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Full year results presentation transcript

Wednesday 22 May 2019

Archie Bethell

Chief Executive Officer

Good morning. Thank you for joining us this morning. I'm going to be supported this morning by our FD, Franco Martinelli, who I'm sure you all know, and also we have our four sector Chief Executives, who will help me field any questions which I'm not sure about.

I'd also like to welcome Ruth Cairnie who has joined us this morning. Ruth, if you want to give a wave. There you are. As you know, we've announced that Ruth will take over from Mike Turner as the Chair at our Annual General Meeting in July. It's a big changeover for Babcock. I'm sure that it will be a strange Board for a little while without having Mike leading it. He's done a tremendous job I think for the Company over the last 10 or 11 years as Chairman and led the Board well. During that period, we've done some amazing things. I'm now looking forward to working with Ruth, who brings with her an impressive background of experience and expertise which I'm sure will help guide the Company over the coming years. So, a major change to the business, but something which I think we're all looking forward to.

Earlier this morning we issued our results for 2019, and through this short presentation, Franco and I will add some colour to the numbers and we will also have a closer look at the key actions we have taken during the year that underpin the numbers, and give us a solid business base to build on over the next few years. I'll then give you the opportunity to ask questions.

Overall, the results show that we have delivered another robust performance, and I'm satisfied with the progress that we have made in the year, particularly against the backdrop of a challenging external environment. Once again, our profit and strong cash flow generation have allowed us to increase our dividend and our pension scheme contributions and at the same time we're reducing our net debt by £157 million and that's a reduction in net debt of 14%, and continues our four-year unbroken run of year-on-year deleveraging.

During 2019, we really buckled down and pushed forward with our plans for developing and improving our business, focusing on defence, aerial emergency services and civil nuclear as our three key markets. We exited, or disposed of, several small businesses that were not core to our longer-term strategy, and as we informed you during the year, we also tackled a number of issues that had the potential to impact negatively on the business going forward. We carried out company restructuring across Europe relating to our aircraft operation certificates in the event of a no deal Brexit.

So, as well as delivering a decent set of results for 2019, we have firmly focused on the future. It's been a busy and successful year for all four of our sector teams. After 15 years of design, manufacture, assembly, integration and commissioning, we have reached the final stages of the Queen Elizabeth Class aircraft carrier alliance project at Rosyth.

We continue to deliver in-service and life extension support to both the surface and submarine naval fleets in the UK and internationally we made good progress in developing our global, naval marine business. For the Army, we made good progress in the transformation of our DSG armoured vehicle engineering support business, and in our rail business, we secured a strong position in the 10-year CP6 and CP7 contract to support rail and signalling maintenance in the Scottish region.

In South Africa we had a very good year in the equipment business, but unfortunately that progress was partially offset by delays in the power generation engineering work we are doing for Eskom,

In the aviation sector, there are a number of highlights. We commenced pilot training on our Fomedec contract in France, retained our large search and rescue contract in Spain, entered Canadian aerial firefighting in Manitoba and remobilised on medical emergency services contracts in Norway, Sweden and Finland.

In the nuclear sector, we made good progress on our Magnox and Dounreay decommissioning programmes, and continued our build-up of work on the Hinkley Point C new build project.

After adding £4.5 billion of new business, we ended the year with our order book and near-term pipeline of new opportunities stable at £31 billion, around the same level as last year.

The order book was down a little at £17 billion, and our bidding pipeline up a little at just over £14 billion. As I've said before in previous presentations, movements of this level are mainly down to the timing of bids converting to new orders, Of course, beyond the £14 billion pipeline, we have a much larger, longer-term tracking pipeline of opportunities. So, we remain in the strong position of having long-term visibility of our order book and the future opportunities both in the UK and internationally.

Our competitive position also remains stable. We've had no significant changes in the make-up of our customers, competitors and key suppliers across any of our key markets, and our new bid and renew win rates remain right in line with our performance in recent years.

Our focus and operational excellence remained a primary focus throughout the year. That applies particularly in the area of health and safety. Across our heavily regulated activities, whether it be in marine, nuclear, aviation or rail, our performance is underpinned by industry-leading health and safety performance. That means all of our people, no matter where they are in the world, go home safe every day.

Supporting our customers to achieve their performance goals is at the core of our business model, whether it be achieving better performance and availability from critical assets, providing critical services such as emergency response services or training and upskilling their people.

