26 February 2019

Meggitt PLC

2018 Full-year results

Strong organic growth in all end markets

Meggitt PLC ("Meggitt" or "the Group"), a leading international engineering company specialising in high performance components and sub-systems for the aerospace, defence and energy markets, today announces audited results for the year ended 31 December 2018.

Group headlines

£m	2018	2017[1]	% change Reported	% change Organic[2]
Orders	2,237.2	2,079.4	8	12
Revenue	2,080.6	1,994.4	4	9
Underlying				
Operating profit[3]	367.3	353.3	4	4
Earnings per share[3]	34.2p	32.0p	7	
Statutory				
Operating profit	256.6	272.7	(6)	
Earnings per share	23.2p	37.8p	(39)	
Free cash flow[4]	167.4	197.4	(15)	
Net debt	1,074.1	1,060.8	1	
Dividend	16.65p	15.85p	5	

Financial highlights

- Organic order growth of 12% underpins expectations for long term revenue growth; book to bill[5] of 1.08x included strong performance in civil aerospace (1.10x book to bill)
- Organic revenue growth of 9% reflects strong performance in growing end-markets; with 7% growth in civil aerospace, 10% in defence and 19% in energy
- Underlying operating margin maintained at 17.7%, with efficiencies from strategic initiatives and lower new product introduction costs, offset by growing free of charge ('FoC') content and extended learning curve costs at composites sites
- Statutory operating profit reflects strong underlying performance and lower exceptional costs, offset by the year on year, non-cash impact of marking to market certain financial instruments
- Free cash flow decreased by £30m to £167m, with 63% cash conversion as a result of a one-off £30m payment to reduce the Group's US pension scheme deficit and a £38m increase in inventory buffers to support growth, site consolidation and Brexit contingency
- ROCE increased to 9.9% (2017: 9.3%)
- Recommended final dividend of 11.35p giving a full year dividend of 16.65p, an increase of 5%

Strategic highlights

Strong progress on strategic initiatives, further enhancing our foundation for revenue growth, margin expansion and cash conversion:

- Completion of three further non-core disposals to increase our focus on attractive markets where we have strong positions
- Transformational wins secured to provide engine composites on the Pratt & Whitney F-135 and F-119

[1] Restated for the effects of IFRS 15, IFRS 16 and IFRS 9 as set out in note 29.
[2] Organic numbers exclude the impact of acquisitions, disposals and foreign exchange.
[3] Underlying profit and EPS are used by the Board to measure the trading performance of the Group as set out in notes 5 and 11.
[4] Free cash flow as set out in note 25.
[5] The ratio of orders received to revenue recognised in a period.

engines and brakes on the Airbus A321neo

- Accelerated progress on site consolidation and purchasing initiatives is contributing to the Group's 2021 margin improvement target with a 20% reduction in footprint and 2% p.a. reduction in purchased costs and further opportunities emerging
- Continued deployment of the Meggitt Production System ('MPS') enabling increased inventory turns of 2.7x (2017: 2.5x) which reduced the investment required to deliver growth by £43m
- New customer aligned organisation implemented in January 2019, with experienced and capable teams in place to accelerate long term growth

Tony Wood, Chief Executive, commented:

"2018 was a landmark year for Meggitt, with strong performance underpinned by our increased content on new aircraft programmes and growing end-markets, enabling the Group to increase organic revenue growth to 9%, ahead of our raised guidance. Our team delivered good progress on our strategic initiatives offsetting extended learning curve costs that we incurred at our fast growing composites sites, enabling an increase in underlying operating profit to £367m.

We have a clear growth strategy and remain focused on driving further improvements in customer and operating performance through our new customer-aligned organisation and the sustained deployment of the Meggitt Production System. Together with our growing installed base of 71,000 aircraft, we are well positioned to sustain growth over the medium term and to deliver our 2021 targets for underlying operating margin and cash.

Reflecting this continuing confidence in the prospects for the Group, the proposed final dividend is 11.35p giving a full year dividend of 16.65p, an increase of 5%. We expect 2019 to be a year of further good progress."

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GROUP OVERVIEW

Meggitt is a global engineering company specialising in high-performance components and sub-systems for the aerospace, defence and energy markets. We have a broad-based and well balanced portfolio, with equipment on over 71,000 aircraft and many ground vehicles and energy applications worldwide. This significant and expanding installed base provides us with an aftermarket revenue stream stretching out for decades. Strong customer relationships and high levels of embedded intellectual property span a broad range of products and capabilities. This has enabled us to increase our content by up to 250% on the new civil aerospace programmes which have recently entered service.

The significant increases in our content on the new aircraft platforms that are now growing rapidly, have enabled us to outperform the market in 2018. The growth of our installed base represents a major refresh of our in-service portfolio and provides a strong platform for future revenue growth. Having passed the peak of development we are focused on operational execution and have four strategic priorities to accelerate growth and improve return on capital employed. These priorities are: Portfolio Strategy, Customers, Competitiveness and Culture.

Portfolio Strategy

In 2018, we have continued to make good progress on our goal to increase our exposure to attractive and growing markets where we have strong competitive positions, through both our investment in differentiated technology and programme of non-core disposals.

Developing innovative products and technologies which enable our customers to achieve a step change in the safety, efficiency and reliability of complex equipment continues to be a critical priority for the Group. In 2018, we made excellent progress on a carefully targeted group of innovative new technology projects designed to enhance our long term competitive position in markets with strong growth potential.

Our applied research into next generation thermal systems is an excellent example of one such innovation project. Building on our strong pedigree in aero-engine thermal management we are developing a system capable of managing the step change in thermal loads that ultra-high bypass ratio engines will generate. In 2018, we have made great progress in developing technology with the potential to overcome this technical hurdle, with a thermal system with significantly lower weight and space requirements to current equivalents.

We have also continued to execute a programme of non-core business disposals. In March, we completed the sale of Linear Motion LLC ('Thomson'), a provider of precision engineered products to Umbra, and in April, we sold chemical etching subsidiary, Precision Micro to Lloyds Development Capital. As a result of these divestments, and five others that preceded them since December 2016, we have increased our exposure to attractive markets where we have a strong competitive position from 66% to 72%, further enhancing our platform for long term growth and returns. We have also reached a definitive agreement to sell the business and assets of one of our French businesses, Meggitt (France) SAS, based in Fleac, France, to a subsidiary of AF Technologies. The sale is expected to complete in April 2019. During the year to 31 December 2018, Meggitt (France) SAS, generated £11m of revenue.

Customers

Organic book to bill of 1.08x reflects good progress in growing our relationships with key customers across all market segments in 2018.

In civil aerospace, the launch of our Smart Support™ offering has been critical to securing a series of long term agreements with aftermarket customers, including Emirates, Delta Airlines, SR Technics and Turkish Technic. Smart Support™ provides a flexible service and support package which enables us to tailor long term agreements with our customers, closely aligning the services we provide with their operations. A combination of new and surplus parts, specialist repairs, exchange pools and technology upgrades enable us to optimise and increase the predictability of aircraft maintenance across the product lifecycle. Building upon the early success of Smart Support™ is a key priority for 2019.

In the defence market, we have secured a number of new orders which have enabled us to significantly increase growth in 2018 and provide further visibility for growth in years to come. These include retrofit fuel tanks for the F/A-18 Super Hornet and UH-60 Black Hawk; a $750m contract for composite parts for the F-119 and F-135 engines; and a $320m extension of our contract to provide brakes across a wide range of platforms for the Defense Logistics Agency.

To further accelerate long term growth, we adopted a new organisation structure in January 2019, moving from six capability based units to four customer-aligned divisions: Airframe Systems, Engine Systems, Energy & Equipment and Services & Support. This structural change continues our evolution to a more integrated and efficient Group and increases our alignment with customers whilst ensuring we maintain a strong focus on innovation across our businesses. Successfully implementing our new organisation and delivering the initial benefits of this transition are an important priority for 2019.

Competitiveness

In 2018, we delivered two notable achievements against the 2021 operational performance targets we announced at our Capital Markets Day in 2017.

As a result of our increasingly centre-led approach to procurement, we met our target to reduce net purchased costs by 2% p.a. Working closely with the Group's preferred suppliers in areas including electronics, fasteners and machining, we have been able to simplify our supply chain whilst better leveraging our scale to reduce cost. This approach has been more than enough to offset tariffs on products sourced from China into our US facilities. Whilst we expect such tariffs to remain a headwind in 2019, we believe the progress we have made in centralised procurement will continue to support our goal to improve underlying operating margin by 200 basis points by 2021.

During the past twelve months, we also met our target to consolidate our footprint by 20% by 2021, with non-core disposals and the closure of our Maidenhead aftermarket facility contributing to a further reduction of three sites. Having reduced our footprint to 45 sites, we continue to target further rationalisation, with 8 site consolidations currently in progress and due to complete over the next three years.

An important contributor to our success in consolidating factories has been our progress in expanding capacity in some of our existing facilities. We have doubled the capacity of our low cost manufacturing facility in Vietnam and significantly expanded our composites facilities in Mexico and San Diego. We have also made excellent progress on our UK super site, with construction activity beginning at Ansty Park, which remains on schedule to complete around the end of 2019.

Inventory turns increased to 2.7x (2017: 2.5x) despite our investment in buffer stocks to support our site consolidation plans and as part of our contingency planning for a no-deal Brexit. We are making good progress at many of our sites and we continue to target inventory turns of 4.0x by 2021.

Our efforts to increase competitiveness and reduce cost continue to be underpinned by the Meggitt Production System, our global approach to continuous improvement. The financial and operational performance improvements at our most advanced facilities continue to demonstrate the potential we can achieve when we move a critical mass of sites to the latter phases of the programme. In 2019, we are focusing central resources to increase MPS maturity and deliver sustainable operational improvements at eight large but early stage sites that constrained overall performance in 2018. This will significantly improve customer service and lay the foundation for further operational efficiency, which is key to delivering our 2021 margin improvement target.

Five Polymer and Composites sites are included within these eight early stage MPS sites. Our fast growing engine composites site in Erlanger, Kentucky incurred significantly higher costs in 2018 due to extended learning curve impacts but exited the year with improving yield and productivity which we expect to continue to steadily improve in the coming year. In total, Meggitt Polymer and Composites was a 150 basis point headwind to Group margin in 2018.

Greater levels of process reliability and increased volume output will also be key to securing the support of our customers to transfer high volume production to our recently expanded composite manufacturing facility in Mexico. We anticipate a progressive improvement in margin throughout 2019 as we execute this plan. These complex components are reliant upon deep proprietary manufacturing know-how which continues to enhance our position in one of the fastest growing areas in aerospace.

Culture

In 2018, we accelerated our High Performance Culture (HPC) programme with training rolled-out to over 2,000 of our leaders. This programme is already having an impact on our business with employee engagement up 4% during a period of significant change across many of our sites. By working more closely across our businesses we will accelerate the benefit we can achieve from centralised purchasing, site consolidations and further focus of our research in differentiated technologies.

As part of our high performance culture we continue to build a more diverse workforce, where our people succeed based on their talent, skills, knowledge and application. In 2019, we will focus on building the pipeline of future leaders to ensure that we increase diversity amongst our executive workforce over the coming years.

A key principle of our corporate culture is our focus on health and safety. In 2018, we have seen further strong performance with our total recordable incident rate improving by 34% and our lost time incident rate improving by 78%. Whilst we are pleased with the progress we have made this year, we continue to develop a culture capable of sustaining upper quartile performance in the safety of our employees and have targeted further ambitious improvements in 2019.

HEADLINE FINANCIALS

Organic order growth of 12% reflects a strong performance, including multi-year orders, across all key market segments. Civil aftermarket (AM) orders grew by 16%, civil original equipment (OE) by 16%, defence by 6% and energy by 6%, supporting a positive outlook for revenue growth over the medium term. Group organic book to bill was encouraging at 1.08x, particularly in civil aerospace where strong demand for OE and aftermarket parts contributed to a book to bill of 1.10x.

Reported Group revenue of £2,080.6m (2017 restated: £1,994.4m) increased by 4% as analysed in the table below:

	£m	% impact
2017 Revenue	1,994.4	
Currency movements	(23.7)	-1
Acquisitions and disposals	(58.6)	-4
Organic growth	168.5	+9
2018 Revenue	**2,080.6**	**+4**

Currency movements reflect the recovery of Sterling against our trading currencies, principally the US dollar, from the low levels in the first half of 2017. Acquisitions and disposals includes the net impact of the disposals of Thomson (sold in March 2018) and Precision Micro (sold in April 2018), together with the full year impact of disposals completed in 2017. Organic growth of 9% reflects strong performance in all of the Group's end-markets. In civil aerospace, organic revenue grew by 7%, in defence by 10% and in energy by 19%.

The Board's preferred non-statutory measure of the Group's trading performance is underlying profit. Underlying operating profit was up 4% to £367.3m (2017 restated: £353.3m), representing a margin of 17.7% (2017 restated: 17.7%). Margin performance reflects the growing financial contribution from the Group's key strategic priorities, including purchasing savings from a more centralised approach to category management and efficiencies from those sites in the latter most stages of MPS. These operational efficiencies together with lower new product introduction costs were offset by continued learning curve costs required to ramp up production of advanced engine composites; and an increase in FoC content on high volume civil programmes and new business jets.

