BAE SYSTEMS
INSPIRED WORK

Preliminary announcement 2015

BAE Systems plc

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Results in brief

	2015	2014
Sales[1]	**£17,904m**	£16,637m
Underlying EBITA[2]	**£1,683m**	£1,702m
Operating profit	**£1,502m**	£1,300m
Underlying earnings[3] per share	**40.2p**	38.0p
Basic earnings per share[4]	**29.0p**	23.4p
Order backlog[1,5]	**£36.8bn**	£40.5bn
Dividend per share	**20.9p**	20.5p
Operating business cash flow[6]	**£681m**	£1,191m
Net debt (as defined by the Group)[7]	**£(1,422)m**	£(1,032)m

Ian King, Chief Executive, said: *"We have delivered another year of solid performance. BAE Systems has a large order backlog generated by a well-balanced portfolio of businesses serving the needs of customers in many of the world's larger accessible markets. The Group is well placed to continue to generate attractive returns for shareholders as defence budgets recover and our commercial adjacencies of cyber and commercial electronics continue to grow."*

Key points

Financial

– Sales[1] increased by £1.3bn to £17.9bn, including a £0.8bn benefit to UK sales from increased aircraft deliveries to Saudi Arabia and sales from the trading of equipment on the European Typhoon programme and the increased activity across the naval business. Exchange translation added £0.2bn compared to prior year.

– Underlying EBITA[2] reduced by £19m, to £1,683m, impacted by both the previously announced Typhoon production slowdown and Australian shipyard impairment and rationalisation charges. There was an exchange translation benefit of £15m.

– Underlying earnings[3] per share was 2.2p higher than in 2014, at 40.2p, including a 2.6p benefit from the previously announced overseas tax provision release and an additional 1.7p benefit from a UK tax provision release.

– The large order backlog[1,5] of £36.8bn underpins confidence in the future prospects for the business.

– Final dividend of 12.5p per share making a total of 20.9p per share for the year (an increase of 2% over 2014).

Operational

- Selected by Boeing to develop and manufacture the next-generation digital electronic warfare system for the US Air Force's Eagle Passive Active Warning Survivability System programme. The upgrade of up to 400 F-15 aircraft could be worth in excess of $1.0bn (£0.7bn) over the life of the programme.
- Major contracts received from the Royal Navy, including an £859m Type 26 frigate demonstration contract and the full £1.3bn contract for the fifth Astute Class submarine.
- Further contracts received in support of the US combat vehicle industrial base, including $104m (£71m) for the engineering and manufacturing development phase as part of the competition for the Amphibious Combat Vehicle 1.1 programme.
- A $100m (£68m) capital investment programme underway at our San Diego, California, shipyard.
- Awarded a five-year contract by the US Army for the Enhanced Night Vision Goggle III and Family of Weapon Sights – Individual programme, with a potential value of $435m (£295m).
- Progressive expansion of the Typhoon aircraft's capabilities, including the integration of the Captor E-Scan radar and additional weapons.
- In Saudi Arabia, a contract was awarded for a further 22 Hawk aircraft, associated ground equipment and training aids.
- Sales growth of 31% in Applied Intelligence and increased investment to support the expansion of the commercial cyber security business.
- Agreement to acquire a 20% interest in Reaction Engines Limited, a company working on a radical new aerospace engine concept, SABRE™, which combines rocket and jet engine functions, made possible by exciting new heat exchanger technology.

Guidance for 2016

Group guidance

In 2016, the Group's underlying earnings[3] per share are expected to be approximately 5% to 10% higher than the adjusted underlying earnings[3] per share of 36.6p* in 2015.

* *Reported underlying earnings[3] per share of 40.2p excluding the two tax provision releases of 2.6p per share and 1.7p per share, and adjusting for a 0.7p per share benefit to an assumed US$1.45 to sterling translation rate.*

Segmental guidance

Electronic Systems:

- Low single-digit sales[1,8] growth is expected in 2016 with margins around the middle of an increased 13% to 15% guidance range.

Cyber & Intelligence comprising the US Intelligence & Security sector (70%[8] of Cyber & Intelligence sales in 2015) and Applied Intelligence:

- Low single-digit sales[1] growth is expected in 2016 with stable sales in Intelligence & Security and good double-digit growth in Applied Intelligence.
- Margins are expected to improve to within a 7% to 9% range, following the high product development investment in the Applied Intelligence business in 2015.

Platforms & Services (US):

- Sales[1] are expected to be some 10% lower, including a reduction in naval ship repair activity as the pivot of the fleet to the West coast takes place.

– Another year of margin improvement, to a range of 7% to 8%, is expected in 2016, absent further charges on commercial shipbuilding contracts.

Platforms & Services (UK):

– Sales[1] are expected to be slightly lower in line with planned lower Typhoon deliveries. Increased submarine programme activity is expected to offset reducing aircraft carrier sales.

– Margins are expected to be at the lower end of a 10% to 12% range.

Platforms & Services (International):

– Sales[1] are expected to grow around 5% in 2016 with increased Typhoon aircraft support.

– Margins are expected to be at the lower end of a 10% to 12% range.

HQ costs are expected to be similar to those in 2015. Underlying finance costs are expected to increase by £35m in 2016. The underlying effective tax rate remains dependent on the geographical mix of profits, but is expected to increase slightly to around 22%.

1. Including share of equity accounted investments.
2. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 8).
3. Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, non-recurring items and, in 2014, a credit in respect of the re-assessment of existing tax provisions (see note 5).
4. Basic earnings per share in accordance with International Accounting Standard 33, Earnings per Share.
5. Comprises funded and unfunded unexecuted customer orders, and is stated after the elimination of intra-group orders.
6. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.
7. Comprises cash and cash equivalents, less loans and overdrafts (including debt-related derivative financial instruments) and cash received on customers' account (see page 9).
8. Adjusted for the transfer of the GEOINT-ISR (Geospatial Intelligence – Intelligence, Surveillance and Reconnaissance) business to Electronic Systems.

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Analyst and investor presentation

A presentation, for analysts and investors, of the Group's Results for 2015 will be available via webcast at 9:00am today (18 February 2016).

Details can be found on **www.baesystems.com/investors**, together with presentation slides and a pdf copy of this report. A recording of the webcast will be available for replay later in the day.

About BAE Systems

At BAE Systems, we provide some of the world's most advanced technology defence, aerospace and security solutions. We employ a skilled workforce of 82,500 people[1] in over 40 countries. Working with customers and local partners, our products and services deliver military capability, protect people and national security, and keep critical information and infrastructure secure.

Preliminary results statement

We have delivered another year of solid performance. BAE Systems has continued to demonstrate resilience in markets constrained by wider economic pressures.

Over the past several years, the Group has navigated through a period of constrained defence budgets. Where sales volumes have been challenged, we have taken actions to protect earnings and deliver attractive shareholder returns. The overall business environment is now improving and the Group is well positioned as we enter this phase.

US

In the US, President Obama signed the Bipartisan Budget Act of 2015, which lifts defence budget caps for fiscal years 2016 and 2017 by $33bn (£22bn) and $23bn (£16bn), respectively. This is expected to enhance the funding environment for the Group's US businesses through 2017.

The Group's electronics businesses have performed well and remain well positioned to address current and evolving priority programme requirements. As a major supplier of electronics equipment on the F-35 Lightning II aircraft, including the electronic warfare system, BAE Systems is positioned to benefit from the commitment to progressive increases in production output over coming years to meet the requirements of US and international customers.

Important new business wins in key technology areas in 2015 included the Eagle Passive Active Warning Survivability System (EPAWSS) electronic warfare upgrade for US Air Force F-15 aircraft and electronics upgrades to US Special Operations Command C-130J aircraft.

We have a strong position in the Intelligence, Surveillance and Reconnaissance domain, providing customers with high-technology sensing solutions, including advanced geospatial intelligence capabilities.

We continue to perform in commercial electronics through our broadly-based flight and engine controls activities. Company-funded investment in innovative commercial aircraft cabin systems took an important step forward with the signing of the first IntelliCabin® in-flight entertainment system airline customer.

The US Navy is redeploying some ships consistent with its stated strategy, to include expanding operations in the Asia-Pacific region. As a leading supplier of ship repair services to the US Navy, BAE Systems is responding to these changes with a reduction in workforce at its Norfolk, Virginia, facility on the Atlantic coast and by investing in additional capacity at its San Diego shipyard. In 2016, the Group expects to deliver the remaining commercial ships currently under construction in Jacksonville, Florida, and Mobile, Alabama.

Whilst much of the Group's US-based activity has proven resilient over recent years through the downturn in US defence spending, land programmes and manpower services have been disproportionately impacted. Both activities performed well in 2015, supporting expectations for an improved outlook going forward.

In land, we continued to make good progress building on the award in 2014 of the Armored Multi-Purpose Vehicle (AMPV) programme and further order intake for M109A7 (Paladin) tracked artillery systems. These two programmes draw on commonality with the Bradley family of vehicles and underpin our strong franchise in tracked combat vehicles. The Group was also down-selected as one of two companies awarded a contract for the engineering and manufacturing development phase of a competition for the US Marine Corps' Amphibious Combat Vehicle programme.

Beyond the US market, FNSS, the Turkish land systems business in which BAE Systems holds a 49% interest, secured further international armoured vehicle orders in the year.

Following external interest in the Group's US-based manpower and services activities, BAE Systems undertook a strategic review of the business. Recognising the performance of the business and its good order intake, the review concluded, in November, that greater value could be derived from retaining the businesses. Throughout the period, Intelligence & Security remained focused on providing leading-edge products and services to customers and delivered solid financial performance, winning re-compete awards and a number of new, multi-year service contracts.

UK
The Group's UK businesses continued to perform well, benefiting from good programme execution and continuity in UK customer requirements. UK government commitments in July 2015 to protect defence and security spend, in a still tightly constrained UK economic environment, were helpful.

In November, the UK government published its Strategic Defence and Security Review (SDSR). The SDSR identified defence and security priorities and set out a plan to spend £178bn on defence equipment and support over the next ten years.

A number of important SDSR commitments for BAE Systems included continued investment in expanding Typhoon capabilities and an extension of the aircraft's expected service life until at least 2040. There was also a commitment to continued joint investment with France in the development of a future unmanned combat air capability. Also in the air domain, the SDSR identified an accelerated UK procurement of F-35 Lightning II aircraft. BAE Systems is a major participant in the F-35 programme, supplying airframe assemblies and electronics equipment.

In the maritime domain, the SDSR included a continued commitment to seven Astute Class submarines and the replacement of the four Vanguard Class submarines. The UK government reaffirmed its commitment to shipbuilding continuity providing clarity and future opportunities for the Group's shipbuilding facilities and workforce in Scotland. A fleet of at least 19 frigates and destroyers is expected to be maintained, including eight Type 26 frigates. The government's SDSR commitments also include a concept study followed by the design and build of a new class of lighter, flexible, general purpose frigates, in addition to two new Offshore Patrol Vessels.

In September, an agreement between Kuwait and Italy was announced relating to the supply of 28 Typhoon aircraft to the Kuwait Air Force. We continue to support the campaign, led by Finmeccanica, to achieve a formal contract. In November, BAE Systems announced a reduction in its build rate for Typhoon assemblies to ensure production continuity at competitive costs over the medium term. We also announced a proposal to reduce the workforce of the Military Air & Information business.

The UK government continues to provide strong support for Typhoon and other export campaigns. Although there can be no certainty as to the timing of orders, discussions with current and prospective operators of the Typhoon aircraft continue to support our expectations for additional Typhoon contract awards.

Consistent with the Group's focused investment in research and technology, in November, BAE Systems announced an agreement to acquire a 20% interest in Reaction Engines Limited (REL). REL is working on a radical new aerospace engine concept, SABRE™, which combines rocket and jet engine functions, made possible by exciting new heat exchanger technology. We expect our involvement to expedite transition of the concept to a working demonstration engine.

