

**Strong execution on strategy with the Group well placed for the recovery**

Meggitt PLC ("Meggitt" or "the Group"), a leading international engineering company specialising in high performance components and sub-systems for the aerospace, defence and selected energy markets, today announces audited results for the twelve months ended 31 December 2020.

**Tony Wood, Chief Executive, commented:**

*"Our focus throughout 2020 and as we move into 2021, continues to be ensuring the safety and well-being of our people, protecting our sites, serving our customers and communities and executing our strategy. I want to thank all of my colleagues for their hard work and dedication in helping us navigate our way through the year.*

*Faced with a reduction in activity and demand in one of our core markets, we acted fast, executed well operationally and took decisive action while positioning the Group for the recovery in civil aerospace. While our full year performance has clearly been impacted by the ongoing effects of COVID-19, it also reflects the resilience and diverse nature of the Group, including the mitigating impact of our defence and energy businesses.*

*The roll-out of vaccines, coupled with significant pent-up demand to travel, provides a supportive backdrop for the recovery in civil aerospace in 2021, although this positive development is likely to take time to feed through into growth in global flight activity and the aftermarket. Based on the significant progress we've made over the last four years to transform the Group, the effective actions we've taken in 2020, diverse end market exposure and leading market positions, we are well placed to benefit from the recovery and to continue to deliver long-term profitable growth."*

**Operational and strategic highlights**

- Introduced measures to ensure the well-being of our people and safe operations at all our global sites
- Rapid and decisive action taken to reduce cost, protect cash and resize the Group
- Continued progress on key strategic initiatives:
  - Completed the streamlining of our portfolio with the sale of our Training Systems business
  - Addition of 14 SMARTSupport® contracts, securing further market share in the aftermarket
  - Further reduction in global footprint, now 34% below 2016 levels
  - Investment in operational capability with the opening and fit out of our new campus in Ansty Park, UK
  - Accelerated our existing sustainability strategy under our People, Planet and Technology framework

**Financial summary**

- Performance of the Group reflects the impact of COVID-19 on the civil aerospace sector
- Group revenue of £1,684m down 22% on an organic basis, with a robust performance in defence, where organic revenue grew 4%
- Underlying operating profit 53% lower at £191m (FY 2019: £403m)
- Statutory operating loss of £297m (FY 2019: profit of £325m) as a result of the non-cash impairment of intangible assets and other asset write downs
- Successful delivery of in-year cash savings of £450m
- Positive free cash flow of £32m (FY 2019: £268m) and reduction of £138m in net debt to £773m (FY 2019: £911m)
- Ratios of net debt:EBITDA of 2.2x and interest cover of 9.8x at 31 December, well within covenant limits
- Robust liquidity position with headroom of £908m on committed facilities of £1,537m at 31 December
- Extended maturity of our debt with a forward start on our RCF to September 2022; and raised \$300m in USPP market in November 2020
- In light of ongoing challenging and uncertain market conditions, the Board has recommended not to pay a final dividend for 2020

**Outlook for 2021**

- While the rollout of vaccines is expected to ease lockdowns and drive a gradual increase in air traffic activity, we anticipate the trends seen in civil aerospace during the second half of 2020 are likely to continue in the first half of 2021, with recovery weighted more towards the second half of the year. Conditions in our defence and energy end markets are expected to remain robust in 2021. Assuming no further disruption to normal operations during the year as a result of additional lockdowns, in 2021 we expect the Group to generate:
  - Revenue broadly in line with 2020;
  - An increase in underlying operating profit versus 2020; and
  - Positive free cash flow.

## Group full year performance

|                               | 2020<br>£'m | 2019<br>£'m | Change     |                        |
|-------------------------------|-------------|-------------|------------|------------------------|
|                               |             |             | Reported % | Organic <sup>1</sup> % |
| Orders                        | 1,547.1     | 2,468.4     | (37)       | (38)                   |
| Revenue                       | 1,684.1     | 2,276.2     | (26)       | (22)                   |
| Underlying <sup>2</sup>       |             |             |            |                        |
| EBITDA <sup>3</sup>           | 296.9       | 507.3       | (41)       | (40)                   |
| Operating profit              | 190.5       | 402.8       | (53)       | (50)                   |
| Profit before tax             | 159.5       | 370.3       | (57)       | (55)                   |
| Earnings per share (p)        | 16.5        | 37.3        | (56)       |                        |
| Statutory                     |             |             |            |                        |
| Operating (loss)/profit       | (297.3)     | 325.3       | (191)      |                        |
| (Loss)/profit before tax      | (334.0)     | 286.7       | (217)      |                        |
| (Loss)/earnings per share (p) | (40.4)      | 28.8        | (240)      |                        |
| Free cash flow <sup>4</sup>   | 31.9        | 267.8       | (88)       |                        |
| Net cash flow <sup>5</sup>    | 136.0       | 205.7       | (34)       |                        |
| Net debt                      | 773.0       | 911.2       | (15)       |                        |
| Dividend (p)                  | -           | 5.55        |            |                        |

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### Analyst presentation

There will be a live webcast of the 2020 Full Year results at 9.30am GMT today, available on the Meggitt website <http://www.meggitt.com/investors/>. Copies of the presentation will be available.

<https://www.investis-live.com/meggitt/6021220249aa2a0e00daf86a/epad>

A live dial-in is available. Please use the below details to join:

UK: 0800 640 6441  
UK Local: 020 3936 2999  
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### Cautionary Statement

This Results Announcement contains forward looking statements with respect to the financial condition, results of operations and businesses of Meggitt PLC and its strategy, plans and objectives. These statements are made in good faith based on the information available at the time this announcement was approved. It is believed that the expectations reflected in these statements are reasonable but they may be affected by a number of risks and uncertainties that are inherent in any forward-looking statement and which could cause actual results to differ materially from those currently anticipated. Meggitt does not intend to update these forward-looking statements. Nothing in this document should be regarded as a profit forecast. This report is intended solely to provide information to shareholders and neither Meggitt PLC nor its directors accept liability to any other person, save as would arise under English law.

<sup>1</sup> Organic numbers exclude the impact of acquisitions, disposals and foreign exchange.

<sup>2</sup> Underlying profit and EPS are used by the Board to measure the trading performance of the Group as set out in notes 6 and 11.

<sup>3</sup> Underlying EBITDA represents underlying operating profit adjusted to add back depreciation, amortisation and impairment losses.

<sup>4</sup> Free cash flow is used by the Board to measure the underlying trading cash performance of the Group as set out in note 26.

<sup>5</sup> Net cash flow represents the movement in net debt in the year, adjusted to exclude new lease liabilities entered, exchange differences and other non-cash movements.

## MARKET CONTEXT AND CONDITIONS

### Civil Aerospace

The outbreak of COVID-19 and subsequent lockdowns across the world caused a significant and unprecedented reduction in commercial air traffic in 2020, with global air traffic, as measured by RPKs and ASKs down 65.9% and 56.5% respectively for the full year 2020, compared with 2019 levels.

While positive signs started to emerge at the end of the second quarter with airlines gradually increasing capacity and future flight schedules, particularly in domestic markets, the level of air traffic and customer demand remained highly sensitive to subsequent spikes in COVID-19 infection rates, the imposition of new lockdowns and other measures such as post-flight quarantining. Accordingly, the recovery in global passenger numbers plateaued in the fourth quarter with global RPKs and ASKs ending the year for the month of December down 69.7% and 56.7% respectively, showing only a slight improvement from September's figures down 72.0% and 60.8%.

While all regions have been adversely affected, there have been variations in the extent of traffic reductions as follows: Asia Pacific down 62%; Europe down 70%; and North America down 65%. There has also been a difference between domestic and international air travel, reflecting the closure of international borders at certain times during the year, with domestic traffic down 49% in 2020 compared with international traffic down 76%. In some domestic markets, notably China and Russia, traffic levels recovered in 2020 to be in line with or slightly above 2019 levels.

Within civil aerospace, the extent to which different platform categories have been affected has also varied, with global business jet utilisation down 21% in the year compared with down 48% for the wider global commercial fleet (which comprises large and regional jets). In the month of December 2020, business jet utilisation had recovered to 95% of the levels seen in December 2019 reflecting its attraction to air travellers as an alternative to commercial flights.

As a result of the severe slowdown across civil aerospace, demand from airlines and operators for new build aircraft significantly reduced in FY 2020, with Airbus and Boeing deliveries down 34% and 59% respectively. Deliveries of regional and business jets in the year were down 46% and 21% respectively. In response to the lower demand for aircraft, airframe and engine OEMs significantly reduced their production rates during the year, a key driver of the Group's OE revenue.

In the first two months of 2021, high infection rates across many countries, border closures and lockdowns have held back the recovery and resulted in the continuation of low overall levels of air traffic activity and passenger numbers. However, against this backdrop, the development and rollout of vaccines globally over the last few months has been encouraging and underpins a positive outlook for the continued recovery in civil aerospace, with the expectation that lockdown restrictions will be eased and passenger confidence returns particularly in the second half of 2021. With overall business jet activity having recovered strongly, ending 2020 close to prior year levels, we expect regional jets and narrow bodies to recover next as short haul and domestic routes are restored, with wide body levels coming back last reflecting a change in consumer attitudes towards long haul, including business travel.

Looking further ahead, most industry commentators now expect air traffic to return to 2019 levels by around 2023/2024 (IATA forecasting 2024) and new aircraft production rates to recover to pre-COVID-19 levels in 2024 /2025. Beyond the recovery period, we firmly believe that the drivers supporting air traffic growth over the long term remain in place with IATA forecasting a growth rate in global passenger journeys of 3.7% per annum over the next 20 years.

### Defence

While the defence sector has not been immune from the effects of COVID-19, spending in the US (which represents over 70% of our annual defence revenue) and overall defence activity levels remained robust in 2020, a trend reflected in our own defence business. For fiscal year 2020, defence spending in the US was up 6%, with spending in RDT&E and procurement both up 12%, with good outlays for major fixed wing and rotary platforms including F-35, KC-46A, F-15EX and AH-64. In January 2021, the US DoD budget of \$696bn for fiscal year 2021 was approved, broadly in line with the level of outlays in 2020, providing a supportive backdrop over the short to medium-term.

### Energy

In energy, both supply and demand side factors led to volatility in the oil price moving from \$57 per barrel in January to below \$20 per barrel in April. While the oil price subsequently increased off its lows, trading in a range of \$37-\$49 per barrel in the second half, this dampened overall capital expenditure levels and delayed certain projects across the oil sector during the year, while LNG and renewables project capex remained robust.

## FAST AND EFFECTIVE ACTION IN RESPONSE TO THE CRISIS

Leveraging our experience of navigating previous downturns in civil aerospace and through close communication with our customers and supply chain, the Group moved quickly to implement a revised demand scenario for planning purposes and adjusted production levels early in the second quarter. During 2020, we took a series of decisive actions in areas within our control in response to the crisis, focused on reducing costs, preserving cash and resizing the business:

- Safeguarding our people – our number one priority and the focus of our COVID-19 Crisis Management Team has been, and continues to be, to ensure the safety of our employees, where we have followed local government and health authority guidelines as they relate to safe working practices at our sites. These measures have included the introduction of social distancing, provision of personal protective equipment, variations in working patterns including split shifts, enhanced cleaning regimes and providing the necessary tools and support for those employees able to work from home.
- Supporting the community – in response to COVID-19, our employees and sites have supported their local communities in the regions where we operate around the world. In the UK, we were part of the Ventilator UK Challenge with responsibility for programme management of the consortium's production of an additional 13,000 ventilators to help patients hospitalised with COVID-19 fight the disease. We have also had numerous examples of employees at our sites leveraging their capabilities to produce a wide range of personal protective equipment for key workers and employees.
- Business continuity – the majority of our manufacturing facilities remained open during the year to support our customers in the critical markets that we serve in defence, energy and in aerospace for repatriation of citizens and transport of food, freight and medical supplies. As part of the US national response to COVID-19, we were granted \$15m in funding under the CARES Act from the US Department of Defense to sustain critical industrial base capability for military grade fuel bladders at our Rockmart, US facility.

Throughout the year, the majority of our employees continued to work at our sites while adhering to enhanced procedures relating to personal protection and cleaning, with the remainder either working from home or on furlough. We have remained agile and reacted to changes in lockdown restrictions on a regional basis allowing more office-based employees to return to work safely where possible. We have also supported our suppliers through supplier financing programmes and increased their awareness of local government support schemes during the year.

- Reducing costs, protecting cash and resizing the Group – in April we announced a series of actions to help the Group navigate the crisis and enable us to deliver substantial cash savings in the year. These actions were based on our scenario planning exercises incorporating the most likely impact on the Group's revenue and cash flow in 2020 and expectations on the timing of the recovery:
  1. *Reducing costs* – cancellation of all pay rises, pay reductions for the Board of Directors and Executive Committee and material cuts in discretionary spend including travel;
  2. *Protecting cash* – in addition to the cost measures, we have also preserved cash through targeted reductions and deferral of certain cash expenditure including: capital expenditure; absolute reduction in inventory levels; and the cancellation of the final dividend for 2019 and interim dividend for 2020; and
  3. *Resizing the Group* – having taken action to reduce variable costs, including accessing furlough schemes and reducing temporary labour, we took the difficult decision to reduce the size of our global workforce to ensure that our internal capacity across our civil aerospace business reflects the reduction in demand. As at the end of December 2020, our total global headcount was 26% lower (including the sale of our Training Systems business) than the end of 2019.

As a result of the hard work and focus of our global teams to deliver our in-year cash savings, the Group generated £31.9m of free cash flow which was slightly better than our expectations at the time of our half year results. The free cash inflow, combined with proceeds from the sale of Training Systems, meant the Group ended the year with net debt of £773.0m, £138.2m lower than 2019, testament to the Group's focus on tight management of the balance sheet during the most challenging of times.

## FULL YEAR RESULTS FOR 2020

### Group Orders and Revenue

Our full year results reflect the effects of COVID-19 and the unprecedented reduction in civil aerospace activity with key financial metrics, both on a statutory and underlying basis, declining in the period.

In our half year results, we reported that Group revenue for the six months ended 30 June 2020 was 14% lower than the comparative period. This reflected the marked deterioration in trading in our civil aerospace business in the second quarter as a result of the significant reduction in commercial air traffic and grounding of a large proportion of the global fleet, which more than offset a strong performance from our defence business.

While the level of global civil aerospace flight activity recovered in the second half, market conditions remained challenging with the recovery impacted by second waves of COVID-19 and further lockdowns in the fourth quarter. In the second half, Group civil aerospace organic revenue was 53% lower than the comparative period, with OE down 51% (large jets -55%, regional -59% and business jets -37%) and aftermarket down 54% (large jets -52%, regional -63% and business jets -49%). After a strong first half with organic growth of 8% (excluding Training Systems), defence revenue was flat in the second half on an organic basis. Energy revenue was down 11% organically in the second half, partly reflecting the timing of projects and phasing of revenue.

For the full year, Group orders were 38% lower on an organic basis with book to bill of 0.88x. Our order book in defence remains robust with an organic book to bill of 1.05x. Group organic revenue was down 22% with lower revenue in civil aerospace and energy more than offsetting a good performance in defence where revenue grew 4%. In civil aerospace, revenue was 41% lower, with sales from civil OE and civil AM down 40% and 41% respectively. Energy revenue was 8% lower on an organic basis. Reported Group revenue of £1,684m (FY 2019: £2,276m) decreased by 26% as analysed in the table below:

|                        | <u>£'m</u>     | <u>Impact %</u> |
|------------------------|----------------|-----------------|
| FY 2019 revenue        | 2,276.2        |                 |
| Business disposals     | (103.9)        | (4)             |
| Currency movements     | (12.4)         | -               |
| Organic movement       | (475.8)        | (22)            |
| <b>FY 2020 revenue</b> | <b>1,684.1</b> | <b>(26)</b>     |

The adjustments for business disposals include the sale of: Angouleme (completed in March 2019); Orange County product lines (completed in June to December 2019); Training Systems (completed in June 2020); and our Dunstable business and associated product lines (completed in January 2021).

Currency movements in the year reflect the slight strengthening of pound sterling against our trading currencies, principally the US dollar. The organic revenue decline reflects the impact of COVID-19 on civil aerospace partially offset by defence.

### Profit and earnings per share

In common with previous years, underlying profit is used by the Board to measure the underlying trading performance of the Group and excludes certain items including: amounts arising on the acquisition, disposal and closure of businesses; amortisation of intangible assets acquired in business combinations; movements in financial instruments; and exceptional operating items.

As a result of the reduction in Group revenue, and notwithstanding the significant action taken to reduce costs to mitigate the impact of lower volumes and under absorption of fixed costs, the Group's underlying operating margins decreased by 640 basis points, to 11.3% (FY 2019: 17.7%), with underlying operating profit 53% lower in the year at £190.5m (FY 2019: £402.8m).

Underlying profit before tax decreased by 57% to £159.5m (FY 2019: £370.3m) with underlying earnings per share down 56% at 16.5 pence (FY 2019: 37.3 pence).