Underlying net finance costs were £32.5m (2017 restated: £33.1m) reflecting a lower net debt level, offset by an increase in interest rates. Underlying profit before tax increased by 5% to £334.8m (2017 restated: £320.2m).

The Group's underlying tax rate decreased to 21.0% (2017 restated: 22.7%) as a result of the US tax reforms enacted at the end of 2017. In 2019, we expect the underlying tax rate to increase to between 22 and 23%. Although the international tax position is clearer following enactment of the recommendations from the Base Erosion and Profit Shifting project in the UK, together with US tax reforms, there are still uncertainties ahead. These include the outcome of the EU's investigation of the

UK Controlled Foreign Companies ('CFC') regime, the impact of Brexit and expected reforms in Swiss tax.

Underlying earnings per share increased by 7% to 34.2p (2017 restated: 32.0p).

On a statutory basis, operating profit for the year was £256.6m (2017 restated: £272.7m) and profit before tax was £216.1m (2017 restated: £228.3m). Statutory profit includes the £10.1m non cash loss (2017: gain of £60.7m), from the marking to market of financial instruments, principally currency hedges, against future transaction exposures as well as the £25.1m net gain (2017: gain of £25.3m) from disposals completed or agreed during the year. Statutory profit for the year was £179.0m (2017 restated: £292.8m).

Statutory earnings per share decreased to 23.2p (2017 restated: 37.8p). 2017 benefitted from a £88.3m one-off non-cash gain on the re-measurement of US deferred tax net liabilities as a result of the decrease in the US federal corporate tax rate and this explains most of the movement between 2017 and 2018. The statutory adjustments between underlying and statutory profit are described in notes 5 and 11.

The 5% increase in the recommended final dividend to 11.35p (2017: 10.80p) gives a full year dividend of 16.65p (2017: 15.85p), an overall increase of 5%. This reflects our on-going confidence in the outlook for the Group and our commitment to a progressive dividend. The full year dividend will be paid on 3 May to shareholders on the register on the record date, 22 March 2019.

Free cash flow decreased by 15% to £167.4m (2017 restated: £197.4m) as a result of an incremental £30.4m contribution to reduce US pension deficits and an increased working capital outflow of £30.1m (2017: £3.0m inflow). The working capital outflow is driven by growth in inventory, with an investment of £37.5m to support growth, site consolidations and Brexit contingency. Inventory turns increased to 2.7x (2017 restated: 2.5x) which reduced the overall investment in inventory that would otherwise have been required to deliver growth by £43.0m in 2018.

The net cash inflow of £52.5m (2017: inflow of £120.2m) after dividend payments, includes the £35.7m net proceeds from the sales of Aviation Mobility, Thomson and Precision Micro.

There are two main financial covenants in our financing agreements. The net debt:EBITDA ratio, which must not exceed 3.5x, was at 1.8x at 31 December 2018 (2017: 1.9x) and interest cover, which must be not less than 3.0x, was 14.7x (2017: 13.6x). The covenants are measured on a frozen GAAP basis and adjust for currency changes during the year. On a reported basis, the net debt:EBITDA ratio was 2.3x (2017: 2.4x). The Group has significant headroom against both key covenant ratios, and net debt:EBITDA is within our target range of 1.5x to 2.5x. The Group has £395.6m of undrawn headroom against committed bank facilities, after taking account of surplus cash (2017: £331.4m).

TRADING SUMMARY

	Revenue		**Growth**	
	2018 £m	2017 £m	Reported %	Organic %
Civil OE	464.3	447.1	4	6
Civil AM	660.5	624.9	6	8
Total civil aerospace	**1,124.8**	**1,072.0**	**5**	**7**
Defence	731.2	681.7	7	10
Energy	128.4	117.7	9	19
Other	96.2	123.0	(22)	9
Total	**2,080.6**	**1,994.4**	**4**	**9**

Civil aerospace

Meggitt operates in three main segments of the civil aerospace market: large jets, regional aircraft and business jets. The large jet fleet includes over 24,000 aircraft, the regional aircraft fleet over 6,000 and business jets around 19,000. The Group has products on virtually all these platforms and hence a very large, and growing, installed base. The split of civil revenue, which accounts for 54% of the Group total, is 59% aftermarket and 41% original equipment (OE).

Civil OE revenue grew 6% organically. Large jet OE, the largest component of our OE revenue, grew 5% driven principally by growth in A320neo and B737MAX platforms. Business jet OE also saw strong growth of 20%, which was partly offset by declining revenue in regional jets (down 14%).

Civil aftermarket revenue grew organically by 8%, within which large jets grew by 10%, driven by B777, B787, A350XWB and the A220 (formerly the Bombardier C Series). Business jets also grew with revenue up 4% for the year with good growth in G-350/450 and G-500 platforms. Revenue in the regional jet aftermarket reflected a strong growth in traffic throughout 2018, which led to organic growth of 6%.

Overall civil aerospace revenue increased by 7% organically.

Deliveries of large jets by Airbus and Boeing are underpinned by a firm order backlog extending over a number of years, which together with our increased shipset content, gives us confidence in the growth outlook for OE revenue. The rate of growth in large jet deliveries is expected to average 6% by 2021. Deliveries of regional aircraft are expected to moderately increase over the medium term and business jets are set to grow to 2021, before starting to decline.

Air traffic, measured in available seat kilometres (ASKs) is a key driver of demand for spares and repairs on large and regional aircraft. ASKs grew 6% globally in 2018, which is above the long-term trend rate of 5%. Industry forecasts for air traffic continue to grow at or above the trend rate in the medium term. Business jet utilisation in the US and Europe was flat in 2018 but our higher value content and growing market share should continue to drive revenue growth over the medium term, even in this subdued market environment. Utilisation of the larger regional jets, where we have strong market share given our braking systems content on aircraft such as the Embraer E-170 and E-190 and Bombardier CRJ 700, CRJ 900 and CRJ 1000, grew by 5% in 2018. Good growth in Europe, the Middle East and North America led to increased aftermarket demand, particularly in the second and third quarters.

Defence

Defence accounted for 35% of Group revenue in 2018. We have equipment on an installed base of around 22,000 fixed wing and rotary aircraft and a significant number of ground vehicles and training applications. Direct sales to US customers accounted for 73% of defence revenue, with 18% to European customers and 9% to the rest of the world.

Defence revenue grew 10% organically. Original equipment revenue grew by 7%, with strong growth in parts for the F-35 Joint Strike Fighter and AH-64 Apache. Aftermarket revenue (which accounts for 44% of total defence revenue) increased by 15% as a result of strong demand for retrofit fuel tanks for the F/A-18 Hornet and UH-60 Black Hawk. These were partly offset elsewhere by lower demand on platforms such as BAE Hawk and AH-1 Cobra.

The outlook for defence expenditure in the US, our single most important defence market, remains healthy. Growth in defence spending in the US is expected to continue given the increases in FY2019 budget and the President's proposed budget for FY2020.

Energy and other

Energy and other revenue (11% of Group total) come from a variety of end markets, including power generation (4%), oil and gas (2%), medical (1%) and automotive (1%). Our energy capabilities centre on providing valves and condition-monitoring equipment for power generation installations, including ground-based gas and wind turbines, and printed circuit heat exchangers used primarily in the oil and gas market.

Energy revenue grew organically by 19% in 2018, driven primarily by the recovery at Heatric which has operated in challenging end-markets following the sharp decline in the oil price in 2014. Trading in the Group's valve and condition monitoring businesses grew 4% on an organic basis, reflecting our success in supporting end users and growth in small frame turbines which offset declining demand for large frame gas turbines.

The long-term growth expectations for our energy businesses, and particularly Heatric, remain good. We have differentiated technology which plays a critical role in the extraction of deep-water offshore gas reserves and good opportunities for use in adjacent markets.

OPERATIONAL PERFORMANCE

The financial performance of the individual divisions is summarised in the table below:

£m								
Revenue					Underlying Operating Profit			
		% Growth					% Growth	
2018	2017	Reported	Organic		**2018**	2017	Reported	Organic
381.8	381.6	+0	+1	Aircraft Braking Systems	**121.5**	133.5	-9	-9
575.6	521.3	+10	+13	Control Systems	**127.0**	117.2	+8	+12
388.9	337.5	+15	+16	Polymers & Composites	**6.0**	23.8	-75	-76
498.6	501.2	-1	+4	Sensing Systems	**84.0**	64.2	+31	+32
235.7	252.8	-7	+12	Equipment Group	**28.8**	14.6	+97	+70
2,080.6	1,994.4	**+4**	**+9**	**Group**	**367.3**	353.3	**+4**	**+4**

Meggitt Aircraft Braking Systems (MABS) provides wheels, brakes and brake control systems for civil and military aircraft, including fixed wing and rotorcraft. It continues to develop innovative technology for new programmes enabling the business to retain its leading position in its target markets, underscored by strong market share gains in recent years, notably on super mid-size and long range business jets. The division represents 18% of Group revenue, generating 91% of its revenue from the aftermarket and 9% from OE.

MABS civil revenue declined organically by 1%. Civil aftermarket revenue grew organically by 1% driven by good growth in regional jets, particularly Embraer E-170 which offset lower demand on Bombardier CRJ900 and a range of smaller aircraft. Large jet aftermarket revenue reduced organically by 17% with strong growth on Airbus A220 offset by significantly lower demand for spares on mature platforms which had been strong during 2017.

MABS defence revenue increased by 8% organically, with increased demand on UH60 Black Hawk, A-10 Thunderbolt, F-16 Falcon and Gripen aircraft partially offset by lower demand for Eurofighter Typhoon and BAE Hawk brakes.

Underlying operating margin decreased from 35.0% to 31.8% in 2018 driven by unfavourable revenue mix and the accelerated growth of FoC hardware which represents a significant refresh of our installed base. This dilutes our near term margins but will drive aftermarket revenues for decades to come.

Meggitt Control Systems (MCS) designs and manufactures products which manage the flow of liquids and gases around aero and industrial turbines, and control the temperature of oil, fuel and air in aircraft engines. The division, which also provides fire protection equipment to engines and airframes, represents 28% of Group revenue, generating 39% of its revenue from OE and 61% from the aftermarket.

Revenue was up by 13% organically. Civil aerospace grew organically by 15%, with strong performance in both OE and aftermarket. OE revenue grew by 10% on an organic basis with good growth on A320neo family, 737MAX and A350XWB partially offset by lower demand on 787 and the A320ceo aircraft. Civil aftermarket revenue grew by 19% on an organic basis with strong growth in large jet demand, particularly on A320, A350XWB, 737, 777 and 787.

Defence revenue increased by 11% on an organic basis driven by good growth in spares on fighter jet programmes, including B1-B Lancer, UH60 Black Hawk and C-130J Hercules. Energy revenue increased by 5% organically driven by growth in demand for small frame industrial gas turbine valves.

Underlying operating margin declined by 40 basis points to 22.1%, reflecting lower overhead recovery at our fire protection site during the fourth quarter as we implemented a change in ERP system.

Meggitt Polymers & Composites (MPC) supplies flexible bladder fuel tanks, complex composites and seals packages for a broad range of civil and defence platforms. These products are linked by their dependence on similar materials technology and manufacturing processes. It supplies over 80% of the US defence requirements for fuel bladders and ballistically-resistant and crashworthy fuel tanks. MPC represents 19% of Group revenue and generated 64% of its revenue from OE and 36% from the aftermarket.

On an organic basis, MPC revenue increased by 16% in 2018, reflecting the strong content we have on new generation civil platforms and growing demand for spares on defence aircraft. Civil revenue grew organically by 10% as a result of strong demand for our engine composites on the fast growth CFM Leap and Pratt & Whitney PurePower engine programmes. Organic order growth of 32% in civil OE underpins a healthy medium term outlook for MPC, with continued demand anticipated for our high temperature engine composites.

Defence revenue grew by 21% on an organic basis as a result of strong demand for composite components on the F-135 engine and for retrofit fuel tanks on programmes including F/A-18 Super Hornet, F-16 Falcon and UH60 Black Hawk.

Underlying operating margin decreased from 7.1% to 1.5% reflecting the full year impact of the elevated and extended learning curve costs at the Group's composite sites which began to impact financial performance in late 2017, together with the productivity drag from our fuel tanks facility which significantly increased capacity in the early part of 2018. The actions we have taken during 2018 have delivered meaningful improvements in operational performance with yield improving across all major parts at our composites sites. The significant growth on these parts, associated with large shipset values on fast growing new engine programmes, means we have prioritised near term operational performance over cost reduction in 2018. Initial yield improvements have enabled us to reduce scrap costs in the second half, and the transfer of production to low cost regions, increases in labour productivity and further yield improvement are all expected to provide good scope for cost reduction in 2019.

The outlook for MPC remains strong given the extensive capability we have acquired, strong platform positions and potential for significant market growth. This is particularly true for composite components on new engine programmes where technical barriers remain high and manufacturing know-how can be a critical differentiator.

Meggitt Sensing Systems (MSS) designs and manufactures highly engineered sensors to measure a variety of parameters such as vibration, temperature, pressure, fluid level and flow as well as power storage, conversion and distribution systems and avionics suites for aerospace applications. Its products are designed to operate effectively in the extreme conditions of temperature, vibration and contamination that exist in an aircraft or ground-based turbine engine. Sensors are combined into broader electronics packages, providing condition data to operators and maintainers of engines, contributing to improved safety and lower operating costs. MSS has migrated these products into other specialist markets requiring similar capabilities, such as test and measurement, crash test and medical. Combining its capabilities with MABS, it has a number of civil aerospace tyre pressure monitoring systems already in service and further systems under development, having secured positions for this technology on 10 aircraft platforms. MSS represents 24% of Group revenue and generated 77% of its revenue from OE and 23% from the aftermarket.