International
We continued to deliver Typhoon aircraft to the Kingdom of Saudi Arabia during 2015 and the Group's extensive in-Kingdom training and support activities are at a high tempo. The Royal Saudi Air Force has achieved high utilisation and aircraft availability across its Typhoon and Tornado fleets, operating under demanding conditions.

We reached agreement with the Saudi customer for the provision of a further 22 Hawk Advanced Jet Trainer aircraft, associated ground equipment and training aids for the Royal Saudi Air Force, which form part of an enhancement to the Kingdom's pilot training capacity.

As the 50th anniversary of the relationship approaches, BAE Systems continues to address current and potential new requirements as part of the long-standing agreements between the UK government and the Kingdom.

In Australia, the second of the two Landing Helicopter Dock (LHD) ships was successfully delivered into service with the Royal Australian Navy. Whilst we welcomed the Australian government's announcement of its intention to launch a naval shipbuilding strategy, the viability of the Williamstown, Melbourne, shipyard remains uncertain. With no near-term prospect of work beyond the LHD programme and Air Warfare Destroyer block manufacture, we announced further headcount reductions in November, together with other cost reduction measures across the Australian businesses. In addition, a non-cash impairment charge has been taken against the carrying value of the Williamstown facility.

In India, BAE Systems has a long-standing relationship with Hindustan Aeronautics Limited (HAL). Delivery of a second batch of HAL-assembled Hawk aircraft continues and negotiations are underway to agree a third batch. The Group has also commenced discussions with HAL for further co-development of Indian Hawk aircraft to meet potential requirements for new capabilities.

The Group continues to discuss the potential sale of M777 howitzers, including prospective local arrangements for assembly, integration and testing, to address India's large requirement for new-generation artillery systems.

BAE Systems is a 37.5% shareholder in the MBDA guided weapons business. MBDA continues to win significant order intake, including naval weapon systems and weapons awards in support of multiple combat aircraft types. The business expects to win further orders from recently announced, and anticipated, international sales of European combat aircraft. MBDA is expected to generate strong growth in later years from this rising order book.

Cyber security

A substantial expansion of the Group's Applied Intelligence business into commercial markets is underway, with significant recruitment and product development alongside integration of the former SilverSky business, acquired at the end of 2014. Sales growth is expected to continue, underpinned by continued good order intake as cyber security becomes an increasingly important part of government security and a core element of stewardship for commercial enterprises.

Acquisitions and disposals

In April, BAE Systems completed the sale of its 75% holding in BAE Systems Land Systems South Africa (Pty) Limited to Denel (SOC) Limited for cash consideration of 655 million Rand (£36m).

In June, we acquired Eclipse Electronic Systems, Inc. from Esterline Corporation. The Texas-based business provides advanced Intelligence, Surveillance and Reconnaissance products and services to the US defence and intelligence community.

Balance sheet and capital allocation

The Group's balance sheet continues to be managed conservatively in line with its policy to retain its investment grade credit rating and to ensure operating flexibility. Consistent with this approach, the Group meets pension obligations, pursues organic investment opportunities, plans to pay dividends in line with its policy of long-term sustainable cover of around two times underlying earnings and to make accelerated returns of capital to shareholders when the balance sheet allows. Investment in value-enhancing acquisitions is considered where market conditions are right and where they deliver on the Group's strategy.

The Group continues to fund the pension deficits of the UK schemes under funding agreements determined following the last UK valuations in 2014. The next valuations of the UK pension schemes are expected to begin in April 2017.

In February 2013, we initiated a share repurchase programme of up to £1bn over three years. As at 31 December 2015, a total of 120.5 million shares had been purchased for £502m under the programme.

The Board and directors

On 15 February 2016, the Company announced that Charles Woodburn would be joining the Board and Executive Committee in the newly-created role of Chief Operating Officer. He will report to the Chief Executive, Ian King, and it is anticipated that his appointment will be effective from a date in the second quarter of 2016.

In June 2015, Carl Symon resigned from the Board having completed seven years' service. Paula Rosput Reynolds has succeeded him as chair of the Remuneration Committee.

Elizabeth Corley has recently joined the Board as a non-executive director.

Led by the Senior Independent Director, Nick Rose, the Board has agreed to extend Sir Roger Carr's term of appointment as Chairman until February 2020.

Dividend

The Board has recommended a final dividend of 12.5p per share making a total of 20.9p per share for the year, an increase of 2% over 2014.

Income statement

	2015 £m	2014 £m
Sales[1]	**17,904**	16,637
Underlying EBITA[2]	**1,683**	1,702
Return on sales	***9.4%***	*10.2%*
Non-recurring items	**26**	–
EBITA	**1,709**	1,702
Amortisation of intangible assets[1]	**(108)**	(184)
Impairment of intangible assets	**(78)**	(170)
Finance costs[1]	**(409)**	(448)
Taxation expense[1]	**(171)**	(148)
Profit for the year	**943**	752

Exchange rates – average	2015	2014
£/$	**1.528**	1.647
£/€	**1.377**	1.241
£/A$	**2.036**	1.827

Exchange rates – sensitivity analysis

Estimated impact on sales[1] of a ten cent movement in the average exchange rate	£m
$	**400**
€	**50**
A$	**30**

Segmental analysis

	Sales[1]		Underlying EBITA[2]	
	2015 £m	2014[3] £m	2015 £m	2014[3] £m
Electronic Systems	**2,638**	2,415	**396**	373
Cyber & Intelligence	**1,848**	1,658	**145**	153
Platforms & Services (US)	**2,779**	2,689	**177**	117
Platforms & Services (UK)	**7,405**	6,623	**721**	772
Platforms & Services (International)	**3,742**	3,572	**335**	366
HQ	**237**	279	**(91)**	(79)
Intra-group	**(745)**	(599)		
	17,904	16,637	**1,683**	1,702

Sales[1] increased by £1.3bn to £17.9bn, including a £0.8bn benefit to UK sales from increased aircraft deliveries to Saudi Arabia and sales from the trading of equipment on the European Typhoon programme and the increased activity across the naval business. Exchange translation added £0.2bn compared to prior year.

Underlying EBITA[2] decreased by £19m to £1,683m (2014 £1,702m), giving a return on sales of 9.4% (2014 10.2%), impacted by both the previously announced Typhoon production slowdown and Australian shipyard impairment and rationalisation charges. There was an exchange translation benefit of £15m.

Non-recurring items in 2015 of £26m includes research and development expenditure credits relating to 2013 and 2014 (£50m), partly offset by a loss on the disposal of the Group's 75% shareholding in the Land Systems South Africa business (£24m).

Amortisation of intangible assets[1] reduced to £108m (2014 £184m) due to acquired intangible assets fully amortising in 2014.

Impairment of intangible assets mainly comprises the impairment of goodwill in the US Intelligence & Security business reflecting lower growth assumptions. In 2014, goodwill impairment charges were taken against the carrying value of the US Support Solutions (£87m) and South African (£74m) businesses.

Finance costs[1] were £409m (2014 £448m). The underlying interest charge, excluding pension accounting, and fair value and foreign exchange adjustments on financial instruments and investments, reduced to £194m (2014 £204m) primarily from a lower level of net present value adjustments. Net interest expense on the Group's pension deficit was higher at £200m (2014 £155m) mainly reflecting the increase in the deficit at the beginning of 2015.

Taxation expense[1] reflects the Group's underlying effective tax rate for the year of 21%, which excludes the change in accounting for UK research and development credits and the benefit of £134m arising from the adjustment of certain tax provisions. Including these items, the underlying effective tax rate is 14%. The underlying effective tax rate for 2016 is expected to be around 22%, with the final rate dependent on the geographical mix of profits.

Looking beyond 2016, the effective tax rate will depend principally on whether there are any changes in tax legislation in the Group's most significant countries of operation, the geographical mix of profits and the resolution of open issues. The Group does not expect the future rate to be materially impacted by the changes to the international tax landscape resulting from the package of measures developed under the OECD/G20 Base Erosion and Profit Shifting project and the investigations and proposals of the European Commission. However, the details of those are yet to be finalised and the Group will keep these under review.

Earnings per share

Underlying earnings[4] **per share** for the year was 2.2p higher than in 2014, at 40.2p (2014 38.0p), including a 2.6p benefit from the previously announced overseas tax provision release and an additional 1.7p benefit from a UK tax provision release.

Basic earnings per share, in accordance with International Accounting Standard 33, Earnings per Share, was 29.0p (2014 23.4p).

1. Including share of equity accounted investments.
2. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.
4. Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, non-recurring items and, in 2014, a credit in respect of the re-assessment of existing tax provisions (see note 5).

Cash flow

Reconciliation of cash inflow from operating activities to net debt (as defined by the Group)

	2015 £m	2014 £m
Cash inflow from operating activities	**924**	913
Capital (expenditure)/proceeds (net) and financial investment	**(284)**	215
Dividends received from equity accounted investments	**41**	63
Operating business cash flow[5]	**681**	1,191
Interest	**(173)**	(145)
Taxation	**(116)**	(92)
Free cash flow	**392**	954
Acquisitions and disposals	**16**	(230)
Cash classified as held for sale	**–**	(6)
Share repurchase programme	**(7)**	(283)
Other net sale of own shares	**8**	2
Equity dividends paid	**(655)**	(642)
Dividends paid to non-controlling interests	**(40)**	(14)
Cash flow from matured derivative financial instruments	**12**	8
Movement in cash collateral	**3**	10
Movement in cash received on customers' account[6]	**–**	1
Total cash outflow	**(271)**	(200)
Foreign exchange translation	**(165)**	(146)
Other non-cash movements	**46**	13
Increase in net debt (as defined by the Group)	**(390)**	(333)
Opening net debt (as defined by the Group)	**(1,032)**	(699)
Closing net debt (as defined by the Group)	**(1,422)**	(1,032)

Operating business cash flow

	2015 £m	2014[3] £m
Electronic Systems	**323**	246
Cyber & Intelligence	**93**	125
Platforms & Services (US)	**100**	147
Platforms & Services (UK)	**220**	173
Platforms & Services (International)	**164**	881
HQ	**(219)**	(381)
Operating business cash flow[5]	**681**	1,191

Components of net debt (as defined by the Group)

	2015 £m	2014 £m
Debt-related derivative financial instrument assets	**53**	10
Cash and cash equivalents	**2,537**	2,314
Less: Cash classified as held for sale	**–**	(6)
Cash (as defined by the Group)	**2,590**	2,318
Loans – non-current	**(3,775)**	(2,868)
Loans and overdrafts – current	**(237)**	(482)
Debt (as defined by the Group)	**(4,012)**	(3,350)
Net debt (as defined by the Group)	**(1,422)**	(1,032)

3. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.
5. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.
6. Cash received on customers' account is the unexpended cash received from customers in advance of delivery which is subject to advance payment guarantees unrelated to Group performance. It is included within trade and other payables in the consolidated balance sheet.

Cash flow

Operating business cash flow[5]

Cash inflow from operating activities was £924m (2014 £913m), which includes cash contributions in respect of pension deficit funding, over and above service costs, for the UK and US schemes totalling £274m (2014 £391m).

The major advances received in 2012 on the Omani Typhoon and Hawk order, and the Saudi training aircraft contract, continue to be consumed. Advances were also utilised in the year on European Typhoon production. Costs are being incurred against provisions created in previous years, including the US commercial shipbuilding programmes and on UK rationalisation. The second of the two payments under the Salam price escalation settlement was received.

Net capital expenditure and financial investment was £284m. In 2014, there was a net cash inflow of £215m, which included the receipt of £418m in respect of the sale and leaseback of two properties in Saudi Arabia.