The level of exceptional costs at £428.7m is significantly higher than forecast at the start of the year, including impairment of goodwill and asset write-downs arising from the unprecedented downturn in civil aerospace during the year, resulting in Group underlying operating profit becoming an operating loss of £297.3m at the statutory level. Within exceptional costs, £374.2m relates to impairment losses and other asset write downs comprising: goodwill (£335.7m); development costs (£24.5m); inventory (£8.6m); and trade receivables (£5.4m). Further details relating to impairment losses and other asset write-downs are set out in note 8.

As a result of the impairment losses and other asset write downs, Group loss before tax was £334.0m (FY 2019: £286.7m profit) and basic loss per share was 40.4 pence (FY 2019: earnings per share of 28.8 pence).

Reconciliation between underlying operating profit and statutory operating loss

|  | <b>2020</b>    |
|--|----------------|
|  | <b>£'m</b>     |
| <b>Underlying operating profit</b>                                     | <b>190.5</b>   |
| Impairment losses and other asset write-downs                          | (374.2)        |
| COVID-19 incremental non-recurring costs                               | (22.0)         |
| Site consolidations  | (33.5)         |
| Other  | 1.0            |
| Exceptional operating items  | (428.7)        |
| Amortisation of intangible assets arising on acquisition of businesses | (88.2)         |
| Financial instruments  | (2.9)          |
| Amounts arising on the acquisition, disposal and closure of businesses | 32.0           |
| <b>Statutory operating loss</b>  | <b>(297.3)</b> |

**Dividends**

The Board concluded that it was prudent not to pay a final dividend for 2019, and in light of ongoing challenging market conditions, the Board did not recommend the payment of an interim or final dividend for 2020. This has helped retain cash within the Group, ensured the continued management of net debt levels and preserved financial flexibility. The Board is very aware of the importance of dividends to our shareholders and looks forward to restoring dividend payments when the recovery in civil aerospace is more established.

**Cash flow**

The Group generated a free cash inflow of £31.9m (FY 2019: £267.8m inflow), which was ahead of our guidance issued in September 2020, reflecting the work done across the Group to offset the impact of the lower operating result, including a reduction in absolute inventory levels and planned levels of capex.

Full year cash flow statement £m

|   | <b>2020</b>    | 2019      |
|---|----------------|-----------|
|   | <b>£'m</b>     | £'m       |
| <b>Underlying operating profit</b>                          | <b>190.5</b>   | 402.8     |
| Depreciation and amortisation                               | <b>106.4</b>   | 104.5     |
| Working capital movements                                   | <b>8.1</b>     | (21.0)    |
| Net interest paid   | <b>(32.1)</b>  | (33.1)    |
| Tax paid  | <b>(42.1)</b>  | (14.4)    |
| Exceptional operating items paid                            | <b>(49.3)</b>  | (27.3)    |
| Purchase of property, plant and equipment                   | <b>(89.7)</b>  | (94.4)    |
| Proceeds from disposal of property, plant and equipment     | <b>1.3</b>     | 23.1      |
| Capitalised development costs/programme participation costs | <b>(43.0)</b>  | (56.7)    |
| Retirement benefit deficit reduction payments               | <b>(21.7)</b>  | (35.2)    |
| Other   | <b>3.5</b>     | 19.5      |
| <b>Free cash flow</b>                                       | <b>31.9</b>    | 267.8     |
| Net proceeds from disposal/acquisition of businesses        | <b>104.2</b>   | 68.9      |
| Dividends paid to Company's shareholders                    | -              | (130.4)   |
| Issue of equity share capital                               | <b>0.3</b>     | -         |
| Other   | <b>(0.4)</b>   | (0.6)     |
| <b>Net cash generated</b>                                   | <b>136.0</b>   | 205.7     |
| Lease liabilities entered                                   | <b>(11.4)</b>  | (54.2)    |
| Lease liabilities disposed with business                    | <b>5.6</b>     | -         |
| Exchange differences  | <b>7.6</b>     | 31.2      |
| Other movements   | <b>0.4</b>     | (19.8)    |
| <b>Net debt movements</b>                                   | <b>138.2</b>   | 162.9     |
| <b>Net debt at 1 January</b>                                | <b>(911.2)</b> | (1,074.1) |
| <b>Net debt at 31 December</b>                              | <b>(773.0)</b> | (911.2)   |

Investment in capital expenditure was £89.7m (FY 2019: £94.4m) and working capital was an inflow of £8.1m (FY 2019: £21.0m outflow). Higher cash tax payments of £42.1m (FY 2019: £14.4m) reflects the phasing of payments in the US and the increase in cash exceptional costs to £49.3m (FY 2019: £27.3m), includes £18.9m of non-recurring COVID-19 related costs and site consolidation costs as we continue to rationalise our global footprint. Deficit payments made in respect of retirement benefit schemes were £21.7m (FY 2019: £35.2m) following an agreement with the trustees of the UK scheme to defer four months of payments totalling £9.6m that will now be spread across the 2021 to 2023 period. The free cash inflow of £31.9m was augmented by proceeds from the sale of Training Systems which generated net proceeds of £117.0m, with a net cash inflow for the Group of £136.0m for the full year (FY 2019: £205.7m inflow).

As a result, at the end of December 2020, our net debt was £773.0m (FY 2019: £911.2m), including lease liabilities of £144.3m, a decrease of £138.2m from December 2019 after taking into account proceeds from the sale of Training Systems and favourable currency movements of £7.6m and we had significant headroom of £908.1m on committed facilities of £1,536.8m.

### **Debt structure and financing**

In June and October 2020, we repaid \$125m and \$150m respectively on the maturity of two separate tranches of 2010 US Private Placement Notes. In November 2020, we raised \$300m in aggregate of three and five year senior notes providing us with additional liquidity and financial flexibility as we look ahead to 2021 and beyond.

In April 2020, the Group was confirmed as an eligible issuer under the Bank of England and HM Treasury's Covid Corporate Financing Facility (CCFF), under which the Group is able to draw up to £600m. While the Group issued commercial paper under this facility during the year, as at the end of December 2020, there were no borrowings under this facility. The Group has retained access to the CCFF and is eligible to issue commercial paper using this facility (subject to certain terms and restrictions) up to and including 22 March 2021, with a maturity date of up to twelve months. In May 2020, we extended the duration of our debt by securing a forward start on our revolving credit facility, with the signing of a new one year \$575m multi-currency facility maturing in September 2022.

There are two main financial covenants in our financing agreements. The net borrowings:underlying EBITDA ratio, which must not exceed 3.5x, was at 2.2x at 31 December 2020 (December 2019: 1.5x) and interest cover, which must be not less than 3.0x, was 9.8x (December 2019: 16.3x). At the end of 2020, the Group had significant headroom against both key covenant ratios, and net borrowings:underlying EBITDA is within our target range of 1.5x to 2.5x.

### **OUTLOOK FOR 2021**

While the rollout of vaccines is expected to ease lockdowns and drive a gradual increase in air traffic activity, which is a positive indicator for the civil aerospace sector and the Group, uncertainties remain in predicting the timing and pace of the civil recovery. At the current time, our assumption is that the trends seen in civil aerospace during the second half of 2020 are likely to continue in the first half of 2021, with recovery weighted more towards the second half of the year. Conditions in our defence and energy end markets are expected to remain robust in 2021.

Assuming no further disruption to normal operations during the year as a result of additional lockdowns, in 2021 we expect the Group to generate:

- Revenue broadly in line with 2020;
- An increase in underlying operating profit versus 2020; and
- Positive free cash flow

We will continually review our assumptions as the year progresses and as we gain greater clarity on the path to recovery in civil aerospace.

While we recognise the need to remain agile and respond quickly to changes in the external environment, based on the significant progress we have made over the last four years to transform the Group, the effective actions we've taken in 2020, our diverse end market exposure and leading market positions, we are well placed to benefit from the recovery in civil aerospace and to deliver long-term profitable growth.

## ENABLING OUR SUSTAINABLE FUTURE

At Meggitt, we work in partnership with all our stakeholders to enable a sustainable future and have adopted a framework to support our ambition of net zero greenhouse gas emissions by 2050, focusing on three core pillars: People, Planet and Technology. This framework is aligned with the United Nations Sustainability Development Goals and the Taskforce on Climate Related Financial Disclosures:

- **People** – through our core values of Teamwork, Integrity and Excellence and our high performance culture we are committed to creating a rewarding, safe and productive working environment for our employees and supporting our local communities. During 2020, we started the rollout of our leadership programme in Operations, introduced our Extraordinary People recognition scheme and expanded the number of Employee Resource Groups to eight with further initiatives planned for 2021.
- **Planet** – our goal is to contribute to a cleaner future by continuously improving and adapting our operational systems across our sites to promote efficiencies and improvements by harnessing green energy, driving operational excellence and reducing harmful emissions, where we have set a target to reduce net carbon emissions by 50% by 2025. While we made progress in a number of areas during the year, including the completion of several sustainability projects at our sites, and from March 2021 sourcing 100% of electricity from green sources in the UK, we recognise that we still have more work to do. We have set reduction targets for our sites in 2021 covering reducing our electricity and natural gas usage, consumption of water and rates of waste to landfill, as we look to build on the progress we have made over the last few years.
- **Technology** – to support the evolving needs of our global customers and building on our rich heritage, we continue to invest in innovative new technologies to support and enable sustainable aviation in areas including thermal and electric aircraft systems, fire protection, composites and optical sensing. In 2020, we made very good progress on a number of these technologies and specific customer projects as set out in our Strategy section.

## STRATEGY UPDATE

### Strategic Portfolio

We focus investment in attractive markets where we have, or can develop, a leading position. This encompasses organic investment in differentiated products and manufacturing technologies; targeted, value-enhancing acquisitions; and selective non-core disposals. More than 70% of revenue is generated from sole-source, life of programme positions underpinned by Meggitt-owned intellectual property. As such, the continued strengthening of our technology portfolio remains a critical priority of the Group.

In June 2020, we further focused our portfolio with the sale of Training Systems, consistent with our strategy to focus on businesses of scale in markets where leading positions offer exposure to aftermarket revenue, greater potential for growth and operational efficiencies. In January 2021, we completed the sale of our Dunstable (UK) business of designing and manufacturing ducting products for a range of space, defence and civil customers. As a result of these disposals, over 80% of our revenue is now generated from businesses in attractive markets and where we have a strong competitive position, above our target set out three years ago.

Despite the challenges posed by COVID-19 and the need to preserve cash, we sustained our investment in differentiated technology. During the year, we met our target of prioritising at least two-thirds of our investment in Applied Research & Technology to enable our customers to deliver the next generation of more sustainable aircraft. Despite changes in normal working patterns, we also maintained strong milestone adherence on our major development and customer programmes. A summary of our key highlights and progress are as follows:

- **Next generation of fuel efficient engines** – we are positioning and promoting the breadth of our technology with our customers to play a critical role in enabling the development of the next generation of fuel efficient engines specifically leveraging our capabilities in: thermal management; high temperature optical sensing; and engine composites. For example, in 2020, our Thermal Systems programme patented technology for six products which will allow a step change in engine thermal management applications.
- **Green fire suppression** – we have made good progress working with major aircraft OEMs with VERDAGENT™, Meggitt's new, proprietary 'green' fire suppressant agent to replace ozone depleting Halon 1301, with further tests in Europe and the US to approve its engine APU and cargo applications scheduled for 2021.
- **Optical sensing** – we successfully completed the first customer trials of our optical dynamic pressure sensing system for ground-based industrial gas turbines and now have an installation running with a major energy customer. We also remain on track to install this new technology on a demonstrator aero engine with a major OEM in 2021.
- **Engine composites** – we made significant progress in development of manufacturing processes for advanced 'gas path' engine composite components with thin wall, high structural integrity requirements.

- Electric flight – working closely with a customer we have supplied electric motors and motor drive units to support the development of a leading electric urban/air mobility prototype which is undergoing trials.

We have also continued to leverage advanced manufacturing technology and processes across our sites:

- Additive layer manufacturing (ALM) – working with our UK joint-venture partner HiETA, we have applied ALM to build prototype heat exchangers to operate at high temperatures for industrial and aero applications. We have also expanded our US additive manufacturing capability to develop flow valves and production tooling.
- Digital manufacturing – the rollout of advanced digital work instructions and greater use of automation at our sites has resulted in a meaningful increase in productivity and quality, and we are working on plans to deploy this technology more extensively across the Group in 2021.

As reported at the half year, we have intensified our focus on driving improved margin and return on capital in braking systems, while continuing to remain highly selective on investing in new opportunities. Recognising the change in fleet dynamics as a result of the downturn in civil aerospace, where possible we have re-phased our investment in both carbon and brakes production capacity with a proportion of our capital commitments in this area moving into 2021 and beyond.

While our focus remains on three core markets: aerospace, defence and selected energy, over the medium-term we also look to increase the application of our aero-derivative intellectual property and technology in adjacent markets, including space and ground vehicles, to further strengthen the portfolio.

## Customers

Our success in moving from a transactional approach to building long term relationships through our customer-aligned divisions, extends our visibility of near term customer requirements and has enabled us to better support the demand for original equipment and spare parts and maintenance, repair and overhaul ('MRO') from our three global hubs for the aftermarket.

During the year, we maintained close contact with our customers which was critical in the creation of our scenarios for planning purposes, including the adjustment of production schedules for original equipment based on new build rates from the OEMs and tracking customer sentiment and buying behaviour by region in the aftermarket.

In the period, we continued to win a number of new customer contracts including orders for:

- \$73m from Bell Textron Inc for the supply of composite ice protection components on the V22 Osprey;
- \$27m for the supply of liquid palletised cooling units for the Boeing P-8A aircraft;
- \$21m for the supply of high temperature cables for a nuclear energy application;
- \$20m from Northrop Grumman for the supply of fuel bladders on the F/A-18 Super Hornet;
- \$15m from the Defence Logistics Agency to support the supply of fuel bladders; and
- £8m from MODEC for the supply of Heatric printed circuit heat exchangers, representing the largest order for that business for over five years

In Services & Support, we saw continued momentum with SMARTSupport®, our long-term contract offering for aftermarket customers, adding an additional 14 agreements, including those with ST Aerospace, Derco and Ameco Beijing, taking the total number to 39 with an aggregate value of £187m, with a number of additional opportunities in the pipeline. These long-term contracts underpin our aftermarket and market share growth in the future and provide better insights into customer requirements and order patterns.

## Competitiveness

While our priority during the year has been to ensure that people and sites operate safely as we respond to the challenges posed by COVID-19, we remained focused on driving operational improvements in line with our strategy.

We made further progress reducing our global footprint, with site closures and consolidations in the UK (Basingstoke) and the US (Orange County) and the divestment of Training Systems. As a result of these actions and the recent sale of our Dunstable (UK) business, we now have 37 Meggitt manufacturing sites, reduced from our original 56 sites in 2016 and 42 sites at the end of December 2019, and have identified additional opportunities to reduce our footprint by 50% from our 2016 baseline by 2023.

In June 2020, we opened our new UK manufacturing and engineering centre for Braking Systems, Thermals systems and Services & Support together with our relocated Group Headquarters at Ansty Park in the Midlands, providing office-based employees that have been working from home with the flexibility to return to the workplace as restrictions allowed. The successful relocation of our teams to Ansty Park will promote more integrated and efficient ways of working across both the Group central functions and the divisions.

Having been deferred due to the disruption caused by COVID-19, the full transition of manufacturing from four UK sites into Ansty Park is well underway, with the capital expenditure associated with this transition also moving into 2021. The transition to Ansty Park is scheduled to be completed by the end of the third quarter in 2021.

On inventory, where we have brought significant improvements in recent years and steadily increased inventory turns from just above 2.0x in 2016 to 2.7x in 2019, our priority in 2020 was to reduce absolute inventory levels as part of our cash preservation measures as we responded to the change in demand from our customers. We used the change in market conditions as an opportunity to tighten our supply parameters and production scheduling (including moving from monthly to weekly deliveries of raw materials). While we made very good progress reducing absolute inventory levels during the year, this will remain a focus area in 2021.

Within purchasing, we continued to offer our suppliers access to an ePayables scheme and supported them gaining access to government schemes in the US, UK and France. Alongside this, we have taken the opportunity to further strengthen and consolidate our supply chain, including identifying opportunities to derive further savings by moving more of our supply base to low cost countries where appropriate.

Our recovery plan in Engine Composites continued as we applied engineering and process improvements to achieve higher quality and further improvements in yields. During the year, our facility in Saltillo, Mexico received approval for the manufacture and direct shipment of additional high volume composite parts to end customers. In addition, lower production of aircraft engines caused by COVID-19 allowed us to accelerate the adoption of new manufacturing technology and transfer of production lines to Mexico, with further high volume parts transitioning in 2021.

## **Culture**

Our priority in 2020 was to ensure the health and well-being of our people across our sites and their response to the crisis has been outstanding, enabling us to support all our stakeholders in what have been extremely challenging circumstances. During the year, our teams used their capabilities to support our local communities in a variety of ways – from supporting the production of critical ventilators for the NHS in the UK, to visors, masks and other protective equipment for key workers.