MSS revenue increased by 4% organically, with 1% growth in civil aerospace driven by business jet OE growth, particularly on Bombardier Global 7500 and Embraer Legacy 450/500, which offset falling revenue on widebody aircraft. Defence revenue increased by 6%, with strong growth on F-35 Lightning II more than sufficient to offset declining spares demand on other fighter jet and rotorcraft platforms. In energy and other markets (including test and measurement, industrial and medical), MSS revenue increased organically by 4% reflecting success in reducing reliance on OEMs and targeting operators of industrial gas turbines; and growing demand in medical markets for our aero-derivative sensing capabilities.

Despite 98% growth in FoC content on new generation engine programmes, underlying operating margin increased by 400 basis points to 16.8% reflecting lower new product introduction costs, purchasing savings from our centre-led approach to category management and good progress in reducing other costs.

We have also reached a definitive agreement to sell the business and assets of one of our French businesses, Meggitt (France) SAS, based in Fleac, France, to a subsidiary of AF Technologies. The sale is expected to complete in April 2019. During the year to 31 December 2018, Meggitt (France) SAS, generated £10.6m of revenue.

Meggitt Equipment Group (MEG) comprises our dedicated defence businesses and Heatric, a provider of printed circuit heat exchangers to the energy sector. The division represents 11% of Group revenue and generates 78% of its revenue from OE and 22% from the aftermarket.

MEG revenue grew by 12% organically, reflecting good growth in defence as a result of strong growth at Meggitt Defense Systems Inc ('MDSI'), a leading provider of thermal systems, ammunition handling and scoring technologies. In energy, revenue increased organically by 86% in 2018, driven by the recovery at Heatric which has operated in challenging end-markets following the sharp decline in the oil price in 2014.

Increased profitability at Heatric together with greater operational leverage at MDSI contributed to good growth in underlying operating margin which increased from 5.8% to 12.2% in 2018.

In March 2018, we completed the sale of Thomson to Umbra and in April 2018, the sale of Precision Micro to Lloyds Development Capital. The two divested businesses generated £11.8m of revenue during 2018.

NEW ORGANISATION STRUCTURE

With effect from 1 January 2019, we have adopted a new customer-aligned reporting structure which will make Meggitt a simpler organisation to do business with and will provide access to the complete suite of our capabilities through one, clear and consistent interface with each of our major customer groups. Pro-forma revenue and underlying operating margin for the year to 31 December 2018, for the new reporting structure is as follows:

£m 2018 Pro-forma	**Airframe Systems**	**Engine Systems**	**Energy & Equipment**	**Services & Support**	**Disposed / For Sale**	**Group**
Revenue	1,158	406	398	400	28	2,389
Intercompany Revenue	(148)	(127)	(26)	(5)	(2)	(308)
External Revenue	**1,009**	**279**	**372**	**395**	**26**	**2,081**
Operating Profit	259	18	31	58	1	367
Operating Margin	**25.7%**	**6.6%**	**8.3%**	**14.7%**	**2.3%**	**17.7%**

INVESTING FOR THE FUTURE

£m	**2018**	2017	% change Reported	Organic
Total research and development (R&D)	**138.3**	157.9	(12)	(11)
Less: Charged to cost of goods sold / WIP	***(31.8)***	*(38.8)*	*(18)*	*(18)*
Capitalised	***(58.6)***	*(62.5)*	*(6)*	*(6)*
Add: Amortisation / impairment	***22.1***	*23.0*	*(4)*	*(4)*
Charge to net operating costs	**70.0**	79.6	(12)	(9)
Programme participation costs	**0.8**	3.4	(76)	
Capital expenditure	**72.3**	78.4	(8)	

Total R&D expenditure reduced in 2018 to £138.3m and was 6.6% of revenue (2017: £157.9m, 7.9%). Applied research, combined with targeted investment in the development of technology, remains critical to our long-term growth. We have significantly increased our content on new aircraft, which represents a major refresh of our in-service portfolio. Therefore, having passed the peak of technology development for the current generation of aircraft, we saw reduced spend on capitalised development costs (down 6% organically). However, we are still investing in our successful applied research and technology (AR&T) programmes, which will develop the next generation products and manufacturing technologies required to enable future programmes.

We also anticipate that customer funded R&D will continue to support AR&T, given our past success in securing such customer funded development programmes and grants. Our investment in programme participation costs ('PPC') excludes investment in FoC hardware which is expensed under IFRS 15 and only comprises cash payments. Such costs are typically associated with programmes in the development phase. In 2018 this investment declined to £0.8m.

The charge to net operating costs, including amortisation and impairment, decreased by 12% (9% organically) to £70.0m (2017: £79.6m).

Capital expenditure on property, plant and equipment and intangible assets was £72.3m (2017: £78.4m). This includes the investment required to support factory consolidations and the expansion at sites in Coventry, Vietnam, Mexico and San Diego.

Capital expenditure is due to increase significantly in 2019, as we accelerate plans to consolidate the Group's manufacturing footprint, including investments at the Ansty Park site and completion of current construction and fit out projects to increase capacity within our existing estate.

Guidance issued at the half year for operating exceptional cash relating to site consolidation activity had anticipated the receipt of £21.0m in December 2018, for the sale of land associated with the move to our Ansty Park site. This payment was delayed but subsequently received in January.

FOREIGN EXCHANGE

The results of foreign subsidiaries are translated into Sterling at weighted average exchange rates. Sterling remained volatile throughout 2018 against all major currencies, trading at between $1.25 and $1.43 against the US dollar. However, over the year as a whole, the average Sterling rate against the US dollar was only marginally stronger at $1.31 (2017: $1.30) providing a modest adverse impact on our reported results for the year. Compared to 2017, the Group's revenue reduced by £15.2m and underlying profit before tax by £2.7m from currency translation movements relating to US Dollar denominated revenues and profits. The sensitivity of revenue and underlying PBT to future exchange rate translation movements, when compared to the 2018 average rates, is shown in the table below:

	2018 average rate	Revenue £'m	Underlying PBT £'m
Impact of 10 cent movement			
US Dollar	1.31	115	16
Euro	1.13	11	2
Swiss Franc	1.30	9	3

Transaction risk arises where revenues and/or costs of our businesses are denominated in a currency other than their own. We hedge known, and some anticipated transaction currency exposures, based on historical experience and projections. Our policy is to hedge at least 70% of the next 12 months' anticipated exposure and to permit the placing of cover up to five years ahead. Compared to 2017, the Group's revenue was adversely impacted by £8.5m and underlying profit before tax for the year benefitted by £1.5m from currency transaction movements. Each ten cent movement in the US Dollar against the average hedge rates achieved in 2018 would affect underlying profit before tax by approximately £9.0m in respect of US Dollar/Sterling exposure, £3.0m in respect of US Dollar/Euro exposure and £4.0m in respect of US Dollar/Swiss Franc exposure.

We typically hedge transaction exposure and the following table details hedging currently in place:

	Hedging in place[6] %	Average transaction Rates[7]
2018		
US Dollar/Sterling		1.44
US Dollar/Euro		1.21
US Dollar/Swiss Franc		1.06
2019		
US Dollar/Sterling	100	1.43
US Dollar/Euro	91	1.19
US Dollar/Swiss Franc	82	1.07
2020 – 2023 inclusive		
US Dollar/Sterling	62	1.37
US Dollar/Euro	16	1.24
US Dollar/Swiss Franc	20	1.11

Taking both translation and transaction benefit into account, 2018 reported revenue reduced by £23.7m and underlying PBT reduced by £1.2m.

RETIREMENT BENEFIT SCHEMES

The Group's principal defined benefit schemes are in the UK and US and are closed to new members. Total deficits decreased to £209.1m (2017: £308.1m). The main drivers of the reduction in net deficit included a reduction of £98.3m (2017: £9.8m) due to re-measurement gains on scheme liabilities, which principally arose from a weakening of AA corporate bond yields in both the UK and US, and net deficit reduction payments of £67.6m (2017: £33.5m). Deficit reduction payments in 2018 included additional contributions into two of the Group's US schemes of £30.4m. These contributions, which represent an acceleration of amounts that would have been due over the next five years, are deductible against the Group's 2017 taxable profits and attract tax relief at the higher rates that prevailed prior to US tax reforms enacted in December 2017.

[6] Based on forecast transaction exposures.
[7] Hedging in place with unhedged exposures based on exchange rates at 31 January 2019.

In the UK, the Group is currently making deficit payments in accordance with a recovery plan agreed with the trustees following the 2015 triennial funding valuation. This recovery plan provides for the deficit to be addressed by payments which gradually increase over the period to March 2024. Under this plan, the Group will make deficit contributions of £32.3m in 2019 (£2018: £30.9m). The 2018 triennial valuation is currently in progress and preliminary results indicate a funding deficit of £163.0m at April 2018. This provisional funding position is approximately £34.0m lower than that projected in the 2015 valuation at the same date. It is expected that a revised recovery plan, addressing this improvement in funding position, will be finalised with the trustees in the first half of 2019 although no change to the level of payments for 2019 is currently expected.

In the US, the level of minimum annual payments is principally driven by regulations, although additional contributions in excess of legislative minimum amounts can be made. Following the additional contributions in 2018, amounts required to be paid will reduce to approximately £4.0m in 2019 and, absent any further changes in legislation, will remain broadly at this level for the next four years.

BOARD CHANGES

In September 2018, we announced that Doug Webb would retire from his role as Executive Director and Chief Financial Officer in December 2018. Doug served as our CFO for over five years, overseeing a critical period in our evolution from a holding company to an integrated group. We thank Doug for the significant role he has played in the development of the Group and we wish him well in his retirement.

Doug has been succeeded by Louisa Burdett who joined Meggitt as Chief Financial Officer after serving as Group Finance Director of Victrex, a FTSE 250 industrial polymers group focused on several strategic markets including aerospace and energy. Louisa has extensive experience in senior financial roles at companies including the Financial Times Group, GE and GlaxoSmithKline and is also a Non-Executive Director and Chair of the Audit Committee of Electrocomponents plc.

Guy Hachey joined the Board as a Non-Executive Director and as a member of the Audit, Remuneration and Nominations committee in January 2019. Previously President and Chief Operating Officer of Bombardier, Guy will bring extensive skills and experience in aerospace and will be a strong successor for Paul Heiden who is retiring on 25 April 2019. We thank Paul for nine years of excellent service and contribution to the Board, particularly since 2012 when he was appointed as Chairman of the Remuneration Committee, leading the Committee through a period of significant change in remuneration reporting requirements, and 2016, when he was appointed as our Senior Independent Director. Paul will be succeeded by Guy Berruyer as Senior Independent Director and Alison Goligher as Chairman of the Remuneration Committee.

In January 2019 we announced that Caroline Silver will join the Board as a Non-Executive Director on 25 April 2019, immediately prior to the AGM. Caroline will also join the Audit, Remuneration and Nominations Committees. Caroline is a Senior Managing Director at Moelis & Company, a leading global independent investment bank where she specialises in financial institutions and fintech advisory and capital raising. Previously, she was Vice Chairman of EMEA Investment Banking at Bank of America Merrill Lynch and spent 14 years at Morgan Stanley where she held a number of senior positions including Global Vice Chairman of Investment Banking and European Head of Financial Institutions. She started her career as a Chartered Accountant with PricewaterhouseCoopers.

GROUP OUTLOOK

The outlook for our civil markets continues to be positive. The fundamental driver of our business is air traffic, which continues to grow ahead of the long run average of 4 to 5% per annum. This is being achieved through increased production of large jets and the increased shipset values we have secured on the latest generation of aircraft will underpin organic civil OE revenue growth over the medium term ahead of overall market growth. This growth will be partly offset by the expectation that regional jet deliveries continue to fall in 2019 and that growth in business jets is slower than the 20% achieved in 2018.

In 2019, we expect civil OE revenue to grow organically by 4 to 6%.

Civil aftermarket revenues will continue to benefit from above average growth in traffic and the reduced availability of used serviceable material given the record low retirement rate in 2018. However, this growth will be partly offset by an anticipation of lower utilisation of both business jets and regional aircraft which account for 46% of Group aftermarket exposures; and a strong comparative period in 2018, in which aftermarket growth was supplemented by non-recurring revenue associated with new distributor agreements signed in late 2017. In 2019, we expect organic civil aftermarket revenue growth of 3 to 5%.

In defence markets the medium-term outlook is positive, particularly in our largest market the US, which accounts for 73% of revenue and where the budget for procurement; research, development, test and evaluation; and operations and maintenance is due to grow by 3% in 2019. Our strong technology offering and broad platform exposure should enable us to outgrow the market and in 2019, we expect to grow organic revenue by 4 to 6%.

The outlook in our energy markets is mixed. At Heatric, we expect the recovery to continue into 2019 given organic order growth of 24% in 2018. This is likely to be offset by more challenging conditions in power generation where we continue to offset falling demand from the industrial gas turbine OEMs with growth in sales to end users. In 2019, we expect organic energy growth of 0 to 5%.