Dividends received from equity accounted investments reduced by £22m to £41m (2014 £63m) reflecting a lower dividend from MBDA.

Interest payments were £28m higher at £173m (2014 £145m) primarily reflecting the timing of interest payments on US dollar bonds and interest receipts in the UK.

The net cash inflow in respect of **acquisitions and disposals** of £16m includes £21m received in respect of the sale of the Group's 75% shareholding in the Land Systems South Africa business, less £5m paid in respect of the acquisition of Eclipse Electronic Systems, Inc. In 2014, there was a net cash outflow of £230m comprising the acquisition of SilverSky (£147m) and Signal Innovations Group (£12m), together with an additional 59% shareholding in Saudi Development and Training Company (£71m).

During 2015, there was a cash outflow of £7m (2014 £283m) under the **share repurchase programme** representing shares purchased and cancelled under the programme announced in February 2013. The return on investment from buying back the Group's own shares reduces as the share price rises and, as a result, activity on the programme has been minimal in the year.

Equity dividends paid in 2015 includes payments in respect of the 2014 final (£389m) and 2015 interim (£266m) dividends.

Dividends paid to non-controlling interests increased to £40m (2014 £14m) reflecting higher dividends paid by both the Group's 75%-owned South African business prior to disposal and a 51%-owned Saudi portfolio company.

Foreign exchange translation, primarily in respect of the Group's US dollar-denominated borrowing, increased reported net debt by £165m.

Net debt (as defined by the Group)

The Group's **net debt**[7] at 31 December 2015 is £1,422m, a net increase of £390m from the net debt position of £1,032m at the start of the year.

A $750m (£481m) 5.2% bond was repaid at maturity in August.

In December, BAE Systems issued $1.5bn (£1.0bn) of bonds in the US capital market comprising a $500m five-year bond at a 2.85% coupon, a $750m ten-year bond at a 3.85% coupon and a $250m 30-year bond maturing in 2044 at a 4.75% coupon.

Cash and cash equivalents of £2,537m (2014 £2,314m) are held primarily for the repayment of debt securities, pension deficit funding, payment of the 2015 final dividend and management of working capital.

5. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.
7. Comprises cash and cash equivalents, less loans and overdrafts (including debt-related derivative financial instruments) and cash received on customers' account (see page 9).

Segmental performance: Electronic Systems

Electronic Systems, with 12,400 employees[1], comprises the US and UK-based electronics activities, including electronic warfare systems, electro-optical sensors, military and commercial digital engine and flight controls, next-generation military communications systems and data links, persistent surveillance capabilities, and hybrid electric drive systems.

Operational and strategic highlights

- Selected for the Eagle Passive Active Warning Survivability System programme with Boeing, potentially worth over $1.0bn (£0.7bn) over the life of the programme, to upgrade up to 400 US Air Force F-15 aircraft
- Delivered the first international order for the Advanced Precision Kill Weapon System (APKWS™)
- Awarded a five-year contract for the US Army's Enhanced Night Vision Goggle III and Family of Weapon Sights – Individual programme, with a potential value of $435m (£295m)
- Acquired Eclipse Electronic Systems, Inc., a provider of leading-edge communications intelligence receivers and services
- Selected by Boeing to provide the entire flight control electronics suite on the next-generation 777X aircraft programme following the award, in 2015, for the remote electronic units
- Opened a state-of-the-art aviation technology manufacturing facility in Fort Wayne, Indiana

Financial performance

	2015	2014
Sales[1]	**£2,638m**	£2,415m
Underlying EBITA[2]	**£396m**	£373m
Return on sales	**15.0%**	15.4%
Cash inflow[3]	**£323m**	£246m
Order intake[1]	**£2,523m**	£2,341m
Order backlog[1,4]	**£4.2bn**	£3.9bn

- Sales[1] compared to 2014 increased marginally to $4.0bn (£2.6bn). The commercial areas of the business now amount to 23% having seen sales growth in the year of 7%. On the defence side, sales were stable with growth on the F-35 Lightning II programme offsetting contracts completing in 2014.
- The return on sales achieved of 15.0% benefited from continued strong programme execution and risk retirement. Last year's return on sales of 15.4% included a 0.5 percentage point non-recurring gain from a contract pricing settlement.
- Cash[3] conversion of underlying EBITA[2] for the year was at 89%, excluding pension deficit funding.
- Order backlog[1,4] was sustained at $6.1bn (£4.2bn) benefiting from awards for Enhanced Night Vision Goggles, F-15 electronic warfare upgrades, production of P-8A Poseidon mission computers and F-35 Lightning II Low-Rate Initial Production Lots 9 to 11.

Operational performance

Electronic Combat

Electronic Systems has sustained its leadership position in the US electronic warfare market and production is ramping up across a number of programmes. Low-Rate Initial Production hardware deliveries on the F-35 Lightning II programme continue with Lot 8 and 9 deliveries, and Lot 10 deliveries expected to commence in 2016. The business has received initial funding for Lot 11, with negotiations anticipated in 2016.

The business is under contracts, from Boeing and Warner Robins Air Logistics Complex, totalling over $1.0bn (£0.7bn) to install the Digital Electronic Warfare System (DEWS) on 84 new F-15 aircraft, upgrade 70 existing F-15 aircraft with DEWS and provide spare units and modules for an international customer. Hardware and software deliveries, and system verification testing remain on schedule.

BAE Systems has been selected by Boeing to develop and manufacture the next-generation digital electronic warfare system for the US Air Force's Eagle Passive Active Warning Survivability System programme to upgrade up to 400 F-15 aircraft. The programme could be worth over $1.0bn (£0.7bn) over its life.

BAE Systems was selected by the US Special Operations Command to develop a new electronic warfare system for its fleet of C-130J aircraft. The initial contract, worth more than $20m (£14m), is the first phase of a multi-phase programme to provide product development and platform integration work over the next 12 months. The lifecycle value of the contract could exceed $400m (£271m).

Due to the sensitive nature of electronic combat systems and technology, many of the business's programmes are classified. As a world leader in electronic warfare systems, the business continues to experience growth in this increasingly important area.

Survivability, Targeting & Sensing
The US Army continues to field the third-generation upgrade to its Common Missile Warning Systems and has placed its first Foreign Military Sales orders for systems to Qatar, the Republic of Korea, Indonesia and Turkey.

Electronic Systems continues to deliver on Advanced Precision Kill Weapon System (APKWS™) Full-Rate Production Lots 3 and 4, now worth a total of $115m (£78m) with the US Navy. BAE Systems received customer recognition for the completion of the 5,000th production unit during September and the first Foreign Military Sales order of 110 systems for Jordan was completed in October. The US Army acquired an initial quantity of APKWS™ laser-guided rockets from the US Navy for use in ongoing operations.

The business continues to perform on the Terminal High-Altitude Area Defence Full-Rate Production contract, valued at $340m (£231m), for 307 infrared missile seekers supporting both the US government and Foreign Military Sales.

A five-year, Indefinite Delivery, Indefinite Quantity (IDIQ) contract to support the US Army's Enhanced Night Vision Goggle III and Family of Weapon Sights – Individual programme was awarded to BAE Systems in March. The contract has a potential value of approximately $435m (£295m). The programme has commenced initial deliveries to support user evaluation and reliability testing.

The next-generation Striker® II helmet-mounted display has completed initial flight trials, successfully demonstrating the performance of the integrated digital night vision camera.

The business was unsuccessful in bidding for the US Army's Common Infrared Countermeasures programme.

Intelligence, Surveillance & Reconnaissance
The business continues to provide Airborne Surveillance capability for the US Air Force and US Army based on two wide-area, high-resolution imaging sensor systems – the Airborne Wide Area Persistent Surveillance System, which has been operational for more than 28,000 hours in theatre, and the Autonomous Real-time Ground Ubiquitous Surveillance – Imaging System.

The business provides state-of-the-art processing capabilities for the US Navy's P-8A Poseidon programme, which has entered Full-Rate Production, and delivered 35 mission computer and display systems during the year. Four systems were purchased by Australia in 2015.

Electronic Systems continues to provide Signals Intelligence capability for the US Army and other US Department of Defense customers. BAE Systems was awarded $28m (£19m) for additional enhancements to the existing two-year contract valued in excess of $95m (£64m) to provide Tactical Signals Intelligence Payloads and associated equipment for the US Army's Gray Eagle unmanned aircraft. Deliveries of pods and ground stations have commenced.

In June, BAE Systems completed the acquisition of Eclipse Electronic Systems, Inc., a Texas-based provider of highly-advanced Intelligence, Surveillance and Reconnaissance products and services to the US defence and intelligence community.

Controls & Avionics
BAE Systems is a major supplier to Boeing for flight controls, and cabin and flight deck systems. In February, the Group was selected to provide the remote electronic units on Boeing's next-generation 777X aircraft programme. With this new award, BAE Systems will now provide the entire flight control suite for 777X aircraft. Delivery of subsystems for the first 737 MAX test aircraft was completed on schedule.

FADEC Alliance, a joint venture between FADEC International (the Group's joint venture with Sagem) and GE Aviation, completed certification of the full authority digital engine controls on the Leap engine for the Airbus A320neo aircraft.

The business completed certification of the flight control electronics for the Embraer Legacy 500 and Bombardier CSeries aircraft, and its flight control electronics enabled first flights of the Gulfstream G500 and Embraer KC-390 aircraft.

Vistara, an Indian airline, became the launch customer for BAE Systems' IntelliCabin® wireless in-flight entertainment system. The first installation of the system was certified in January 2016.

A new state-of-the-art manufacturing facility in Fort Wayne, Indiana, officially opened in September for the production of commercial aircraft electronics.

On the F-35 Lightning II programme, BAE Systems completed Low-Rate Initial Production (LRIP) Lot 7 deliveries of 38 production shipsets, plus spares, of the vehicle management computer and active inceptor system equipment to Lockheed Martin. Both systems are currently in production for LRIP Lot 8 and under contract for LRIP Lot 9.

HybriDrive® Solutions

With the recent delivery of its 5,000th hybrid propulsion system, the business is continuing to meet the needs of an environmentally-conscious global transit bus market with its new anti-idling technology and zero-emission drive modes. Cities including London, Paris, Boston and Seattle are now using engine-off technology to save fuel, reduce noise and improve local air quality.

Other

In July, the Communications & Control line of business was realigned across the three remaining defence businesses.

From 2016, Cyber & Intelligence's Geospatial Intelligence – Intelligence, Surveillance and Reconnaissance business will be reported in Electronic Systems.

Looking forward

In the US, further clarity regarding potential market improvement was gained after Congress reached agreement on a new budget deal that provides for defence and domestic programme spending above the Budget Control Act caps through 2017.

Whilst the longer-term outlook retains some uncertainty, Electronic Systems remains well positioned to address changing US Department of Defense priorities. Its focus remains on maintaining a diverse portfolio of defence and commercial products and capabilities for US and international customers, while sustaining its emphasis on cost reduction and research and development.

The business expects to benefit from its franchise positions, particularly on the F-35 Lightning II and F-15 programmes, and its ability to apply innovative technology solutions that meet defence customers' changing requirements. In the commercial aviation market, Electronic Systems' technology innovations are enabling the business to renew long-standing customer positions and win new business.

1. Including share of equity accounted investments.
2. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.
4. Comprises funded and unfunded unexecuted customer orders.

Segmental performance: Cyber & Intelligence

Cyber & Intelligence, with 12,900 employees[1], comprises the US-based Intelligence & Security business and UK-headquartered Applied Intelligence business, and covers the Group's cyber security, secure government, and commercial and financial security activities.