We work closely with our customers often in highly complex environments and we always work hard to meet and beat their expectations of us. Most of the time we succeed, and when we don't we simply work even harder together until we find and deliver the best solution. This principle is at the heart of the strategic partnering program. We invest more in innovative technologies that are now driving performance and productivity improvements across the Group.

We are the largest engineering support provider in the UK defence sector and the second largest supplier to the Ministry of Defence. During the year, we were awarded a number of new contracts and saw our scope expanded on a number of existing contracts, such as DSG, Astute and MSSP who we provide QEC and Type-45 equipment support. We were also awarded our first in-service support contract for HMS Queen Elizabeth now returning to service from Rosyth after undergoing a package of inspection and maintenance work. In Cavendish Nuclear, we won additional work at Dounreay and Sellafield, and in aviation, we expanded our UK military air business and our UK onshore emergency services contracts.

Through the MARTASS contract win, we consolidated our position as a key provider of training infrastructure and services to the UK Armed Forces.

We also built on our strong early-stage positions on a number of long-term contracts. These contracts include the UK-US Trident replacement submarine programmes, the UK submarine disposal programme, and the nuclear new-build project at Hinkley Point.

As we focus on our three key markets, defence, aerial emergency services and civil nuclear, we continue to strengthen our position in the UK, but growth and development of our international business remains a key priority. In 2019, international business represented 30% of our revenue, and as you can see here, international opportunities now account for over 40% of the short-term bidding pipeline.

In Australia, we already operate in the defence and aerial emergency services markets, and in 2019 we strengthened our sustainment position with the Royal Australian Navy and we were awarded a long-term contract to support their two largest warships, the Canberra Class amphibious LHDs.

Our success in winning the Manitoba fire-fighting contract also broadens our presence in Canada with us now operating in both the defence and aerial emergency services markets, and there is also the opportunity to enter the Canadian civil nuclear market at some point in the future. In France, Spain and Italy, there is also good potential to develop multi-market and multi-sector operations in the coming years.

As we told you at the half-year, we've opened office and workshop facilities in Korea. In Busan, we're focusing on both naval equipment support for the South Korean Navy, and also the provision of Liquid Gas Marine transportation systems to the South Korean shipyards. In Japan, our engineering office is focused on supporting their decommissioning programme.

But as I said right up-front, this has been a year where we have taken actions to further strengthen and improve the business. We tackled the challenges of our North Sea Helicopter Services business by right-sizing the fleet and we dealt with the financial impact of the permanent grounding of our 13 Airbus EC225s.

We also took important steps to maintain balance and momentum in our marine and civil nuclear market. We adjusted for two of our largest long-term contracts coming to an end, and of course I'm referring to the aircraft carrier build alliance contract and the early termination of the Magnox nuclear decommissioning contract. We plan to say more about right-sizing the business at our Capital Markets Day in a couple of weeks' time.

As I said earlier, we completed a restructuring of our European aerial emergency services business to accommodate the potential impacts on our aviation operations in the event of a no deal Brexit. With our programmes of exits and disposals, we exited activities mainly in the marine and land sectors where we no longer consider them to be strategic to our plans.

But whilst taking positive actions to address these issues which will strengthen the Group in the longer term, they result in a step-down in revenue of £410 million with a corresponding step-down in operating profit. We highlighted this issue earlier in our February trading statement, and Franco will cover this point in detail. I will also come back to it in my summary. But in the meantime, I'll now hand over to Franco.

Franco Martinelli

Group Finance Director

Thank you, Archie, and good morning. I'd like to start with a summary of our results. While our revenue was down slightly, our operating profit was up, and in a minute I'll take you through that. As Archie said, we had significant change to business to strengthen it for the future, and those changes led to the exceptional charge we first reported in H1. We recognised £120 million in the first half and there was a further £41 million in the second half, £31 million of which was pensions. The net cash element of the exceptional charge will be relatively small at around £26 million over the next years.

As you know, this is a cash generative business and this year's cash performance provides further evidence of what I mean. Our operating cash flow conversion, post CapEx increased to 104%. That's a record for us and our free cash flow after pensions was £324 million, again a record.

The strong cash performance led to the fourth consecutive year of debt reduction and we ended the year with net debt to EBITDA at 1.4 times, as we had expected.

Underlying earnings per share is up 1.2% and the full year dividend is up 1.7%.