Over the last three years we have worked hard to build and nurture a high performance culture (HPC) and improve engagement where our ambitious and diverse teams help us to accelerate the execution of our strategy. The progress we have made in this area and the support of our employees has been instrumental in the Group being able to respond strongly to the crisis during 2020. While our focus on responding to the crisis necessitated deferring a lot of planned HPC activities into 2021, we did deliver a number of training sessions virtually and in person during the year.

In addition, our customer-aligned organisational structure and more integrated approach to working across teams has been a key enabler as we moved quickly to respond to a significant adjustment in demand across our civil business. Despite the huge challenges presented by the need to respond to the pandemic and the re-sizing of the business, our Group-wide Engagement score was maintained at the High Performance Norm<sup>6</sup> with our scores for Alignment and Agility increasing by 2% and 4% respectively, providing reassuring feedback on the manner in which the Group engaged with all employees as we responded to the COVID-19 crisis.

We further strengthened our commitment to Diversity and Inclusion, including a series of activities during our Inclusion Week in October 2020 and the introduction of an additional three Employee Resource Groups, bringing the total number of groups to eight.

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<sup>6</sup> Culture IQ employee survey benchmark

## END MARKET TRADING SUMMARY

|                    | Revenue (£'m)  |                | Growth (%)  |             |
|--------------------|----------------|----------------|-------------|-------------|
|                    | 2020           | 2019           | Reported    | Organic     |
| Civil OE           | 306.0          | 518.6          | (41)        | (40)        |
| Civil AM           | 419.6          | 715.9          | (41)        | (41)        |
| <b>Total civil</b> | <b>725.6</b>   | <b>1,234.5</b> | <b>(41)</b> | <b>(41)</b> |
| Defence            | 768.4          | 824.6          | (7)         | 4           |
| Energy             | 131.1          | 142.7          | (8)         | (8)         |
| Other              | 59.0           | 74.4           | (21)        | 11          |
| <b>TOTAL</b>       | <b>1,684.1</b> | <b>2,276.2</b> | <b>(26)</b> | <b>(22)</b> |

### 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 7,000 and business jets around 20,000. The Group has products on the vast majority of these platforms and hence a large, installed base. With 54% of our civil aftermarket revenue (for full year 2019) generated from platforms under 10 years old, we are well placed to continue to generate good returns over the coming years as the market recovers.

The split of civil revenue in the full year, which accounted for 43% of the Group total, was 58% aftermarket and 42% original equipment (OE).

In the year, civil OE revenue was down 40% organically reflecting lower demand for original equipment from the OEMs, with large jets, the largest component of our OE revenue, down 44% and regional jets down 46%. Business jet OE was down 25%. Within the year, civil OE was down 29% and 51% in the first and second halves respectively.

As a result of lower levels of air traffic activity in the period, civil aftermarket revenue was down 41% organically as airlines and other aftermarket customers deferred orders for spare parts and repairs, with large jets down 41%, regional down 49% and business jets down 32%. Within the year, civil AM was down 26% and 54% in the first and second halves respectively.

Overall, Group civil aerospace revenue (OE and AM combined) was 41% lower in the year on an organic basis.

### Defence

Our defence business accounted for 46% of Group revenues in 2020 (including Training Systems) generating 59% of revenue from OE and 41% from the aftermarket. We have equipment on an installed base of around 22,000 fixed wing and rotary aircraft and a significant number of ground vehicles and are well placed having secured strong positions on some of the newest and hardest worked platforms. Direct sales to US customers accounted for 74% of defence revenue, with 18% to European customers and 8% to the rest of the world.

Defence spending remained robust during the year with continuing good outlays by the US DoD and our order book remains healthy with an organic book to bill of 1.05x, underpinned by a number of multi-year contracts.

Defence revenue grew 4% on an organic basis (excluding Training Systems) with strong growth in the first half of 8%. Defence revenue was flat in the second half on an organic basis (compared with the same period in 2019). In OE, revenue grew 14% organically driven by continuing strong growth on parts for the F-35 Joint Strike Fighter, Eurofighter, F/A-18 Hornet and in rotary wing, the AH-64 Apache. Aftermarket revenue was 7% lower organically reflecting the disruption to military exercises caused by COVID-19, with growth in fighters more than offset by lower revenue in rotary wing and military transports.

### Energy and other

Energy and other revenues, which represents 11% of Group total, come from a variety of end markets of which the single most significant is energy (8% of Group total). 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. Other markets (3% of Group total) include the automotive, industrial, test, consumer goods and medical sectors.

Energy revenue was down 8% on an organic basis, reflecting volatile end market conditions in the first half and some disruption in both the supply chain and our sites caused by COVID-19 towards the end of the year. In Heatric, organic revenue was down 7% with revenue derived from our valve and condition monitoring business 12% lower on an organic basis. Revenue from other markets was up 11% organically on the comparative period.

The near-term and medium-term outlook for our energy businesses remains good, with a robust order book as we entered

2021. We have differentiated aero-derivative technologies which play a critical role in the extraction of deep water offshore gas reserves and the growth in demand for alternative, lower carbon energy sources including renewables, positions this business well for the future.

## DIVISIONAL PERFORMANCE

The focus across all four divisions during 2020 has been to protect our people, support our communities and keep our sites open and operating safely to support our customers. Faced with the reduction in civil aerospace demand, the divisions responded quickly to reduce costs and preserve cash, each making an important contribution to the overall Group cash targets during the year.

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

|                    | Revenue        |                          |                      |                     | Underlying Operating Profit/(Loss) |                          |                      |                     |
|--------------------|----------------|--------------------------|----------------------|---------------------|------------------------------------|--------------------------|----------------------|---------------------|
|                    | 2020<br>£'m    | 2019 <sup>7</sup><br>£'m | % Growth<br>Reported | % Growth<br>Organic | 2020<br>£'m                        | 2019 <sup>7</sup><br>£'m | % Growth<br>Reported | % Growth<br>Organic |
| Airframe Systems   | 793.1          | 1,029.5                  | (23.0)               | (22.4)              | 120.5                              | 247.7                    | (51.4)               | (52.2)              |
| Engine Systems     | 233.6          | 329.5                    | (29.1)               | (28.4)              | (13.2)                             | 27.2                     | (148.5)              | (150.4)             |
| Energy & Equipment | 335.0          | 412.5                    | (18.8)               | 6.5                 | 42.4                               | 53.4                     | (20.6)               | 18.1                |
| Services & Support | 322.4          | 499.1                    | (35.4)               | (34.8)              | 40.8                               | 74.0                     | (44.9)               | (44.5)              |
| Other <sup>8</sup> | -              | 5.6                      | (100.0)              | -                   | -                                  | 0.5                      | (100.0)              | -                   |
| <b>Total Group</b> | <b>1,684.1</b> | <b>2,276.2</b>           | <b>(26.0)</b>        | <b>(22.3)</b>       | <b>190.5</b>                       | <b>402.8</b>             | <b>(52.7)</b>        | <b>(50.5)</b>       |

**Airframe Systems** provides Braking Systems, Fire Protection & Safety Systems, Power & Motion, Fuel Systems, Avionics & Sensors and Polymer Seals for around 51,000 in-service civil and 22,000 defence aircraft. As well as increasing our content on the new generation aircraft by as much as 250%, we also have a strong presence on all of the fastest growing and hardest worked defence platforms. As such, we have strong relationships with all of the major OEMs, whether commercial, defence or business jet; fixed wing or rotorcraft; US, European or Rest of World. The division represents 47% of Group revenue, generating 55% of its revenue from OE sales and 45% from the aftermarket derived mainly from Braking Systems, with the remaining aftermarket revenue from other product groups reported in Services and Support.

### Operational and strategic highlights

- Continued to support customers on new product development and testing across a number of platforms
- Good progress on development of new technologies, including new 'green' fire suppression agent VERDAGENT™
- Transfer of products associated with further footprint consolidation, including moves out of Orange County, US to Airframe Systems sites in the US, UK and Europe
- Secured \$15m of funding under the CARES Act to support critical industrial base capability for military grade fuel bladders at our Rockmart, US facility
- Deferral of capital expenditure relating to carbon capacity expansion in Braking Systems

### Financial performance

Organic revenue was down 22% in the period. Civil OE revenue was down 34% with large jets and regional jets OE down 39% and 38% respectively, reflecting lower end market demand for new aircraft and OEMs reducing new build rates. Business jet OE was down 18% outperforming large and regional jets on a relative basis.

Civil aftermarket revenue was 42% lower on an organic basis reflecting the reduction in commercial air traffic and lower demand for spares. Organic aftermarket revenue in large, regional and business jets was down 38%, 52% and 32% respectively.

Defence revenue was flat, with OE 6% higher driven by growth in fighters, including the F-35 and Typhoon. In the aftermarket, revenue was 5% lower than the prior year, with growth on Typhoon, F/A-18 and light attack platforms more than offset by declining demand on rotary wing and special mission.

As a result of the lower volumes in civil OE and reduction in higher margin civil aftermarket revenues, underlying operating margin was 890 basis points lower than the comparative period at 15.2% (FY 2019: 24.1%).

In 2021, responsibility for all aftermarket activities in Braking Systems including spares and repairs, will transfer to the Services & Support division and be managed across the Group's three regional aftermarket hubs.

<sup>7</sup> We have restated 2019 comparatives to reflect the transfer of the UK braking systems MRO business that took place on 1 January 2020. The impact is that AS revenue and operating profit for 2019 are £27.9m and £2.8m lower respectively than we published in 2019, with a corresponding increase for S&S.

<sup>8</sup> Those businesses which were disposed of prior to the effective date of the new divisional structure on 1 January 2019, or were classified as held for sale at that date are presented separately as 'Other'.

**Engine Systems** has market-leading positions in advanced engine composites, thermal and safety systems with a broad range of technologies including vibration monitoring and engine health management systems. This division also provides aerospace engine flow control and sensing solutions. Strong positions on high volume platforms mean we are well positioned for growth in Engine Systems. The division represents 14% of Group revenue, generating 89% of its revenue from OE and 11% from the aftermarket as a result of its principal route to the aftermarket being through the Services & Support division.

#### *Operational and strategic highlights*

- Good progress developing new products in the engine core to displace heat, increase efficiency, and reduce fuel, particularly projects to support next generation engine demonstrators
- Transfer of high volume engine composite parts to Saltillo, Mexico and direct shipments from Mexico to end customers
- Transfer of Engine Sensing products from Basingstoke to Airframe Systems Fareham in the UK as part of ongoing footprint consolidation
- In Defence, continued strong growth including to support the F-135 engine programme
- Completed sale of our ducting business based in Dunstable (UK) in January 2021

#### *Financial performance*

Revenue decreased by 28% on an organic basis with good growth in defence more than offset by lower demand for OE parts across civil aerospace. Civil OE revenue was 49% lower on an organic basis, with the absolute reduction in revenue mainly driven by large jets. In defence, revenue grew by 9% on an organic basis with particularly strong growth on the F-135 programme and the F-22 Raptor.

Despite the work done within the division to significantly reduce costs in response to the reduction in civil OE and AM volumes across all product groups, Engine Systems generated an underlying operating loss in the year of £13.2m (FY 2019: profit of £27.2m).

Within our Engine Composites business, we continued to make good progress with operational improvements including the transfer of additional high volume parts to our facility in Mexico. We remain firmly focused on our recovery plan in Engine Composites and returning this product group to mid-teens margins having delivered a number of operational improvements. However, as reported at the half year, due to the severe and sudden downturn in civil OE volumes, margin recovery will now take longer and extend beyond our previous timeline of the end of 2021.

**Energy & Equipment** consists of our energy product groups and businesses that provide products directly to defence customers. Energy Sensors & Controls provides a range of valves, actuators, sensor and condition monitoring systems for oil and gas applications. Heatric provides innovative printed circuit heat exchanger technology for offshore gas applications. Defense Systems provides a series of complex engineered products to defence agencies in electronic cooling, ammunition handling and scoring systems. Training Systems was sold on 30 June 2020 and revenue from this product group (FY 2020: revenue of £32.8m) is excluded from organic figures. Energy & Equipment represents 20% of Group revenue and generates 83% of its revenue from OE and 17% from the aftermarket.

#### *Operational and strategic highlights*

- Strong Defence performance across ground vehicle cooling systems, countermeasures and ammunition handling
- Sale of the Training Systems business in June 2020
- Continued footprint consolidation with closure of the Orange County site and the transfer of products to other sites in the US and Europe
- Continued transfer of production volumes to low cost countries

#### *Financial performance*

Revenue was up 7% organically (down 19% on a reported basis with the inclusion of Training Systems) with a strong performance from Defense Systems and strong OE growth on the Apache AH-64 and other rotary wing. In energy, despite the volatility in market conditions during the year, revenue was 12% lower on an organic basis, reflecting a strong order book as we entered the year. Underlying operating margins in Energy & Equipment at 12.7% were 20 basis points lower than the comparative period (FY 2019: 12.9%).

With the US defence budget agreed for 2021, a healthy order book and a number of promising commercial opportunities in both energy and defence, the outlook for 2021 is encouraging. As well as focusing on the conversion of these opportunities, our focus in Energy & Equipment will continue to be the delivery of further operational improvements across all sites.

**Services & Support (S&S)** provides a full service aftermarket offering including spares distribution and MRO to our commercial, business jet and defence customer base, throughout the lifecycle of our products. The division represents 19% of Group revenue and generates 100% of its revenue from the aftermarket.

#### Operational and strategic highlights

- Continued delivery of strategic initiatives with consolidation of repair capabilities in our three regional centres of excellence: Ansty Park in the UK, Singapore and Miami in the US
- Expansion of Singapore aftermarket capability and footprint
- Enhanced maintenance forecasting capabilities leveraging best in class technologies to improve inventory management, reduce lead times and enhance customer service levels
- Introduction of 'Smart Scoping' in our three regional hubs to leverage engineering capabilities to increase efficiency and reduce MRO costs

#### Financial performance

Within S&S, order intake in civil aftermarket was down 49% in the year as our aftermarket customers deferred orders for both spare parts and MRO. In APAC, orders were down 37% with the recovery in the Chinese domestic market underpinning the region; order intake was down 48% in the Americas with the 737MAX grounding negatively influencing demand for spare parts and, as a result of repeated lockdowns and associated border controls, within EMEA order intake was down 59% in the year.

Divisional revenue was 35% lower organically with civil aerospace revenue down 40%. Large jet revenue, which represented 82% of S&S civil revenue, was down 41% organically in the year, with regional and business jets down 39% and 32% respectively. In defence, revenue was 11% lower on an organic basis.

On a regional basis, organic revenue was down 32% in APAC and 34% and 36% in Americas and EMEA respectively. Underlying operating margin was 210 basis points lower at 12.7% (FY 2019: 14.8%).

In the coming year, our core priorities within S&S will be to ensure the smooth integration of brakes spares and repairs into the division, drive an increase in market share through signing additional SMARTSupport® contracts and investing further in our three regional aftermarket centres of excellence.

## INVESTING FOR THE FUTURE

|  | 2020          | 2019   | % Change |          |
|--|---------------|--------|----------|----------|
|  | £'m           | £'m    | Organic  | Reported |
| Total research and development (R&D)     | <b>97.9</b>   | 118.5  | (14)     | (17)     |
| Less: Charged to cost of sales / WIP     | <b>(20.8)</b> | (23.8) | (12)     | (13)     |
| Less: Capitalised                        | <b>(41.4)</b> | (54.7) | (20)     | (24)     |
| Add: Amortisation / Impairment           | <b>32.6</b>   | 28.7   | 24       | 14       |
| Charge to underlying net operating costs | <b>68.3</b>   | 68.7   | 4        | (1)      |
| Capital expenditure                      | <b>89.7</b>   | 94.4   |          |          |

While we have scaled back expenditure on R&D in the year as part of our overall cash saving initiative, we have continued to invest in sustainable technologies to support new product development and future growth opportunities. Accordingly, total R&D expenditure in the full year of £97.9m was broadly in line with the prior year as a percentage of revenue at 5.8% (FY 2019: 5.2%). The charge to underlying net operating costs, including amortisation and impairment, decreased by 1% (increased by 4% on an organic basis) to £68.3m (2019: £68.7m).

Capital expenditure of £89.7m in 2020 was slightly lower than the prior year (FY 2019: £94.4m) and below our initial guidance of around £130m issued in February 2020. This reflects the actions we have taken to preserve cash and the associated deferral of capital expenditure relating to the transfer of production to Ansty Park and investment in carbon capacity, which will now be incurred in 2021 and beyond as these projects are completed.

For full year 2021, we expect to invest around £90m on R&D and £80m on capital expenditure, as we complete major projects deferred from 2020.