Operational and strategic highlights

Intelligence & Security

- Strategic review of manpower and services businesses determined that retaining the businesses delivers greater value
- Secured a ten-year contract with an expected value of over \$1.0bn (£0.7bn) to provide information technology services to high priority US government agencies
- Secured a five-year, \$278m (£189m) re-compete award to provide logistics and sustainment engineering services for radar, optical and telemetry systems

Applied Intelligence

- Integration of the acquired SilverSky business substantially completed
- Significant investment in engineering capabilities and product development
- Strong performance in commercial cyber security products, with multi-year contracts awarded
- Launch and initial take-up of cloud-based cyber security products in Europe, Canada and Asia-Pacific
- Continued growth of security and digital services projects in government and critical national infrastructure in the UK and internationally

Financial performance

	2015	2014[2]
Sales[1]	**£1,848m**	£1,658m
Underlying EBITA[3]	**£145m**	£153m
Return on sales	**7.8%**	9.2%
Cash inflow[4]	**£93m**	£125m
Order intake[1]	**£2,029m**	£1,784m
Order backlog[1,5]	**£2.4bn**	£2.0bn

- In aggregate, sales[1] increased by 3% to \$2.8bn (£1.8bn). The US business saw just a 1% decrease largely in government IT services. Growth in the Applied Intelligence business was at 31%, of which 13% came from the acquisition of SilverSky and 18% organically, largely from non-UK government customers.
- The return on sales reduced to 7.8% (2014 9.2%) due to a higher level of costs expensed in Applied Intelligence as the business focuses on further growth.
- Cash[4] conversion of underlying EBITA[3] for the year was at 82%, excluding pension deficit funding.
- In aggregate, order backlog[1,5] increased to \$3.5bn (£2.4bn). Order backlog in the US business grew by 13% largely on imagery analysis and cyber support awards. In the Applied Intelligence business, order backlog increased by 21% over the year driven mainly by international and commercial awards.

Operational performance

Intelligence & Security

GEOINT-ISR (Geospatial Intelligence – Intelligence, Surveillance and Reconnaissance)

Intelligence & Security continues to mature its capabilities in software-based data analytics with an emphasis on big data, production, automation and efficiencies to help the intelligence and defence communities transform data into actionable intelligence.

The business continues to build on its legacy of support to the National Geospatial-Intelligence Agency. Under the Consolidated Library programme, the business was awarded a 15-month, \$18m (£12m) contract for a Flexible Content Management System that provides new flexible and adaptable capabilities that can be deployed to enhance intelligence collection and tradecraft.

Since winning the Geospatial Data Services Foundational GEOINT Content Management programme in 2014, the business has been awarded orders valued at over \$104m (£71m).

The business is performing well on two new contracts awarded in 2015 to assist new US intelligence community customers with the development of advanced GEOINT data processing and next-generation geospatial intelligence data collection solutions.

The Mobility Air Force Automated Flight Planning Service programme is developing advanced mission planning software for US Air Force non-combat aircraft. The software generates four-dimension optimised flight plans to minimise fuel consumption and take advantage of new and evolving air space regulations. The latest software version has been delivered to the customer for formal qualification testing and is on track to be operational in 2016.

Signal Innovations Group, Inc., acquired in 2014, has been integrated into the Geospatial eXploitation Products business. The new organisation is combining enhanced full motion video imagery capabilities with existing geospatial analytic software products to pursue new opportunities in the US intelligence and defence communities.

From 1 January 2016, the GEOINT-ISR business will be managed and reported within Electronic Systems.

Global Analysis & Operations
In full motion video and intelligence, surveillance and reconnaissance analysis, the business has more than 500 analysts globally sustaining mission critical activities on programmes worth over $400m (£271m).

The business secured a five-year re-compete contract worth up to $145m (£98m) to provide counter-terrorism analysis services.

Integrated Electronics & Warfare Systems
The business secured a five-year, $278m (£189m) re-compete award to provide logistics and sustainment engineering services for US Department of Defense radar, optical and telemetry systems used by the Department of Defense, Department of Energy and NASA, as well as international government agencies.

On the US Air Force's Intercontinental Ballistic Missile Integration Support Contractor programme, the business has been awarded $174m (£118m) in additional engineering scope change proposals in 2015. Since assuming control of the programme in 2014, the team has supported five successful missile test launches.

The business was awarded a five-year US Marine Corps Air Traffic Control and Landing Systems re-compete contract, with a potential total value of $77m (£52m).

The US Army awarded BAE Systems a five-year contract, potentially worth $76m (£52m), to test Command, Control, Communications, Computers and Intelligence (C4i) systems for tactical vehicles, and then prototype, engineer and upgrade more than 2,000 vehicles per year.

IT Solutions
Intelligence & Security was selected to provide information technology services to the US government in a single-award contract with a potential value of over $1.0bn (£0.7bn) over a ten-year period.

The business secured a five-year re-compete award with a potential ceiling value of $47m (£32m) to continue its support of the US Department of Homeland Security Office of Biometric Identity Management with large-scale, mission-critical fingerprint analysis and verification services.

The business was selected for three important Indefinite Delivery, Indefinite Quantity (IDIQ) contracts in the year. Under the Network Operations and Infrastructure and Application Services Full and Open multiple-award contracts, the business is pursuing task orders to expand its IT services footprint with the US Air Force. The third IDIQ contract award positions the business to pursue task orders for mission support services to the Federal Bureau of Investigation.

Applied Intelligence

Applied Intelligence's markets are highly competitive with fast-changing customer requirements. It typically faces competition from multiple vendors. Whilst it has won positions on a number of framework agreements, business tendered under these contracts is still competitive. Whilst continuing to grow in the UK market, it was disappointing to note the loss in the Metropolitan Police Service Integration and Applications Management competition this year. The business continues to focus on delivering a value-for-money service to all its current and prospective customers in this area of government business.

The strategy for the Applied Intelligence business is to create market-leading positions in the commercial cyber security market and increasing the scale of systems and service integration contracts to the UK government and for government customers overseas.

The integration of the SilverSky business in the US, acquired in 2014 to accelerate the drive into the commercial cyber security market, has been a success and is substantially completed.

During the year, the business has invested in engineering and product development and the sales team to support growth. In 2015, Applied Intelligence recruited 1,200 employees, including 700 engineers.

Commercial Solutions

Commercial Solutions focuses on the provision of cyber security, counter-fraud and compliance software and solutions, primarily to commercial organisations.

The sale of products and services which provide multi-year or recurring revenue streams has continued to grow. Applied Intelligence's cloud-based email protection products, launched in Europe, Canada and Asia-Pacific during the year, have been deployed by a leading international airline and a leading UK media producer and broadcaster.

New managed security services awards include a three-year contract to provide advanced threat detection services to an international law firm and a three-year networking security monitoring services contract with one of the main national UK television broadcasters.

The CyberReveal™ threat analytics solution, which defends organisations against sophisticated cyber attacks, continues to receive orders from both new and existing customers, including major financial institutions in Europe and North America.

During the year, new NetReveal® wins included Metro Bank in the UK to provide a range of anti-money laundering services and a large credit union in the US to provide an enterprise fraud solution. Growth in existing accounts has included the procurement of a trade finance fraud solution by a large financial institution. The year also saw the successful implementation of a managed fraud analytics platform for Canadian National Insurance Crime Services (CANATICS), the largest insurance consortium in Canada.

UK Services

UK Services is a provider of systems integration and consulting services to UK government, national security customers and critical national infrastructure providers, with a particular focus on digital, data analytics and cyber security. The business has continued to grow.

The business has strengthened its relationship with Network Rail, being awarded a three-year contract for its business intelligence IT portfolio, winning a contract to provide cyber security systems integration services to help mitigate the cyber threats to the UK's national rail network and winning a contract to support the digital enablement of the UK rail network as part of Network Rail's Digital Railway Initiative.

Demand for Applied Intelligence's cyber security services continues, with contracts awarded for a cyber security and information assurance managed service at the Ministry of Justice, for digital identity and fraud analytics at the Department for Work and Pensions and to provide cyber threat intelligence strategy consulting services for a major international financial services group. The business has also been awarded a position on the UK government's Defence Science and Technology Laboratory framework for electronic warfare and cyber research.

Applied Intelligence's digital and data transformation business continues to grow, with new contracts including a data migration strategy project for the Atomic Weapons Establishment, a secure, cloud-based, open-source IT platform for Lloyd's Register and a digital capability assessment project for a leading UK television and broadband provider in support of its digital transformation programme.

International Services & Solutions

International Services & Solutions focuses on cyber and communications intelligence services and solutions for international governments and communications service providers, pulling through Applied Intelligence's commercial product-based solutions where relevant.

The business continues to see demand in Asia-Pacific and the Middle East in support of protection against national threats. In Europe, the business was awarded a contract to provide a long-term government partner with a solution to investigate new concepts for situational awareness using the IntelligenceReveal™ all-source analysis solution.

In the second half of the year, the business won major contracts to provide integrated intelligence solutions to support the missions of South European and Asian customers. It also won a substantial cyber security services contract in Asia to build an advanced Security Operations Centre.

Looking forward

Intelligence & Security

In the US, further clarity regarding potential market improvement was gained after Congress reached agreement on a new budget deal that provides for defence and domestic programme spending above the Budget Control Act caps through 2017.

In April, BAE Systems announced that it had engaged advisers to support a strategic assessment of the Intelligence & Security sector's Global Analysis & Operations, Integrated Electronics & Warfare Systems and IT Solutions businesses. The review determined that retaining the businesses within BAE Systems, Inc. delivers greater value.

Following a period of market contraction in the US government services sector, the Group believes the outlook is now stabilising.

Intelligence & Security has reduced costs to address government budgets, whilst pursuing growth opportunities, particularly in critical, mission-focused areas.

Applied Intelligence

Applied Intelligence has invested in engineering and product development and the sales team to grow further its order backlog and pipeline of opportunities from commercial and government customers in North America, Europe, Asia-Pacific and the Middle East.

1. Including share of equity accounted investments.
2. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.
3. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
4. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.
5. Comprises funded and unfunded unexecuted customer orders.

Segmental performance: Platforms & Services (US)

Platforms & Services (US), with 11,500 employees[1] and operations in the US, UK and Sweden, produces combat vehicles, weapons and munitions, and delivers US-based services and sustainment activities, including ship repair and the management of government-owned munitions facilities.

Operational and strategic highlights

– Award of a five-year contract worth up to $332m (£225m) to perform technical support for the US Army's Bradley Fighting Vehicle and M113 family of vehicles
– Low-Rate Initial Production contract options awarded, worth $245m (£166m), for US Army M109A7 (Paladin) self-propelled howitzers
– Contract worth $104m (£71m) awarded for the engineering and manufacturing development phase of the competition for the Amphibious Combat Vehicle 1.1 programme
– Secured naval gun system contracts with the US, Canada and Brazil
– FNSS received a new export order for the PARS wheeled armoured vehicle
– Continued challenges on commercial shipbuilding programmes
– Workforce reductions announced in commercial shipbuilding, ship repair and BAE Systems Hägglunds
– Sale of 75% interest in Land Systems South Africa completed

Financial performance

	2015	2014[2]
Sales[1]	**£2,779m**	£2,689m
Underlying EBITA[3]	**£177m**	£117m
Return on sales	**6.4%**	4.4%
Cash inflow[4]	**£100m**	£147m
Order intake[1]	**£2,737m**	£2,565m
Order backlog[1,5]	**£3.9bn**	£4.7bn

– Sales[1] reduced by 4% to $4.2bn (£2.8bn), or by just 1% on a like-for-like basis after adjusting for exchange translation and the South African business disposal. Higher than expected sales were seen on both ship repair activity and munitions volume.
– The business has delivered an improved return on sales of 6.4% (2014 4.4%). Whilst further charges had to be taken in the year on the commercial shipbuilding programmes, these were partly offset by improvements to the Radford munitions contract.
– Cash[4] conversion of underlying EBITA[3] was impacted by the utilisation of provisions on commercial shipbuilding programmes and of customer advances on the CV90 Norway contract, as well as the investment in the new floating dry dock facilities in San Diego.
– Order backlog[1,5] reduced to $5.8bn (£3.9bn) largely for the trading out of the five-year Multi-Ship, Multi-Option contracts in the ship repair business and the CV90 Norway programme.

