31.7 million) and the debt assumed on acquisition. Cash flow from operating activities was £25.3 million, after excluding operating exceptionals this translated to a conversion rate of 84% on Group operating profit. Cash flows include the receipt of £20.6 million from Network Rail which included compensation for the early termination of three track maintenance contracts in June 2004.

Profit on ordinary activities after taxation was £13.5 million up from £8.0 million last year. Earnings per share was 7.72p (2003: 5.50p). Before goodwill and exceptional items, earnings per share was 7.73p against 6.69p last year, up 16%.

Goodwill and exceptional items

A number of operating and non-operating exceptional items are reported in the first six months. These are summarised below:

	Cash £m	Non-cash £m	Total £m
Reorganisation of marine design and goodwill impairment	(0.8)	(4.6)	(5.4)
Exceptional gain on termination of rail maintenance contracts	10.0	–	10.0
Peterhouse rationalisation costs	(1.5)	–	(1.5)
Disposals – non-operating	(1.2)	(0.4)	(1.6)
	6.5	(5.0)	1.5

The standard goodwill amortisation charge was £2.7 million of which £1.0 million relates to the newly acquired Peterhouse businesses.

Financial items

Net interest payable increased to £2.7 million from £1.0 million (pre-exceptional) last year following the increase in net debt arising from the acquisition of Peterhouse.

Tax is charged at 24% of profits, which is expected to be the relevant rate for the 2004/05 financial year. The Group benefits from a tax rate lower than the standard UK corporation tax rate of 30% as a result of differential overseas tax rates applied to certain earnings and the utilisation of prior year's tax losses.

Dividends

The Directors have declared an interim dividend of 1.35p per ordinary share, an increase of 8% from last year.

The final dividend for the year ended 31 March 2004 exceeded the amount accrued by £1.2 million as a result of the additional shares issued in connection with the acquisition of Peterhouse Group PLC. This amount is reflected in this year's Profit and Loss account.

Operational review

Defence Services (Turnover £107.9 million)

A very satisfactory first half for our Defence Services businesses with sales up by 30% and operating profit (pre-goodwill) increasing by 70% compared with the same period last year. The highlights of the first half were the start of the Regional Prime South West and RAF Valley contracts. Both activities have performed well in the initial period with our customers expressing satisfaction on service delivery. In both cases our preparatory work was of a high standard and we have therefore had no surprises on going live.

Naval services also performed well in the first half, gaining some additions to the initial contract and improving margins as we became increasingly confident that we will achieve better than contracted savings over the lifetime of the contract.

Progress on bids for the Ministry of Defence remains difficult as the Ministry comes to terms with its budget problems, however there does appear to be some progress on the Royal School of Military Engineering which now has an agreed timetable to approval and contract award. The withdrawal by the Ministry of the Airfield Support Project after four years of bidding activity was disappointing. We will continue to be selective in deploying company resource only on bids where we believe our chances of contract award are good.

Technical Services (Turnover £82.8 million)

The programme at Rosyth was, in the first half year, driven by work on the refit of HMS Illustrious. This £100 million programme is on time and under budget and the customer has expressed great satisfaction with the partnering arrangements and the quality of the work. We have won a number of refit contracts in competition in the last few months the most important of which were HMS Edinburgh and HMS Northumberland. The refit market will continue to be challenging over the next two years and we will be bidding aggressively to secure further contracts. Terminal 5 work is building up quickly and will continue to increase until the First Quarter of 2005. Further contracts for modules on Terminal 5 remain to be let and we are hopeful of success on a number of these. If successful these would provide significant work through to the end of next year. Supply Chain Services, the business created two years ago, continued to grow profitably while Design and Technology and MEF both increased profits during the period.

A restructuring at Rosyth was carried out to reorganise its division into separate business lines. This resulted in the loss of some 325 jobs.

A detailed review of our two marine design businesses FBM and ATA was carried out during the period. As a result of the review both were downsized significantly and the resultant goodwill write-off and restructuring costs of £5.4 million are included in the results.