Turning now to the revenue bridge slide, FX and the disposals we made during the year had a significant impact on our reported revenue. They accounted for around 2% of revenue. Archie has already talked about our programme of exits and disposals of those businesses that are no longer strategic to our plans. In addition to the impact of the disposals I just mentioned, exits in financial year '19 had an impact of £51 million. I expect there will be some small exits and disposals going forward.

While we had some weakness in procurement and short-cycle business, in our focus markets, excluding QEC, we grew by around 3%.

Looking now at our operating profit bridge, you can see the FX and disposals had an impact, but relatively less than on revenue. That made a small contribution to our margin improvement. Organic profit was up as a result of good contract performance in our businesses, including increased contributions from our joint ventures, and we continue to benefit from our operational efficiency programmes.

Our total margin improved to 11.4% with an increase in the year in the JV performance. Excluding JVs, we sustained margin at 10.1% broadly in line with what we've done in the last couple of years.

Moving now to the reconciliation of underlying to statutory profit, our exceptional charge is a reconciling item this year and is our first exceptional charge for five years. The remaining reconciling items are the same as in previous years. The JV profit contribution is higher this year given the strong performance in land and aviation.

Next year as Magnox and Holdfast steps down, JVs will become a smaller part of the Group, and so the contribution will obviously be lower. Similarly, both IFRIC 12 income and the charge for amortisation of acquired intangibles reduced this year and will reduce again next year, particularly acquired intangibles.

Our actions to strengthen and right-size the business result in exceptional charges. Our first half charge of £120 million came primarily from the reshaping of the oil and gas business. In addition, it also reflected the capacity reductions as we scale down QEC, Magnox and rail. Of course, the exits and disposals we've already talked about.

The H2 charge of £41 million mainly relates to pensions and further exits we made.

Our pension liabilities have increased by £31 million. That's mainly due to £26 million for the equalisation of guaranteed minimum pension benefits for men and women, but we also had a £5 million charge for the bulk transfer of £110 million of liabilities back to the customer. Over time, the cash cost of this will be part of the pension funding cash flows. In addition, we had a one-off tax charge of £10 million for the restructure of our aviation business in preparation for Brexit. Excluding the pension charges, the net cash impact of these exceptional items will be relatively small at around £26 million of which £11 million relates to financial year '19 just finished.

There will be a cash outflow of £28 million in financial year '20 including the Brexit tax charge, followed by cash in-flows in future years dependent on the sale of surplus helicopters.

I'll now take you through each sector starting with marine.

The step-down in QEC revenue this year is around £60 million, and together with our exits from renewals, reduced revenue. But if you exclude these factors, the revenue is up slightly. That's the result of increased activity on UK naval ships, and whilst infrastructure spend was initially delayed, it's now starting. Equipment spend was also slow to start as you'll remember and is also now picking up, both of which will be initially at low margin.

We broadly maintained our margin and that reflects the positive margin impact of exiting renewals and the step-down in QEC revenue, offset by a contract mix and contract performance elsewhere.

This year, we expect good revenue growth excluding QEC with margins slightly lower due to contract mix.

Our performance in land was specifically impacted by FX exits and disposals, Together, they accounted for half in the fall in revenue. In addition, we were affected by lower defence procurement spend, reduced activity in rail and UK power, and by weak trading in our South Africa power business.

Operating performance benefited from better contract performance, Holdfast JV and increasing profits from our South Africa equipment business. This year, we expect slight revenue growth excluding exits and margins maintained excluding the normalisation of the Holdfast JV.

In aviation, Fomedec drove revenue growth. This was partially offset by lower fire-fighting activity, especially in the second half, as a hot May and June was followed by cooler weather.

Oil and gas remains challenging. Over-supply and intense competition affects the market. The steps we've taken in the year to right-size the business will improve the performance going forward.

Contract performance in both our joint ventures and in our group business were better and together with our ongoing cost reduction programmes meant we held margins. This year, we expect slight revenue growth as Fomedec doesn’t repeat, with stable margins excluding the £10 million related Brexit costs.

As expected, we had lower levels of decommissioning work but good growth across the nuclear services businesses. So, we kept revenue broadly flat.

Margin was lower this year reflecting both gainshare at the end of contracts last year and lower margins in the early phases of contracts this year. This year, we expect low revenue growth, excluding Magnox step-down of £256 million, but higher margins reflecting the mix.