The Group has carefully considered a range of scenarios and implemented mitigating actions that arise from the risk of a potential no-deal Brexit. These include investment in buffer inventories, the recruitment of additional customs administrators and application for third-country EASA status, enabling us to continue to support European registered aircraft under these circumstances. Given that less than 5% of the Group's revenues are transacted between the UK and the EU, Brexit is not considered to be a significant risk for the Group in 2019.

On the basis of the above, the Group expects organic revenue growth of 3 to 5% in 2019.

The Group expects underlying operating margin growth of 0 to 50 basis points in 2019. The increasing momentum in our strategic initiatives, greater volume leverage and gradual improvement in margin in engine composites are likely to be partly offset by continued growth of FoC units and unfavourable revenue mix, with civil OE and defence growth expected to be our fastest growing segments.

We remain confident in delivering our 2021 margin target of at least 19.9% and inventory turns of 4.0x, with the pace of our strategic initiatives continuing to accelerate as headwinds from unfavourable revenue mix are expected to ease as the rate of new aircraft deliveries slows in the early 2020s.

Consolidated income statement
For the year ended 31 December 2018

	Notes	2018 £'m	2017 Restated (note 29) £'m
Revenue	3	**2,080.6**	1,994.4
Cost of sales		**(1,320.1)**	(1,235.2)
Gross profit		**760.5**	759.2
Net operating costs		**(503.9)**	(486.5)
Operating profit[1]	5	**256.6**	272.7
Finance income	8	**1.0**	1.4
Finance costs	9	**(41.5)**	(45.8)
Net finance costs		**(40.5)**	(44.4)
Profit before tax[2]		**216.1**	228.3
Tax (charge)/credit	10	**(37.1)**	64.5
Profit for the year attributable to equity owners of the Company		**179.0**	292.8
Earnings per share:			
Basic[3]	11	**23.2p**	37.8p
Diluted[4]		**22.8p**	37.1p

Non-GAAP measures			
[1] Underlying operating profit	5	**367.3**	353.3
[2] Underlying profit before tax	5	**334.8**	320.2
[3] Underlying basic earnings per share	11	**34.2p**	32.0p
[4] Underlying diluted earnings per share	11	**33.7p**	31.3p

Consolidated statement of comprehensive income
For the year ended 31 December 2018

	Notes	2018 £'m	2017 Restated (note 29) £'m
Profit for the year attributable to equity owners of the Company		**179.0**	292.8
Items that may be reclassified to the income statement in subsequent periods:			
Currency translation movements		**90.7**	(147.5)
Movements in fair value of financial liabilities arising from changes in credit risk		**0.8**	(2.1)
Cash flow hedge movements		**(0.3)**	(0.2)
Tax effect		**2.5**	(2.4)
	28	**93.7**	(152.2)
Items that will not be reclassified to the income statement in subsequent periods:			
Remeasurement of retirement benefit obligations	21	**46.2**	66.6
Tax effect		**(7.3)**	(27.1)
		38.9	39.5
Other comprehensive income/(expense) for the year		**132.6**	(112.7)
Total comprehensive income for the year attributable to equity owners of the Company		**311.6**	180.1

Consolidated balance sheet

At 31 December 2018

	Notes	**31 Dec 2018**	31 Dec 2017 Restated (note 29)	1 Jan 2017 Restated (note 29)
		£'m	£'m	£'m
Non-current assets				
Goodwill	14	**2,035.3**	1,944.9	2,095.7
Development costs	14	**557.1**	495.8	543.0
Programme participation costs	14	**18.2**	17.1	17.0
Other intangible assets	14	**610.4**	672.1	817.6
Property, plant and equipment	15	**404.0**	406.2	424.4
Investments	16	**12.9**	13.6	14.8
Trade and other receivables		**21.5**	38.7	58.4
Contract assets		**61.1**	49.7	56.9
Derivative financial instruments	19	**10.0**	28.5	21.8
Deferred tax assets		**16.3**	26.3	28.8
		3,746.8	3,692.9	4,078.4
Current assets				
Inventories		**441.2**	393.4	443.0
Trade and other receivables		**413.6**	389.7	394.7
Contract assets		**47.9**	39.7	33.4
Derivative financial instruments	19	**9.3**	3.6	4.2
Current tax recoverable		**6.4**	4.3	4.4
Cash and cash equivalents	26	**181.9**	118.5	173.8
Assets classified as held for sale	17	**10.3**	9.7	-
		1,110.6	958.9	1,053.5
Total assets	4	**4,857.4**	4,651.8	5,131.9
Current liabilities				
Trade and other payables		**(452.5)**	(402.1)	(419.1)
Contract liabilities		**(47.9)**	(52.5)	(31.7)
Derivative financial instruments	19	**(18.8)**	(17.3)	(31.2)
Current tax liabilities		**(39.5)**	(39.6)	(35.6)
Lease liabilities	18	**(16.1)**	(16.9)	(17.8)
Bank and other borrowings	26	**(10.2)**	(71.4)	(175.7)
Provisions	20	**(33.0)**	(65.7)	(53.6)
Liabilities directly associated with assets classified as held for sale	17	**-**	(7.8)	-
		(618.0)	(673.3)	(764.7)
Net current assets		**492.6**	285.6	288.8
Non-current liabilities				
Trade and other payables		**(1.3)**	(5.5)	(4.8)
Contract liabilities		**(43.9)**	(23.1)	(19.3)
Derivative financial instruments	19	**(17.4)**	(14.6)	(45.7)
Deferred tax liabilities		**(161.9)**	(142.2)	(235.5)
Lease liabilities	18	**(81.4)**	(85.2)	(88.5)
Bank and other borrowings	26	**(1,148.3)**	(1,005.8)	(1,170.6)
Provisions	20	**(83.7)**	(82.5)	(131.8)
Retirement benefit obligations	21	**(209.1)**	(308.1)	(414.7)
		(1,747.0)	(1,667.0)	(2,110.9)
Total liabilities		**(2,365.0)**	(2,340.3)	(2,875.6)
Net assets		**2,492.4**	2,311.5	2,256.3
Equity				
Share capital		**38.8**	38.8	38.8
Share premium		**1,223.9**	1,222.2	1,219.8
Other reserves		**15.7**	15.7	15.7
Hedging and translation reserves		**493.8**	400.1	552.3
Retained earnings		**720.2**	634.7	429.7
Total equity attributable to owners of the Company		**2,492.4**	2,311.5	2,256.3

Consolidated statement of changes in equity
For the year ended 31 December 2018

	Equity attributable to owners of the Company					
	Share capital	Share premium	Other reserves	Hedging and translation reserves	Retained earnings	Total equity
	£'m	£'m	£'m	£'m	£'m	£'m
At 1 January 2017 (Restated see note 29)	38.8	1,219.8	15.7	552.3	429.7	2,256.3
Profit for the year	-	-	-	-	292.8	292.8
Other comprehensive (expense)/income for the year	-	-	-	(152.2)	39.5	(112.7)
Total comprehensive (expense)/income for the year	-	-	-	(152.2)	332.3	180.1
Employee share schemes:						
Value of services provided	-	-	-	-	12.7	12.7
Purchase of own shares for employee share schemes	-	-	-	-	(19.0)	(19.0)
Issue of equity share capital	-	2.4	-	-	(2.4)	-
Dividends	-	-	-	-	(118.6)	(118.6)
At 31 December 2017 (Restated see note 29)	38.8	1,222.2	15.7	400.1	634.7	2,311.5
Profit for the year	**-**	**-**	**-**	**-**	**179.0**	**179.0**
Other comprehensive income for the year	-	-	-	93.7	38.9	132.6
Total comprehensive income for the year	**-**	**-**	**-**	**93.7**	**217.9**	**311.6**
Employee share schemes:						
Value of services provided	-	-	-	-	16.1	16.1
Purchase of own shares for employee share schemes	-	-	-	-	(22.6)	(22.6)
Issue of equity share capital	-	1.7	-	-	(1.7)	-
Dividends	-	-	-	-	(124.2)	(124.2)
At 31 December 2018	**38.8**	**1,223.9**	**15.7**	**493.8**	**720.2**	**2,492.4**

Consolidated cash flow statement
For the year ended 31 December 2018

	Notes	2018 £'m	2017 Restated £'m
Non-GAAP measures			
Cash inflow from operations before business acquisition and disposal expenses and exceptional operating items		**364.0**	417.0
Cash outflow from business acquisition and disposal expenses		**(3.8)**	(3.9)
Cash outflow from exceptional operating items	7	**(12.0)**	(13.8)
Cash inflow from operations	25	**348.2**	399.3
Interest received		**0.2**	0.2
Interest paid		**(33.1)**	(37.5)
Tax paid		**(20.0)**	(24.1)
Cash inflow from operating activities		**295.3**	337.9
Business acquired		**-**	(19.4)
Businesses disposed	27	**35.7**	83.7
Capitalised development costs	14	**(58.6)**	(62.6)
Capitalised programme participation costs		**(0.8)**	(3.4)
Purchase of intangible assets		**(21.8)**	(18.3)
Purchase of property, plant and equipment		**(52.6)**	(62.0)
Proceeds from disposal of property, plant and equipment		**2.1**	1.9
Cash outflow from investing activities		**(96.0)**	(80.1)
Dividends paid to Company's shareholders		**(124.2)**	(118.6)
Purchase of own shares for employee share schemes		**(22.6)**	(19.0)
Proceeds from bank and other borrowings		**85.5**	64.9
Repayments of bank and other borrowings		**(66.8)**	(224.2)
Repayments of lease liabilities		**(14.3)**	(11.4)
Cash outflow from financing activities		**(142.4)**	(308.3)
Net increase/(decrease) in cash and cash equivalents		**56.9**	(50.5)
Cash and cash equivalents at start of the year		**118.5**	173.8
Exchange gains/(losses) on cash and cash equivalents		**6.5**	(4.8)
Cash and cash equivalents at end of the year		**181.9**	118.5

NOTES TO THE FINANCIAL STATEMENTS
For the year ended 31 December 2018

1. General information and basis of preparation

This document contains abridged preliminary financial information for the year ended 31 December 2018 together with comparatives.

The information presented has been prepared in accordance with those parts of the Companies Act 2006 applicable to companies reporting under International Financial Reporting Standards ('IFRSs) as adopted by the European Union and in accordance with the FSA Listing Rules. It has been prepared on a going concern basis and under the historical cost convention, as modified by the revaluation of certain financial assets and financial liabilities (including derivative financial instruments) at fair value.

The financial information contained in this document does not constitute Group statutory accounts as defined in Sections 404 and 435 of the Companies Act 2006. It is based on, and is consistent with, that in the Group's statutory accounts for the year ended 31 December 2018 and those financial statements will be delivered to the Registrar of Companies following the Company's Annual General Meeting. The auditors' report on those accounts is unqualified, does not draw attention to any matters by way of emphasis and does not contain a statement under Section 498(2) or (3) of the Companies Act 2006.

Group statutory accounts for the year ended 31 December 2017 were approved by the Board of Directors on 26 February 2018 and have been filed with the Registrar of Companies. The auditors' report on those accounts was unqualified, did not draw attention to any matters by way of emphasis and did not contain a statement under Section 498(2) or (3) of the Companies Act 2006.

2. Accounting policies

The consolidated financial statements have been prepared using the same accounting policies adopted in the Group's financial statements for the year ended 31 December 2017, except as described below.

A number of new accounting standards have been adopted for the financial year. The Group has updated its accounting policies to reflect these standards, which has resulted in a restatement of prior period comparatives as described in note 29. The standards which have been adopted for the first time and have had a significant impact on the consolidated financial statements are:

- IFRS 15, 'Revenue from contracts with customers';
- IFRS 16, 'Leases'; and
- IFRS 9, 'Financial instruments'.

3. Revenue

The Group's revenue is analysed as follows:

	2018	2017 Restated
	£'m	£'m
At a point in time	**1,916.5**	1,871.3
Over time: Power by the hour/Cost per brake landing	**45.0**	39.1
Over time: Other	**119.1**	84.0
Total	**2,080.6**	1,994.4

4. Segmental analysis

The Group managed its businesses for the year ended 31 December 2018 under the key segments of Meggitt Aircraft Braking Systems, Meggitt Control Systems, Meggitt Polymers & Composites, Meggitt Sensing Systems and the Meggitt Equipment Group.

Year ended 31 December 2018

	Meggitt Aircraft Braking Systems	Meggitt Control Systems	Meggitt Polymers & Composites	Meggitt Sensing Systems	Meggitt Equipment Group	Total
	£'m	£'m	£'m	£'m	£'m	£'m
Gross segment revenue	389.1	577.1	391.3	541.0	253.0	2,151.5
Inter-segment revenue	(7.3)	(1.5)	(2.4)	(42.4)	(17.3)	(70.9)
Revenue from external customers	**381.8**	**575.6**	**388.9**	**498.6**	**235.7**	**2,080.6**
At a point in time	349.3	570.7	385.0	489.9	121.6	1,916.5
Over time: Power by the hour/Cost per brake landing	31.9	4.9	-	8.2	-	45.0
Over time: Other	0.6	-	3.9	0.5	114.1	119.1
Revenue by basis of recognition	**381.8**	**575.6**	**388.9**	**498.6**	**235.7**	**2,080.6**
Underlying operating profit*	**121.5**	**127.0**	**6.0**	**84.0**	**28.8**	**367.3**

* A reconciliation of operating profit to underlying operating profit is shown in note 5.