As we have previously stated, Babcock is participating in discussion with the government and other key players in UK shipbuilding and repair on the future of the industry. We will evaluate any proposals that may emerge from discussions, in the light of their ability to generate shareholder value.

Engineering and Plant Services (Turnover £52.7 million)

A good half-year for Engineering and Plant Services as a result of continued progress in our African business. Sales increased by 13% and operating profits (pre-goodwill) rose by more than 25%. Contracts for power station refurbishment in Libya helped the results as did a continuing gain in Volvo market share in Southern Africa. A number of significant contracts are currently being bid. Eagleton, the oil pipeline business, continued to suffer from a very slow market and appropriate steps have been taken to downsize the business.

Networks (Turnover £28.7 million in 3.5 months)

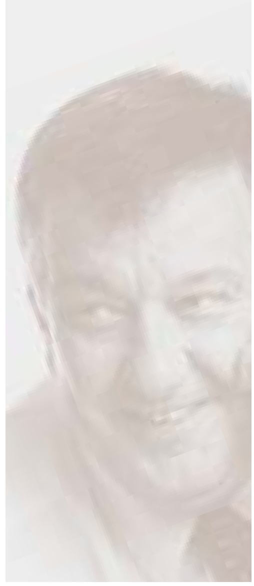
The Eve networks business has progressed well since acquisition. The transmission business in particular has delivered excellent performance – it has continued to perform above our initial expectations and a number of substantial tenders have been issued by National Grid Transco in recent weeks. The telecoms business performed steadily and there are now clear signs that the network operators are gearing up for the expected expansion following launch of 3G technology. Since the acquisition of Turner and Partners a number of acquire design and build contracts have been won. Our range of services in the cellular market now allows us to promote a comprehensive range of services which none of our competitors provide. Trakway had a reasonable summer period but activity over the traditionally slow autumn and winter period will determine the outcome for the year – wet weather is a significant help to this business. We continue to review our options for Trakway.

Rail (Turnover £62.4 million in 3.5 months)

The rail business has performed in line with our expectations at the time of acquisition with activity now beginning to build. The contracts for 'plain line' renewals are functioning well, although activity in the signalling and communications areas remain slow as Network Rail prioritises its requirements. We expect activities in these areas to increase in the next year. The contract win for high output track renewal (a technology which enables new track to be laid much more quickly than traditional methods) will ensure that we are in a leading position in the drive for increased productivity in this area. The maintenance contracts and the associated people were successfully transferred to Network Rail at the end of June and there was an initial restructuring of the business to address the need to reduce costs following the transfer.

Summary and prospects

The operating management of both Babcock and the former Peterhouse business deserve credit for delivering a strong result despite the considerable distractions of the bid. Looking ahead, the integration process is going well, and the projected synergies are on course to be achieved or exceeded. We expect contract activity at the Ministry of Defence to pick up again in the medium term. The markets served by both our Rail and Networks businesses are entering a period of growth, and we are optimistic about the prospects for these former Peterhouse operations. Overall, we view the future of the enlarged Babcock with confidence.