## OTHER FINANCIAL INFORMATION

### Foreign Exchange

The Group is exposed to both translation and transaction risk due to changes in foreign exchange rates. These risks principally relate to the US Dollar/Sterling rate, although exposure also exists in relation to other currency pairs, principally translation risk for the Sterling/Euro and Sterling/Swiss Franc and transaction risk for the US Dollar/Euro and US Dollar/ Swiss Franc.

|  | <b>2020</b> | 2019 |
|--|-------------|------|
| <i>Average translation rates against Sterling:</i> |             |      |
| US Dollar  | <b>1.29</b> | 1.28 |
| Euro   | <b>1.14</b> | 1.14 |
| Swiss Franc  | <b>1.22</b> | 1.27 |
| <i>Average transaction rates:</i>                  |             |      |
| US Dollar/Sterling                                 | <b>1.38</b> | 1.42 |
| US Dollar/Euro                                     | <b>1.17</b> | 1.19 |
| US Dollar/Swiss Franc                              | <b>1.09</b> | 1.06 |
| <i>Year-end rates against Sterling:</i>            |             |      |
| US Dollar  | <b>1.37</b> | 1.32 |
| Euro   | <b>1.11</b> | 1.18 |
| Swiss Franc  | <b>1.20</b> | 1.28 |

The results of foreign subsidiaries are translated into Sterling at weighted average exchange rates. Sterling remained volatile throughout 2020, trading at between \$1.15 and \$1.37 against the US Dollar. Over the year as a whole, the average Sterling rate against the US Dollar was \$1.29 (2019: \$1.28) providing a modest negative impact on our reported results for the year. Compared to 2019, translation of results from overseas businesses decreased Group revenue by £8.6m and decreased underlying profit before tax (PBT) by £0.1m in the year.

The sensitivity of full-year revenue and underlying PBT to exchange rate translation movements against sterling, when compared to the 2020 average rates, is shown in the table below:

|                                     | <b>Average rate</b> | <b>Revenue £'m</b> | <b>Underlying PBT £'m</b> |
|-------------------------------------|---------------------|--------------------|---------------------------|
| <i>Impact of 10 cent movement*:</i> |                     |                    |                           |
| US Dollar                           | 1.29                | 85                 | 5                         |
| Euro                                | 1.14                | 9                  | 1                         |
| Swiss Franc                         | 1.22                | 6                  | 1                         |

\* As measured against 2020 actual full-year revenue and underlying PBT.

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 2019, the Group's revenue was unfavourably impacted by £3.8m and underlying PBT for the year benefited by £2.5m from currency transaction movements.

Each ten cent movement in the US Dollar against the average hedge rates achieved in 2020 would affect underlying PBT by approximately £7.0m in respect of US Dollar/Sterling exposure, £2.0m in respect of US Dollar/Euro exposure and £2.0m in respect of US Dollar/Swiss Franc exposure.

The following table details hedging currently in place:

|                               | <b>Hedging in place<sup>8</sup><br/>%</b> | <b>Average transaction rates<sup>9</sup></b> |
|-------------------------------|---|--|
| <i>2021:</i>                  |   |  |
| US dollar/Sterling            | 100                                       | 1.36   |
| US dollar/Euro                | 100                                       | 1.16   |
| US dollar/Swiss Franc         | 100                                       | 1.13   |
| <i>2022 – 2024 inclusive:</i> |   |  |
| US dollar/Sterling            | 70  | 1.33   |
| US dollar/Euro                | 25  | 1.21   |
| US dollar/Swiss Franc         | 0   | N/A  |

<sup>8</sup>Based on forecast transaction exposures.

<sup>9</sup> Hedging in place with unhedged exposures based on exchange rates at 29 January 2021.

Taking translation and transaction benefit into account, the impact of changes in foreign exchange rates in FY 2020 compared with FY 2019 rates was to decrease reported revenue by £12.4m and increase underlying PBT by £2.4m.

At the end of the year, sterling strengthened against the US dollar. Should the current level of sterling against the US dollar as at the date of this report be maintained throughout 2021, it will generate a headwind for both Group revenue and profit.

### **Finance costs**

Underlying net finance costs were £31.0m (2019: £32.5m) principally reducing as a result of lower USD interest rates on our floating rate debt, partly offset by the full year impact of interest arising from the new Ansty Park lease, which commenced in H2 2019. With the raising of the USD 300m private placement debt in November 2020, a higher proportion of the Group's borrowings are now subject to fixed interest rates, which will result in a modest headwind to underlying net finance costs for 2021.

### **Taxation**

The Group's underlying tax rate for the year was 19.7% (FY 2019: 22.0%).

As reported in 2019, the Group is impacted by the EU Commission ruling that the UK CFC regime constituted partial state aid. The Group maintains the provision held at 31 December 2019 of £18.3m in respect of this matter. During the period the Group has been in dialogue with HMRC and continues to appeal against the ruling, in parallel with the UK government's own appeal, to the European General Court. While dates for these appeals to be heard have not been set, the UK tax authority is obliged to collect amounts it considers state aid and in late February 2021 the Group received assessments from the UK tax authority. The assessments are in line with the provision held and we shall be making a cash payment in respect of the CFC regime in the first half of 2021.

As expected, cash tax increased in the year to £42.1m (FY 2019: £14.4m) driven by the phasing of payments and an increase in the cash tax rate. Over the next two to three years, we expect the cash tax rate to start converging with the P&L tax rate as historical tax reliefs and allowances come to an end and tax relief on certain capital expenditure is received over a longer time period. As a result of this and the payment in respect of the UK CFC regime, we expect the level of cash tax to be around £60m for full year 2021.

### **Capital allocation priorities**

The unprecedented impact of COVID-19 in 2020 meant we had to adjust our normal capital allocation approach, as we focused on a series of measures to reduce costs and preserve cash.

Notwithstanding this, our prime objective continues to be to invest cash organically in developing differentiated technologies, to accelerate the Group's growth and maintain its strong market positions across a number of product categories, and operational efficiencies. A mainstay of our capital allocation approach over several decades has been to maintain a progressive dividend policy and the payment of a regular dividend to our shareholders. The decision not to pay a dividend in 2020 was difficult and so we look forward to restoring dividend payments when the recovery in civil aerospace is more established.

At present, the Board continues to believe that in maintaining an efficient balance sheet with ample covenant headroom and investment capacity, a net debt:EBITDA ratio of between 1.5x and 2.5x is appropriate, while preserving flexibility to move outside this range in certain situations, of which COVID-19 is one. The Board will keep this policy under review.

### **Retirement benefit schemes**

The Group's principal defined benefit pension schemes are in the UK and US. On 1 February 2021, the Group announced, following a consultation process with employees, that the UK plan would be closed to future accrual with effect from 6 April 2021. Once this change takes effect, and following the closure of one of the Group's US schemes during 2020, none of the UK or US defined benefit pension schemes will be open to future accrual.

Total scheme deficits in 2020 increased to £295.4m (2019: £267.9m) with the principal drivers of the net increase being:

- an increase of £136.1m (2019: increase of £142.7m) relating to re-measurement losses on scheme liabilities, principally arising from the significant weakening of AA corporate bond yields in both the UK and US;
- a reduction of £93.5m (2019: reduction of £53.5m) due to re-measurement gains on scheme assets; and
- net deficit reduction payments in the year of £21.7m (2019: £35.2m). In the UK, following the COVID-19 outbreak, the Group agreed with the trustees to defer four months of deficit contributions amounting to £9.6m, which will now be made over the remainder of the current recovery plan to August 2023. Deficit contributions recommenced in Q3 of 2020. In the US, legislation was passed in response to COVID-19 allowing companies to defer contributions due in 2020 to January 2021, as a result of which the Group deferred £2.4m of payments planned for 2020.

In the UK, the Group is currently making deficit payments in accordance with a recovery plan agreed with the trustees following the 2018 triennial funding valuation, amended in 2020 following the four month deferral of deficit contributions. This amended recovery plan provides for the 2018 deficit to be addressed by payments which gradually increase over the period to August 2023. Under the plan, the Group will make deficit contributions of £38.4m in 2021, £40.2m in 2022 and £29.9m in 2023.

At 31 December 2020, principally due to the significant fall in bond yields since the date of the 2018 valuation, the current UK funding position is approximately £135m lower than that projected in the 2018 valuation. This funding shortfall will, should it remain, be addressed through a revised recovery plan as part of the April 2021 triennial valuation, which we would expect to be finalised during H1 2022. Deficit contributions to address any additional deficit would commence at a date to be agreed with the trustees once the valuation is finalised.

## CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2020

|  | Notes | 2020<br>£'m      | 2019<br>£'m |
|--|-------|------------------|-------------|
| <b>Revenue</b>   | 4     | <b>1,684.1</b>   | 2,276.2     |
| <b>Non-GAAP measures</b>   |       |                  |             |
| Exceptional Impairment losses and other asset write-downs                      | 8a    | <b>(8.6)</b>     | -           |
| Other cost of sales  |       | <b>(1,192.0)</b> | (1,458.0)   |
| Cost of sales  |       | <b>(1,200.6)</b> | (1,458.0)   |
| <b>Gross profit</b>  |       | <b>483.5</b>     | 818.2       |
| <b>Non-GAAP measures</b>   |       |                  |             |
| Exceptional Impairment losses and other asset write-downs                      | 8a    | <b>(365.6)</b>   | -           |
| Other operating costs  |       | <b>(452.7)</b>   | (541.9)     |
| Operating costs  |       | <b>(818.3)</b>   | (541.9)     |
| Operating income   | 5     | <b>37.5</b>      | 49.0        |
| Net operating costs  |       | <b>(780.8)</b>   | (492.9)     |
| <b>Operating (loss)/profit <sup>1</sup></b>                                    |       | <b>(297.3)</b>   | 325.3       |
| Finance income   |       | <b>0.5</b>       | 2.2         |
| Finance costs  |       | <b>(37.2)</b>    | (40.8)      |
| Net finance costs  | 9     | <b>(36.7)</b>    | (38.6)      |
| <b>(Loss)/profit before tax <sup>2</sup></b>                                   |       | <b>(334.0)</b>   | 286.7       |
| Tax credit/(charge)  | 10    | <b>19.8</b>      | (64.1)      |
| <b>(Loss)/profit for the year attributable to equity owners of the Company</b> |       | <b>(314.2)</b>   | 222.6       |
| <b>(Loss)/earnings per share:</b>  |       |                  |             |
| Basic <sup>3</sup>   | 11    | <b>(40.4)p</b>   | 28.8p       |
| Diluted <sup>4</sup>   | 11    | <b>(40.4)p</b>   | 28.3p       |

| <b>Non-GAAP Measures</b>                           |       |              |       |
|--|-------|--------------|-------|
| <sup>1</sup> Underlying operating profit           | 4 & 6 | <b>190.5</b> | 402.8 |
| <sup>2</sup> Underlying profit before tax          | 6     | <b>159.5</b> | 370.3 |
| <sup>3</sup> Underlying basic earnings per share   | 11    | <b>16.5p</b> | 37.3p |
| <sup>4</sup> Underlying diluted earnings per share | 11    | <b>16.2p</b> | 36.7p |

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2020

|   | Notes | 2020<br>£'m    | 2019<br>£'m |
|---|-------|----------------|-------------|
| <b>(Loss)/profit for the year attributable to equity owners of the Company</b>                        |       | <b>(314.2)</b> | 222.6       |
| <b>Items that may be reclassified to the income statement in subsequent periods:</b>                  |       |                |             |
| Currency translation movements  | 28    | <b>(79.9)</b>  | (68.7)      |
| Movements in fair value of financial liabilities arising from changes in credit risk                  |       | <b>1.8</b>     | -           |
| Tax effect  |       | <b>1.6</b>     | 0.3         |
|   |       | <b>(76.5)</b>  | (68.4)      |
| <b>Items that will not be reclassified to the income statement in subsequent periods:</b>             |       |                |             |
| Remeasurement of retirement benefit obligations   |       | <b>(42.6)</b>  | (89.2)      |
| Tax effect  |       | <b>10.8</b>    | 11.9        |
|   |       | <b>(31.8)</b>  | (77.3)      |
| <b>Other comprehensive expense for the year</b>   |       | <b>(108.3)</b> | (145.7)     |
| <b>Total comprehensive (expense)/income for the year attributable to equity owners of the Company</b> |       | <b>(422.5)</b> | 76.9        |

## CONSOLIDATED BALANCE SHEET

At 31 December 2020

|   | Notes   | 2020<br>£'m      | 2019<br>£'m      |
|---|---------|------------------|------------------|
| <b>Non-current assets</b>   |         |                  |                  |
| Goodwill  | 14      | 1,519.5          | 1,966.6          |
| Development costs   | 14      | 531.9            | 575.9            |
| Programme participation costs   | 14      | 18.7             | 18.0             |
| Other intangible assets   | 14      | 401.1            | 503.6            |
| Property, plant and equipment   | 15      | 458.8            | 449.4            |
| Investments   | 16      | 20.8             | 14.1             |
| Other receivables   |         | 16.5             | 17.0             |
| Contract assets   |         | 59.6             | 55.2             |
| Derivative financial instruments  | 20      | 15.0             | 14.6             |
| Deferred tax assets   |         | 19.2             | 23.3             |
|   |         | <b>3,061.1</b>   | <b>3,637.7</b>   |
| <b>Current assets</b>   |         |                  |                  |
| Inventories   |         | 426.9            | 489.8            |
| Trade and other receivables   |         | 251.1            | 379.9            |
| Contract assets   |         | 48.8             | 66.3             |
| Derivative financial instruments  | 20      | 5.4              | 3.8              |
| Current tax recoverable   |         | 11.5             | 11.1             |
| Cash and cash equivalents   |         | 178.6            | 155.3            |
| Assets classified as held for sale                                      | 17      | 14.7             | -                |
|   |         | <b>937.0</b>     | <b>1,106.2</b>   |
| <b>Total assets</b>   | 4       | <b>3,998.1</b>   | <b>4,743.9</b>   |
| <b>Current liabilities</b>  |         |                  |                  |
| Trade and other payables  |         | (296.5)          | (464.5)          |
| Contract liabilities  |         | (50.8)           | (50.5)           |
| Derivative financial instruments  | 20      | (21.6)           | (16.5)           |
| Current tax liabilities   |         | (56.9)           | (81.6)           |
| Lease liabilities   |         | (14.7)           | (16.4)           |
| Bank and other borrowings   | 19 & 20 | (10.5)           | (219.4)          |
| Provisions  | 21      | (32.6)           | (36.2)           |
| Liabilities directly associated with assets classified as held for sale | 17      | (3.7)            | -                |
|   |         | <b>(487.3)</b>   | <b>(885.1)</b>   |
| <b>Net current assets</b>   |         | <b>449.7</b>     | <b>221.1</b>     |
| <b>Non-current liabilities</b>  |         |                  |                  |
| Other payables  |         | (8.5)            | (2.1)            |
| Contract liabilities  |         | (73.9)           | (77.0)           |
| Derivative financial instruments  | 20      | (0.3)            | (4.6)            |
| Deferred tax liabilities  |         | (93.4)           | (155.3)          |
| Lease liabilities   |         | (129.6)          | (136.2)          |
| Bank and other borrowings   | 19 & 20 | (796.8)          | (694.5)          |
| Provisions  | 21      | (80.3)           | (64.4)           |
| Retirement benefit obligations  | 22      | (295.4)          | (267.9)          |
|   |         | <b>(1,478.2)</b> | <b>(1,402.0)</b> |
| <b>Total liabilities</b>  |         | <b>(1,965.5)</b> | <b>(2,287.1)</b> |
| <b>Net assets</b>   |         | <b>2,032.6</b>   | <b>2,456.8</b>   |
| <b>Equity</b>   |         |                  |                  |
| Share capital   |         | 39.0             | 38.8             |
| Share premium   |         | 1,226.6          | 1,226.5          |
| Other reserves  |         | 15.7             | 15.7             |
| Hedging and translation reserves  |         | 348.9            | 425.4            |
| Retained earnings   |         | 402.4            | 750.4            |
| <b>Total equity attributable to owners of the Company</b>               |         | <b>2,032.6</b>   | <b>2,456.8</b>   |

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2020

|   | 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            |
| <b>At 1 January 2019</b>                          | 38.8   | 1,223.9        | 15.7           | 493.8                            | 720.2             | 2,492.4        |
| Profit for the year                               | -  | -              | -              | -                                | 222.6             | 222.6          |
| Other comprehensive expense for the year          | -  | -              | -              | (68.4)                           | (77.3)            | (145.7)        |
| Total comprehensive (expense)/income for the year | -  | -              | -              | (68.4)                           | 145.3             | 76.9           |
| Employee share schemes:                           |  |                |                |                                  |                   |                |
| Value of services provided                        | -  | -              | -              | -                                | 17.9              | 17.9           |
| Issue of equity share capital                     | -  | 2.6            | -              | -                                | (2.6)             | -              |
| Dividends   | -  | -              | -              | -                                | (130.4)           | (130.4)        |
| <b>At 31 December 2019</b>                        | <b>38.8</b>                                  | <b>1,226.5</b> | <b>15.7</b>    | <b>425.4</b>                     | <b>750.4</b>      | <b>2,456.8</b> |
| <b>Loss for the year</b>                          | <b>-</b>                                     | <b>-</b>       | <b>-</b>       | <b>-</b>                         | <b>(314.2)</b>    | <b>(314.2)</b> |
| Other comprehensive expense for the year          | -  | -              | -              | (76.5)                           | (31.8)            | (108.3)        |
| <b>Total comprehensive expense for the year</b>   | <b>-</b>                                     | <b>-</b>       | <b>-</b>       | <b>(76.5)</b>                    | <b>(346.0)</b>    | <b>(422.5)</b> |
| Employee share schemes:                           |  |                |                |                                  |                   |                |
| Value of services provided                        | -  | -              | -              | -                                | (1.7)             | (1.7)          |
| Issue of equity share capital                     | 0.2  | 0.1            | -              | -                                | (0.3)             | -              |
| <b>At 31 December 2020</b>                        | <b>39.0</b>                                  | <b>1,226.6</b> | <b>15.7</b>    | <b>348.9</b>                     | <b>402.4</b>      | <b>2,032.6</b> |

## CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2020

|   | Notes | 2020<br>£'m    | 2019<br>£'m |
|---|-------|----------------|-------------|
| <b>Non-GAAP measures</b>  |       |                |             |
| Cash inflow from operations before business disposal expenses and exceptional operating items |       | <b>282.9</b>   | 451.1       |
| Cash outflow from business disposal expenses  | 29    | <b>(5.2)</b>   | (9.4)       |
| Cash outflow from exceptional operating items   | 8     | <b>(49.3)</b>  | (27.3)      |
| <b>Cash inflow from operations</b>  | 26    | <b>228.4</b>   | 414.4       |
| Interest received   |       | <b>0.1</b>     | 1.8         |
| Interest paid   |       | <b>(32.2)</b>  | (34.9)      |
| Tax paid  |       | <b>(42.1)</b>  | (14.4)      |
| <b>Cash inflow from operating activities</b>  |       | <b>154.2</b>   | 366.9       |
| Investment acquired   | 16    | <b>(7.6)</b>   | -           |
| Businesses disposed   | 29    | <b>117.0</b>   | 78.3        |
| Capitalised development costs   | 14    | <b>(41.4)</b>  | (54.7)      |
| Capitalised programme participation costs   |       | <b>(1.6)</b>   | (2.0)       |
| Purchase of intangible assets   |       | <b>(11.0)</b>  | (17.2)      |
| Purchase of property, plant and equipment   |       | <b>(80.8)</b>  | (77.2)      |
| Government grants received in respect of purchase of property, plant and equipment            |       | <b>2.1</b>     | -           |
| Proceeds from disposal of property, plant and equipment                                       |       | <b>1.3</b>     | 23.1        |
| <b>Cash outflow from investing activities</b>   |       | <b>(22.0)</b>  | (49.7)      |
| Dividends paid to Company's shareholders  | 12    | -              | (130.4)     |
| Issue of equity share capital   |       | <b>0.3</b>     | -           |
| Proceeds from bank and other borrowings   |       | <b>618.6</b>   | 0.4         |
| Repayments of bank and other borrowings   |       | <b>(705.8)</b> | (213.0)     |
| Debt issue costs paid   |       | <b>(2.4)</b>   | -           |
| Reverse lease premium received  | 26    | <b>3.5</b>     | 18.9        |
| Repayments of lease liabilities   | 18    | <b>(15.4)</b>  | (16.2)      |
| <b>Cash outflow from financing activities</b>   |       | <b>(101.2)</b> | (340.3)     |
| <b>Net increase/(decrease) in cash and cash equivalents</b>                                   |       | <b>31.0</b>    | (23.1)      |
| Cash and cash equivalents at start of the year  |       | <b>155.3</b>   | 181.9       |
| Exchange losses on cash and cash equivalents  |       | <b>(7.7)</b>   | (3.5)       |
| <b>Cash and cash equivalents at end of the year</b>   |       | <b>178.6</b>   | 155.3       |

## NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2020

### 1. General information and basis of preparation

This document contains abridged preliminary financial information for the year ended 31 December 2020 together with comparatives.

Meggitt PLC is a public limited company listed on the London Stock Exchange, domiciled and incorporated in the United Kingdom with the registered number 432989. Meggitt PLC is the parent company of a Group whose principal activities during the year were the design and manufacture of high performance components and sub-systems for aerospace, defence and other specialist markets, including energy, medical, industrial and test.

The information presented has been prepared in accordance with both international accounting standards in conformity with the requirements of the Companies Act 2006 and international financial reporting standards adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union. 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 2020 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 2019 were approved by the Board of Directors on 24 February 2020 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.

#### Going concern

The directors have formed a judgement, at the time of approving the consolidated financial statements, that there is a reasonable expectation that the Group has adequate resources to continue in operational existence for a period of at least 12 months from the date of approval of the Annual Report. For this reason, the directors continue to adopt the going concern basis in preparing the consolidated financial statements.

In making a judgement as to whether the going concern principle should be adopted, the directors have considered the period starting with the date the consolidated financial statements were approved by the Board and ending on 31 March 2022.

#### Actions taken to preserve cash and liquidity

In response to the COVID-19 pandemic, the Group implemented a number of actions to reduce costs, preserve cash and resize the business. These actions are described on page 4. Additionally, to preserve liquidity, during 2020 the Group:

- Arranged a forward start on its revolving USD 750m revolving credit facility, due to mature in September 2021, by the signing of a new one-year USD 575m revolving credit facility maturing in September 2022; and
- Issued USD 300m loan notes to private placement investors which mature in 2023 and 2025.

## 1. General information and basis of preparation (continued)

### Current liquidity

At 31 December 2020, the Group had the following committed credit facilities with its relationship banks and private placement investors:

|   | Maturity date            |                   |                   |              |                | Total<br>£'m   |
|---|--------------------------|-------------------|-------------------|--------------|----------------|----------------|
|   | During assessment period |                   |                   | Subtotal     | Later<br>£'m   |                |
|   | H1<br>2021<br>£'m        | H2<br>2021<br>£'m | Q1<br>2022<br>£'m |              |                |                |
|   |                          |                   |                   | £'m          | £'m            |                |
| USD 750m multi-currency syndicated revolving credit facility* | -                        | 128.2             | -                 | 128.2        | 421.2          | 549.4          |
| USD loan notes issued to private placement investors in 2010  | -                        | -                 | -                 | -            | 91.6           | 91.6           |
| USD bilateral facilities                                      | -                        | -                 | -                 | -            | 91.5           | 91.5           |
| Sterling bilateral facilities                                 | -                        | -                 | -                 | -            | 145.0          | 145.0          |
| USD loan notes issued to private placement investors in 2016  | -                        | -                 | -                 | -            | 439.5          | 439.5          |
| USD loan notes issued to private placement investors in 2020  | -                        | -                 | -                 | -            | 219.8          | 219.8          |
| <b>Total committed credit facilities</b>                      | <b>-</b>                 | <b>128.2</b>      | <b>-</b>          | <b>128.2</b> | <b>1,408.6</b> | <b>1,536.8</b> |

- \* Comprises USD 175m maturing in September 2021, with the balance of USD 575m covered by the additional forward start facility that matures in September 2022.

Additionally, the Group has been confirmed as an eligible issuer under the Bank of England's and HM Treasury's Covid Corporate Financing Facility ('CCFF'), under which the Group can draw up to £600m. The Group is eligible to issue commercial paper under this facility (subject to certain terms and restrictions) up to and including 22 March 2021, with a maturity period of up to 12 months. The Group has no commercial paper issued under this facility at 31 December 2020 or at the date these consolidated financial statements were approved by the Board.

At 31 December 2020, the Group had the following headroom against its committed credit facilities:

|  | Total<br>£'m |
|--|--------------|
| Committed credit facilities                | 1,536.8      |
| Bank and other borrowings                  | 807.3        |
| Less: Cash                                 | (178.6)      |
| Net borrowings excluding lease liabilities | 628.7        |
| <b>Headroom</b>                            | <b>908.1</b> |

### Covenants

The committed credit facilities set out above contain two financial ratio covenants – net debt/EBITDA and interest cover. The covenant calculations are drafted to protect the Group from potential volatility caused by accounting standard changes, sudden movements in exchange rates and exceptional items. This is achieved by measuring EBITDA on a frozen GAAP basis, excluding exceptional operating items and retranslating net debt and EBITDA at similar average exchange rates. Covenant ratios are required to be measured on a trailing 12 month basis twice a year (at 30 June and 31 December), with net debt/EBITDA not to exceed 3.5x and interest cover to be not less than 3.0x. At 31 December 2020, net debt/EBITDA was 2.2x and interest cover was 9.8x. The covenant with the least headroom during the assessment period is net debt/EBITDA at 30 June 2021, which will reflect a full trailing 12 months performance post COVID-19, before an anticipated recovery in H2 2021. No covenant waivers have been sought by the Group.

## 1. General information and basis of preparation (continued)

### **Base case scenario**

The impact on the commercial aerospace segment following the outbreak of COVID-19 is substantial and unprecedented, affecting many areas of the Group's business including its employees, supply chain, customer base and shareholders. To model the expected impact on the Group, a base case model was developed in Q2 2020, which has been regularly updated subsequently to reflect the Group's current view of the most likely impact on its revenues and how this impacts profit and cash flows over the next five years. The current model was prepared for, and reviewed by, the Board in October 2020. In assessing whether the going concern principle remains appropriate, the Group has used the outputs from this model covering the period to 31 March 2022. Where appropriate, the outputs have been adjusted to reflect market dynamics between October 2020 and the date of approval of the Annual Report – these adjustments were also reviewed by the Board. Over the period covered by the going concern assessment, the key assumptions within the base case scenario are:

- For civil AM, ASKs in 2021 are assumed to be approximately 60% of 2019 levels, with recovery weighted towards H2 2021 as the vaccine roll-out enables the easing of lock down restrictions and consumer demand for flights progressively increases. The progressive recovery is assumed to continue into Q1 2022. The Group's civil AM revenue reflects these market factors, its exposure to specific platforms/customers and an assumed spares/MRO mix similar to prior periods.
- For civil OE, aircraft production rates increase modestly in 2021, reflecting emerging build rates from the Group's customer base and the extent to which 2021 aircraft deliveries will be met from existing inventory held by OEMs, particularly on the 737 MAX. Aircraft production rates increase further in 2022, but remain significantly below 2019 levels.
- US defence spending in 2021 remains broadly flat, consistent with the US DOD budget approved in January 2021. No significant changes in levels of US defence spending in 2022 are assumed.
- A modest improvement in the Group's overall gross margin percentage in H1 2021, driven by the full period impact of the cost saving initiatives actioned in 2020, price increases and savings from the Group's footprint initiatives. The Group's gross margin percentage increases progressively over the remainder of the assessment period driven principally by the assumed increase in civil aftermarket volumes, as ASKs start to recover, with a similar civil AM mix assumed to prior periods.
- At a free cash flow level, capital expenditure in 2021 remains at similar levels to 2020, before reducing modestly in 2022 following completion of the Antsy Park facility; UK pension deficit payments continue to be made in accordance with the existing 2018 recovery plan agreed with UK trustees, including certain 2020 deferred payments; and tax payments reflect the payment in H1 2021, notwithstanding the ongoing appeals, of the liability recognised in respect of the Controlled Foreign Company regime.

Under the base case scenario, the Group has sufficient existing committed credit facilities to meet its obligations as they fall due and does not breach either of the financial covenant ratios.

### **Downside scenario ("severe but plausible scenario")**

Due to inherent uncertainty over the extent and pace of recovery in the Group's commercial aerospace markets in particular, the Group also developed a downside scenario in Q2 2020 covering the same period as the base case scenario, and has subsequently updated this regularly as its view of a severe but plausible scenario has evolved. The current model was also prepared for, and reviewed by, the Board in October 2020. To stress test the assumption that the going concern principle remains appropriate under a severe but plausible scenario, the Group has used the outputs from this model covering the period to 31 March 2022. Where appropriate, outputs have been adjusted to reflect market dynamics between October 2020 and the date of approval of the Annual Report – these adjustments were also reviewed by the Board. The downside scenario assumes:

- For civil AM, delays in the global vaccine roll-out programme and the emergence of new COVID-19 variants adversely impact consumers' ability and confidence to resume traveling as quickly as anticipated in the base case. Under this scenario, civil AM revenues are around 8% lower than the base case for 2021. This approximates to a decline in ASKs of 7-10 percentage points compared to the base case, with the reduction significantly weighted towards H2. However, as noted above, the Group's civil AM revenue reflects its exposure to specific platforms/customers and an assumed spares/MRO mix, and does not correlate perfectly to macro ASK drivers.

**1. General information and basis of preparation** (continued)  
**Downside scenario ("Severe but plausible scenario")** (continued)

- For civil OE, weaker customer demand causes airlines to further defer purchases, resulting in reduced production build rates for OEM deliveries, which remain broadly flat over the assessment period.
- Additionally, as a result of the wider impact of a more prolonged pandemic, higher levels of government borrowing lead to defence spending falling modestly from 2020 levels in the assessment period.
- Reduced volumes have a consequential adverse impact on gross margin in the assessment period.
- The Group takes further appropriate mitigating actions to reduce its cost base and to preserve cash flows.

Under the downside scenario, the Group has sufficient financing to be able to meet its obligations as they fall due in the period under assessment. The continued availability of the CCFF during the period has not been assumed. During the assessment period, the Group does not breach either of the financial covenant ratios.

**Principal risks**

The Group has also considered whether its principal risks (as described in note 30) have been appropriately reflected in the downside scenario. In making this assessment, the Group has considered the likelihood of the risks taking place during the going concern assessment period and, were they to occur, the extent to which the impacts would be experienced during this period and the timing of mitigation actions available to the Group. The Group has not assumed that any of the catastrophic events described within its business interruption risk (see note 30) occur during the going concern assessment period. The Board has regularly reviewed these risks throughout the period since the start of the COVID-19 outbreak and up to the date of the financial statements, and has approved an updated Group risk appetite statement with associated risk tolerances to ensure that risks are managed within acceptable limits. The Group has concluded that the downside scenario has been appropriately adjusted to reflect these risks.

**Conclusion**

Based on the above, the directors have therefore concluded there are no material uncertainties around the Group's or Company's ability to continue as a going concern and it is appropriate to adopt the going concern principle in the financial statements.

**2. Accounting policies**

During the year, no new accounting standards, amendments or revisions to existing standards, or interpretations have become effective which had a significant impact on the Group's consolidated financial statements.

**Recent accounting developments**

*Amendments to IAS 37 "Onerous contracts – costs of fulfilling a contract"*

Under IAS 37, a contract is onerous when the unavoidable costs of meeting the contractual obligations exceed the economic benefits arising from the contract. Prior to the amendments to IAS 37, there was diversity in practice as to whether the costs of meeting contractual obligations should comprise only incremental costs (e.g. direct materials and direct labour) or also include an allocation of other direct costs (e.g. factory overheads) which would be incurred regardless of whether the contract was being performed or not. Under the Group's current accounting policy, it only includes incremental direct costs in measuring the costs to fulfil a contract under IAS 37. The IAS 37 amendments clarify however, that the costs of fulfilling a contract should include an allocation of other direct costs. The Group has yet to assess the impact of these amendments, which may result in the recognition of additional onerous contracts and will result in the measurement of existing onerous contract provisions increasing. The amendments are effective for accounting periods beginning on, or after, 1 January 2022 to open contracts at that date, with any additional amounts required to be recognised as an adjustment to retained earnings at that date. These amendments have not been early adopted.

A number of other additional new standards and amendments and revisions to existing standards have been published and are mandatory for the Group's future accounting periods. These have not been early adopted and are not expected to have a significant impact on the Group's consolidated financial statements when they are adopted.

### 3. Critical accounting estimates and judgements

In applying the Group's accounting policies, the Group is required to make certain estimates and judgements concerning the future. These estimates and judgements are regularly reviewed and revised as necessary. The estimates and judgements that have the most significant effect on the amounts included in the consolidated financial statements are described below.

#### **Critical accounting estimates**

##### ***Impairment of goodwill and other assets***

The COVID-19 pandemic has had a dramatic impact in the year on the commercial aerospace industry, with significant uncertainty over the duration of the current disruption to air traffic movements and the eventual pace and extent of the recovery. Forward-looking assessments of Available Seat Kilometres (ASKs) and new aircraft production build rates, which impact the Group's civil aftermarket and OE revenues and hence its cash flows, are therefore subject to significant estimation uncertainty. The area most impacted by this estimation uncertainty is the assessment by the Group of the extent to which goodwill has become impaired (see note 14).

Forward-looking assessments have also significantly impacted the Group's estimates of the recoverable value of development costs, net realisable value of inventory and expected credit losses on trade receivables. Note 8 sets out the impairment losses and other asset write-downs recognised by the Group having completed these assessments. Based on available current information, the Group does not believe any reasonably foreseeable changes in the estimates made would require a material change to the impairment losses or other asset write-downs recognised in respect of these individual asset classes in the next 12 months and accordingly these areas are not considered to be critical estimates.

##### ***Retirement benefit obligations***

The liability recognised in respect of retirement benefit obligations is dependent on a number of estimates, principally those relating to mortality, inflation, salary increases and the rate at which liabilities are discounted. External actuarial advice is taken with regard to the most appropriate assumptions to use (see note 22).

#### **Critical accounting judgements**

##### ***Going concern***

The judgement made by the directors that the going concern basis is appropriate in preparing the consolidated financial statements is a new critical judgement for 2020. The basis for making the judgement, the assumptions made in reaching the judgement and the results of the stress testing performed are set out in note 1.