Operational performance

As the US defence market stabilises, the business retains its focus on sustaining its franchise programmes and building a strong domestic and international pipeline, whilst optimising competitiveness by shaping and scaling operations.

US Combat Vehicles

In May, the US Army awarded BAE Systems a contract worth $110m (£75m) to convert 36 M88A1 recovery vehicles to the M88A2 Heavy Equipment Recovery Combat Utility Lift Evacuation System (HERCULES) configuration. The M88 plays an important role in maintaining the combat vehicle industrial base, with the first vehicle delivery scheduled for 2017. In October, BAE Systems received awards worth $31m (£21m) from the US Army to produce six M88A2 HERCULES vehicles and associated spare parts for the Australian government, as well as an additional vehicle and parts for the US Marine Corps.

Work has commenced on the US Army's Armored Multi-Purpose Vehicle (AMPV) programme and a preliminary design review was completed in June. BAE Systems is producing 29 vehicles under the engineering and manufacturing development phase. The total potential contract value for the initial programme phases is $1.2bn (£0.8bn), including options to produce 289 vehicles under Low-Rate Initial Production (LRIP). Anticipated full-rate production is expected to approach 3,000 vehicles.

The business was awarded a $29m (£20m) follow-on contract for trade studies and analysis related to the future infantry fighting vehicle. Under the contract, BAE Systems will develop concepts that span from modernising the Bradley vehicle to a new design, and will capitalise on technology created under the Ground Combat Vehicle programme.

In July, the US Army awarded BAE Systems a five-year contract worth up to $332m (£225m) to support ongoing service and improvements for the Bradley Fighting Vehicle and the M113 family of vehicles.

The business was notified in August that the Lockheed Martin Joint Light Tactical Vehicle team, of which BAE Systems was a member, was not selected for the LRIP contract. This competition outcome is currently in litigation.

In October, the business was awarded the final LRIP contract options, worth $245m (£166m), for the M109A7 self-propelled howitzers (Paladin) and their associated ammunition carriers. In March, the business delivered the first vehicles to the US Army under the previously awarded $335m (£227m) LRIP contract. The US Army's total acquisition objective is for 581 vehicle sets.

During the fourth quarter, BAE Systems completed contractor testing of six Bradley Engineering Change Proposal (ECP) 2 vehicles. Efforts are now underway to build an additional ten vehicles for US Army testing, with deliveries to begin in 2016. The Bradley ECP 2 programme helps to restore automotive performance to the Bradleys with a modified engine and transmission, and an upgraded generator and power distribution system.

In November, the US Marine Corps awarded BAE Systems, along with partner IVECO Defence, a contract worth $104m (£71m) for the engineering and manufacturing development phase of the Amphibious Combat Vehicle 1.1 programme. The award is one of two contracts for this phase, during which the BAE Systems team will produce 16 prototypes for Marine Corps testing. This competition outcome is currently being protested.

In 2015, BAE Systems was awarded two international Assault Amphibious Vehicle (AAV) contracts: an $82m (£56m) contract for the Brazilian Marine Corps under the US government's Foreign Military Sales programme to upgrade 23 vehicles, with deliveries expected in 2017; and an award from another international customer for advance work related to an expected production order for AAVs in 2016.

Weapon Systems and Munition Operations

In May, BAE Systems was awarded a contract for five Bofors 40 Mk4 naval guns for the Brazilian Navy. Series production of the guns has commenced, including local content in Brazil. Deliveries are scheduled to begin in 2016.

BAE Systems continues to work with the governments of India and the US to secure an award for M777 155mm lightweight howitzers. BAE Systems has proposed the establishment of an assembly, integration and test facility in partnership with an Indian company, which supports the Indian prime minister's 'Make in India' initiative.

In August, the business was awarded a contract to deliver up to six modified 25mm Mk 38 machine gun systems for the Royal Canadian Navy's Arctic Offshore Patrol Ship programme. Also in August, the US Navy awarded BAE Systems an $80m (£54m) contract to upgrade six Mk 45 naval guns to the Mod 4 configuration, with an option for four additional guns for an additional $50m (£34m) expected to be exercised in 2016.

In September, the business confirmed its selection by the UK Ministry of Defence as the preferred bidder to provide the gun system, known as the Maritime Indirect Fires System, for the Type 26 frigate. Subject to contract award, the business will provide the integrated gunnery system, which includes the Mk 45 Mod 4 naval gun system, along with an automated ammunition handling system, gun fire control system and qualified ammunition.

BAE Systems is executing on the re-baselined Archer artillery system for the Swedish government. The business delivered the first system in September, with deliveries planned to continue at a rate of two guns per month during 2016.

BAE Systems continues its partnership with the US Navy on the development of the Hyper Velocity Projectile and an Electromagnetic Railgun.

BAE Systems continues to manage operations at the Holston and Radford Army ammunition plants, receiving a $50m (£34m) contract for the continued production of MK 90 propellant grains, as well as a $30m (£20m) contract to modernise the Insensitive Munitions ingredient facility at Holston. In September, the business received $35m (£23m) in closing an historical pricing agreement. The business remains focused on enhancing performance under major facility modernisation contracts.

US Ship Repair and Modernisation
In the first quarter of 2015, BAE Systems announced a $100m (£68m) capital improvement programme at its San Diego, California, shipyard, principally for the construction of a new dry dock in anticipation of increased activity to support the US Navy's re-balance to the Pacific coast.

In the second half of 2015, the business received a number of fixed-price orders as the US Navy began to transition its contracting strategy for ship modernisation and repair. For over a decade, the Navy had awarded Multi-Ship, Multi-Option cost-plus contracts, which effectively bundled the maintenance of a class of ships into one multi-year contract. Starting on the East coast in the first half of 2016, the Navy is expected to award Indefinite Delivery, Indefinite Quantity repair orders with fixed-price terms on a ship-to-ship basis. During the year, the ship repair business received a total of $1.2bn (£0.8bn) in orders from the US Navy.

The Jacksonville, Florida, shipyard delivered its third Platform Support Vessel (PSV) during the summer for service in the Gulf of Mexico. In early 2016, the business delivered the fourth and final ship of the PSV class to the customer. Four additional ships are in various stages of construction in Jacksonville, Florida, and Mobile, Alabama, and the business expects to deliver these ships in 2016. The commercial shipbuilding business continued to experience challenges in the year, taking a $73m (£48m) charge against ongoing contracts, principally driven by the Mobile shipbuilding programmes.

The business is responding to lower demand due to declining US Navy ship repair and commercial shipbuilding and repair work by reducing workforce numbers. Redundancies initiated in 2015 could impact approximately 1,100 employees in Norfolk, Virginia, and Jacksonville, Florida, through the first quarter of 2016.

BAE Systems Hägglunds
Series production has commenced on the $865m (£587m) contract for CV90 Infantry Fighting Vehicles to Norway. The business completed BvS10 vehicle deliveries to Sweden in 2015 and will continue to execute retrofitting and provide spare parts and documentation.

In September, the business launched a new vehicle based on the BvS10 called the BvS10 BEOWULF, a highly mobile, modular and fully-amphibious vehicle with an impressive payload.

At the September Defence and Security Equipment International trade show in London, BAE Systems launched its BattleView 360 system that employs cutting-edge display and sensor technology to improve situational awareness for soldiers inside combat vehicles.

In 2015, the business completed 130 redundancies related to the unsuccessful CV90 Armoured Personnel Carrier bid in Denmark. With two major production programmes winding down, in the first quarter of 2016, the business initiated an additional redundancy notification that could impact up to 150 employees during the second half of the year.

FNSS
FNSS, the Turkish land systems joint venture, has continued production under the $524m (£356m) programme to produce 259 8x8 wheeled armoured vehicles for the Royal Malaysian Army.

FNSS received a new export order for the PARS wheeled armoured vehicle. Under this new contract, FNSS will deliver the PARS vehicle to its new customer in multiple configurations.

Production is underway on a contract to upgrade M113 tracked armoured personnel carriers for the Royal Saudi Land Forces.

Four competitive proposals have been submitted for combat vehicle programmes in Turkey and the Middle East, with award decisions expected in 2016 or 2017.

Business disposal
In April, the Group completed the sale of its shareholding in Land Systems South Africa.

Looking forward

In the US, further clarity regarding potential market improvement was gained after Congress reached agreement on a new budget deal that provides for defence and domestic programme spending above the Budget Control Act caps through 2017.

The business is underpinned by strong positions on key franchise programmes. These include, in the land domain, the US Army's AMPV, Bradley and Paladin programmes, and the CV90 for Norway. In the maritime domain, the Group has a strong position on naval gun programmes and US Navy ship repair. Some near-term reduction in ship repair and construction activity is anticipated as commercial shipbuilding contracts are completed and with expected changes to the basing of US Navy ships. Actions to address reduced workload at the Group's US East and Gulf coast shipyards are underway alongside measures to support anticipated subsequent expansion of ship repair operations in San Diego, California.

The business continues to pursue a range of domestic and international opportunities in combat vehicles, weapon systems and maritime support services.

1. Including share of equity accounted investments.
2. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.
3. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
4. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.
5. Comprises funded and unfunded unexecuted customer orders.

Segmental performance: Platforms & Services (UK)

Platforms & Services (UK), with 29,600 employees[1], comprises the Group's UK-based air, maritime, combat vehicle, munitions and shared services activities.

Operational and strategic highlights

- The Strategic Defence and Security Review announced in November 2015 provided clarity, continuity and stability for the UK business
- Contracts awarded for the expansion of Typhoon's capabilities
- £203m of F-35 Lightning II Lot 9 Low-Rate Initial Production orders received
- £859m demonstration phase contract awarded for the Type 26 frigate programme
- Full £1.3bn contract awarded for the fifth Astute Class submarine
- Artful, the third Astute Class submarine, accepted by the Royal Navy in November
- Third and final Khareef Class corvette accepted by the Royal Navy of Oman
- €188m (£139m) contract award for 515 cased-telescopic cannons for the Ministry of Defence secured by our 50% joint venture, CTA International

Financial performance

	2015	2014
Sales[1]	**£7,405m**	£6,623m
Underlying EBITA[2]	**£721m**	£772m
Return on sales	**9.7%**	11.7%
Cash inflow[3]	**£220m**	£173m
Order intake[1]	**£4,944m**	£5,386m
Order backlog[1]	**£17.8bn**	£20.1bn

- Sales[1] of £7.4bn were 12% higher than 2014. The increase came from a higher number of Saudi aircraft deliveries, trading of Radar and Defensive Aids Sub-System equipment on the European Typhoon Tranche 3 programme and the increasing activity in the Submarines business.
- The return on sales was at 9.7% (2014 11.7%). An impact from lower pension discount rates has been that the service cost charged to the income statement increases and, in 2015, that amounted to 0.5 percentage points of margin compared with 2014. In addition, the 2015 result includes the in-year impact from the announced Typhoon production slowdown decision.
- Cash performance was as expected with a cash inflow[3] of £220m (2014 £173m). Consumption of customer advances occurred on the Omani, Saudi and European Typhoon contracts. There have also been rationalisation costs charged against provisions created in prior years.
- Order backlog[1] reduced to £17.8bn (2014 £20.1bn) primarily from trading on the Typhoon aircraft and aircraft carrier programmes.