We had anticipated another strong year on cash and achieved cash conversion of 104% post CapEx, which was ahead of our post CapEx new target of 90% and a record performance. It was led by a strong working capital performance with an inflow of £87 million which I will come onto in a minute.

The timing of aircraft deposits and deliveries impacted the net CapEx spend in the year and it will reverse next year when these purchases convert to operating uses.

I thought it would be helpful if I set out the key receivables and payables balances. We are just showing the key figures here. The full details are in our annual report and we included these notes in the back of our statement this morning to save you waiting to see them. As you can see on the slide, trade receivables and payables are both down about £30 million. Unbilled receivables are down £119 million year-on-year. We had the positive Fomedec reversal and an improvement in Devonport unbilled receivables. They were partially offset by an increase in the crude income in DSG which will reverse this year.

Unbilled receivables vary throughout the year with the phasing of contracts. Our customers throughout the world tend to agree invoicing towards the end of the year. That does lead to fluctuations in our working capital throughout the year which has always been part of our business and we have managed this dynamic for many years.

On the payables side, contract liabilities were stable with advanced payments up slightly and deferred income down slightly.

The improvement we generated in operating cash flow was broadly carried forward into free cash flow performance which increased to £324 million with cash conversion compared to net income up significantly to 76%. I have included a full free cash flow to net income reconciliation in the appendix.

JV dividends were slightly lower than expected caused by Magnox delays which will catch up in financial year '20 when the contract ends.

With this cash performance, we de-geared again this year and net debt is £958 million. That's £157 million lower than last year. You can see in the chart that net debt has been coming down every year for the last four years, and we continue to expect to reduce net debt in March 2020 before we include the impact of IFRS16.

During this time, we've paid over five and a half million of dividends and made nearly £200 million contributions to the pension scheme and still managed to reduce debt.

As I'm sure you're all aware IFRS16 comes into effect for our financial year '20 and that means operating leases will be capitalised onto the balance sheet. On 1 April around £600 million of operating leases were brought onto the balance sheet with around 80% of these being aircraft leases in our aviation sector, which are overwhelmingly matched to customer contracts.

We've set out the expected impacts to financial year '20 from IFRS on this slide - IFRS 16 on this slide. The main ones are operating profit up around £25 million, and net debt to EBITDA up around 0.5 times. To be clear, the financial year '20 guidance we have given this morning is based on old accounting and does not include the impact of IFRS 16 as set out on this slide.

Moving now on to pensions, as this slide shows, our IAS 19 deficit at the end of the year was £28 million. That's up on the prior year, as a result of lower discount rates and higher inflation. The GMP equalisation and the transfer of bulk liabilities, I talked about earlier.

Our technical provisions deficit is estimated at around £400 million, reflecting more conservative assumptions and discount rates than used under IAS 19. I would expect that we will make cash contributions to make good this deficit over the next six years or so.

Pensions actions we are taking include the bulk transfer of liabilities back to the customer and closing Babcock Group pension scheme to future accruals. We continue to negotiate the level of increase to Rosyth scheme funding.

This slide sets out the key financials of our JVs. Our future JV dividend stream is supported by the future profit stream and current distributable reserves within our JVs. Our share of those distributable reserves currently stands at around £150 million. I currently expect that dividends for the next three years will be stable, followed by a step down beyond that.

Our share of JV net debt was £311 million, compared to last year's £354 million. The sale of Helidax in March 2019 reduced our share of net - JV net debt by £29 million. All JV net debt is non-recourse to the Group and it is mainly in AirTanker, which our partners are Airbus, Rolls Royce, Cobham and Thales, and the customer is the UK Government. You can see that the JVs hold significant cash balances for scheduled debt repayment.

This should be a familiar slide to you all, because it sets out our capital allocation priorities, which have not changed. Our first priority is to invest in the business to drive growth. We are highly disciplined, and we require all investments to meet our return on capital hurdles.

Secondly, we will continue to de-gear the balance sheet. Our balance sheet strength gives us the flexibility to make sure we're well positioned, whatever the environment, and we think de-gearing the balance sheet is particularly important during this period of political and economic uncertainty. It also safeguards our credit rating, and provides additional funding for our pension schemes.

Thirdly, we want to return capital to shareholders. We do that primarily through a sustainable dividend. Our ordinary dividend is firmly supported by our strong free cash flow. As we continue to reduce debt, we will have scope for additional returns in the future.