##### ***Capitalisation of development costs***

The Group is required to make judgements as to when development costs meet the criteria to be recognised as intangible assets. The majority of capitalised development costs relate to technology developed for aerospace programmes. In such cases, costs are typically not capitalised until a contract to develop the technology is awarded by a customer as, prior to this date, it is generally not possible to reliably estimate the point at which research activities conclude and development activities commence. Absent a contract to develop the technology, the Group also does not believe there is generally sufficient certainty over the future economic benefits that will be generated from the technology, to allow capitalisation of costs. Once such a contract is awarded, the Group capitalises development costs provided it expects to retain the intellectual property in the technology throughout substantially all of the life of the aircraft or engine and it is probable that future economic benefits will flow to the Group. In making a judgement as to whether economic benefits will flow to the Group, the Group makes estimates of aircraft or engine volumes (taking into account the extent to which the Group has a sole-source position), aftermarket revenues which are dependent on aircraft utilisation, fleet lives and operator service routines, costs of manufacture and costs to complete the development activity. During 2020, the Group recognised £41.4m (2019: £54.7m) of development costs as an intangible asset (see note 14).

#### 4. Segmental analysis

The Group manages its businesses under four customer-aligned divisions: Airframe Systems, Engine Systems, Energy & Equipment and Services & Support.

The key performance measure reviewed by the Chief Operating Decision Maker ('CODM') is underlying operating profit. The CODM has been identified as the Board.

##### Year ended 31 December 2020

|   | Airframe<br>Systems<br>£'m | Engine<br>Systems<br>£'m | Energy &<br>Equipment<br>£'m | Services &<br>Support<br>£'m | Other *<br>£'m | Total<br>£'m   |
|---|----------------------------|--------------------------|------------------------------|------------------------------|----------------|----------------|
| Gross segment revenue                                   | 972.7                      | 338.8                    | 358.5                        | 326.6                        | -              | 1,996.6        |
| Inter-segment revenue                                   | (179.6)                    | (105.2)                  | (23.5)                       | (4.2)                        | -              | (312.5)        |
| <b>Revenue from external customers</b>                  | <b>793.1</b>               | <b>233.6</b>             | <b>335.0</b>                 | <b>322.4</b>                 | -              | <b>1,684.1</b> |
| At a point in time                                      | 754.2                      | 219.9                    | 161.2                        | 315.2                        | -              | 1,450.5        |
| Over time: Power by the hour/ Cost<br>per brake landing | 22.2                       | 4.4                      | -                            | 7.2                          | -              | 33.8           |
| Over time: Other  | 16.7                       | 9.3                      | 173.8                        | -                            | -              | 199.8          |
| Revenue by basis of recognition                         | <b>793.1</b>               | <b>233.6</b>             | <b>335.0</b>                 | <b>322.4</b>                 | -              | <b>1,684.1</b> |
| <b>Underlying operating profit/(loss)**</b>             | <b>120.5</b>               | <b>(13.2)</b>            | <b>42.4</b>                  | <b>40.8</b>                  | -              | <b>190.5</b>   |

##### Year ended 31 December 2019 (restated)\*\*\*

|   | Airframe<br>Systems<br>£'m | Engine<br>Systems<br>£'m | Energy &<br>Equipment<br>£'m | Services &<br>Support<br>£'m | Other *<br>£'m | Total<br>£'m   |
|---|----------------------------|--------------------------|------------------------------|------------------------------|----------------|----------------|
| Gross segment revenue                                   | 1,451.7                    | 341.2                    | 450.3                        | 519.0                        | 5.6            | 2,767.8        |
| Inter-segment revenue                                   | (422.2)                    | (11.7)                   | (37.8)                       | (19.9)                       | -              | (491.6)        |
| Revenue from external customers                         | <b>1,029.5</b>             | <b>329.5</b>             | <b>412.5</b>                 | <b>499.1</b>                 | <b>5.6</b>     | <b>2,276.2</b> |
| At a point in time                                      | 984.3                      | 312.6                    | 244.3                        | 487.5                        | 5.6            | 2,034.3        |
| Over time: Power by the hour/ Cost<br>per brake landing | 35.2                       | 7.2                      | -                            | 11.6                         | -              | 54.0           |
| Over time: Other  | 10.0                       | 9.7                      | 168.2                        | -                            | -              | 187.9          |
| Revenue by basis of recognition                         | <b>1,029.5</b>             | <b>329.5</b>             | <b>412.5</b>                 | <b>499.1</b>                 | <b>5.6</b>     | <b>2,276.2</b> |
| Underlying operating profit**                           | <b>247.7</b>               | <b>27.2</b>              | <b>53.4</b>                  | <b>74.0</b>                  | <b>0.5</b>     | <b>402.8</b>   |

\* Those businesses which were disposed of prior 1 January 2019, the effective date of the new divisional structure, or were classified as held for sale at that date, are presented separately as 'Other'.

\*\* Central costs are allocated using a variety of bases designed to reflect the beneficial relationship between costs and segments. Bases include headcount, payroll costs, gross assets and revenue. A detailed reconciliation of underlying operating profit to operating profit is shown in note 6.

\*\*\* Prior year figures have been restated to reflect the transfer of the external customer facing relationships for the UK braking systems maintenance, repair and overhaul business from Airframe Systems to Services & Support with effect from 1 January 2020. The restatement comprised external revenue of £27.9m and underlying operating profit of £2.8m.

#### 4. Segmental analysis continued

##### Segmental assets

|   | 2020<br>£'m    | 2019**<br>£'m  |
|---|----------------|----------------|
| Airframe Systems                                  | 1,036.5        | 1,142.0        |
| Engine Systems                                    | 356.2          | 437.5          |
| Energy & Equipment                                | 234.3          | 306.8          |
| Services & Support                                | 90.4           | 82.7           |
| <b>Total segmental trading assets</b>             | <b>1,717.4</b> | <b>1,969.0</b> |
| Centrally managed trading assets*                 | 167.4          | 162.1          |
| Goodwill  | 1,519.5        | 1,966.6        |
| Other intangible assets excluding software assets | 328.6          | 424.0          |
| Investments                                       | 20.8           | 14.1           |
| Derivative financial instruments – non-current    | 15.0           | 14.6           |
| Deferred tax assets                               | 19.2           | 23.3           |
| Derivative financial instruments – current        | 5.4            | 3.8            |
| Current tax recoverable                           | 11.5           | 11.1           |
| Cash and cash equivalents                         | 178.6          | 155.3          |
| Assets classified as held for sale                | 14.7           | -              |
| <b>Total assets</b>                               | <b>3,998.1</b> | <b>4,743.9</b> |

\* 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.

\*\* Prior year figures have been restated to reflect the transfer of the external customer facing relationships for the UK braking systems maintenance, repair and overhaul business from Airframe Systems to Services & Support with effect from 1 January 2020. The restatement comprised segmental trading assets of £5.4m.

#### 5. Operating income

Operating profit is stated after crediting:

|  | 2020<br>£'m | 2019<br>£'m |
|--|-------------|-------------|
| Gain on disposal of property, plant and equipment                                | -           | 0.9         |
| Amounts arising on the acquisition, disposal and closure of businesses (note 6a) | 32.0        | 23.5        |
| Financial instruments – gain   | -           | 15.0        |
| Net foreign exchange gains   | -           | 3.4         |
| Share of profit after tax of joint venture                                       | -           | 1.7         |
| Other income   | 5.5         | 4.5         |
| <b>Operating income</b>  | <b>37.5</b> | <b>49.0</b> |

## 6. Reconciliations between profit and underlying profit

Underlying profit is used by the Board to monitor and measure the underlying trading performance of the Group. Items excluded from underlying profit measures are treated consistently with the way performance is measured under the Group's short-term and long-term incentive plans and with covenant requirements defined in the Group's committed credit facilities.

|   | 2020<br>£'m    | 2019<br>£'m |
|---|----------------|-------------|
| <b>Operating (loss)/profit</b>  | <b>(297.3)</b> | 325.3       |
| Amounts arising on the acquisition, disposal and closure of businesses (a)    | <b>(32.0)</b>  | (23.5)      |
| Amortisation of intangible assets acquired in business combinations (note 14) | <b>88.2</b>    | 89.8        |
| Financial instruments loss/(gain) (note 7)                                    | <b>2.9</b>     | (15.0)      |
| Exceptional operating items (note 8)  | <b>428.7</b>   | 26.2        |
| Adjustments to operating profit*  | <b>487.8</b>   | 77.5        |
| <b>Underlying operating profit</b>  | <b>190.5</b>   | 402.8       |
| <b>(Loss)/profit before tax</b>   | <b>(334.0)</b> | 286.7       |
| Adjustments to operating profit per above                                     | <b>487.8</b>   | 77.5        |
| Net interest expense on retirement benefit obligations (note 9)               | <b>5.7</b>     | 6.1         |
| Adjustments to profit before tax  | <b>493.5</b>   | 83.6        |
| <b>Underlying profit before tax</b>   | <b>159.5</b>   | 370.3       |
| <b>(Loss)/profit for the year</b>   | <b>(314.2)</b> | 222.6       |
| Adjustments to profit before tax per above                                    | <b>493.5</b>   | 83.6        |
| Tax effect of adjustments to profit before tax                                | <b>(51.2)</b>  | (17.5)      |
| Adjustments to profit for the year  | <b>442.3</b>   | 66.1        |
| <b>Underlying profit for the year</b>   | <b>128.1</b>   | 288.7       |

\* Of the adjustments to operating profit, £39.0m (2019: £8.1m) relating to exceptional operating items has been charged to cost of sales, with the balance of £448.8m (2019: £69.4m) 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 acquired businesses or receivable in respect of disposed businesses and costs directly attributable to the acquisition and disposal of businesses.

|   | 2020<br>£'m   | 2019<br>£'m |
|---|---------------|-------------|
| Gain on disposal of businesses in the current year (note 29)                  | <b>(33.3)</b> | (23.5)      |
| Amounts recognised in respect of disposals in prior periods                   | <b>1.3</b>    | -           |
| <b>Amounts arising on the acquisition, disposal and closure of businesses</b> | <b>(32.0)</b> | (23.5)      |

## 7. Financial instruments

To ensure appropriate and timely commercial decisions are made as to when and how to mitigate the Group's foreign currency and interest rate exposures, gains and losses arising from the marking to market of financial instruments that are not hedge accounted are excluded from underlying profit measures.

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.

When interest rate derivatives qualify to be hedge accounted, any difference recognised in the income statement as hedge ineffectiveness between movements in fair value of derivatives and fair value of fixed rate borrowings is excluded from underlying profit measures.

|  | 2020<br>£'m   | 2019<br>£'m |
|--|---------------|-------------|
| Movement in fair value of foreign currency forward contracts                     | <b>(15.9)</b> | (25.7)      |
| Impact of retranslating net foreign currency assets and liabilities at spot rate | <b>6.5</b>    | (0.2)       |
| Movement in fair value of interest rate derivatives                              | <b>1.6</b>    | (0.3)       |
| Movement in fair value of fixed rate borrowings due to interest rate risk        | <b>(1.6)</b>  | (0.1)       |
| Movement in fair value of cross currency derivatives                             | <b>12.8</b>   | 11.8        |
| Movement in fair value of treasury lock derivative                               | <b>(0.5)</b>  | (0.5)       |
| <b>Financial instruments – loss/(gain)</b>                                       | <b>2.9</b>    | (15.0)      |

## 8. Exceptional operating items

Delivery of the Group's strategy includes the restructuring of its cost base to deliver operational improvements. The exclusion from underlying profit measures of significant items arising from site consolidations, business restructuring and integration of acquired businesses is designed by the Board to align short-term operational decisions with this longer-term strategy. In addition, the impact of the global COVID-19 pandemic, and the resulting uncertainty facing the commercial aerospace industry, have given rise to significant non-recurring impairment losses and asset write-downs which have been treated as exceptional operating items.

|   | Note | Income statement |             | Cash flow    |             |
|---|------|------------------|-------------|--------------|-------------|
|   |      | 2020<br>£'m      | 2019<br>£'m | 2020<br>£'m  | 2019<br>£'m |
| Impairment losses and other asset write-downs | a    | <b>374.2</b>     | -           | -            | -           |
| COVID – 19 incremental non-recurring costs    | b    | <b>22.0</b>      | -           | <b>18.9</b>  | -           |
| Site consolidations                           | c    | <b>33.5</b>      | 20.1        | <b>31.6</b>  | 22.4        |
| Business restructuring costs and other items  | d    | <b>(1.0)</b>     | 6.1         | <b>(1.2)</b> | 4.9         |
| <b>Exceptional operating items</b>            |      | <b>428.7</b>     | 26.2        | <b>49.3</b>  | 27.3        |

- a. The Group has recognised material impairment losses and other reductions in asset values arising from the current uncertainty facing the commercial aerospace industry. These have been aggregated and classified as an exceptional operating item given their size and that they all arise from the unprecedented circumstances that the industry has experienced in 2020. This treatment is consistent with the Group's policy, with impairment losses and other asset write downs following the cancellation of the Dassault 5X programme, treated as an exceptional operating item in 2017.

Following the COVID-19 outbreak, governments have imposed strict travel restrictions contributing to a dramatic reduction in flight numbers and passenger load factors, the parking by operators of record numbers of aircraft, several airlines filing for bankruptcy and OE customers significantly reducing production levels. These events, together with uncertainty over the extent and pace of recovery in the sector, have impacted the reliability of forecasts for commercial aerospace more generally and also for specific aircraft platforms. Whilst management believes the COVID-19 outbreak is directly responsible for substantially all of the amounts recorded, it recognises the inherent difficulties in making a reliable estimate of the impact directly attributable to the pandemic and accordingly has not disclosed the amounts as related solely to COVID-19 or attempted to quantify the COVID-19 specific element.

## 8. Exceptional operating items continued

The amounts recognised in the year comprise:

|  | Cost of sales<br>£'m | Operating costs<br>£'m | Total<br>£'m |
|--|----------------------|------------------------|--------------|
| Impairment of goodwill* (note 14)                    | -                    | 335.7                  | 335.7        |
| Impairment of development costs (note 14)            | -                    | 24.5                   | 24.5         |
| Write down of inventory to net realisable value      | 8.6                  | -                      | 8.6          |
| Expected credit losses on trade receivables          | -                    | 5.4                    | 5.4          |
| <b>Impairment losses and other asset write-downs</b> | <b>8.6</b>           | <b>365.6</b>           | <b>374.2</b> |

- \* The goodwill impairment charge is lower than that recognised in the interim condensed consolidated financial statements solely due to retranslation of the amounts relating to foreign currency denominated goodwill at the average exchange rates for the year.

To the extent any of the impairment losses or asset write-downs recognised in the current year are reversed in a subsequent period, the reversals will be recognised as exceptional operating items.

The tax credit in respect of these items was £18.8m.

- b. In 2020, given its significance, the Group has excluded income and expenditure directly attributable to the global COVID-19 pandemic, and which is not expected to recur in future periods, from its underlying profit measures. This principally relates to severance costs arising from the Group's announcement on 23 April 2020 that it would be reducing its global workforce by around 15% in response to the COVID-19 outbreak. Other amounts include additional cleaning costs; the purchase of personal protective equipment; and shift premiums and other associated costs arising from social distancing measures. Of the amounts classified as exceptional operating items, £11.5m has been recognised within cost of sales, with the balance of £10.5m recognised within other operating costs. The tax credit in respect of these items was £4.9m.
- c. Amounts principally relate to costs incurred in respect of the Group's previously announced plans to reduce its footprint by the end of 2021. Cumulative costs since the announcement are £97.2m. In 2020, costs are principally in respect of the move to the new facility at Ansty Park in the West Midlands, UK which will enable the Group to consolidate a range of manufacturing, engineering and support operations into a single centre of excellence and the move of one of its Energy & Equipment businesses following the disposal of a number of its product lines in 2019. Of the amounts classified as exceptional operating items, £18.9m has been recognised within cost of sales with the balance of £14.6m recognised within other operating costs. The tax credit in respect of these items was £8.8m.
- d. In 2020, this includes a credit of £1.5m relating to the reversal of amounts previously recognised as exceptional operating items, following the recovery of costs from a third party.

## 9. Net finance costs

|  | 2020<br>£'m | 2019<br>£'m |
|--|-------------|-------------|
| Interest on bank deposits  | 0.1         | 1.4         |
| Unwinding of interest on other receivables                           | 0.2         | 0.5         |
| Other finance income   | 0.2         | 0.3         |
| <b>Finance income</b>  | <b>0.5</b>  | 2.2         |
| Interest on bank borrowings  | 1.3         | 1.2         |
| Interest on senior notes   | 24.5        | 29.4        |
| Interest on lease liabilities  | 6.0         | 5.0         |
| Unwinding of discount on provisions (note 21)                        | 0.7         | 1.2         |
| Net interest expense on retirement benefit obligations (note 6)      | 5.7         | 6.1         |
| Amortisation of debt issue costs                                     | 0.8         | 0.7         |
| Less: amounts capitalised in the cost of qualifying assets (note 14) | (1.8)       | (2.8)       |
| <b>Finance costs</b>   | <b>37.2</b> | 40.8        |
| <b>Net finance costs</b>   | <b>36.7</b> | 38.6        |

## 10. Tax

The statutory tax credit for the year was £19.8m (2019: charge of £64.1m) based on the reported loss before tax of £334.0m (2019: profit of £286.7m). Based on underlying profit before tax of £159.5m (2019: £370.3m) the Group's underlying tax rate for the current year was 19.7% (2019: 22.0%).