Operational performance

Military Air & Information

In the year, 18 Typhoon aircraft were delivered from the UK final assembly facility, of which 12 were delivered to Saudi Arabia. Cumulative aircraft deliveries to the UK, Germany, Italy and Spain total 227 of the contracted 236 Tranche 2 aircraft and 22 of the contracted 88 Tranche 3 aircraft. The 2014 issues delaying acceptance of Typhoon Tranche 3 aircraft from the Group's partners in Germany, Italy and Spain were resolved.

The Oman Typhoon and Hawk aircraft programme continues to meet all contractual milestones and is on track for commencement of deliveries in 2017.

In order to meet existing and anticipated orders and delivery schedules, BAE Systems is reducing the rate of Typhoon major unit production. This will help reduce production discontinuity and provide a more sustainable and competitive position for Typhoon manufacturing in the years ahead. The action involves a proposed workforce reduction of up to 371 roles.

Typhoon's capabilities continue to expand with the integration of the Captor E-Scan radar and Brimstone 2 missile.

BAE Systems continues to successfully support its UK and European customers' Typhoon and Tornado aircraft in delivering their operational commitments. The business supports its UK customer through availability-based service contracts, and contract extensions totalling £147m were received in the year.

On the F-35 Lightning II programme, BAE Systems completed delivery of 43 aft fuselage assemblies for the Low-Rate Initial Production (LRIP) Lot 8 contract. A £203m contract on LRIP Lot 9 for 57 aircraft sets was received in the year, with 11 aft fuselage assemblies completed. The forward price for LRIP Lot 10 for 94 aircraft sets has been agreed, with full contract award for both Lots 9 and 10 anticipated during 2016. A proposal for LRIP Lot 11 has been submitted to Lockheed Martin in advance of negotiations commencing in 2016.

Support continues to be provided to users of Hawk trainer aircraft around the world. In 2015, the Indian Navy and Air Force received five and 15 Hawk aircraft, respectively, built under the Batch 2 licence for 57 aircraft by Hindustan Aeronautics Limited. An order for a further 20 Hawk aircraft from the Indian Air Force is currently being negotiated.

Orders for £255m were received in the year for continued support to the RAF advanced jet training facility in North Wales.

Working jointly with Dassault Aviation, progress is being made in maturing and demonstrating critical technology and operational aspects for an unmanned combat air system.

Taranis, the stealthy unmanned combat air vehicle demonstrator designed and built by BAE Systems with UK industry partners and the Ministry of Defence, has successfully completed further phases of flight trials in the year.

During 2015, the business concluded 236 management redundancies following the announcement in October 2014, with a further 204 potential redundancies mitigated through redeployment within either the business or the wider Group.

In October, BAE Systems agreed to invest £20.6m in Reaction Engines Limited (REL) to acquire 20% of its share capital and also enter into a working partner relationship. REL is a privately-held company based in the UK developing the technologies needed for SABRE™ (Synergetic Air-Breathing Rocket Engine), a new aerospace engine class.

Maritime

The consolidation of BAE Systems' UK shipbuilding operations into Glasgow concluded in 2015.

Following completion of the assessment phase contract for the Type 26 frigate in March, an £859m demonstration phase contract was secured, covering detailed design activities and enabling BAE Systems to subcontract for key equipment with companies throughout the supply chain. The programme continues to employ over 1,000 employees.

The government's reaffirmed commitment to shipbuilding continuity in November's UK Strategic Defence and Security Review provides clarity and future opportunities for the Group's shipbuilding facilities and workforce in Scotland. This includes maintaining a fleet of 19 frigates and destroyers, including eight Type 26 frigates and a planned concept study followed by the design and build of a new class of lighter, flexible, general purpose frigates. There is also a commitment to build two additional Offshore Patrol Vessels.

On the aircraft carrier programme, HMS Queen Elizabeth commenced the commissioning of its key systems, which will continue through to the second half of 2016. Construction of HMS Prince of Wales continued, with the integration of the bow, forward island and bridge during the year. The final manufacturing block was delivered to Rosyth in December.

HMS Forth, the first of a second batch of River Class Offshore Patrol Vessels for the Royal Navy, is planned for delivery in 2017. The construction of HMS Medway, the second ship, commenced in June and the third ship, HMS Trent, in October. This programme supports shipbuilding skills and provides the springboard to transform the business between the carrier programme and the start of manufacture for the Type 26 frigate programme.

Following successful sea trials, final acceptance of the third and final Khareef Class corvette for the Royal Navy of Oman was achieved during the second half of the year.

Under the five-year, £600m Maritime Support Delivery Framework contract, secured in 2014, the business provides services at HM Naval Base Portsmouth and support to half of the Royal Navy's surface fleet. The provision of services under the contract progresses well with cost savings remaining on target.

BAE Systems manages the support, maintenance and upgrade of the Royal Navy's fleet of Type 45 destroyers.

Successful completion of the first in-water trials was achieved on the £270m Spearfish torpedo upgrade programme. The demonstration phase of the contract is planned to complete in 2019 prior to full manufacture.

The first phase of the joint UK and French Maritime Mine Counter Measures demonstrator programme, which may form the basis of a future Royal Navy unmanned system to combat the threat of underwater sea mines, progresses.

Following handover and customer acceptance in November, Artful, the third Astute Class attack submarine, is now being operated by the Royal Navy. Good progress continues on the remaining four boats. The full £1.3bn contract for the fifth boat was secured in November and further limit of liability funding of £30m for the seventh boat was also received.

The Successor submarine, the replacement for the Vanguard Class fleet, continues to advance functional and spatial design as the programme approaches its production stage. Preparations include a major programme of building works to ensure the Barrow site will be ready to begin manufacturing when the anticipated UK Ministry of Defence's investment decision is approved in 2016. At 31 December, BAE Systems has almost 8,000 employees and contractors in the Submarines business.

Combat Vehicles (UK)
The final five Terrier combat engineering vehicles were completed in the year.

A £7m contract for the assessment phase of the upgrade to the British Army land bridging system was secured in December.

Other orders totalling £50m for ongoing support to the previously supplied armoured and bridging vehicles were received in the year.

Munitions
Negotiations on the pricing for the next five years of the 15-year Munitions Acquisition Supply Solution partnering agreement with the Ministry of Defence, secured in 2008, continue.

A €188m (£139m) contract for 515 cased-telescopic cannons for the Ministry of Defence was secured in March by CTA International, a 50% joint venture between BAE Systems and Nexter.

Looking forward

Platforms & Services (UK) has a strong order backlog of long-term committed programmes and an enduring support business. The Strategic Defence and Security Review announced in November 2015 provided clarity, continuity and stability for the UK business.

In Military Air & Information, sales are underpinned by Typhoon and F-35 Lightning II aircraft production and in-service support. There are opportunities to secure future Typhoon export sales, supported by the announcement made in September relating to the supply of 28 aircraft for the Kuwait Air Force.

In Maritime, sales are underpinned by the design and subsequent build of the Successor submarine and Type 26 frigates, and the build of the Queen Elizabeth Class aircraft carriers, River Class Offshore Patrol Vessels and Astute Class submarines. The through-life support of existing and new platforms, together with their associated command and combat systems, provides a sustainable business in technical services and mid-life upgrades.

Combat Vehicles (UK) continues to pursue obsolescence management and upgrade programmes.

The Munitions business is underpinned by the 15-year Munitions Acquisition Supply Solution partnering agreement with the Ministry of Defence secured in 2008.

With the aim of continuously improving business delivery and efficiency, the Combat Vehicles (UK) and Munitions businesses, with effect from 1 January 2016, merged to form one business, BAE Systems Land (UK).

1. Including share of equity accounted investments.
2. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.

Segmental performance: Platforms & Services (International)

Platforms & Services (International), with 13,600 employees[1], comprises the Group's businesses in Saudi Arabia, Australia and Oman, together with its 37.5% interest in the pan-European MBDA joint venture.

Operational and strategic highlights

- 12 Typhoon aircraft delivered to Saudi Arabia in the year
- Continued support to the operational capabilities of the Royal Saudi Air Force and Royal Saudi Naval Forces
- Contract awarded in Saudi Arabia for a further 22 Hawk aircraft
- Re-organisation of portfolio of interests in industrial companies in Saudi Arabia progressed
- Customer acceptance of the second of two Landing Helicopter Dock ships in Australia
- Headcount reductions and an impairment of assets at the Williamstown shipyard
- Announced a consolidation of Australian operating divisions to reduce management costs and remain competitive
- The UK and French governments signed a treaty relating to complex weapons technology
- MBDA secured weapons package orders with Egypt and Qatar worth €1.1bn (£0.8bn) as part of agreed export contracts for Rafale aircraft

Financial performance

	2015	2014
Sales[1]	**£3,742m**	£3,572m
Underlying EBITA[2]	**£335m**	£366m
Return on sales	**9.0%**	10.2%
Cash inflow[3]	**£164m**	£881m
Order intake[1]	**£3,046m**	£3,398m
Order backlog[1]	**£10.2bn**	£11.6bn

- Sales[1] of £3.7bn were 5% up over 2014, or 9% on a constant currency basis, due to higher levels of support to the Salam Typhoon aircraft now in service and higher volumes of weapon systems.
- Underlying EBITA[2] of £335m (2014 £366m) is after charges totalling £53m in respect of the impairment and rationalisation in the Australian business.
- There was an operating cash inflow[3] of £164m (2014 £881m) which includes the second payment under the Salam Variation of Price agreement. However, some £200m of receivables were collected in December 2014, ahead of the contracted 2015 dates. In addition, customer advances were utilised against the Saudi aircraft training programme.
- Order backlog[1] continues to reduce as the 2013 awards of the five-year support contracts in Saudi Arabia trade out.

Operational performance

Saudi Arabia

On the Salam Typhoon programme, 12 aircraft were delivered in the year and, as at 31 December, 57 aircraft had been delivered to the Royal Saudi Air Force. Work on enhancing Typhoon's air-to-ground capability is progressing to schedule.

The Typhoon support contracts are operating well with all Key Performance Indicators meeting contractual levels.

Through the Saudi British Defence Co-operation Programme, the business continues to support the operational capabilities of the Royal Saudi Air Force (RSAF) and Royal Saudi Naval Forces. The modernisation of the RSAF's training aircraft fleet has been extended with an agreement for the supply of a further 22 Hawk aircraft, associated ground equipment and training aids. The original contract continues on schedule, with all 22 Hawk aircraft in advanced stages of production and the first aircraft having flown in September. Deliveries are due to commence in 2016. As at 31 December, a total of 46 of the 55 Pilatus PC-21 aircraft had been delivered. Training and support under five-year contracts continues.

The upgrade of Tornado aircraft and associated equipment procurement continues.

Under the Royal Saudi Naval Forces' Minehunter mid-life update programme, acceptance of the second ship is now expected in 2016 following the delayed completion of sea trials during the year. The third ship is due to be initiated into the upgrade programme in 2016. However, delivery timescales will be impacted by previous programme delays.

The planned re-organisation of the Group's portfolio of interests in a number of industrial companies in Saudi Arabia continues. Riyadh Wings Aviation Academy LLC has contracted to acquire a 49% shareholding in a Group subsidiary, Overhaul and Maintenance Company. The re-organisation supports BAE Systems' strategy to expand the customer base of its In-Kingdom Industrial Participation programme, promoting training, development and employment opportunities in line with the Saudi National Objective. As part of the re-organisation, the business plans to transfer a material proportion of its Saudi-based workforce to one of the local Saudi industrial companies. Work is ongoing to secure the necessary regulatory and stakeholder approvals to allow this to commence.

The In-Kingdom Industrial Participation programme continues to progress, with the Al Salam Aircraft Company being accredited as a repair agent for Typhoon windscreens and transparencies. Advanced Electronics Company, in which BAE Systems has a 50% shareholding, has secured further accreditations as a repair agent for Typhoon avionics equipment and produced critical avionics for use on the Hawk trainer aircraft. These capability transfer successes demonstrate BAE Systems' long-standing commitment to the development and growth of the Saudi Arabian aerospace industry, which plays a significant and increasing role in the delivery of its contracts in the country.