In this slide I have set out the step downs to our financial year '19 results we outlined in our statement this morning. Step downs of around £410 million to revenue and around £63 million to profit. These relate to the end of the QEC and Magnox contracts, the impact of the exits and disposal decisions we have made, normalisation of the JV profit contribution from Holdfast, and of course, the Brexit-related restructuring costs for aviation. The step downs have increased, due to the further exits and the actual trading results achieved in March.

Building on that, let me take you through guidance for financial year '20. As we look at this year, we are guiding to revenue of around £4.9 billion. Margins are expected in a 10.7% to 11% range. Operating profit guidance is in the range of £515 million to £535 million.

We expect free cash flow to be over £250 million, with again, performance weighted half two particularly for cash flow.

Here's some detailed cash flow guidance. As I said earlier, net CapEx to depreciation is likely to decline towards one times. Working capital will normalise to an outflow after the very strong financial year '19, and I said we expect an increase in our pension contribution guidance in part to reflect the Rosyth negotiations.

Taking these movements and the lack of Fomedec inflows from this year, £50 million, we currently expect the free cash flow financial year '20 to be over £250 million.

Before I hand back to Archie, I'd like to revisit the financial priorities we set out at the half year. (1) to sustain our margins, (2) to manage our operating cash flow, (3) to continue and de-gear ROIC - and this should drive shareholder value. This year, despite the challenging environment, we progressed on all of these measures.

I'll hand you back to Archie.

**Archie Bethel**

**Chief Executive Officer**

Okay, thank you. Thank you, Franco. Before opening up for questions, I'd just like to emphasise a few points about next year, if I may. We've talked about QEC, Magnox and the business exits and disposals. These will not be part of our business, going forward, and the guidance Franco walked you through from next year reflects this.

At our Capital Markets Day, on 5 June, we'll look to the future and we'll look at the long-term, sustainable growth opportunities that we have in front of us. Our three core businesses in defence, aerial emergency services and civil nuclear, are robust and resilient. We have strong market leadership positions in all three, and when we combine the strong market position with our focus on innovative technology, we are confident of continuing to win new business across these markets, both in the UK and around the world, just as we are currently doing.

So let me finish the presentation by re-emphasising a few points. Our financial performance in 2019 was robust and crucially, we achieved our main financial goals of improving cash flows, maintaining margins, reducing net debt, as well as exiting poor performing businesses.

Our £31 billion order book and pipeline, combined with strong positions in our three primary markets, give us real confidence that we can grow the business steadily over the next few years, and once again, we grew the business faster internationally than we did in the UK and we expect this trend to continue.

We have dealt decisively with the loss of the Magnox contract, we dealt decisively with the Airbus EC225 issues, and we dealt decisively with the end of the QEC contract and our exit from low value business lines, so we are creating a strong base to grow from, and we have delivered consistently for our customers around the world, and that was against the backdrop of a challenging political and economic environment.

This is a truly fantastic business, supported by great people, and we are now ready to push forward and demonstrate our underlying strengths and value to our customers and to our investors.

So I'll now be happy to take questions. That one here. I think these two first.

## Q&A Session

### Robert Plant - Panmure Gordon & Co

Thanks, it's Rob Plant from Panmure. You mentioned that conditions are quite challenging. Politically the UK faces a lot of uncertainty. Do you think your guidance bakes in what's happening in terms of Brexit and General Election risk and what's happening on the ground in terms of government and outsourcing decisions? Thanks.

### Archie Bethel

I think we have. We've hit the direct problems of Brexit right up front, so things like stocking and we've talked about the air operating certificates. I think it's difficult to predict beyond that. I think, like everyone, we're watching the UK politics that's going on and we have to play through these. I think the main thing we've been trying to do is ground the business strongly for whatever comes forward, so we can react. We're strengthening the balance sheet, we're getting out of areas which are not contributing. I think we're doing things that have very much got an eye on what might happen in the future.

In terms of the short-term and the - all the place - to be honest, we have seen a general softening through this year and next year on some of the short cycle type work. We also saw a major contract ASDOT in the air side for the air force - we saw that being cancelled, but there are still a number of big opportunities in the pipeline in the future - none of which we've baked into our forecast, by the way, but which we will be participating in. Projects like project Selborne, in the training side, type 31s, FSS in the marine side. These are big opportunities and we expect to see more on the nuclear side.