Year ended 31 December 2017 (Restated)

	Meggitt Aircraft Braking Systems	Meggitt Control Systems	Meggitt Polymers & Composites	Meggitt Sensing Systems	Meggitt Equipment Group	Total
	£'m	£'m	£'m	£'m	£'m	£'m
Gross segment revenue	388.1	522.5	339.4	525.8	266.4	2,042.2
Inter-segment revenue	(6.5)	(1.2)	(1.9)	(24.6)	(13.6)	(47.8)
Revenue from external customers	381.6	521.3	337.5	501.2	252.8	1,994.4
At a point in time	353.6	517.9	337.5	492.6	169.7	1,871.3
Over time: Power by the hour/Cost per brake landing	28.0	3.4	-	7.7	-	39.1
Over time: Other	-	-	-	0.9	83.1	84.0
Revenue by basis of recognition	381.6	521.3	337.5	501.2	252.8	1,994.4
Underlying operating profit*	133.5	117.2	23.8	64.2	14.6	353.3

* A reconciliation of operating profit to underlying operating profit is shown in note 5.

4. Segmental analysis (continued)

Segmental assets

	31 December 2018 £'m	31 December 2017 Restated £'m
Meggitt Aircraft Braking Systems	**534.3**	513.4
Meggitt Control Systems	**418.2**	346.0
Meggitt Polymers & Composites	**282.5**	234.1
Meggitt Sensing Systems	**489.5**	450.8
Meggitt Equipment Group	**176.6**	199.2
Total segmental trading assets	**1,901.1**	1,743.5
Centrally managed trading assets*	**146.1**	166.9
Goodwill	**2,035.3**	1,944.9
Other intangible assets	**527.8**	592.0
Investments	**12.9**	13.6
Derivative financial instruments – non-current	**10.0**	28.5
Deferred tax assets	**16.3**	26.3
Derivative financial instruments – current	**9.3**	3.6
Current tax recoverable	**6.4**	4.3
Cash and cash equivalents	**181.9**	118.5
Assets classified as held for sale	**10.3**	9.7
Total assets	**4,857.4**	4,651.8

* Centrally managed trading assets principally include amounts recoverable from insurers and other third parties in respect of environmental issues relating to former sites, other receivables and property, plant and equipment of central companies.

5. Reconciliations between profit and underlying profit

Underlying profit is used by the Board to monitor and measure the underlying trading performance of the Group. It excludes certain items as described below:

	Note	2018 £'m	2017 Restated £'m
Operating profit		**256.6**	272.7
Amounts arising on the acquisition, disposal and closure of businesses	a	**(25.1)**	(25.3)
Amortisation of intangible assets acquired in business combinations (note 14)		**91.5**	93.5
Financial instruments (note 6)		**10.1**	(60.7)
Exceptional operating items (note 7)		**34.2**	73.1
Adjustments to operating profit*		**110.7**	80.6
Underlying operating profit		**367.3**	353.3
Profit before tax		**216.1**	228.3
Adjustments to operating profit per above		**110.7**	80.6
Net interest expense on retirement benefit obligations (note 21)		**8.0**	11.3
Adjustments to profit before tax		**118.7**	91.9
Underlying profit before tax		**334.8**	320.2
Profit for the year		**179.0**	292.8
Adjustments to profit before tax per above		**118.7**	91.9
Tax effect of adjustments to profit before tax		**(29.1)**	(49.0)
Impact of reduction in the US rate of federal corporate tax (note 10)		**(4.1)**	(88.3)
Adjustments to profit for the year		**85.5**	(45.4)
Underlying profit for the year		**264.5**	247.4

* Of the adjustments to operating profit, £18.1m (2017 restated: £8.5m) relating to exceptional operating items has been charged to cost of sales with the balance of £92.6m (2017 restated: £72.1m) included within net operating costs.

a. The Group separately presents amounts arising on the acquisition, disposal and closure of businesses. These include gains or losses made on the disposal or closure of a business, adjustments to the fair value of contingent consideration payable in respect of an acquired business or receivable in respect of a disposed business and costs directly attributable to the acquisition and disposal of businesses.

	2018 £'m	2017 £'m
Gain on disposal of businesses before disposal expenses	**(30.4)**	(40.3)
Costs related to the disposal of businesses in the current period	**2.5**	0.6
Gain on disposal of businesses (note 27)	**(27.9)**	(39.7)
Costs related to the disposal of businesses in prior periods	**0.3**	-
Costs related to the acquisition of businesses	**-**	0.2
Remeasurement of fair value of contingent consideration payable relating to previously acquired businesses	**(3.6)**	-
Impairment of assets classified as held for sale (note 17)	**6.1**	14.2
Total	**(25.1)**	(25.3)

6. Financial instruments

Although the Group uses foreign currency forward contracts to hedge against foreign currency exposures, it has decided that the costs of meeting the extensive documentation requirements to be able to apply hedge accounting under IFRS 9 'Financial Instruments' are not merited. The Group's underlying profit figures exclude amounts which would not have been recognised if hedge accounting had been applied.

Where interest rate derivatives qualify to be hedge accounted, any difference recognised in the income statement between the movements in fair value of the derivatives and in the fair value of fixed rate borrowings is excluded from underlying profit. Where cross currency derivatives and treasury lock derivatives do not qualify to be hedge accounted, movements in fair value of the derivatives are excluded from underlying profit.

	2018	2017 Restated
	£'m	£'m
Movement in fair value of foreign currency forward contracts	**27.9**	(73.8)
Impact of retranslating net foreign currency assets and liabilities at spot rate	**(1.0)**	0.5
Movement in fair value of interest rate derivatives	**5.4**	8.1
Movement in fair value of fixed rate borrowings due to interest rate risk	**(4.9)**	(8.9)
Movement in fair value of cross currency derivatives	**(16.8)**	13.9
Movement in fair value of treasury lock derivative	**(0.5)**	(0.5)
Total – Loss/(gain)	**10.1**	(60.7)

7. Exceptional operating items

Items which are significant by virtue of their size or nature and which are considered non-recurring are classified as exceptional operating items.

		Income statement		**Cash expenditure**	
	Notes	**2018**	2017 Restated	**2018**	2017
		£'m	£'m	**£'m**	£'m
Site consolidations	a	**28.7**	7.9	**8.2**	8.5
Impairment loss arising from cancellation of Dassault Falcon 5X programme	b	**-**	58.0	**-**	-
Business restructuring costs		**3.1**	2.7	**3.1**	0.8
Guaranteed Minimum Pension equalisation (note 21)		**1.7**	-	**-**	-
Integration of acquired businesses		**0.7**	4.5	**0.7**	4.5
Total		**34.2**	73.1	**12.0**	13.8

a. This relates to costs incurred in respect of the Group's previously announced plans to reduce its footprint by 20% by the end of 2021. Cumulative costs since the announcement are £43.6m (2017: £14.9m). In 2018, costs are principally in respect of the move to a new facility being constructed at Ansty Park in the West Midlands which will enable the Group to consolidate a range of manufacturing, engineering and support operations into a single centre of excellence. The charge in 2018 includes impairment losses in respect of property, plant and equipment of £3.6m (note 15) and assets classified as held for sale of £4.6m (note 17).

b. On 13 December 2017, Dassault Aviation announced the cancellation of its Falcon 5X programme. The cancellation resulted in a cost of £58.0m being recognised in 2017, comprising an impairment loss of £54.4m in respect of capitalised development costs and £3.6m in respect of the reduction of inventory to net realisable value.

8. Finance income

	2018 £'m	2017 £'m
Interest on bank deposits	**-**	0.1
Unwinding of interest on other receivables (note 20)	**0.8**	1.2
Other finance income	**0.2**	0.1
Total	**1.0**	1.4

9. Finance costs

	2018 £'m	2017 Restated £'m
Interest on bank borrowings	**2.6**	2.2
Interest on senior notes	**28.0**	30.0
Interest on lease liabilities	**3.7**	3.8
Unwinding of discount on provisions (note 20)	**1.7**	2.0
Net interest expense on retirement benefit obligations (note 21)	**8.0**	11.3
Amortisation of debt issue costs	**0.8**	0.9
Less: amounts capitalised in the cost of qualifying assets (note 14)	**(3.3)**	(4.4)
Total	**41.5**	45.8

10. Tax

On 22 December 2017, the US government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act ("TCJA"). The TCJA made substantial changes to the Internal Revenue Code of 1986, as amended. Among those changes was a significant reduction in the generally applicable US federal corporate tax rate from 35% to 21%, with effect from 1 January 2018. The Group's deferred tax balances relating to its US operations were remeasured in 2017 to reflect this rate reduction, with the impact excluded from the Group's underlying tax charge for 2017 (note 5). In 2018, the Group made an additional USD40.0m deficit contribution into certain of its US pension schemes. This contribution is deductible against the Group's US taxable profits for the year ended 31 December 2017 and accordingly attracts federal tax relief at 35%. The £4.1m difference between the tax relief at 35% and the deferred tax recognised on this deficit at 21% at 31 December 2017 has been excluded from the Group's underlying tax charge for 2018 (note 5).

The Finance (No 2) Act 2015 and Finance Act 2016, included legislation to reduce the main rate of corporation tax in the UK from 19% to 17% with effect from 1 April 2020. As these changes were substantively enacted in prior years, they have had no significant impact on the tax charge for the current year.

11. Earnings per ordinary share

Earnings per ordinary share ('EPS') is calculated by dividing the profit attributable to owners of the Company of £179.0m (2017 restated: £292.8m) by the weighted average number of shares in issue during the year of 773.2m (2017: 774.2m shares).

Underlying EPS is based on underlying profit for the year (note 5) and is reconciled to basic EPS below:

	2018	2017 Restated
	Pence	Pence
Basic EPS	**23.2**	37.8
Adjust for effects of:		
Amounts arising on the acquisition, disposal and closure of businesses	**(3.2)**	(3.1)
Amortisation of intangible assets acquired in business combinations	**9.1**	7.8
Financial instruments	**1.0**	(6.3)
Exceptional operating items	**3.8**	6.2
Net interest expense on retirement benefit obligations	**0.8**	1.0
Impact of reduction in the US rate of federal corporate tax	**(0.5)**	(11.4)
Underlying basic EPS	**34.2**	32.0

The calculation of diluted EPS adjusts the weighted average number of shares to reflect the assumption that all potentially dilutive ordinary shares convert. For the Group, this means assuming all share awards in issue are exercised. The weighted average number of shares used in the calculation of diluted EPS is 785.9m (2017: 789.2m).

Diluted underlying EPS for the year is 33.7p (2017 restated: 31.3p).

12. Dividends

The Board is recommending a final dividend of 11.35p per share (2017: 10.80p per share). Taken with the interim dividend of 5.30p (2017: 5.05p) paid in the year, this gives a total dividend of 16.65p (2017: 15.85p), an increase of 5.0%. Subject to approval at the Annual General Meeting on 25 April 2019, the proposed dividend will be paid on 3 May 2019 to shareholders on the register at the close of business on 22 March 2019. A dividend reinvestment plan will be made available, in respect of the final dividend, for shareholders who wish to elect for shares in lieu of cash.

13. Related party transactions

During the year, the Group made sales to the joint venture of £3.3m (2017: £3.7m) and purchases from the joint venture of £0.2m (2017: £0.4m). Transactions between the Company and its subsidiaries have been eliminated on consolidation. The remuneration of key management personnel of the Group, which is defined for 2018 as members of the Board and the Group Executive Committee, is set out below.

	2018	2017
	£'m	£'m
Salaries and other short-term employee benefits	**11.1**	11.7
Retirement benefit expense	**-**	0.2
Share-based payment expense	**4.1**	2.3
Total	**15.2**	14.2

14. Intangible assets

	Goodwill	Development Costs	Programme participation costs	Other intangible assets
	£'m	£'m	£'m	£'m
At 1 January 2017 (Restated)	2,095.7	543.0	17.0	817.6
Exchange rate adjustments	(140.9)	(36.8)	(1.3)	(53.2)
Business acquired	10.6	-	-	9.7
Businesses disposed	(20.5)	-	-	(12.7)
Additions	-	62.6	2.0	20.4
Transfer to assets classified as held for sale	-	-	-	(1.2)
Interest capitalised	-	4.4	-	-
Impairment loss*	-	(55.3)	-	-
Disposals	-	-	-	(0.3)
Amortisation**	-	(22.1)	(0.6)	(108.2)
At 31 December 2017 (Restated)	1,944.9	495.8	17.1	672.1
Exchange rate adjustments	91.2	24.1	1.0	29.2
Businesses disposed (note 27)	(0.8)	-	-	(0.1)
Additions	-	58.6	0.9	19.3
Interest capitalised (note 9)	-	3.3	-	-
Transfer to assets classified as held for sale (note 17)	-	(2.6)	-	(0.5)
Disposals	-	-	-	(0.3)
Amortisation**	-	(22.1)	(0.8)	(109.3)
At 31 December 2018	**2,035.3**	**557.1**	**18.2**	**610.4**

* Of the 2017 impairment loss, £54.4m in respect of development costs was charged to exceptional operating items following cancellation of the Dassault Falcon 5X programme (note 7).

** Included within amortisation of other intangible assets is £91.5m (2017: £93.5m) relating to intangible assets acquired in business combinations and which is excluded from the Group's underlying profit figures (note 5).