The Finance Act 2020 introduced legislation to cancel the planned reduction in the main rate of corporation tax in the UK from 19% to 17%. The legislation which was substantively enacted in the year, has resulted an increase in the current tax charge of £1.3m.

## 11. (Loss)/earnings per ordinary share

Earnings per ordinary share ('EPS') is calculated by dividing the loss attributable to equity owners of the Company of £314.2m (2019: profit of £222.6m) by the weighted average number of shares in issue during the year of 777.8m (2019: 773.7m). The weighted average number of shares excludes shares bought by the Group and held during the year by an independently managed Employee Share Ownership Plan Trust. The weighted average number of own shares excluded is 3.6m shares (2019: 4.0m shares).

Underlying EPS is based on underlying profit for the year (note 6) and the same number of shares used in the calculation of basic EPS. It is reconciled to basic EPS below:

|  | 2020<br>Pence | 2019<br>Pence |
|--|---------------|---------------|
| <b>Basic EPS</b>   | <b>(40.4)</b> | 28.8          |
| Adjust for effects of:   |               |               |
| Amounts arising on the acquisition, disposal and closure of businesses | (4.2)         | (2.0)         |
| Amortisation of intangible assets acquired in business combinations    | 9.2           | 8.8           |
| Financial instruments – loss/(gain)                                    | 0.3           | (1.6)         |
| Exceptional operating items  | 51.0          | 2.7           |
| Net interest expense on retirement benefit obligations                 | 0.6           | 0.6           |
| <b>Underlying basic EPS</b>  | <b>16.5</b>   | 37.3          |

Diluted EPS for the year is (40.4p) (2019: 28.3p). 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 789.4m (2019: 785.8m). Underlying diluted EPS for the year is 16.2p (2019: 36.7p). The calculation of underlying diluted EPS is based on underlying profit (note 6) and the same weighted average number of shares used in the calculation of diluted EPS.

## 12. Dividends

On 27 March 2020, the Group announced that the Board had decided that it was prudent to withdraw the recommendation to pay the final dividend in respect of the year ended 31 December 2019 of 11.95 pence per share. That action, together with a series of significant measures to reduce costs and tightly manage cash flow, was taken to further strengthen the financial position and liquidity of the Group. The directors did not recommend the payment of an interim dividend in respect of 2020 and no final dividend in respect of 2020 is to be proposed at the Annual General Meeting on 29 April 2021 for the same reasons.

## 13. Related party transactions

The remuneration of key management personnel of the Group, which is defined for 2020 as members of the Board and the Group Executive Committee, is set out below.

|   | 2020<br>£'m | 2019<br>£'m |
|---|-------------|-------------|
| Salaries and other short-term employee benefits | 4.7         | 10.8        |
| Share-based payment (credit)/expense            | (0.5)       | 2.5         |
| <b>Total</b>                                    | <b>4.2</b>  | <b>13.3</b> |

## 14. Intangible assets

|   | Goodwill<br>£'m | Development<br>Costs<br>£'m | Programme<br>participation<br>costs<br>£'m | Other<br>intangible<br>assets<br>£'m |
|---|-----------------|-----------------------------|--|--------------------------------------|
| At 1 January 2019   | 2,035.3         | 557.1                       | 18.2                                       | 610.4                                |
| Exchange rate adjustments                                   | (57.9)          | (16.3)                      | (0.7)                                      | (15.0)                               |
| Businesses disposed   | (10.8)          | (0.9)                       | -  | -                                    |
| Additions   | -               | 54.7                        | 1.6  | 17.2                                 |
| Interest capitalised (note 9)                               | -               | 2.8                         | -  | -                                    |
| Transfers from contract assets                              | -               | 7.2                         | -  | -                                    |
| Disposals   | -               | -                           | -  | (0.4)                                |
| Amortisation*   | -               | (28.7)                      | (1.1)                                      | (108.6)                              |
| At 31 December 2019   | 1,966.6         | 575.9                       | 18.0                                       | 503.6                                |
| Exchange rate adjustments                                   | (22.9)          | (7.6)                       | (0.7)                                      | (7.3)                                |
| Businesses disposed (note 29)                               | (84.8)          | (19.7)                      | -  | (0.1)                                |
| Additions   | -               | 41.4                        | 2.6  | 13.2                                 |
| Interest capitalised (note 9)                               | -               | 1.8                         | -  | -                                    |
| Transferred to assets classified as held for sale (note 17) | (3.7)           | -                           | -  | -                                    |
| Transfers to contract assets                                | -               | (1.8)                       | -  | -                                    |
| Disposals   | -               | (1.0)                       | -  | (0.4)                                |
| Impairment losses*  | (335.7)         | (25.6)                      | -  | -                                    |
| Amortisation**  | -               | (31.5)                      | (1.2)                                      | (107.9)                              |
| <b>At 31 December 2020</b>                                  | <b>1,519.5</b>  | <b>531.9</b>                | <b>18.7</b>                                | <b>401.1</b>                         |

\* Included within impairment losses is £335.7m (2019: £Nil) relating to goodwill and £24.5m (2019: £Nil) relating to development costs which have been recognised as exceptional operating items and excluded from the Group's underlying profit figures (note 6)

\*\* Included within amortisation of other intangible assets is £88.2m (2019: £89.8m) relating to intangible assets acquired in business combinations and which is excluded from the Group's underlying profit figures (note 6).

## 14. Intangible assets continued

### Goodwill

#### Impairment testing – trigger event

On 19 March 2020, the Group released a trading update in response to the COVID-19 pandemic including an announcement that in light of the highly fluid market and global macro-economic situation, it was too early to provide earnings guidance for the remainder of the 2020. The Group considered this to be the date a trigger event under IAS 36 'Impairment of Assets' occurred and therefore performed an additional impairment test of its goodwill balances at the end of March, the closest month end date to this announcement.

For the purpose of impairment testing, the Group used value-in-use calculations to determine recoverable amounts as it did not believe reliable estimates of fair value less costs of disposal existed given the current market uncertainty. No changes were made in 2020 to the level at which impairment testing was performed. The key assumptions for the value in use calculations for all CGUs and groups of CGUs are discussed in note 14 of the 2020 Interim Results on pages 29 to 30 together with details of sensitivity testing.

As a result of the impairment test, impairment losses of £335.7m have been recognised as an exceptional operating item (see note 8). The impairment charge in the year is analysed by CGU or group of CGUs as follows:

|                               | <u>£'m</u>          |
|-------------------------------|---------------------|
| Airframe Systems              | 122.3               |
| Engine Systems                | 199.7               |
| Energy & Equipment - Fribourg | 13.7                |
| <b>Total (note 8)*</b>        | <b><u>335.7</u></b> |

- \* The goodwill impairment charge is lower than that recognised in the interim condensed consolidated financial statements solely due to retranslation of the amounts relating to foreign currency denominated goodwill at the average exchange rates for the year.

#### Impairment testing subsequent to the trigger event

The Group has assessed whether, at 31 December 2020, there are indicators that an additional impairment charge would be required and concluded that such indicators do not exist. This was supported by a review of:

- Assets allocated to each of the CGUs and groups of CGUs, for which an impairment loss was recognised following the trigger event impairment testing. These had decreased modestly between the trigger event impairment test date (after recording the impairment losses) and 31 December 2020;
- Cash flow estimates for the periods covered by management estimates. The Group's current five year base case and downside scenarios, the earlier years of which were used in the going concern assessment judgement (see note 1), and the probability weightings that management would assign to these scenarios, were compared with the equivalent scenarios used for the trigger event impairment test. Between the trigger event impairment testing date and 31 December 2020, whilst a second wave of global lockdown restrictions has taken place, there were also a number of vaccines announced which were in the process of obtaining regulatory approval and which subsequent to the balance sheet date have received approval and are being rolled out globally. When comparing the current cash flow estimates, which capture a greater part of the anticipated recovery in the aerospace industry by using the five-year period to 31 December 2025, rather than the five-year period to 31 March 2025 at the impairment test trigger event date, no indicators of an additional impairment were identified;
- Growth rates for periods beyond those covered by management estimates. Management's own estimates of long term growth rates had not changed and long term inflation forecasts for the countries in which the CGUs and groups of CGUs operate have either remained at the same levels, or increased modestly at 31 December 2020, since the trigger event impairment test date; and
- Discount rates at 31 December 2020. These were recalculated at 31 December 2020 and had decreased since the trigger event impairment test for all CGUs and groups of CGUs.

## 15. Property, plant and equipment

|  | 2020<br>£'m  | 2019<br>£'m  |
|--|--------------|--------------|
| At 1 January   | 449.4        | 404.0        |
| Exchange rate adjustments                                | (6.8)        | (11.2)       |
| Businesses disposed (note 29)                            | (6.8)        | (6.2)        |
| Additions  | 83.0         | 132.9        |
| Transfer to assets classified as held for sale (note 17) | (1.7)        | -            |
| Disposals  | (1.6)        | (12.8)       |
| Depreciation *   | (56.7)       | (57.3)       |
| <b>At 31 December</b>                                    | <b>458.8</b> | <b>449.4</b> |

- \* The depreciation charge for the year includes £3.8m which has been charged to exceptional operating items (2019: £1.4m).

## 16. Investments

The Group's investments in its joint ventures, Meggitt UTC Aerospace Systems, LLC and HiETA Technologies Limited are accounted for using the equity method and are stated as follows:

|                                  | 2020<br>£'m | 2019<br>£'m |
|----------------------------------|-------------|-------------|
| At 1 January                     | 14.1        | 12.9        |
| Exchange rate adjustments        | (0.5)       | (0.5)       |
| Additions*                       | 10.4        | -           |
| Share of (loss)/profit after tax | (3.2)       | 1.7         |
| <b>At 31 December</b>            | <b>20.8</b> | <b>14.1</b> |

- \* In January 2020, the Group acquired a 33% investment in HiETA Technologies Ltd, a UK company with world-leading capabilities in metal additive manufacturing and a focus on developing new ways to make heat exchangers using additive manufacturing technology. The investment comprised £7.6m paid in cash in the year and contingent consideration of £2.8m.

## 17. Assets classified as held for sale

In December 2020, the sale of the Group's aircraft ducting business, based in Dunstable UK, together with a small product line from one of the Group's other businesses was agreed. Accordingly, the related assets of the business have been classified as a disposal group held for sale and are presented separately at the balance sheet date together with directly associated liabilities. The sale completed on 30 January 2021 for a cash consideration of £20.2m, subject to an adjustment for working capital in the business at the date of disposal.

|                            | 2020  |   | Total<br>£'m |
|----------------------------|---|---|--------------|
|                            | Assets<br>classified as<br>held for sale<br>£'m | Liabilities directly<br>associated with<br>assets classified<br>as held for sale<br>£'m |              |
| At 1 January 2020          | -   | -   | -            |
| Additions                  | 14.7  | (3.7)   | 11.0         |
| <b>At 31 December 2020</b> | <b>14.7</b>                                     | <b>(3.7)</b>  | <b>11.0</b>  |

  

|  | Total<br>£'m |
|--|--------------|
| Goodwill (note 14)   | 3.7          |
| Property, plant and equipment (note 15)  | 1.7          |
| Inventories  | 5.2          |
| Trade and other receivables  | 4.1          |
| <b>Assets classified as held for sale</b>                                      | <b>14.7</b>  |
| Trade and other payables   | (1.4)        |
| Contract liabilities   | (1.1)        |
| Provisions (note 21)   | (0.1)        |
| Lease liabilities  | (1.1)        |
| <b>Liabilities directly associated with assets classified as held for sale</b> | <b>(3.7)</b> |

## 18. Lease Liabilities

The Group leases various factories, warehouses, offices, plant and equipment. The following amounts are included in respect of its leases:

|   | 2020<br>£'m | 2019<br>£'m |
|---|-------------|-------------|
| Depreciation charge for right-of-use assets               | 16.0        | 16.5        |
| Additions to right-of-use assets*                         | 11.4        | 55.5        |
| Net book amount of right-of-use assets                    | 104.6       | 116.0       |
| Interest on lease liabilities (note 9)                    | 6.0         | 5.0         |
| Expense related to short-term leases and low-value assets | 0.6         | 0.1         |
| Net cash outflow for leases**                             | 17.9        | 1.4         |

\* In 2019, this includes £38.4m relating to the new Ansty Park site which has a lease term of 30 years.

\*\* Comprises capital payments of £15.4m (2019: £16.2m) and interest payments of £6.0m (2019: £4.1m), less a reverse lease premium received of £3.5m (2019: £18.9m) relating to the new Ansty Park site.

## 19. Bank and other borrowings

|                            | Current<br>£'m | Non-current<br>£'m | Total<br>£'m |
|----------------------------|----------------|--------------------|--------------|
| At 1 January 2020          | 219.4          | 694.5              | 913.9        |
| Exchange rate adjustments  | 9.1            | (22.2)             | (13.1)       |
| Proceeds                   | 132.1          | 486.5              | 618.6        |
| Repayments                 | (347.2)        | (358.6)            | (705.8)      |
| Debt issue costs paid      | -              | (2.4)              | (2.4)        |
| Other movements            | (2.9)          | (1.0)              | (3.9)        |
| <b>At 31 December 2020</b> | <b>10.5</b>    | <b>796.8</b>       | <b>807.3</b> |

### Analysed as:

|                            | 2020<br>£'m  | 2019<br>£'m  |
|----------------------------|--------------|--------------|
| Bank loans                 | 2.2          | 0.2          |
| Other loans*               | 8.3          | 219.2        |
| <b>Current portion</b>     | <b>10.5</b>  | <b>219.4</b> |
| Bank loans                 | 43.7         | 141.4        |
| Other loans                | 753.1        | 553.1        |
| <b>Non-current portion</b> | <b>796.8</b> | <b>694.5</b> |

## 20. Financial Instruments – fair value measurement

For trade and other receivables, contract assets, cash and cash equivalents, trade and other payables and contract liabilities, fair values approximate to book values due to the short maturity periods of these financial instruments. For trade and other receivables and contract assets, allowances are made within their book value for credit risk. As required by IFRS 7 'Financial Instruments: Disclosures', a comparison of book values and fair values for certain other financial instruments is provided below:

|  | Book value     |                | Fair value     |                |
|--|----------------|----------------|----------------|----------------|
|  | 2020<br>£'m    | 2019<br>£'m    | 2020<br>£'m    | 2019<br>£'m    |
| Derivative financial instruments – non-current | 15.0           | 14.6           | 15.0           | 14.6           |
| Derivative financial instruments – current     | 5.4            | 3.8            | 5.4            | 3.8            |
| <b>Financial assets</b>                        | <b>20.4</b>    | <b>18.4</b>    | <b>20.4</b>    | <b>18.4</b>    |
| Derivative financial instruments – current     | (21.6)         | (16.5)         | (21.6)         | (16.5)         |
| Bank and other borrowings – current            | (10.5)         | (219.4)        | (10.5)         | (220.7)        |
| Derivative financial instruments – non-current | (0.3)          | (4.6)          | (0.3)          | (4.6)          |
| Bank and other borrowings – non-current        | (796.8)        | (694.5)        | (813.1)        | (702.7)        |
| <b>Financial liabilities</b>                   | <b>(829.2)</b> | <b>(935.0)</b> | <b>(845.5)</b> | <b>(944.5)</b> |
| <b>Total</b>                                   | <b>(808.8)</b> | <b>(916.6)</b> | <b>(825.1)</b> | <b>(926.1)</b> |

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. Credit risk is not significant for these instruments.