### Allen Wells -Exane

Hey, good morning, Allen Wells from Exane. Just a couple from me, please. Just looking at the rebased numbers on slide 30 for '19, and thinking about your guidance, obviously it implies about £150 million of incremental revenues and plus £10 million, minus £10 million, on incremental profits. I guess two questions on that.

Firstly, on the incremental revenue side, maybe you can just touch on what are the bigger moving parts on the growth side? So thinking about things like Norwegian helicopter contract, et cetera, on that side. Then on the profit bridge, if you look at that plus or £10 million minus - plus or minus £10 million, I guess it suggests a plus £6 million, minus £6 million incremental EBIT margin on the new work, on the £150 million? It feels quite low for the type of work you guys typically win. I wonder if you could comment on if I'm doing something wrong or on how you think about that?

### Archie Bethel

Well, Franco does the sums. What I'd say about the next year's forecast, I mean, what we've done is look at that underlying performance this year, and as Franco's slide shows, if you take out the things that are not in next year, underlying we grew by about 3%. If you look at the £4.9 billion as the guidance for next year, that's basically saying that underlying business will grow again about 3%.

I think across the sectors that's likely to be different. If I look at defence, our assumption there is that it will be pretty flat in the UK - so we've taken a fairly flat view of what might happen in defence. International defence we've been a bit more optimistic about, in Canada, Australia in particular, but also in South Korea, as we mentioned and opening up there to support the programme we've got there. We see a bit more growth in the international.

In the aerial - I mean this is services again - we've had a very strong growth there for the last four or five years. We expect to see that to continue again, over the next two or three years. In nuclear, again, we are predicting a fairly flat position there for the next couple of years.

So the mixture of these together has given us the guidance numbers.

In terms of margins, I mean we've seen a 10.7% to 11% - that's basically been our margin. We've never been outside that in the last 10 years, so all we're basically saying there is we're not spotting anything that's particularly different in the market. We've achieved 11% before - that's totally possible - 10.7%, I think would be - we're signalling as the low point, depending on that mix of business and as we've talked about before, we do have a portion of business that's in short cycle, lower margin business, and that is the main factor depending on how much of that is in the mix, whether we'll be at the 10.7% or the 11% range.

I don't know, Franco, do you want to add?

### Franco Martinelli

No, I think - good morning, Alan. I don't think I look at it quite in the way that you've looked at it, as a marginal movement. I think you look across the £525 million of profit as the mid of the range, and within that, there's a small range of outcomes, and to be honest, 0.33% range on that is quite small, on the level of contracts that we have. I think it's an overall view, rather than reconciling it for the movement.

### Archie Bethel

Joe?

### Joe Brent - Liberum Capital

Good morning. Joe Brent, from Liberum. Three questions, if I may? Firstly, can you help us reconcile the movement in the pipeline? Clearly, a lot's moved into orders, but interested in what new has come into that? Secondly, historically, you've talked about target leverage of 1 times debt to EBITDA, but clearly, IFRS 16 makes that a bit more complicated. Do you include the IFRS 16 adjustment in that one times debt to EBITDA number? Thirdly, you talk about a technical deficit, which I assume is an actuarial deficit, and you talk about recovering that over six years, so are we right just to take the £400 million and divide by six as the cash outflow, going forward?

Archie Bethel

Right, Franco, I'll let you do the…

Franco Martinelli

I'll do the pensions, okay, because that's the one everyone's most interested in. The answer is, yeah, that really is the funding deficit. Will it be evenly over the six years? I think for modelling that's what you should do. I think the negotiation we have with Rosyth is ongoing, which may create some more lumpiness. I don't expect that this year. I expect a slight increase for Rosyth this year, as indicated in the guidance, but I think it could be lumpier than straight line, is the answer to that question.

Archie Bethel

Your first question again?

Joe Brent - Liberum Capital

It was on the pipeline.

Archie Bethel

Oh, reconciling the pipeline. Yeah, I mean, the pipeline - that's a moving thing all the time, but it ended the year at just over £14 billion, which was up a little bit, I guess gone up a little bit again since we did that.

I mean, I think generally across the four sectors, the pipeline stays steadily with the growth opportunities coming into that. There's some big opportunities in that. What we tend to do on really big projects, like the one-offs, is we factor them in - a factor of the number, so that we don't have the big dislocation, so big contracts like Selborne or FSS or Type 31 will be in there somewhere, but at much lower values than maybe what they're going to end up at. We try and balance the pipeline value to match really the long-term pattern that we've had of conversion.