Peter Rogers
Chief Executive

Summarised group profit and loss account

For the six months ended 30 September 2004

Year ended 31 March 2004 Total £m		Note	Six months ended 30 September 2004 Before goodwill and exceptional items (unaudited) £m	Goodwill and exceptional items (unaudited) £m	Total (unaudited) £m	Six months ended 30 September 2003 Before goodwill and exceptional items (unaudited) £m	Goodwill and exceptional items (unaudited) £m	Total (unaudited) £m
	Group turnover							
438.0	Existing operations		243.4	–	243.4	214.9	–	214.9
–	Acquisitions		95.8	–	95.8	–	–	–
438.0	Continuing operations		339.2	–	339.2	214.9	–	214.9
14.0	Discontinued operations		–	–	–	10.2	–	10.2
452.0		3	339.2	–	339.2	225.1	–	225.1
	Group operating profit/(loss)							
22.2	Existing operations		15.4	(7.1)	8.3	12.3	(1.6)	10.7
–	Acquisitions		4.9	7.5	12.4	–	–	–
22.2	Continuing operations		20.3	0.4	20.7	12.3	(1.6)	10.7
(0.3)	Discontinued operations		–	–	–	(0.2)	–	(0.2)
21.9		3	20.3	0.4	20.7	12.1	(1.6)	10.5
0.1	Share of operating profit of joint ventures and associates		0.2	–	0.2	–	–	–
(1.7)	Provision for loss on sale of operations	5	–	(1.6)	(1.6)	–	(1.8)	(1.8)
20.3	**Profit/(loss) on ordinary activities before interest**		20.5	(1.2)	19.3	12.1	(3.4)	8.7
(0.5)	Net interest and similar charges		(2.7)	–	(2.7)	(1.0)	1.7	0.7
19.8	**Profit/(loss) on ordinary activities before taxation**		17.8	(1.2)	16.6	11.1	(1.7)	9.4
(3.4)	Tax on profit/(loss) on ordinary activities	6			(3.1)			(1.4)
16.4	**Profit on ordinary activities after taxation**				13.5			8.0
(4.9)	Dividends paid and proposed	8			(3.9)			(1.8)
11.5	**Retained profit for the financial period**				9.6			6.2
	Earnings per share	7						
11.31p	– Basic				7.72p			5.50p
11.28p	– Diluted				7.70p			5.47p
	Earnings per share before exceptional items and goodwill	7						
13.60p	– Basic				7.73p			6.69p
13.57p	– Diluted				7.72p			6.66p

Group balance sheet

As at 30 September 2004

As at 31 March 2004 (as restated) £m		Note	As at 30 September 2004 (unaudited) £m	As at 30 September 2003 (unaudited) (as restated) £m
	Fixed assets			
	Intangible assets			
0.7	Development costs		–	0.8
	Goodwill			
81.5	– Goodwill		**144.2**	83.6
(4.7)	– Negative goodwill		**(3.8)**	(5.6)
76.8			**140.4**	78.0
77.5			**140.4**	78.8
12.2	**Tangible assets**		**38.7**	15.0
	Investments			
	Investments in joint ventures			
2.4	– Share of gross assets		**1.7**	2.1
(2.7)	– Share of gross liabilities		**(1.3)**	(2.6)
0.9	– Loans to joint ventures		**0.1**	1.1
0.6			**0.5**	0.6
0.1	Other investments		**5.2**	0.1
0.7			**5.7**	0.7
90.4			**184.8**	94.5
	Current assets			
29.7	Stocks		**23.8**	28.0
75.2	Debtors – due within one year		**178.3**	92.1
64.0	Debtors – due after more than one year		**105.1**	65.4
139.2			**283.4**	157.5
17.5	Cash and bank balances	11	**39.1**	14.0
186.4			**346.3**	199.5
	Creditors – amounts due within one year			
(17.2)	– Borrowings	11	**(103.1)**	(24.8)
(117.5)	– Other		**(199.4)**	(132.2)
(134.7)			**(302.5)**	(157.0)
51.7	**Net current assets**		**43.8**	42.5
142.1	**Total assets less current liabilities**		**228.6**	137.0
	Creditors – amounts due after more than one year			
(15.7)	– Borrowings	11	**(7.1)**	(15.8)
(0.3)	– Other		–	(0.1)
(16.0)			**(7.1)**	(15.9)
(29.0)	**Provisions for liabilities and charges**		**(50.5)**	(31.1)
97.1	**Net assets**		**171.0**	90.0
	Capital and reserves			
90.1	Called up share capital		**124.6**	89.2
38.6	Share premium account		**69.0**	38.2
30.6	Capital redemption reserve		**30.6**	30.6
(62.2)	Profit and loss account		**(53.2)**	(68.1)
97.1	**Shareholders' funds**		**171.0**	89.9
–	Equity minority interests		–	0.1
97.1			**171.0**	90.0