15. Property, plant and equipment

	2018	2017 Restated
	£'m	£'m
At 1 January	**406.2**	424.4
Exchange rate adjustments	**16.2**	(23.3)
Business acquired	**-**	0.2
Businesses disposed (note 27)	**(3.5)**	(7.7)
Additions	**61.6**	76.8
Transfer to assets classified as held for sale (note 17)	**(14.6)**	(5.6)
Disposals	**(4.7)**	(2.7)
Impairment loss (note 7)	**(3.6)**	(2.0)
Depreciation	**(53.6)**	(53.9)
At 31 December	**404.0**	406.2

16. Investments

The Group's investment in its joint venture, Parkway-HS, LLC has been accounted for using the equity method and is stated as follows:

	2018	2017
	£'m	£'m
At 1 January	**13.6**	14.8
Exchange rate adjustments	**0.8**	(1.3)
Share of (loss)/profit after tax	**(1.5)**	0.6
Dividends received	**-**	(0.5)
At 31 December	**12.9**	13.6

17. Assets classified as held for sale

On 26 March 2018, the Group completed the disposal of Linear Motion LLC, previously classified as a disposal group.

During the year, the Group decided to dispose of the trade and assets of Meggitt (France) SAS, based in Fléac, France and at 31 December 2018, determined that a sale was highly probable. Accordingly, the related assets have been classified as a disposal group held for sale and are presented separately at the balance sheet date together with directly associated liabilities. An impairment loss of £6.1m (note 5) was recognised to reduce the assets to their recoverable value. The business is reported within Meggitt Sensing Systems.

Additionally, in 2018 the Group has transferred £14.0m in respect of land and buildings relating to its manufacturing facilities in Coventry, West Midlands, UK to assets classified as held for sale. An impairment loss of £4.6m was recognised to reduce the assets to their recoverable value (note 7). These facilities were subject to a sale and leaseback transaction that commenced in the year and completed in January 2019.

	2018		
	Assets classified as held for sale	**Liabilities directly associated with assets classified as held for sale**	**Total**
	£'m	**£'m**	**£'m**
At 1 January 2018	9.7	(7.8)	1.9
Exchange rate adjustments	(0.5)	0.4	(0.1)
Change in carrying value of held for sale assets and liabilities up to date of disposal	0.8	4.1	4.9
Business disposed	(10.0)	3.3	(6.7)
Additions	21.1	(0.1)	21.0
Impairment loss	(10.8)	0.1	(10.7)
At 31 December 2018	**10.3**	**-**	**10.3**

17. **Assets classified as held for sale (continued)**

	2018		
	Carrying value before classification as held for sale	**Allocated impairment loss**	**Total**
	£'m	**£'m**	**£'m**
Development costs (note 14)	2.6	(2.6)	-
Other intangible assets (note 14)	0.5	(0.5)	-
Property, plant and equipment (note 15)	14.6	(5.2)	9.4
Inventories	2.9	(2.0)	0.9
Trade and other receivables	0.5	(0.5)	-
Assets classified as held for sale	**21.1**	**(10.8)**	**10.3**
Trade and other payables	0.1	(0.1)	-
Liabilities directly associated with assets classified as held for sale	**0.1**	**(0.1)**	-

18. **Lease Liabilities**

The Group leases various factories, warehouses, offices, plant and equipment. The following amounts are included in the Group's consolidated financial statements in respect of its leases:

	2018	2017
	£'m	£'m
Depreciation charge for right-of-use assets	**14.4**	13.8
Additions to right-of-use assets	**4.6**	15.9
Net book amount of right-of-use assets	**79.1**	85.1
Interest expense on lease liabilities (note 9)	**3.7**	3.8
Expense related to short-term leases and low-value assets	**0.7**	0.7
Total cash outflow for leases comprising interest and capital payments	**18.0**	15.2

At 31 December 2018, the Group had the following significant lease commitments:

- A lease relating to its new facility being constructed at Ansty Park, West Midlands, UK (note 7). The Group expects to recognise this lease in 2019, when it obtains control of the right-of-use asset and to recognise a lease liability and right-of-use asset of approximately £60.0m at that date. The lease term is 30 years. At the date the lease is recognised, the Group expects undiscounted cash flows to be: £9.0m inflow in one year or less; £11.0m outflow in more than one year but not more than five years; and £99.0m outflow in more than five years.

- In January 2019, the Group completed a sale and leaseback of its existing manufacturing facilities in Coventry, West Midlands, UK. Lease liabilities and right-of-use assets of approximately £11.0m will be recognised and the lease terms range from two years for the main manufacturing facilities to 25 years for one of the Group's specialised operations. An impairment loss of £7.6m has been recognised in 2018 in respect of the carrying value of the facilities and is included within exceptional operating items (note 7). At the date the leases are recognised, the Group expects undiscounted cash outflows to be: £0.9m in one year or less; £2.4m in more than one year but not more than five years; and £13.4m in more than five years.

19. Financial Instruments – fair value measurement

For trade and other receivables, contract assets, cash and cash equivalents, trade and other payables, contract liabilities and the current portion of floating rate bank and other borrowings, fair values approximate to book values due to the short maturity periods of these financial instruments. For trade and other receivables, allowances are made within their book value for credit risk. The fair values of lease liabilities approximate to their book values due to the measurement of lease liabilities at the Group's incremental borrowing rate which has not changed significantly since the inception of the lease liabilities presented. Leases are also negotiated at market rates with independent, unrelated third parties and are subject to periodic rental reviews.

For other financial instruments, a comparison of book values and fair values is provided below:

	Book value		Fair value	
	2018	2017	**2018**	2017
	£'m	£'m	**£'m**	£'m
Derivative financial instruments – non-current	**10.0**	28.5	**10.0**	28.5
Derivative financial instruments – current	**9.3**	3.6	**9.3**	3.6
Financial assets	**19.3**	32.1	**19.3**	32.1
Derivative financial instruments – current	**(18.8)**	(17.3)	**(18.8)**	(17.3)
Bank and other borrowings – current	**(10.2)**	(71.4)	**(10.2)**	(71.4)
Derivative financial instruments – non-current	**(17.4)**	(14.6)	**(17.4)**	(14.6)
Bank and other borrowings – non-current	**(1,148.3)**	(1,005.8)	**(1,136.5)**	(1,001.9)
Financial liabilities	**(1,194.7)**	(1,109.1)	**(1,182.9)**	(1,105.2)
Total	**(1,175.4)**	(1,077.0)	**(1,163.6)**	(1,073.1)

Derivative financial instruments measured at fair value are classified as level 2 in the fair value measurement hierarchy, as they have been determined using significant inputs based on observable market data. The fair values of interest rate derivatives have been derived from forward interest rates based on yield curves observable at the balance sheet date and contractual interest rates. The fair values of foreign currency forward contracts have been derived from forward exchange rates observable at the balance sheet date and contractual forward rates. The fair values of cross currency derivatives have been derived from forward interest rates based on yield curves observable at the balance sheet date, forward exchange rates observable at the balance sheet date and contractual interest and forward rates.

The non-current portion of bank and other borrowings measured at fair value is classified as level 3 in the fair value measurement hierarchy, as it has been determined using significant inputs which are a mixture of those based on observable market data (interest rate risk) and those not based on observable market data (credit risk). The fair value attributable to interest rate risk has been derived from forward interest rates based on yield curves observable at the balance sheet date and contractual interest rates, with the credit risk margin kept constant. The fair value attributable to credit risk has been derived from quotes from lenders for borrowings of similar amounts and maturity periods. The same methods of valuation have been used to derive the fair value of the non-current portion of bank and other borrowings which is held at amortised cost, but for which fair values are provided in the table above.

The book value of bank and other borrowings is analysed as follows:

	2018	2017
	£'m	£'m
Held at fair value through profit and loss	**242.7**	235.2
Held at amortised cost	**915.8**	842.0
Total	**1,158.5**	1,077.2

There were no transfers of assets or liabilities between levels of the fair value hierarchy in the year.

20. Provisions

	2018 Environmental receivables* £'m	2018 Provisions £'m
At 1 January (Restated)	(64.1)	148.2
Exchange rate adjustments	(2.6)	6.3
Additional provisions/(receivables recognised) in year	(2.5)	19.6
Unused amounts reversed	-	(9.6)
(Credit)/charge to net finance costs (notes 8 and 9)	(0.8)	1.7
Transfers to trade and other payables	-	(3.7)
Utilised	35.9	(45.8)
At 31 December	**(34.1)**	**116.7**

	2018 £'m	2017 Restated £'m
Disclosed as:		
Current	**33.0**	65.7
Non-current	**83.7**	82.5
At 31 December	**116.7**	148.2
Analysed as:		
Environmental	**80.6**	99.9
Onerous contracts	**13.7**	21.8
Warranty costs	**15.7**	18.9
Other	**6.7**	7.6
At 31 December	**116.7**	148.2

* Included within trade and other receivables in respect of amounts recoverable from insurers and other third parties in respect of environmental issues relating to historic sites.

21. Retirement benefit obligations

	2018 £'m	2017 £'m
At 1 January	**308.1**	414.7
Exchange rate adjustments	**7.8**	(14.9)
Service cost	**16.1**	16.6
Past service cost (note 7)	**1.7**	-
Past service credit*	**(5.4)**	(7.1)
Net interest cost (note 9)	**8.0**	11.3
Contributions – Group	**(83.7)**	(50.1)
Remeasurement of retirement benefit obligations	**(46.2)**	(66.6)
Administrative expenses borne directly by schemes	**2.7**	4.2
At 31 December	**209.1**	308.1
Analysis of retirement benefit obligations:		
Pension schemes	**161.5**	258.3
Healthcare schemes	**47.6**	49.8
At 31 December	**209.1**	308.1

* Relates to the Group's decision to freeze two of the US schemes to future accrual for existing members.

21. Retirement benefit obligations (continued)

Key financial assumptions used to calculate scheme liabilities	2018	2017
UK scheme:		
Discount rate	**2.90%**	2.55%
Inflation rate	**3.20%**	3.20%
Salary increases	**2.95%**	4.20%
Current life expectancy: Male aged 65 years	**21.7 to 23.5**	21.6 to 23.1
US schemes:		
Discount rate	**4.15%**	3.55%
Salary increases	**N/A**	4.43%
Current life expectancy: Male aged 65 years	**20.2 to 20.8**	20.2 to 20.8

Group cash contributions paid during the year included deficit reduction payments of £67.6m (2017: £33.5m).

22. Issued share capital

	2018 No. m	2017 No. m
Allotted and fully paid	**776.9**	776.4

23. Contingent liabilities

The Company has given guarantees in respect of credit facilities for certain of its subsidiaries, some property and other leases, and the performance by some current and former subsidiaries of certain contracts. Also, there are similar guarantees given by certain other Group companies. The directors do not believe that the effect of giving these guarantees will have a material adverse effect upon the Group's financial position.

The Company and various of its subsidiaries are, from time to time, parties to legal proceedings and claims which arise in the ordinary course of business. The directors do not anticipate that the outcome of these proceedings, actions and claims, either individually or in aggregate, will have a material adverse effect upon the Group's financial position.

24. Capital commitments

	2018 £'m	2017 £'m
Contracted for but not incurred:		
Intangible assets	**0.6**	2.8
Property, plant and equipment	**14.3**	18.8
At 31 December	**14.9**	21.6

25. Cash inflow from operations

	2018 £'m	2017 Restated £'m
Profit for the year	**179.0**	292.8
Adjustments for:		
Finance income (note 8)	**(1.0)**	(1.4)
Finance costs (note 9)	**41.5**	45.8
Tax	**37.1**	(64.5)
Depreciation (note 15)	**53.6**	53.9
Amortisation (note 14)	**132.2**	130.9
Impairment loss (notes 14 and 15)	**3.6**	57.3
Loss on disposal of property, plant and equipment	**3.0**	0.8
Loss on disposal of software and other intangible assets	**-**	0.3
Gain on disposal of businesses (note 5)	**(30.4)**	(40.3)
Impairment of assets classified as held for sale (note 17)	**10.7**	14.2
Remeasurement of fair value of contingent consideration payable (note 5)	**(3.6)**	-
Financial instruments (note 6)	**10.1**	(60.7)
Share of loss/(profit) after tax of joint venture (note 16)	**1.5**	(0.6)
Dividend income from joint venture (note 16)	**-**	0.5
Change in carrying value of held for sale assets and liabilities up to date of disposal	**(2.0)**	-
Retirement benefit obligation deficit payments (note 21)	**(67.6)**	(33.5)
Share-based payment expense	**13.5**	8.0
Changes in working capital	**(33.0)**	(4.2)
Total	**348.2**	399.3

The Board uses free cash flow to monitor and measure the underlying trading cash performance of the Group. It is reconciled to cash from operating activities below:

	2018 £'m	2017 Restated £'m
Cash inflow from operating activities	**295.3**	337.9
Add back cash outflow from business acquisition and disposal expenses	**3.8**	3.9
Capitalised development costs	**(58.6)**	(62.6)
Capitalised programme participation costs	**(0.8)**	(3.4)
Purchase of intangible assets	**(21.8)**	(18.3)
Purchase of property, plant and equipment	**(52.6)**	(62.0)
Proceeds from disposal of property, plant and equipment	**2.1**	1.9
Free cash inflow	**167.4**	197.4

26. Movements in net debt

	2018 £'m	2017 Restated £'m
At 1 January	**1,060.8**	1,278.8
Cash inflow from operating activities	**(295.3)**	(337.9)
Cash outflow from investing activities	**96.0**	80.1
Dividends paid to Company's shareholders	**124.2**	118.6
Purchase of own shares for employee share schemes	**22.6**	19.0
Net cash generated	**(52.5)**	(120.2)
Debt acquired with business	**-**	0.6
Debt disposed with businesses	**-**	(0.8)
Lease liabilities entered	**4.6**	15.9
Exchange rate adjustments	**65.5**	(105.0)
Other non-cash movements	**(4.3)**	(8.5)
At 31 December	**1,074.1**	1,060.8

	2018 £'m	2017 Restated £'m
Analysed as:		
Bank and other borrowings – current	**10.2**	71.4
Bank and other borrowings – non-current	**1,148.3**	1,005.8
Lease liabilities – current	**16.1**	16.9
Lease liabilities – non-current	**81.4**	85.2
Cash and cash equivalents	**(181.9)**	(118.5)
Total	**1,074.1**	1,060.8

27. Business disposals

On 12 January 2018, the Group disposed of 100% of the equity in Aviation Mobility, LLC ('Aviation Mobility') for a consideration of USD14.0m. Aviation Mobility was previously reported within Meggitt Control Systems.