Joe Brent - Liberum Capital

Would ASDOT comes out of that?

Archie Bethel

ASDOT's out of that, yeah, which was a - quite a big number we had it in at. It still wasn't the full amount that was cancelled, but it was still a significant number.

Franco Martinelli

In addition, there are opportunities in Australia, opportunities in Canada, in defence. Some big ones there. We're now working on the ALC re-let, which is a bigger - much bigger programme, which is called Project MITER, so there's a bunch of stuff that's coming over the year.

Archie Bethel

Yeah, I mean one of the things I'm very pleased that is the fact that looking at that pipeline, we're 42% of that - and remember, in that pipeline we're showing that stuff we expect to be sentenced in the next 12 months, so it's not long term beyond that - maybe a little bit longer than that, but it's no more than - it's things that we're now actually working on - working on bids, proposals, so it's not the tracking pipeline, so to be at 42% international, I think is a pretty good sign.

Franco Martinelli

Your second question, Joe, again, sorry?

Joe Brent - Liberum Capital

The third question was on historically you've talked about target leverage of 1 times debt to EBITDA and now you've got IFRS 16 muddying the water.

Franco Martinelli

I think as - okay. Where we are with this is that, yeah, okay, the metric is moving. We need to see how the market will expect that move. We've seen various people look at it, and some people exclude it completely and some people include it. We need to just understand how the market affects it.

I still think in the next one to two years we'll be in a position to pay additional money back to shareholders, because we will continue to pay down debt.

Archie Bethel

Yeah. Ed.

Ed Steele – Citi group

Morning. Ed Steele, from Citi. Two or three things for me, please, as well. First of all, on the Magnox step down, which you've given us some data on. I thought that contract was going to end, end of August, is that right? So, you've got £24 million operating profit step down, but I mean the whole of Cavendish Nuclear JV last year was £37 million. Obviously, there's a bit of Dounreay in there, so why is there such a big step down in Magnox, for only half year impact, please?

Franco Martinelli

Because the £24 million is obviously the right number. The contract which is Magnox is a complex contract, as you would imagine, and there are various KPIs that earn fee and then there's a base contract, but it's multiple layers away earning fee, and we achieved a lot of the KPIs early, and then there's groupings of KPIs, and if you achieve all of those groupings, then you get to pay the dividend, so that's why there's a little bit of delay in dividend. So we've actually achieved more of the KPIs in this year than we would have been expecting to - or than we hoped to.

It's quite - it's a complicated - so basically, you earn a fee per KPI.

Ed Steele – Citi group

Is there any Magnox profit inside the 100% owned Cavendish Nuclear profit stream, please?

Franco Martinelli

No, nothing of significance.

Ed Steele – Citi group

No. Okay, thank you. Second area. Your guidance for aviation is for I think slight growth in 2020 for top line. How much pass through type revenue was there in Fomedec in 2019 that will give you a tough comp effect in 2020, please? Or the equipment post…

Franco Martinelli

The equipment was not pass through, to use the phrase that you're saying. We earned a margin on it. The step down, I would say, allowing for the contract that we get, which is the ongoing maintenance contract, is around £100 million.

Ed Steele – Citi group

That's fully factored in the guidance for growth?

Franco Martinelli

Correct.

**Ed Steele – Citi group**

Yeah, okay. Thanks. Then a third question, was there any material change in your factoring of receivables in 2019 - second half - so full year numbers - and will you be disclosing your factoring receivables in this year's annual report, please? Because you haven't done it before.

**Franco Martinelli**

The answer is it's around £90 million, compared to last year around £80 million. It - I don't think it is in the stats. No, it's not in the stats, but it's around £90 million compared to £80 million.

**Ed Steele – Citi group**

I think there's been a lot of pressure from the FRC to disclose this stuff, so why are you not doing it still, please?

**Franco Martinelli**

Because it's only £90 million on a total balance. It's not significant. We give it when we're asked - as I've just done for you today.

**Ed Steele – Citi group**

Okay. Thanks very much.

**Archie Bethel**

Any other questions? Okay, yes, Kean.

**Kean Marden - Jeffries International Ltd**

Morning. It's Kean Marden from Jeffries. Could we just touch on some of the operational parts of the business? Just on DSG, which, for various reasons, has been in the press a little bit over the last few weeks. If you can give us an update on contract performance and also the potential for scope extension within that contract, that would be helpful.