## 20. Financial Instruments – fair value measurement continued

The current and non-current elements of fixed rate bank and other borrowings measured at fair value, are classified as level 3 in the fair value measurement hierarchy, as they have 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 values attributable to interest rate risk have 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 values attributable to credit risk have been derived from quotes from lenders for borrowings of similar amounts and maturity years. The same methods of valuation have been used to derive the fair values of the current and non-current elements of fixed rate bank and other borrowings which are 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:

|  | 2020<br>£'m  | 2019<br>£'m  |
|--|--------------|--------------|
| Held at fair value through profit and loss | 95.0         | 234.6        |
| Held at amortised cost                     | 712.3        | 679.3        |
| <b>Total</b>                               | <b>807.3</b> | <b>913.9</b> |

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

The Group designates loans that are in a hedge relationship with interest rate swaps as fair value through profit and loss. The difference between fair values and contractual amounts at maturity of the current and non-current elements of bank and other borrowings designated as fair value through profit and loss is as follows:

|  | 2020<br>£'m | 2019<br>£'m  |
|--|-------------|--------------|
| Contractual amount payable at maturity                                       | 91.6        | 227.1        |
| Cumulative fair value adjustments arising from changes in interest rate risk | 4.8         | 6.4          |
| Cumulative fair value adjustments arising from changes in credit risk        | (1.5)       | 0.3          |
| Accrued interest and debt costs  | 0.1         | 0.8          |
| <b>Fair value</b>  | <b>95.0</b> | <b>234.6</b> |

Changes in fair value in the year are as follows:

|   | 2020<br>£'m | 2019<br>£'m  |
|---|-------------|--------------|
| Bank and other borrowings at fair value through profit and loss:                                |             |              |
| At 1 January  | 234.6       | 242.7        |
| Exchange rate adjustments   | 2.6         | (8.1)        |
| Settled upon maturity   | (138.1)     | -            |
| Gain recognised in net operating costs due to interest rate risk                                | (1.6)       | (0.1)        |
| (Gain)/loss recognised in net finance costs due to movements in accrued interest and debt costs | (0.7)       | 0.1          |
| Gain recognised in other comprehensive income due to changes in credit risk                     | (1.8)       | -            |
| <b>At 31 December</b>   | <b>95.0</b> | <b>234.6</b> |

The largest movement in credit spread seen in a six-month period since inception of the borrowings is 100 basis points. A 100 basis point movement in the credit spread, used as an input in determining fair values at 31 December 2020, would impact other comprehensive income by approximately £1.4m.

## 21. Provisions

|   | <b>2020</b>  |
|---|--------------|
|   | <b>£'m</b>   |
| At 1 January  | 100.6        |
| Exchange rate adjustments                                   | (2.8)        |
| Businesses disposed   | (0.8)        |
| Transferred to assets classified as held for sale (note 17) | (0.1)        |
| Additional provisions                                       | 41.2         |
| Unused amounts reversed                                     | (4.8)        |
| Charge to net finance costs (note 9)                        | 0.7          |
| Transfers to trade and other payables                       | (0.5)        |
| Amounts utilised  | (20.6)       |
| <b>At 31 December</b>                                       | <b>112.9</b> |

|                       | <b>2020</b>  | 2019  |
|-----------------------|--------------|-------|
|                       | <b>£'m</b>   | £'m   |
| <b>Disclosed as:</b>  |              |       |
| Current               | <b>32.6</b>  | 36.2  |
| Non-current           | <b>80.3</b>  | 64.4  |
| <b>At 31 December</b> | <b>112.9</b> | 100.6 |
| <b>Analysed as:</b>   |              |       |
| Environmental*        | <b>72.7</b>  | 66.7  |
| Onerous contracts     | <b>13.0</b>  | 13.3  |
| Warranty costs        | <b>16.0</b>  | 14.8  |
| Other                 | <b>11.2</b>  | 5.8   |
| <b>At 31 December</b> | <b>112.9</b> | 100.6 |

\* Included within other receivables is £18.8m (2019: £17.0m) in respect of amounts recoverable from insurers and other third parties in respect of environmental issues relating to historic sites.

## 22. Retirement benefit obligations

|   | 2020<br>£'m  | 2019<br>£'m  |
|---|--------------|--------------|
| At 1 January                                      | 267.9        | 209.1        |
| Exchange rate adjustments                         | (1.8)        | (4.0)        |
| Service cost                                      | 15.2         | 12.8         |
| Past service cost                                 | 0.1          | -            |
| Net interest expense (note 9)                     | 5.7          | 6.1          |
| Contributions – Group                             | (36.9)       | (48.0)       |
| Administrative expenses borne directly by schemes | 2.6          | 2.7          |
| Remeasurement of retirement benefit obligations   | 42.6         | 89.2         |
| <b>At 31 December</b>                             | <b>295.4</b> | <b>267.9</b> |
| Analysis of retirement benefit obligations:       |              |              |
| Pension schemes                                   | 248.7        | 222.0        |
| Healthcare schemes                                | 46.7         | 45.9         |
| <b>At 31 December</b>                             | <b>295.4</b> | <b>267.9</b> |

### Key financial assumptions used to calculate scheme liabilities

|   | 2020         | 2019         |
|---|--------------|--------------|
| UK scheme:                                  |              |              |
| Discount rate                               | 1.40%        | 2.05%        |
| Inflation rate                              | 3.00%        | 3.00%        |
| Salary increases                            | 2.80%        | 2.85%        |
| Current life expectancy: Male aged 65 years | 21.7 to 23.6 | 21.6 to 23.4 |
| US schemes:                                 |              |              |
| Discount rate                               | 2.30%        | 3.10%        |
| Current life expectancy: Male aged 65 years | 19.7 to 20.6 | 19.8 to 20.6 |

Group cash contributions paid during the year included deficit reduction payments of £21.7m (2019: £35.2m).

## 23. Issued share capital

|                                | 2020<br>No. m | 2019<br>No. m |
|--------------------------------|---------------|---------------|
| <b>Allotted and fully paid</b> | <b>781.2</b>  | <b>777.5</b>  |

## 24. 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 believe that the probability of an outflow of economic benefits arising from the guarantees is remote.

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.

## 25. Capital commitments

|                                  | 2020<br>£'m | 2019<br>£'m |
|----------------------------------|-------------|-------------|
| Contracted for but not incurred: |             |             |
| Intangible assets                | 3.8         | 3.7         |
| Property, plant and equipment    | 24.0        | 46.9        |
| <b>Total</b>                     | <b>27.8</b> | <b>50.6</b> |

## 26. Cash inflow from operations

|   | 2020<br>£'m  | 2019<br>£'m  |
|---|--------------|--------------|
| (Loss)/profit for the year  | (314.2)      | 222.6        |
| Adjustments for:  |              |              |
| Finance income (note 9)   | (0.5)        | (2.2)        |
| Finance costs (note 9)  | 37.2         | 40.8         |
| Tax   | (19.8)       | 64.1         |
| Depreciation (note 15)  | 56.7         | 57.3         |
| Amortisation (note 14)  | 140.6        | 138.4        |
| Impairment losses (note 14)   | 361.3        | -            |
| Loss/(gain) on disposal of property, plant and equipment                                | 1.4          | (0.9)        |
| Gain on disposal of businesses (note 6)   | (32.0)       | (23.5)       |
| Costs arising on disposal of businesses (note 29)                                       | (3.8)        | (12.2)       |
| Financial instruments – loss/(gain) (note 7)  | 2.9          | (15.0)       |
| Impact of retranslating net foreign currency cash at spot rate                          | (0.4)        | (0.6)        |
| Share of loss/(profit) after tax of joint venture (note 16)                             | 3.2          | (1.7)        |
| Change in carrying value of held for sale assets and liabilities up to date of disposal | -            | (0.5)        |
| Retirement benefit obligation deficit payments (note 22)                                | (21.7)       | (35.2)       |
| Share-based payment (credit)/expense  | (2.5)        | 10.1         |
| Changes in working capital  | 20.0         | (27.1)       |
| <b>Total</b>  | <b>228.4</b> | <b>414.4</b> |

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:

|  | 2020<br>£'m | 2019<br>£'m  |
|--|-------------|--------------|
| Cash inflow from operating activities                              | 154.2       | 366.9        |
| Add back cash outflow from business disposal expenses              | 5.2         | 9.4          |
| Add back impact of retranslating net foreign currency at spot rate | 0.4         | 0.6          |
| Capitalised development costs (note 14)                            | (41.4)      | (54.7)       |
| Capitalised programme participation costs                          | (1.6)       | (2.0)        |
| Purchase of intangible assets                                      | (11.0)      | (17.2)       |
| Purchase of property, plant and equipment (net of grants received) | (78.7)      | (77.2)       |
| Proceeds from disposal of property, plant and equipment            | 1.3         | 23.1         |
| Reverse lease premium received*                                    | 3.5         | 18.9         |
| <b>Free cash inflow</b>  | <b>31.9</b> | <b>267.8</b> |

\* Prior to any discussions with the lessor, the Group had negotiated terms for the purchase of land and subsequent construction of the building at Ansty Park, with a number of third parties. The lessor received the benefit of these negotiated terms when it contracted with those same third parties, and in return agreed to make a reverse lease premium payment to the Group, the majority of which was received in 2019 at inception of the lease with the balance received in 2020. The receipt of the reverse lease premium of £3.5m (2019: £18.9m) has been included in free cash flow consistent with the treatment of capital expenditure incurred by the Group relating to the Ansty Park site.

## 27. Movements in net debt

|  | 2020<br>£'m  | 2019<br>£'m  |
|--|--------------|--------------|
| At 1 January                                       | 911.2        | 1,074.1      |
| Cash inflow from operating activities              | (154.2)      | (366.9)      |
| Cash outflow from investing activities             | 22.0         | 49.7         |
| Cash (inflow)/outflow from financing activities    | (0.3)        | 130.4        |
| Lease liabilities entered                          | 11.4         | 54.2         |
| Businesses disposed or classified as held for sale | (5.6)        | -            |
| Exchange rate adjustments                          | (7.6)        | (31.2)       |
| Other non-cash movements                           | (3.9)        | 0.9          |
| <b>At 31 December</b>                              | <b>773.0</b> | <b>911.2</b> |

|   | 2020<br>£'m  | 2020<br>£'m  |
|---|--------------|--------------|
| Analysed as:                            |              |              |
| Bank and other borrowings – current     | 10.5         | 219.4        |
| Bank and other borrowings – non-current | 796.8        | 694.5        |
| Lease liabilities – current             | 14.7         | 16.4         |
| Lease liabilities – non-current         | 129.6        | 136.2        |
| Cash and cash equivalents               | (178.6)      | (155.3)      |
| <b>Total</b>                            | <b>773.0</b> | <b>911.2</b> |

## 28. Currency translation movements

|   | 2020<br>£'m   | 2019<br>£'m   |
|---|---------------|---------------|
| Arising in the year                           | (35.9)        | (68.7)        |
| Transferred to the income statement (note 29) | (44.0)        | -             |
| <b>Currency translation movements - loss</b>  | <b>(79.9)</b> | <b>(68.7)</b> |

## 29. Business disposals

On 30 June 2020, the Group disposed of Meggitt Training Systems (MTS), for a cash consideration of USD155.7m. The transaction is consistent with the Group's strategy to focus on businesses of scale in markets where its leading positions offer greater potential for growth and operational efficiencies. The business disposed was not a major line of business or geographical area of operation of the Group. The net assets of the business at the date of disposal were as follows:

|   | <u>£'m</u>   |
|---|--------------|
| Goodwill (note 14)  | 84.8         |
| Development costs (note 14)                                 | 19.7         |
| Other intangible assets (note 14)                           | 0.1          |
| Property, plant and equipment (note 15)                     | 6.8          |
| Inventories   | 11.6         |
| Trade and other receivables - current                       | 9.4          |
| Contract assets - current                                   | 22.6         |
| Cash and cash equivalents                                   | 9.8          |
| Trade and other payables - current                          | (15.4)       |
| Contract liabilities – current                              | (4.4)        |
| Lease liabilities – current                                 | (1.5)        |
| Provisions – current  | (0.1)        |
| Deferred tax  | (6.7)        |
| Lease liabilities – non-current                             | (3.0)        |
| <b>Net assets</b>   | <b>133.7</b> |
| Currency translation gain transferred from equity (note 28) | (44.0)       |
| Business disposal expenses                                  | 3.8          |
| Gain on disposal (note 6a)                                  | 33.3         |
| <b>Total consideration received in cash</b>                 | <b>126.8</b> |
| Cash inflow arising on disposal:                            |              |
| Total consideration received in cash                        | 126.8        |
| Less: cash and cash equivalents disposed of                 | (9.8)        |
| Business disposed   | 117.0        |
| Less: business disposal expenses paid *                     | (5.2)        |
| <b>Total cash inflow</b>                                    | <b>111.8</b> |

\* Of the total business disposal expenses paid, £3.5m were in respect of the disposal of MTS, with the balance relating to disposals in the prior year.

### 30. Principal risks and uncertainties

#### Strategic – Industry changes

##### *Description*

Significant variation in demand for air travel and/or our products due to aerospace and defence business downcycles coinciding; serious political, economic, pandemic (including the on-going impacts of COVID-19) or terrorist events; or industry consolidation that materially changes the competitive landscape.

##### *Impact*

Volatility in revenue and underlying profitability.

##### *How we manage it*

- Demand is managed by monitoring external economic and commercial environment and long-lead indicators whilst maintaining focus on balanced portfolio.
- Monitoring international political and tax developments to assess implications of future legislation.

#### 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 including SMART Support™ packages to create tailored solutions for customers throughout the product lifecycle enabling more effective performance monitoring and more predictable pricing.
- Investment in research and development to maintain and enhance Meggitt's intellectual property.

#### Strategic – Climate change

##### *Description*

Failure to adapt to the transition and physical impacts of climate change, including:

- Government legislation to limit air travel;
- Regulations limiting greenhouse gas emissions from aviation come into effect faster than technical solutions;
- Societal attitudes shifting against air travel (e.g. 'flight shaming');
- Acute physical risks such as the increased likelihood of extreme weather events; and
- Chronic physical risks such as changing weather patterns including rising temperatures and sea levels.

##### *Impact*

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

##### *How we manage it*

- Continued dialogue with governments, industry bodies and customers to maintain awareness of evolving aviation sector requirements.
- Continued focus on developing technologies to support sustainable aviation and on reducing the carbon intensity of our production operations.
- Allocation of two-thirds of innovation budget to sustainable solutions.
- Reduction in Group carbon footprint through new facilities and more efficient production processes.
- Comprehensive business continuity plans across the Group, supported by an insurance programme subject to annual renewal.
- Long-term weather considerations as part of site footprint strategy.

## **Operational – Quality escape/equipment failure**

### *Description*

Defective product leading to in-service failure, accidents, the grounding of aircraft or prolonged production shut-downs 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 (MPS).
- Supplier quality assurance process.

## **Operational – Business interruption**

### *Description*

A catastrophic event such as natural disasters (including earthquake - the Group has a significant operational presence in Southern California); civil unrest, military conflict or terrorist activity; or a pandemic (including further impacts from COVID-19) could lead to infrastructure disruption and/or 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 and also invoked during 2020 in response to COVID-19.
- 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 or delays, notably the 737 MAX.

### *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 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 resulting in 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 – IT/Systems failure**

### *Description*

A breach of IT security due to increasingly more sophisticated 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 poorly 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*

- Information Security infrastructure, policies and procedures supported by a Group wide security awareness programme.
- Intelligence sharing on threats with government and security bodies including the FBI, CPNI and NCSC
- Group wide intellectual property protection programme.
- Management of third party service providers and risks, including resilience and disaster recovery processes.
- Rolling programme of system upgrades (including SAP implementation) to replace legacy systems.
- Defined vulnerability management policy with monitoring capability to ensure that vulnerabilities are identified and appropriately patched.
- Dedicated cyber-security protective monitoring resources, employing industry leading technical controls and procedures.

## **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 and investments in new carbon manufacturing facilities in the USA.

### *Impact*

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

### *How we manage it*

- PMO oversight of large capital projects.
- Dedicated site consolidation and property management teams for Ansty Park.
- Regular monitoring by Executive Committee 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*

- Embedding of High Performance Culture.
- Action plans to improve employee engagement.
- Graduate and apprentice programmes in partnership with schools and universities.
- Regular oversight by Executive Committee.
- Creation of Employee Resource Groups to foster diversity, boost employee engagement and enable global collaboration.

## **Corporate – Legal & compliance**

### *Description*

Significant breach of increasingly complex trade compliance, bribery and corruption, US Government contracting, ethics, intellectual property, data protection or 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 Corporate Responsibility Committee.
- On-going trade compliance programme including third-party audits.
- Comprehensive ethics programme including training, anti-corruption policy and 'Speak Up' line.
- Third-party and internal audits including HS&E and Anti-Bribery & Corruption.
- MPS implementation to enhance safety measures, validated by third-party audits.

## **Financial – Pension funding**

### *Description*

The Group operates defined benefit pensions schemes in the UK, US and Switzerland. The level of deficits in these schemes may be affected adversely by investment returns, interest rates, increasing life expectancy and changes in the regulatory environment. The rates at which deficits are funded is subject to agreement with the trustees in the UK and is dependent on legislation in the US and Switzerland.

### *Impact*

Higher pension scheme funding contributions resulting in decreased cash and profit.

### *How we manage it*

- Triennial valuation process and deficit funding agreement with UK Pension Trustees.
- Continued monitoring of asset allocations and funding levels for all schemes.
- Closure of UK and US schemes to future accrual.

## **Financial – Liquidity**

### *Description*

The Group has debt funding and committed credit facilities from diverse sources which could be at risk in the event of the Group being unable to raise funds when required at a normal price owing to financial market disruption or an unwaived breach of the related financial covenants.

### *Impact*

Inability to access financing on normal commercial terms.

### *How we manage it*

- Maintaining sufficient headroom in committed credit facilities and against covenants in those facilities
- Arranging funding with maturities spread over several years or the ability to terminate early at little or no cost to the Group.

## **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 international accounting standards in conformity with the requirements of the Companies Act 2006 and adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union, 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  
3 March 2021

L Burdett  
Director  
3 March 2021

**- ENDS -**