On 14 November 2017, the Group agreed to the disposal of 100% of the equity of Linear Motion LLC ('Linear Motion') subject to certain regulatory clearances being obtained. The related assets were classified as a disposal group held for sale and were presented separately at 31 December 2017 together with directly associated liabilities. The disposal subsequently completed on 26 March 2018 for a consideration of USD4.2m. Linear Motion was previously reported within the Meggitt Equipment Group.

On 21 April 2018, the Group disposed of 100% of the ordinary shares of Precision Micro Limited ('Precision Micro') for a consideration of £21.9m. The company specialised in production photo etching for the automotive and medical sectors, where synergies with the rest of the Group were limited. Precision Micro was previously reported within the Meggitt Equipment Group.

On 24 December 2018, the Group disposed of a small number of product lines from within one of its sensing systems businesses for a consideration of USD10.0m. These product lines were previously reported within Meggitt Sensing Systems.

The businesses disposed were not a major line of business or geographical area of operation of the Group.

27. Business disposals (continued)

The net assets of the businesses at the date of disposed were as follows:

	Aviation Mobility £'m	Linear Motion £'m	Precision Micro £'m	Sensing product Lines £'m	Total £'m
Goodwill (note 14)	-	-	0.8	-	**0.8**
Other intangible assets (note 14)	-	-	0.1	-	**0.1**
Property, plant and equipment (note 15)	-	-	3.5	-	**3.5**
Inventories	-	-	1.1	0.8	**1.9**
Trade and other receivables – current	0.3	-	3.4	-	**3.7**
Cash and cash equivalents	-	-	0.7	-	**0.7**
Assets classified as held for sale (note 17)	-	10.0	-	-	**10.0**
Trade and other payables – current	-	-	(1.9)	-	**(1.9)**
Liabilities directly association with assets classified as held for sale (note 17)	-	(3.3)	-	-	**(3.3)**
Net assets	**0.3**	**6.7**	**7.7**	**0.8**	**15.5**
Currency translation gain transferred from equity (note 28)					**(3.0)**
Business disposal expenses					**2.5**
Deferred consideration receivable					**(7.9)**
Difference between fair value of consideration and amounts received					**1.8**
Gain on disposal (note 5)					**27.9**
Total consideration received in cash					**36.8**

	£'m
Cash inflow arising on disposal:	
Total consideration received in cash	**36.8**
Less: cash and cash equivalents disposed of	**(0.7)**
Less: cash paid in respect of businesses disposed of in prior periods	**(0.4)**
Businesses disposed	**35.7**
Less: business disposal expenses paid	**(3.8)**
Total cash inflow	**31.9**

28. Components of other comprehensive income

	2018 £'m	2017 Restated £'m
Arising in the year	**93.7**	(138.9)
Transferred to the income statement (note 27)	**(3.0)**	(8.6)
Currency translation movements – gain/(loss)	**90.7**	(147.5)
Movement in fair value of financial liabilities arising from changes in credit risk	**0.8**	(2.1)
Cash flow hedge movements: transferred to the income statement	**(0.3)**	(0.2)
Other comprehensive income before tax	**91.2**	(149.8)
Tax effect	**2.5**	(2.4)
Items that may be reclassified to the income statement in subsequent periods	**93.7**	(152.2)

29. Restatement of prior period comparatives

This note explains the impact on the consolidated financial statements of the adoption of IFRS 15 'Revenue from contracts with customers' and IFRS 9 'Financial instruments' which became effective for the financial year beginning 1 January 2018 and of IFRS 16 'Leases' which the Group has early adopted. As a result of changes required to the Group's accounting policies arising from adoption of these standards, prior period comparatives have been restated.

In addition, in 2018 the Group finalised the fair values of assets and liabilities of Elite Aerospace, Inc. ('Elite') which was acquired on 28 March 2017. IFRS 3 requires fair value adjustments to be recorded with effect from the date of acquisition and consequently has resulted in a restatement of previously reported results.

The following tables show the impact of these changes on each line item affected. Line items which are not impacted by the restatement have been aggregated within the relevant sub-totals. The impact of each new standard is also explained in more detail within the footnotes that follow the tables.

Consolidated income statement (extract)

	2017 As previously reported £m	IFRS 15 £m	IFRS 16 £m	IFRS 9 £m	Elite £'m	2017 Restated £m
Revenue	2,027.3	(32.9)	-	-	-	1,994.4
Cost of sales	(1,234.0)	(1.2)	-	-	-	(1,235.2)
Gross profit	793.3	(34.1)	-	-	-	759.2
Net operating costs	(489.1)	(0.2)	0.7	2.1	-	(486.5)
Operating profit	304.2	(34.3)	0.7	2.1	-	272.7
Net finance costs	(41.8)	-	(2.6)	-	-	(44.4)
Profit before tax	262.4	(34.3)	(1.9)	2.1	-	228.3
Tax credit/(charge)	87.6	(21.2)	(0.2)	(0.4)	(1.3)	64.5
Profit for the year	350.0	(55.5)	(2.1)	1.7	(1.3)	292.8
Earnings per share (EPS):						
Basic (pence)	45.2	(7.2)	(0.2)	0.2	(0.2)	37.8
Diluted (pence)	44.3	(7.0)	(0.2)	0.2	(0.2)	37.1
Non-GAAP measures:						
Underlying operating profit	388.4	(35.8)	0.7	-	-	353.3
Underlying profit before tax	357.9	(35.8)	(1.9)	-	-	320.2
Underlying basic EPS (pence)	35.3	(3.2)	(0.1)	-	-	32.0
Underlying diluted EPS (pence)	34.6	(3.2)	(0.1)	-	-	31.3

Consolidated statement of comprehensive income (extract)

	2017 As previously reported £m	IFRS 15 £m	IFRS 16 £m	IFRS 9 £m	Elite £m	2017 Restated £m
Profit for the year	350.0	(55.5)	(2.1)	1.7	(1.3)	292.8
Items that may be reclassified to the income statement in subsequent periods:						
Currency translation movements	(161.6)	13.7	0.4	-	-	(147.5)
Movements in fair value of financial liabilities arising from changes in credit risk	-	-	-	(2.1)	-	(2.1)
Cash flow hedge movements	(0.2)	-	-	-	-	(0.2)
Tax effect	(2.8)	-	-	0.4	-	(2.4)
	(164.6)	13.7	0.4	(1.7)	-	(152.2)
Items that will not be reclassified to the income statement in subsequent periods	39.5	-	-	-	-	39.5
Other comprehensive (expense)/income	(125.1)	13.7	0.4	(1.7)	-	(112.7)
Total comprehensive income for the year	224.9	(41.8)	(1.7)	-	(1.3)	180.1

Consolidated balance sheet (extract)

	1 January 2017 As previously reported £m	IFRS 15 £m	IFRS 16 £m	IFRS 9 £m	Elite £m	1 January 2017 Restated £m
Net assets	2,456.4	(196.5)	(3.6)	-	-	2,256.3
Equity						
Hedging and translation reserves	551.5	-	-	0.8	-	552.3
Retained earnings	630.6	(196.5)	(3.6)	(0.8)	-	429.7
Other equity	1,274.3	-	-	-	-	1,274.3
Total equity	2,456.4	(196.5)	(3.6)	-	-	2,256.3

Consolidated balance sheet (extract)

	31 December 2017 As previously reported	IFRS 15	IFRS 16	IFRS 9	Elite	31 December 2017 Restated
	£m	£m	£m	£m	£m	£m
Non-current assets						
Goodwill	1,947.0	-	-	-	(2.1)	1,944.9
Development costs	482.3	13.5	-	-	-	495.8
Programme participation costs	332.1	(315.0)	-	-	-	17.1
Property, plant and equipment	322.9	-	83.3	-	-	406.2
Trade and other receivables	39.2	(0.5)	-	-	-	38.7
Contract assets	-	49.7	-	-	-	49.7
Deferred tax assets	11.5	14.7	0.1	-	-	26.3
Other non-current assets	714.2	-	-	-	-	714.2
	3,849.2	(237.6)	83.4	-	(2.1)	3,692.9
Current assets						
Inventories	404.1	(10.7)	-	-	-	393.4
Trade and other receivables	437.1	(47.4)	-	-	-	389.7
Contract assets	-	39.7	-	-	-	39.7
Other current assets	136.1	-	-	-	-	136.1
	977.3	(18.4)	-	-	-	958.9
Total assets	4,826.5	(256.0)	83.4	-	(2.1)	4,651.8
Current liabilities						
Trade and other payables	(445.5)	37.6	5.8	-	-	(402.1)
Contract liabilities	-	(52.5)	-	-	-	(52.5)
Lease liabilities	(0.1)	-	(16.8)	-	-	(16.9)
Provisions	(64.2)	-	-	-	(1.5)	(65.7)
Other current liabilities	(136.1)	-	-	-	-	(136.1)
	(645.9)	(14.9)	(11.0)	-	(1.5)	(673.3)
Net current assets	331.4	(33.3)	(11.0)	-	(1.5)	285.6
Non-current liabilities						
Contract liabilities	-	(23.1)	-	-	-	(23.1)
Deferred tax liabilities	(201.7)	55.7	1.5	-	2.3	(142.2)
Lease liabilities	(6.0)	-	(79.2)	-	-	(85.2)
Other non-current liabilities	(1,416.5)	-	-	-	-	(1,416.5)
	(1,624.2)	32.6	(77.7)	-	2.3	(1,667.0)
Total liabilities	(2,270.1)	17.7	(88.7)	-	0.8	(2,340.3)
Net assets	2,556.4	(238.3)	(5.3)	-	(1.3)	2,311.5
Equity						
Hedging and translation reserves	386.9	13.7	0.4	(0.9)	-	400.1
Retained earnings	892.8	(252.0)	(5.7)	0.9	(1.3)	634.7
Other equity	1,276.7	-	-	-	-	1,276.7
Total equity	2,556.4	(238.3)	(5.3)	-	(1.3)	2,311.5

Impact of IFRS 15

In accordance with the transition provisions in IFRS 15, the standard has been adopted retrospectively with restatements made to prior year comparatives. A summary of the principal areas of IFRS 15 that have impacted the Group are shown in the tables below and footnotes that follow.