Then secondly, I'm intrigued on your comments about opportunities in Canadian civil nuclear. When you went through the Chalk River bid process, I suppose you came runner up in that process, so what's changed to make you believe that you have an opportunity to bid? I presume that's not Chalk River coming back to market, so presumably there are other opportunities that are coming through in Canadian civil, so if you can give me some background on that, that would be helpful.

**Archie Bethel**

Let me start off while John thinks about DSG.

The answer on Chalk River is easy. We moved it from Roger to Simon. I mean, I think when we did - Chalk River, we had a good go at, but probably part of the weakness was that we weren't well enough established in Canada, in that side of it, so since we lost Chalk River, we learned a lot about the market through that process and we're now taking a different approach to that.

Under Cavendish Nuclear, and Simon now, we are looking at other entries. It's a big market in Canada. It's almost as big as the UK market. Canada's got a really big nuclear - it's well served. It's not a so mature market, but I think, from the experiences that we've now learned, from Dounreay, from Magnox, we definitely have skills and capabilities and offerings I think will be attractive in that Canadian business.

I'll maybe get you come back to that after John tells us about DSG.

Take Kean's mike.

**Kean Marden - Jeffries International Ltd**

Take my one.

Archie Bethel

There you go.

John Davies

Hello. Okay. Yeah, DSG. I'll mention the word Boatman. Perhaps I shouldn't. Boatman, I think, we'll just stick to the facts. There were certain allegations made. I'd answer it in very simple terms. Firstly, Boatman said - it was a cost-plus contract. It's a fixed price. Boatman said we bought it in 2014 - bought it in 2015. Boatman said that protected mobility had been withdrawn - we hadn't secured it. We actually won it last year. We announced it to the City. Boatman said that Ajax was an opportunity that had been missed. It was actually awarded to GD before we even bought the business. I could carry on for quite a long time, but I won't do. Those are the kind of inaccuracies.

So I'll move on from there to say that DSG is performing well. We have done some really good work under the auspices of the Cabinet Office transformation programme. We've been working on that for some time and we have worked in a very collaborative way, and I'll say more about that at the Capital Markets Day, but there's been some good work done.

We've secured business. Over the last year we've secured Leconfield Garrison, where we've taken on the civil servants, 70 civil servants have TUPEd across to us. We've run protected mobility. We've one division replacing the Royal Electrical and Mechanical Engineer in the field, doing maintenance on vehicles, and that probably totals about £120 million, £140 million.

So we continue to work well in DSG, and in terms of future, again, I'll say a bit more at the Capital Markets Day, but projects like Warrior and Challenger and - contract churn - we do get quite a bit every year, just from contract churn. Also, just to leave you with this, taking a potential gain share on the procurement pass-through, which will be a very significant development.

I'll leave it there, if I may, unless there are any other questions on DSG.

Archie Bethel

Thank you, John. Simon, give us a quick one on Canada.

Simon Bowen

Good morning. Simon Bowen. Canada's an interesting market for us. Chalk River, I think, was an opportunist bid that we went into a partnership with - and you're absolutely correct, we weren't successful. I think we've re-evaluated Canada, with the help of our marine team, so our in-country team have given us a lot more intelligence in terms of the way to get into the market, and what we're doing is going into the market with a different offering.

It's much more of the capabilities that we've got in our nuclear services business, so it's technologies that we have in terms of things like in-cell decommissioning, with robotics and with AI - artificial intelligence. It's obsolescence management, to help Bruce Power and Ontario Power with some of their major obsolescence issues, and all of the work that we're doing with EDF on lifetime extension.

Those are discrete technology offerings, which will give us organic growth, in partnership with a number of Canadian companies that we're talking about. So it's a much more organic approach to it.

We would still consider doing something of the scale of Chalk River, because Chalk River is - would be a big opportunity and it may well come back to market, we're not quite sure, but this focus is all about nuclear services, differentiated offering of the stuff that we do here, which is not available in the Canadian market.

Archie Bethel

Thank you, Simon. Any further questions? If there's not, can I end by just thanking you for coming along this morning and I would like to remind you that on 5 June we are holding a Capital Markets Day, where we do intend to provide a great deal of detail and information about how we see the business moving forward in the next three years, and we hope that most you who are here will manage to make it on that day. So thank you. Thank you again.

Ends