Summarised group cash flow statement

For the six months ended 30 September 2004

Year ended 31 March 2004 (as restated) £m		Note	Six months ended 30 September 2004 (unaudited) £m	Six months ended 30 September 2003 (unaudited) (as restated) £m
28.0	Cash inflow from operating activities	9	**25.3**	13.4
(0.4)	Returns on investments and servicing of finance		**(2.4)**	0.8
(1.6)	Taxation		**(2.5)**	(0.7)
(1.8)	Net capital expenditure and financial investment		**0.4**	(0.8)
1.4	Acquisitions and disposals		**(24.7)**	1.1
(4.5)	Equity dividends paid		**(4.3)**	(2.7)
21.1	Cash (outflow)/inflow before management of liquid resources and financing		**(8.2)**	11.1
0.2	Management of liquid resources		**0.9**	0.2
(19.2)	Financing		**34.2**	(5.9)
2.1	**Increase in cash in the period**	11	**26.9**	5.4

Group statement of total recognised gains and losses

For the six months ended 30 September 2004

Year ended 31 March 2004 £m		Six months ended 30 September 2004 (unaudited) £m	Six months ended 30 September 2003 (unaudited) £m
16.4	Profit for the financial period	**13.5**	8.0
0.6	Currency translation differences on foreign currency net investments and related loans	**–**	0.7
17.0	Total recognised gains and losses relating to the period	**13.5**	8.7

Reconciliation of movements in shareholders' funds

For the six months ended 30 September 2004

Year ended 31 March 2004 (as restated) £m		Note	Six months ended 30 September 2004 (unaudited) £m	Six months ended 30 September 2003 (unaudited) (as restated) £m
87.3	Shareholders' funds at start of period, as previously reported		**101.1**	87.3
(3.9)	Prior year adjustment	12	**(4.0)**	(3.9)
83.4	Shareholders' funds at start of period, as restated		**97.1**	83.4
1.7	Shares issued in the period		**64.8**	0.5
17.0	Total recognised gains and losses relating to the period		**13.5**	8.7
(4.9)	Dividends		**(3.9)**	(1.8)
(0.1)	Movement on Employee Share Ownership Plan		**(0.5)**	(0.9)
13.7	Net movement in shareholders' funds		**73.9**	6.5
97.1	Shareholders' funds at end of period		**171.0**	89.9

Notes to the financial statements

For the six months ended 30 September 2004

1 Accounting policies

The interim financial statements have been prepared in accordance with the accounting policies adopted in the preparation of the financial statements for the year ended 31 March 2004, as set out in the annual report for that year except the adoption of UITF 38: Accounting for ESOP trusts. The cumulative effect of this change in accounting policy has been recognised as a prior year adjustment and comparative figures have been restated. The effect on the financial statements is set out in note 12.

2 Basis of preparation

The comparative figures for the year ended 31 March 2004 and the other financial information contained in this interim report do not constitute statutory accounts within the meaning of section 240 of the Companies Act 1985. The financial information in the interim report is unaudited.

Statutory accounts for the year ended 31 March 2004 have been delivered to the Registrar of Companies. The auditors have reported on those accounts, their report was not qualified and did not contain a statement under section 273(2) or (3) of the Companies Act 1985.

The interim report for the six months ended 30 September 2004 was approved by the Directors on 24 November 2004.