	Programme participation costs (a) £m	Programme participation costs (b) £m	Customer funding on development programmes (c) £m	Other (d) £m	Reclass (e) £m	2017 Impact £m
Revenue	-	(2.5)	-	(30.4)	-	(32.9)
Cost of sales	(21.4)	2.5	-	17.7	-	(1.2)
Gross loss	(21.4)	-	-	(12.7)	-	(34.1)
Net operating costs	-	-	-	(0.2)	-	(0.2)
Operating loss	(21.4)	-	-	(12.9)	-	(34.3)
Tax charge						(21.2)
Loss for the year						(55.5)

	Programme participation costs (a) £m	Programme participation costs (b) £m	Customer funding on development programmes (c) £m	Other (d) £m	Reclass (e) £m	1 January 2017 Impact £m
Net assets	(188.3)	-	-	(8.2)	-	(196.5)

	Programme participation costs (a) £m	Programme participation costs (b) £m	Customer funding on development programmes (c) £m	Other (d) £m	Reclass (e) £m	31 December 2017 Impact £m
Development costs	-	-	13.5	-	-	13.5
Programme participation costs	(285.4)	(29.6)	-	-	-	(315.0)
Trade and other receivables – non-current	-	-	-	8.9	(9.4)	(0.5)
Contract assets – non-current	-	26.8	-	(6.5)	29.4	49.7
Deferred tax assets	14.7	-	-	-	-	14.7
Inventories	-	-	-	4.5	(15.2)	(10.7)
Trade and other receivables – current	-	-	-	(16.6)	(30.8)	(47.4)
Contract assets – current	-	2.8	-	7.8	29.1	39.7
Trade and other payables – current	-	-	-	(17.5)	55.1	37.6
Contract liabilities – current	-	-	(0.3)	6.0	(58.2)	(52.5)
Contract liabilities – non-current	-	-	(13.2)	(9.9)	-	(23.1)
Deferred tax liabilities	50.8	-	-	4.9	-	55.7
Net assets	(219.9)	-	-	(18.4)	-	(238.3)

Impact of IFRS 15 continued

a) Programme participation costs – Free of charge/deeply discounted manufactured parts
Programme participation costs consist of incentives given to OEMs in connection with their selection of the Group's products for installation onto new aircraft where the Group has obtained principal supplier status. Where these incentives comprise the supply of initial manufactured parts on a free of charge or deeply discounted basis, amounts are recognised within costs of sales as incurred. Under the Group's previous accounting policy, amounts were recognised as an intangible asset and amortised over their useful lives to cost of sales over periods typically up to 15 years.

b) Programme participation costs – Cash payments
Where programme participation costs are in the form of cash payments, the treatment depends on the contractual relationship between the Group and the third party to whom the payment is made. Where the payment is made to a third party under a revenue contract (as defined by IFRS 15), or the award of future IFRS 15 revenue contracts on the programme from the same party is highly probable, payments are recognised as a contract asset and amortised, as a deduction from revenue, over the periods expected to benefit from those contracts. This situation most frequently arises where the payment is made to the same party to whom original equipment and/or aftermarket parts are sold. Other payments are recognised as an intangible asset and amortised as a charge to cost of sales. Under the Group's previous accounting policy, all programme participation cash payments were recognised as intangible assets and amortised as a charge to cost of sales.

c) Customer funding towards development costs
Where a customer contributes to the Group's development costs and those costs meet the criteria under IAS 38 to be recognised as an intangible asset, the funding is recognised as a contract liability and is amortised, as an increase to revenue, over the periods expected to benefit from future revenue from the customer over the life of the programme. Under the Group's previous accounting policy, customer funding was netted off amounts recognised as development costs and accordingly reduced the subsequent amortisation charged to net operating costs.

d) Other
A number of other revenue timing differences, none of which is individually significant, arose from the adoption of IFRS 15:

i. Revenue recognised over time
The Group recognises revenue under power by the hour and cost per brake landing type contracts over time using costs incurred as the measure of contract completion. Under the Group's previous accounting policy, revenue was recognised based on the number of aircraft flying hours or the number of aircraft landings.

Where the Group builds a product with no alternative use and has an enforceable right to payment from the customer for costs incurred, plus a reasonable margin, throughout the life of the contract then revenue is recognised over time using costs incurred as the measure of contract completion. Under the Group's previous accounting policy, the majority of contracts that met this requirement were accounted for in a similar way using contract accounting, although the method of measuring progress has, in some cases, changed. For instance, funded research and development contracts were previously recognised as revenue over time using customer agreed milestones achieved as a measure of contract completion. Additionally a small number of contracts for which contract accounting was previously applied no longer meet the IFRS 15 criteria to be recognised over time, particularly certain contracts in the Heatric business, and are now recognised at a point in time, usually when the goods are delivered to the customer. Conversely, certain defence contracts for which revenue was previously recognised as goods were delivered to the customer meet the IFRS 15 over time criteria and accordingly revenue is recognised as costs are incurred.

ii. Revenue recognised at a point in time
The timing of revenue on the substantial majority of the Group's contracts, previously recognised at a point in time, has not been significantly affected by IFRS 15, with revenue continuing to be recognised as goods are delivered to the customer and at the price agreed with the customer for those goods. A minority of contracts required changes to the timing of revenue recognition to reflect IFRS 15 guidance on areas such as whether multiple deliveries and services provided to a customer should be accounted for individually or as a single performance obligation, variable consideration and material rights.

Impact of IFRS 15 (continued)

e) Reclassifications

Certain balances representing amounts recoverable on contracts, previously included within trade and other receivables and deferred income and advance payments received from customers, previously included within trade and other payables, have been reclassified to contract assets and contract liabilities as appropriate.

Impact of IFRS 16

The Group has early adopted IFRS 16 using the full retrospective approach on transition. Under IFRS 16, except for certain short term leases and leases of low-value assets, a liability is recognised at lease inception equal to the present value of payments due under the lease. The lease liability is subsequently measured using the effective interest rate method, with interest charged to finance costs. At lease inception, a right-of-use asset is recognised equal to the lease liability, adjusted to reflect any lease incentives paid to or received from the lessor, asset restoration and other direct costs. The right-of-use asset is depreciated over the shorter of the life of the asset or the lease term to either costs of sales or net operating costs as appropriate.

Under the Group's previous accounting policy, the majority of the Group's leases were accounted for as operating leases with rentals charged to cost of sales or net operating costs on a straight-line basis over the lease term, with no element of the rentals charged to finance costs. No right-of-use asset or lease liability was recognised on the Group's balance sheet for these leases.

Impact of IFRS 9

Under IFRS 9, where financial liabilities are subsequently measured at fair value, any element of the fair value gain or loss arising that is attributable to changes in credit risk is recognised in other comprehensive income. Under the Group's previous accounting policy, such amounts were recognised within net operating costs. Overall, IFRS 9 does not have a significant impact since the majority of the Group's financial assets continue to be held at amortised cost. The Group is also not exposed to a significant concentration of credit risk, and accordingly the impact of applying an expected credit loss model to its financial assets was not significant.

Principal risks and uncertainties

Strategic – Business model

Description
Failure to respond to fundamental changes in our aerospace business model, primarily the evolving aftermarket. This includes more durable parts requiring less frequent replacement, a growing supply of surplus parts, OE customers seeking greater control of their aftermarket supply chain and accelerated pace of new aircraft deliveries leading to the earlier retirement of older aircraft.

Impact
Decreased revenue and profit.

How we manage it
- Alignment of Group, divisional and functional strategy processes.
- Dedicated full-service aftermarket organisation.
- Long-term customer agreements as part of maintaining and monitoring pricing strategy.
- Investment in research and development to maintain and enhance Meggitt's intellectual property.

Strategic – Industry changes

Description
Significant variation in demand for products should civil aerospace, defence and energy business downcycles coincide; a serious political, economic or terrorist event that adversely affects the aerospace industry occur or consolidation that materially changes the competitive landscape.

Impact
Volatility in underlying profitability.

How we manage it
- Monitoring external economic and commercial environment and long-lead indicators whilst maintaining focus on balanced portfolio.
- EASA (European Aviation Safety Agency) has acknowledged our application for "third country" certification that mirrors the existing EASA certifications held by UK Meggitt sites. We have now started to be issued with the third country certificates which allow continued trading with our European customers.
- Maintaining sufficient headroom in committed credit facilities and against covenants in those facilities whilst implementing appropriate cost-base contingency plans.

Strategic – Technology strategy

Description
Failure to develop and implement meaningful technology strategies to meet customers' needs.

Impact
Restriction of ability to compete on new programmes with consequent decrease in revenue and profit.

How we manage it
- Management of technology development plans that align technology readiness, market needs and financial returns using a gated process.
- Recruiting and training first-class engineers and scientists with appropriate technology skills.
- Ring-fenced budgets focused on longer-term technology developments.
- Leveraging our R&D budget through partnerships including government, academia and other companies.

Operational – Quality escape/equipment failure

Description
Defective product leading to in-service failure, accidents, the grounding of aircraft or prolonged production shutdowns for the Group and its customers.

Impact
Decreased revenue and profit, damage to operational performance and reputation.

How we manage it
- System safety analysis, verification and validation policy and processes, combined with quality and customer audits and industry certifications.
- Meggitt Production System.
- Supplier quality assurance process.

Operational – Business interruption

Description
A catastrophic event such as an earthquake (the Group has a significant operational presence in Southern California) or fire could lead to infrastructure and property damage which prevents the Group from fulfilling its contractual obligations.

Impact
Decreased revenue and profit, damage to operational performance and reputation.

How we manage it
- Group-wide business continuity and crisis management plans, subject to regular testing.
- Comprehensive insurance programme, renewed annually and subject to property risk assessment visits.

Operational – Project/programme management

Description
Failure to meet new product development programme milestones and certification requirements and successfully transition new products into manufacturing as production rates increase. This also covers lower than expected production volumes, including programme cancellations.

Impact
Failure to deliver financial returns against investment and/or significant financial penalties leading to decreased profit and damage to reputation.

How we manage it
- Rigorous commercial and technological reviews of bids and contractual terms before entering into programmes.
- Continuous review of programme performance through the Programme Lifecycle Management (PLM) process including:
  - regular monitoring of the end market performance of key OE programmes;
  - internal review process, to stress-test readiness to proceed at each stage of the key programmes; and
  - regular monitoring of the financial health of customers.

Operational – Customer satisfaction

Description
Failure to meet customers' cost, quality and delivery standards or qualify as preferred suppliers.

Impact
Failure to win future programmes, decreased revenue and profit.

How we manage it
- Creation of a customer facing organisational structure including a dedicated aftermarket division.
- Regular monitoring of customer scorecards and ensuring responsiveness to issues via Voice of the Customer process.
- Functional excellence in operations, project management and engineering.
- Increased utilisation of low-cost manufacturing base.

Operational – Acquisition integration/performance

Description
Failure to effectively integrate acquisitions and failure to realise financial returns from the advanced composites acquisitions.

Impact
Decreased revenue and profit.

How we manage it
- Internal pre-acquisition due diligence supplemented by external experts.
- Increase in local capabilities to manage production ramp-up and delivery of the financial model, including cost synergies, under Group PMO oversight.
- Standard Meggitt processes implemented as part of a proven post-merger process led by incumbent divisional management, supported by experienced dedicated operational teams with a senior oversight committee.

Operational – Cyber breach

Description
A breach of IT security due to cyber crime/terrorism resulting in intellectual property or other sensitive information being lost, made inaccessible, corrupted or accessed by unauthorised users. This also includes the loss of critical systems such as SAP due to badly-executed implementation or change of control; poor maintenance, business continuity or back-up procedures and the failure of third parties to meet service level agreements.

Impact
Decreased revenue and profit, damage to operational performance and reputation.

How we manage it
- IT security infrastructure, policies and procedures.
- Group-wide intellectual property protection programme.
- Management of third party service providers and risks, including resilience and disaster recovery processes.
- Implementation of rolling programme of system upgrades (including SAP implementation) to replace legacy systems.

Operational – Supply chain

Description
Failure or inability of critical suppliers to supply unique products, capabilities or services preventing the Group from satisfying customers or meeting contractual requirements.

Impact
Decreased revenue and profit, damage to operational performance and reputation.

How we manage it
- Supplier excellence framework combined with integrated commercial and procurement approach to contractual terms and conditions including development of long-term agreements.
- Local sourcing strategy to improve operational efficiency and minimise potential impacts and disruption from cross-border tariffs.
- Maintenance of buffer inventory for critical and sole-source suppliers.
- Implementation of measures to mitigate counterfeit and fraudulent parts at high-risk facilities.

Operational – Group change management

Description
Failure to successfully, simultaneously, deliver the significant change programmes currently in process and planned, including site consolidation activity such as Ansty Park.

Impact
Decreased revenue and profit, increased costs, damage to operational performance and reputation.

How we manage it
- Creation of dedicated site consolidation and property management teams for Ansty Park.
- Regular monitoring by Executive Leadership Team through operational and project reviews.
- MPS implementation at new/expanded sites.

Operational – People

Description
Failure to attract, retain or mobilise people due to factors including industrial action, workforce demographics, lack of training, availability of talent and inadequate compensation.

Impact
Decreased revenue and profit, damage to operational performance.

How we manage it
- Roll-out of High Performance Culture.
- Employee engagement programmes.
- Graduate and apprentice programmes in partnership with schools and universities.
- Regular monitoring by Executive Leadership Team.

Corporate – Legal & compliance

Description
Significant breach of increasingly complex trade compliance, bribery & corruption, US Government contracting, ethics, intellectual property, data protection, competition/antitrust laws and facilitation of tax evasion.

Impact
Damage to reputation, loss of supplier accreditations, suspension of activity, fines from civil and criminal proceedings.

How we manage it
- Continuing investment in compliance programmes, including Board approved policies and roll out of training and IT solutions.
- Regular monitoring by Ethics and Trade Compliance Committee, supported by ongoing trade compliance programme including third party audits.
- Comprehensive ethics programme including training, anti-corruption policy and Ethics line.
- Third party audits including HS&E and the Criminal Finance Act.
- MPS implementation to enhance safety measures, validated by third party audits.

Financial – Taxation

Description
Tax legislation is complex and compliance can be subject to interpretation. Events such as the OECD BEPS programme, the US tax and tariff changes and the impact of Brexit create uncertainty which could negate the effectiveness of the Group's current, well established, tax-efficient international structures, including those used to finance acquisitions.

Impact
Higher effective tax rates resulting in decreased profit.

How we manage it
- Monitoring international tax developments to assess implications of future legislation.
- Maintenance of a low-risk rating with UK HMRC and other tax authorities through open dialogue and, where possible, pre-agreement of arrangements to confirm compliance with legislation.
- Assessment of options to mitigate impact of legislative changes on the Group's effective tax rate.
- Use of multiple expert third party tax advisors.

DIRECTORS' RESPONSIBILITIES STATEMENT

Each of the persons who is a director at the date of the approval of this report confirm that, to the best of their knowledge:

- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Strategic report and the Directors' report include 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; and
- the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position, performance, business model and strategy.

By order of the Board:

A Wood
Director
25 February 2019

L Burdett
Director
25 February 2019

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