3 Segmental analysis

	Six months ended 30 September 2004				Six months ended 30 September 2003			
	Group turnover £m	Group operating profit before goodwill and exceptionals £m	Goodwill and operating exceptionals £m	Group operating profit £m	Group turnover £m	Group operating profit before goodwill and exceptionals £m	Goodwill and operating exceptionals £m	Group operating profit £m
Existing operations								
Defence Services	**107.9**	**8.5**	**–**	**8.5**	82.6	5.0	–	5.0
Technical Services	**82.8**	**6.7**	**(5.4)**	**1.3**	85.8	7.2	–	7.2
Engineering & Plant Services	**52.7**	**2.8**	**–**	**2.8**	46.5	2.2	–	2.2
Unallocated costs, other income and goodwill	**–**	**(2.6)**	**(1.7)**	**(4.3)**	–	(2.1)	(1.6)	(3.7)
	243.4	**15.4**	**(7.1)**	**8.3**	214.9	12.3	(1.6)	10.7
Acquisitions								
Networks	**28.7**	**3.0**	**–**	**3.0**	–	–	–	–
Rail	**62.4**	**2.9**	**10.0**	**12.9**	–	–	–	–
H,S&E	**4.7**	**(0.6)**	**–**	**(0.6)**	–	–	–	–
Unallocated costs, other income and goodwill	**–**	**(0.4)**	**(2.5)**	**(2.9)**	–	–	–	–
	95.8	**4.9**	**7.5**	**12.4**	–	–	–	–
Total continuing operations	**339.2**	**20.3**	**0.4**	**20.7**	214.9	12.3	(1.6)	10.7
Discontinued operations	**–**	**–**	**–**	**–**	10.2	(0.2)	–	(0.2)
Group total	**339.2**	**20.3**	**0.4**	**20.7**	225.1	12.1	(1.6)	10.5

Goodwill charge on continuing business for the six months to 30 September 2004 was £1.7 million (2003: £1.6 million), and on acquisitions was £1.0 million (2003: nil).

The results of the Peterhouse business included above, are consolidated from the effective date of acquisition – 14 June 2004.

Notes to the financial statements continued

4 Operating exceptional items
Within continuing businesses an operating exceptional loss of £5.4 million (2003: nil) was realised representing £0.8 million of restructuring costs and £4.6 million of goodwill write-off on the downsizing of the Group's marine design subsidiaries. Within acquired businesses an operating exceptional profit of £10.0 million reflects income from the transfer of rail maintenance contracts back to Network Rail offset by costs of the transfer and restructuring costs within the Rail business. There is also £1.5 million of operating exceptional costs for the closure of the Peterhouse head office.

5 Non-operating exceptional items
The non-operating exceptional loss of £1.6 million (2003: £1.8 million) was made up of the following; a loss of £1.2 million provided in the period for disposal costs of previously disposed of businesses, a loss of £0.4 million was recognised on the sale of CMR Consultants Limited and a write down of the carrying value of the joint venture of FBMA which was sold on 10 October 2004.

6 Taxation
The charge for taxation has been based on the estimated effective tax rate for the year ended 31 March 2005. The tax effect in respect of operating exceptional items and goodwill is a £1.2 million credit (2003: nil). There is no tax effect on the non-operating exceptional items.

7 Earnings per share
The basic earnings per share has been calculated on the profit for the period of £13.5 million (2003: profit of £8.0 million) and the weighted average number of ordinary shares in issue throughout the period of 174,971,031 (2003: 144,696,659).

The diluted earnings per share has been calculated after taking account of 1,794,503 dilutive share options where the exercise price is less than the average market price of the company's own shares during the period.

The basic and diluted earnings per share before exceptional items and goodwill have been calculated using the same weighted average number of ordinary shares in issue as above and after adjusting for goodwill amortisation of £2.7 million (2003: £1.6 million), the loss on the sale of operations of £1.6 million (2003: £1.8 million) and operating exceptional items of £3.1 million (2003: nil) and also adjusting for the tax effect (credit £1.2 million) on exceptionals. The 2003 number also included an adjustment for the exceptional interest income of £1.7 million.

8 Dividends
An interim dividend of 1.35p per 60p ordinary share (2003: 1.25p per 60p ordinary share) will be paid on 21 January 2005 to shareholders registered on 17 December 2004. The final dividend for the year ended 31 March 2004 exceeded the amount accrued by £1.2 million as a result of the additional shares issued following the acquisition of Peterhouse Group PLC.

9 Reconciliation of operating profit to cash flow from operating activities

Year ended 31 March 2004 £m		**Six months ended 30 September 2004 (unaudited) £m**	Six months ended 30 September 2003 (unaudited) £m
21.9	Group operating profit	**20.7**	10.5
4.7	Depreciation	**3.3**	2.4
0.2	Amortisation and impairment of development costs	**0.7**	0.1
3.3	Amortisation of goodwill	**2.7**	1.6
–	Impairment of goodwill	**4.7**	–
(2.0)	Movement on working capital	**(7.4)**	(1.2)
(0.1)	Other items	**0.6**	–
28.0	Cash inflow from operating activities	**25.3**	13.4

10 Movement in net debt

Year ended 31 March 2004 £m		Six months ended 30 September 2004 (unaudited) £m	Six months ended 30 September 2003 (unaudited) £m
2.1	Increase in cash in the period	**26.9**	5.4
(0.2)	Decrease in liquid resources in the year	**(0.9)**	(0.2)
20.5	Cash flow from the (increase)/decrease in debt and lease financing	**(34.6)**	5.4
22.4	Change in net debt resulting from cash flows	**(8.6)**	10.6
–	Loans and finance leases acquired with subsidiaries	**(47.1)**	–
(0.1)	New finance leases	**–**	–
(0.5)	Foreign currency translation differences	**–**	(0.1)
21.8	Movement in net debt in the period	**(55.7)**	10.5
(37.2)	Net debt at the start of the period	**(15.4)**	(37.2)
(15.4)	Net debt at the end of the period	**(71.1)**	(26.7)

11 Changes in net debt

	At 1 April 2004 £m	Cash flow £m	Acquisitions and disposals £m	Exchange and other non-cash changes £m	At 30 September 2004 £m
Cash and bank balances	14.6	(5.4)	27.9	–	**37.1**
Bank overdrafts	(11.3)	15.3	(10.9)	–	**(6.9)**
	3.3	9.9	17.0	–	**30.2**
Debt	(20.5)	(35.7)	(37.3)	–	**(93.5)**
Finance leases	(1.1)	1.1	(9.8)	–	**(9.8)**
	(21.6)	(34.6)	(47.1)	–	**(103.3)**
Liquid resources	2.9	(0.9)	–	–	**2.0**
Total	(15.4)	(25.6)	(30.1)	–	**(71.1)**

12 Prior year adjustment

The results for the six months to 30 September 2003 and year end to 31 March 2004 have been restated following the adoption of UITF Abstract 38 'Accounting for ESOP Trusts'. Shares held by the Babcock International Group PLC ESOP Trust, previously shown in the balance sheet as fixed asset investments, are now required to be shown as a deduction from shareholders' funds.

The impact of the treatment above is to reduce investments by £4.8 million as at 30 September 2003 and by £4.0 million at 31 March 2004.

The consolidated cash flow statement has been restated to reflect the reallocation of the cash payments to the purchase of shares from 'Capital expenditure and financial investment' to 'Financing'. There is no material impact on profit before tax in either current or prior periods.

13 Acquisitions and disposals

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

	Peterhouse book value	Provisional fair value adjustments	Provisional fair value
Tangible fixed assets	37.8	(6.8)	31.0
Investments	5.1	–	5.1
Total fixed assets	42.9	(6.8)	36.1
Stocks	5.2	1.6	6.8
Debtors	104.8	32.5	137.3
Cash	27.8	–	27.8
Creditors	(92.1)	(3.2)	(95.3)
Finance leases	(9.9)	–	(9.9)
Borrowings	(48.2)	–	(48.2)
Provisions for liabilities and charges	(14.8)	(7.0)	(21.8)
Net current assets	(27.2)	23.9	(3.3)
Net assets acquired	15.7	17.1	32.8
Fair value consideration			
Cash			31.7
Shares			64.7
Costs			2.7
			99.1
Goodwill arising			66.3

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

During the six months to 30 September 2004 the Group also acquired Turner & Partners (10 September 2004) and sold CMR Consultants Limited (13 July 2004).

14 Distribution

Copies of this interim report will be distributed to all holders of the company's ordinary shares. Copies will also be available at the company's registered office: 2 Cavendish Square, London W1G 0PX. In addition, this report will be available on the company's website: www.babcock.co.uk

Design and production: Radley Yeldar
Cover photography: Richard Learoyd