Australia

The second and final Landing Helicopter Dock warship, HMAS Adelaide, was accepted by the Australian customer in October and was commissioned into the fleet in December. In-service support to both Landing Helicopter Dock ships is provided by BAE Systems under a four-year contract.

Construction of ship blocks for the Air Warfare Destroyer (AWD) programme at the Williamstown shipyard continues, with production complete and acceptance achieved on 18 of the 21 contracted blocks at 31 December.

There is no contracted shipbuilding programme for the Williamstown shipyard following completion of the Landing Helicopter Dock programme in 2015 and delivery of the remaining AWD blocks in early 2016. As a result, BAE Systems announced, on 12 November, workforce reductions of up to 340 shipbuilding roles, of which 200 had been completed as at 31 December, with the remainder in the first half of 2016. Rationalisation and restructuring charges relating to these workforce reductions totalling A$37m (£18m) have been taken. In addition, a non-cash impairment charge of A$48m (£24m) has been taken against the carrying value of the Williamstown facility.

The fourth of the seven Anzac Class frigates to be modernised under the current Anti-Ship Missile Defence programme was accepted in September as planned. The fifth and sixth ships are undergoing their refits at the Henderson shipyard and are scheduled for acceptance during 2016.

BAE Systems has been selected as the Asia-Pacific regional prime contractor to undertake airframe maintenance, repair and overhaul for the F-35 Lightning II programme. This represents a significant growth opportunity and is expected to underpin the Group's aerospace sustainment activities in Australia over the next decade and beyond.

Negotiations have been completed with the Commonwealth on a revised delivery schedule for the delayed JP 2008 Phase 3F programme for enhanced satellite communications services to the Australian Defence Force.

In September, the business submitted its proposal for the multi-billion Australian dollar Land 400 Phase 2 Combat Reconnaissance Vehicle programme to the Commonwealth. The successful tenderers are participating in funded risk mitigation trials during 2016.

On 12 November, further headcount reductions were announced as part of a restructuring to improve efficiency and management costs that reduced the number of operating divisions from three to two.

Oman

The two major contracts in Oman, the Typhoon and Hawk aircraft programme and the Khareef Class corvette programme, are being undertaken by Platforms & Services (UK).

The Typhoon and Hawk programme continues to meet all contracted milestones.

The third of three Khareef Class corvettes achieved final acceptance during the year.

BAE Systems has provided a significant proportion of Oman's in-service military equipment and the Group works closely with the Omani armed forces in supporting this equipment.

The business continues to fulfil its industrial participation obligations in Oman through delivery of an agreed training and knowledge transfer programme. An expansion of this programme has been contracted and, when delivered, will satisfy all of the Group's outstanding industrial participation obligations.

MBDA

Following completion of the Meteor development programme at the end of 2014, deliveries of production-standard missiles ordered by the six partner nation customers and first export customer continue to plan.

MBDA has secured a contract, worth £89m to BAE Systems, for the UK Advanced Short Range Air-to-Air Missile (ASRAAM) development and production programme.

The German government has announced its intention to buy the Medium Extended Air Defence System (MEADS) missile defence system being developed by MBDA in partnership with Lockheed Martin. Contract signature is expected in 2016, subject to German political approval. This decision provides an opportunity for MEADS to compete for significant export opportunities worldwide.

In November, a treaty was signed between the UK and French governments under which both countries committed to principles of inter-dependency and joint sovereignty in the field of key complex weapons technology.

MBDA has been awarded weapons package orders, worth €1.1bn (£0.8bn) to BAE Systems, as part of agreed export contracts for Rafale aircraft in Egypt and Qatar.

A significant number of ground-based air defence export campaigns continue to be pursued in central Europe and the Gulf region.

Looking forward

In the Kingdom of Saudi Arabia, the Group expects to sustain its long-term presence through delivering current programmes and industrialisation, and developing new business in support of the Saudi military forces. The planned re-organisation of the Group's portfolio of interests in a number of industrial companies in Saudi Arabia is intended to increase growth prospects and reinforce an ongoing commitment to support the national objectives of local skills and technology development, increasing employment and developing an indigenous defence industry.

In Australia, the 2015 Federal Budget statement confirmed the government's commitment to increasing annual defence expenditure to 2% of Gross Domestic Product within a decade of the budget. The Group continues to reinforce its commitment to Australia and is exploring further opportunities to provide leading defence capabilities across all domains.

In Oman, the business continues to provide support to its products in service to position for future requirements. The Typhoon and Hawk aircraft programme is on track for commencement of deliveries in 2017.

MBDA continues to build on the effective partnerships it has established with its domestic customers and has secured export opportunities that underpin future growth.

1. Including share of equity accounted investments.
2. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3. Net cash inflow from operating activities after capital expenditure (net), financial investment and dividends from equity accounted investments.

Consolidated income statement
for the year ended 31 December

	Notes	2015 £m	2015 Total £m	2014 £m	2014 Total £m
Continuing operations					
Combined sales of Group and share of equity accounted investments	2		**17,904**		16,637
Less: share of sales of equity accounted investments	2		**(1,117)**		(1,207)
Revenue	2		**16,787**		15,430
Operating costs			**(15,622)**		(14,387)
Other income			**227**		174
Group operating profit			**1,392**		1,217
Share of results of equity accounted investments			**110**		83
Underlying EBITA[1]		**1,683**		1,702	
Non-recurring items		**26**		–	
EBITA		**1,709**		1,702	
Amortisation of intangible assets		**(108)**		(184)	
Impairment of intangible assets		**(78)**		(170)	
Financial income/(expense) of equity accounted investments		**3**		(30)	
Taxation expense of equity accounted investments		**(24)**		(18)	
Operating profit	2		**1,502**		1,300
Financial income		**241**		241	
Financial expense		**(653)**		(659)	
Finance costs	3		**(412)**		(418)
Profit before taxation			**1,090**		882
Taxation expense	4		**(147)**		(130)
Profit for the year			**943**		752
Attributable to:					
Equity shareholders			**918**		740
Non-controlling interests			**25**		12
			943		752
Earnings per share	5				
Basic earnings per share			**29.0p**		23.4p
Diluted earnings per share			**28.9p**		23.3p

1. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.

Consolidated statement of comprehensive income

for the year ended 31 December

	2015			2014		
	Other reserves £m	**Retained earnings £m**	**Total £m**	Other reserves £m	Retained earnings £m	Total £m
Profit for the year	**–**	**943**	**943**	–	752	752
Other comprehensive income						
Items that will not be reclassified to the income statement:						
Remeasurements on retirement benefit schemes:						
Subsidiaries	**–**	**864**	**864**	–	(2,023)	(2,023)
Equity accounted investments	**–**	**21**	**21**	–	(73)	(73)
Tax on items that will not be reclassified to the income statement	**–**	**(261)**	**(261)**	–	503	503
Items that may be reclassified to the income statement:						
Currency translation on foreign currency net investments:						
Subsidiaries	**260**	**–**	**260**	277[1]	–	277[1]
Equity accounted investments	**(45)**	**–**	**(45)**	(13)[1]	–	(13)[1]
Reclassification of cumulative currency translation reserve on disposal	**20**	**–**	**20**	–	–	–
Fair value (loss)/gain on available-for-sale financial assets	**–**	**(1)**	**(1)**	–	4	4
Amounts credited/(charged) to hedging reserve:						
Subsidiaries	**11**	**–**	**11**	(92)	–	(92)
Equity accounted investments	**(36)**	**–**	**(36)**	–	–	–
Tax on items that may be reclassified to the income statement	**5**	**–**	**5**	19	–	19
Total other comprehensive income for the year (net of tax)	**215**	**623**	**838**	191	(1,589)	(1,398)
Total comprehensive income for the year	**215**	**1,566**	**1,781**	191	(837)	(646)
Attributable to:						
Equity shareholders	**216**	**1,541**	**1,757**	191	(849)	(658)
Non-controlling interests	**(1)**	**25**	**24**	–	12	12
	215	**1,566**	**1,781**	191	(837)	(646)

1. Restated.

Consolidated statement of changes in equity

for the year ended 31 December

	Attributable to equity holders of the parent						
	Issued share capital £m	Share premium £m	Other reserves £m	Retained earnings £m	Total £m	Non-controlling interests £m	Total equity £m
At 1 January 2015	87	1,249	5,061	(4,555)	1,842	35	1,877
Profit for the year	–	–	–	918	918	25	943
Total other comprehensive income for the year	–	–	216	623	839	(1)	838
Share-based payments	–	–	–	44	44	–	44
Net sale of own shares	–	–	–	1	1	–	1
Ordinary share dividends	–	–	–	(655)	(655)	(40)	(695)
Disposal of non-controlling interest	–	–	–	–	–	(6)	(6)
At 31 December 2015	**87**	**1,249**	**5,277**	**(3,624)**	**2,989**	**13**	**3,002**
At 1 January 2014	89	1,249	4,868	(2,825)	3,381	37	3,418
Profit for the year	–	–	–	740	740	12	752
Total other comprehensive income for the year	–	–	191	(1,589)	(1,398)	–	(1,398)
Share-based payments	–	–	–	42	42	–	42
Net purchase of own shares	(2)	–	2	(281)	(281)	–	(281)
Ordinary share dividends	–	–	–	(642)	(642)	(14)	(656)
At 31 December 2014	87	1,249	5,061	(4,555)	1,842	35	1,877

Consolidated balance sheet
as at 31 December

	Notes	**2015 £m**	2014 £m
Non-current assets			
Intangible assets		**10,117**	9,983
Property, plant and equipment		**1,698**	1,589
Investment property		**120**	129
Equity accounted investments		**250**	229
Other investments		**6**	7
Other receivables		**275**	347
Retirement benefit surpluses	6	**193**	162
Other financial assets		**107**	38
Deferred tax assets		**985**	1,327
		13,751	13,811
Current assets			
Inventories		**726**	690
Trade and other receivables including amounts due from customers for contract work		**2,940**	2,850
Current tax		**4**	7
Other financial assets		**105**	46
Cash and cash equivalents		**2,537**	2,308
Assets held for sale		**20**	76
		6,332	5,977
Total assets		**20,083**	19,788
Non-current liabilities			
Loans		**(3,775)**	(2,868)
Other payables		**(1,020)**	(932)
Retirement benefit obligations	6	**(4,694)**	(5,530)
Other financial liabilities		**(72)**	(79)
Deferred tax liabilities		**(13)**	(21)
Provisions		**(354)**	(436)
		(9,928)	(9,866)
Current liabilities			
Loans and overdrafts		**(237)**	(482)
Trade and other payables		**(6,162)**	(6,670)
Other financial liabilities		**(130)**	(107)
Current tax		**(315)**	(448)
Provisions		**(301)**	(315)
Liabilities held for sale		**(8)**	(23)
		(7,153)	(8,045)
Total liabilities		**(17,081)**	(17,911)
Net assets		**3,002**	1,877
Capital and reserves			
Issued share capital		**87**	87
Share premium		**1,249**	1,249
Other reserves		**5,277**	5,061
Retained earnings – deficit		**(3,624)**	(4,555)
Total equity attributable to equity holders of the parent		**2,989**	1,842
Non-controlling interests		**13**	35
Total equity		**3,002**	1,877

Approved by the Board on 17 February 2016 and signed on its behalf by:

I G King	**P J Lynas**
Chief Executive	Group Finance Director

Consolidated cash flow statement

for the year ended 31 December

	Notes	**2015 £m**	2014 £m
Profit for the year		**943**	752
Taxation expense		**147**	130
Research and development expenditure credits		**(65)**	–
Share of results of equity accounted investments		**(110)**	(83)
Finance costs		**412**	418
Depreciation, amortisation and impairment		**460**	657
Profit on disposal of property, plant and equipment		**(28)**	(20)
Profit on disposal of investment property		**(41)**	(12)
Profit on disposal of non-current other investments		**(1)**	–
Loss on disposal of businesses		**24**	–
Fair value gain		**–**	(47)
Cost of equity-settled employee share schemes		**44**	42
Movements in provisions		**(139)**	(153)
Decrease in liabilities for retirement benefit obligations		**(234)**	(345)
(Increase)/decrease in working capital:			
Inventories		**(6)**	(1)
Trade and other receivables		**60**	197
Trade and other payables		**(542)**	(622)
Cash inflow from operating activities		**924**	913
Interest paid		**(180)**	(152)
Taxation paid		**(116)**	(92)
Net cash inflow from operating activities		**628**	669
Dividends received from equity accounted investments		**41**	63
Interest received		**7**	7
Purchase of property, plant and equipment, and investment property		**(359)**	(263)
Purchase of intangible assets		**(54)**	(59)
Proceeds from sale of property, plant and equipment, and investment property		**136**	539
Proceeds from sale of non-current other investments		**1**	–
Purchase of subsidiary undertakings		**(5)**	(233)
Cash and cash equivalents acquired from purchase of subsidiary undertakings		**–**	3
Equity accounted investment funding		**(8)**	(2)
Proceeds from sale of subsidiary undertakings		**34**	–
Cash and cash equivalents disposed of with subsidiary undertakings		**(13)**	–
Net cash (outflow)/inflow from investing activities		**(220)**	55
Net sale/(purchase) of own shares		**1**	(281)
Equity dividends paid	7	**(655)**	(642)
Dividends paid to non-controlling interests		**(40)**	(14)
Cash inflow from matured derivative financial instruments		**12**	8
Cash inflow from movement in cash collateral		**3**	10
Cash inflow from loans		**1,625**	679
Cash outflow from repayment of loans		**(1,135)**	(398)
Net cash outflow from financing activities		**(189)**	(638)
Net increase in cash and cash equivalents		**219**	86
Cash and cash equivalents at 1 January		**2,313**	2,222
Effect of foreign exchange rate changes on cash and cash equivalents		**5**	5
Cash and cash equivalents at 31 December		**2,537**	2,313
Comprising:			
Cash and cash equivalents		**2,537**	2,308
Cash and cash equivalents (included within assets held for sale)		**–**	6
Overdrafts		**–**	(1)
Cash and cash equivalents at 31 December		**2,537**	2,313

Notes to the accounts

1. Preparation

The consolidated financial statements of BAE Systems plc have been prepared on a going concern basis and in accordance with EU-endorsed International Financial Reporting Standards (IFRS) and the Companies Act 2006 applicable to companies reporting under IFRS.

The consolidated financial statements are presented in pounds sterling and, unless stated otherwise, rounded to the nearest million. They have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, and other relevant financial assets and financial liabilities (including derivative instruments).

2. Segmental analysis

Sales and revenue by reporting segment

	Combined sales of Group and share of equity accounted investments		Less: sales by equity accounted investments		Add: sales to equity accounted investments		Revenue	
	2015 £m	2014[1] £m	**2015 £m**	2014 £m	**2015 £m**	2014 £m	**2015 £m**	2014[1] £m
Electronic Systems	**2,638**	2,415	**(72)**	(74)	**72**	74	**2,638**	2,415
Cyber & Intelligence	**1,848**	1,658	**–**	–	**–**	–	**1,848**	1,658
Platforms & Services (US)	**2,779**	2,689	**(101)**	(83)	**–**	–	**2,678**	2,606
Platforms & Services (UK)	**7,405**	6,623	**(1,524)**	(1,207)	**1,438**	1,104	**7,319**	6,520
Platforms & Services (International)	**3,742**	3,572	**(785)**	(793)	**–**	–	**2,957**	2,779
HQ	**237**	279	**(237)**	(279)	**–**	–	**–**	–
	18,649	17,236	**(2,719)**	(2,436)	**1,510**	1,178	**17,440**	15,978
Intra-group sales/revenue	**(745)**	(599)	**–**	–	**92**	51	**(653)**	(548)
	17,904	16,637	**(2,719)**	(2,436)	**1,602**	1,229	**16,787**	15,430

Reporting segment result

	Underlying EBITA[2]		Non-recurring items[3]		Amortisation of intangible assets[4]		Impairment of intangible assets		Reporting segment result	
	2015 £m	2014[1] £m	**2015 £m**	2014 £m	**2015 £m**	2014[1] £m	**2015 £m**	2014[1] £m	**2015 £m**	2014[1] £m
Electronic Systems	**396**	373	**–**	–	**(18)**	(14)	**–**	(1)	**378**	358
Cyber & Intelligence	**145**	153	**–**	–	**(57)**	(61)	**(78)**	(4)	**10**	88
Platforms & Services (US)	**177**	117	**(24)**	–	**(13)**	(15)	**–**	(165)	**140**	(63)
Platforms & Services (UK)	**721**	772	**50**	–	**(11)**	(84)	**–**	–	**760**	688
Platforms & Services (International)	**335**	366	**–**	–	**(9)**	(10)	**–**	–	**326**	356
HQ[5]	**(91)**	(79)	**–**	–	**–**	–	**–**	–	**(91)**	(79)
	1,683	1,702	**26**	–	**(108)**	(184)	**(78)**	(170)	**1,523**	1,348
Financial income/(expense) of equity accounted investments									**3**	(30)
Taxation expense of equity accounted investments									**(24)**	(18)
Operating profit									**1,502**	1,300
Finance costs									**(412)**	(418)
Profit before taxation									**1,090**	882
Taxation expense									**(147)**	(130)
Profit for the year									**943**	752

1. Re-presented for the reallocation of the Integrated Electronics & Warfare Systems activities from Platforms & Services (US) to Cyber & Intelligence.
2. Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3. In 2015, Platforms & Services (US) comprises a loss on the sale of the Group's 75% holding in BAE Systems Land Systems South Africa (Pty) Limited and Platforms & Services (UK) includes research and development expenditure credits relating to 2013 and 2014.
4. The reduction in amortisation of intangible assets primarily reflects acquired intangible assets fully amortising in 2014 in the Group's Maritime business within Platforms & Services (UK).
5. In 2014, HQ included a £30m benefit from re-assessment of a long-term liability.

3. Finance costs

	2015 £m	2014 £m
Interest income	**17**	28
Gain on remeasurement of financial instruments at fair value through profit or loss	**167**	99
Foreign exchange gains	**57**	114
Financial income	**241**	241
Interest expense on bonds and other financial instruments	**(175)**	(177)
Facility fees	**(4)**	(4)
Net present value adjustments	**(29)**	(48)
Net interest expense on retirement benefit obligations	**(192)**	(147)
Loss on remeasurement of financial instruments at fair value through profit or loss	**(72)**	(75)
Foreign exchange losses	**(181)**	(208)
Financial expense	**(653)**	(659)
Finance costs	**(412)**	(418)

Additional analysis

	2015 £m	2014 £m
Finance costs:		
Group	**(412)**	(418)
Share of equity accounted investments	**3**	(30)
	(409)	(448)
Analysed as:		
Underlying interest expense:		
Group	**(191)**	(201)
Share of equity accounted investments	**(3)**	(3)
	(194)	(204)
Other:		
Group:		
Net interest expense on retirement benefit obligations	**(192)**	(147)
Fair value and foreign exchange adjustments on financial instruments and investments	**(29)**	(70)
Share of equity accounted investments:		
Net interest expense on retirement benefit obligations	**(8)**	(8)
Fair value and foreign exchange adjustments on financial instruments and investments	**14**	(19)
	(409)	(448)

4. Taxation expense

Reconciliation of taxation expense

The following table reconciles the theoretical income tax expense, using the UK corporation tax rate, to the reported tax expense. The reconciling items represent, besides the impact of tax rate differentials and changes, non-taxable benefits or non-deductible expenses arising from differences between the local tax base and the reported financial statements.

	2015 £m	2014 £m
Profit before taxation	**1,090**	882
UK corporation tax rate	**20.25%**	21.5%
Expected income tax expense	**(221)**	(190)
Effect of tax rates in foreign jurisdictions, including US state taxes	**(69)**	(46)[1]
Effect of intra-group financing	**13**	13[1]
Expenses not tax effected	**(13)**	(12)
Income not subject to tax	**41**	32[1]
Research and development tax credits and patent box benefits	**7**	29
Non-deductible goodwill impairment	**(15)**	(35)
Chargeable gains and non-taxable gains/non-deductible losses on disposal of businesses	**(7)**	–
Utilisation of previously unrecognised tax losses	**4**	3
Adjustments in respect of prior years[2]	**115**	61
Adjustments in respect of equity accounted investments	**22**	18
Tax rate adjustment	**(5)**	–
Other	**(19)**	(3)
Taxation expense	**(147)**	(130)

Calculation of the underlying effective tax rate

	2015 £m	2014 £m
Profit before taxation	**1,090**	882
Add back:		
Taxation expense of equity accounted investments	**24**	18
Loss on disposal of businesses	**24**	–
Goodwill impairment	**75**	161
Adjusted profit before taxation	**1,213**	1,061
Taxation expense	**(147)**	(130)
Taxation expense of equity accounted investments	**(24)**	(18)
Exclude: Re-assessment of existing tax provisions[2]	**–**	(51)
Adjusted taxation expense (including equity accounted investments)	**(171)**	(199)
Underlying effective tax rate	**14%**	19%
Adjusted profit before taxation (above)	**1,213**	1,061
Exclude: Research and development expenditure credits[3]	**(77)**	–
	1,136	1,061
Adjusted taxation expense (including equity accounted investments) (above)	**(171)**	(199)
Exclude: Adjustments relating to research and development expenditure credits[3]	**68**	–
Exclude: Adjustment of tax provisions[2]	**(134)**	–
	(237)	(199)
Underlying effective tax rate, excluding research and development expenditure credits[3] and adjustment of tax provisions[2]	**21%**	19%

1. Re-presented.
2. 2015 includes credits totalling £134m in respect of the adjustment of certain UK and overseas tax provisions in the light of clarification and rulings received. 2014 included a £51m credit in respect of the re-assessment of existing tax provisions where information received in the year enabled the estimate to be updated, which was excluded from the calculation of the underlying effective tax rate.
3. In 2013, UK legislation changed so that UK government credits for research and development spend are now accounted for as part of operating profit rather than as part of taxation expense. This treatment was optional for the first three years. During 2015, the Group exercised that option, effective from 2013, and has reflected this change in the 2015 accounts. The adjustment reverses this treatment to show an underlying effective tax rate that is comparable with the prior year. The £77m excluded from profit before taxation comprises £50m included in non-recurring items relating to 2013 and 2014 and £27m included in underlying EBITA relating to 2015, of which £12m relates to the Group's share of equity accounted investments. The £68m includes £45m relating to the £50m included in non-recurring items.

5. Earnings per share

	2015			2014		
	£m	**Basic pence per share**	**Diluted pence per share**	£m	Basic pence per share	Diluted pence per share
Profit for the year attributable to equity shareholders	**918**	**29.0**	**28.9**	740	23.4	23.3
(Deduct)/add back:						
Re-assessment of existing tax provisions	**–**			(51)		
Non-recurring items, post tax	**19**			–		
Net interest expense on retirement benefit obligations, post tax[1]	**158**			126		
Fair value and foreign exchange adjustments on financial instruments and investments, post tax[1]	**12**			72		
Amortisation and impairment of intangible assets, post tax[1]	**88**			156		
Impairment of goodwill	**75**			161		
Underlying earnings, post tax	**1,270**	**40.2**	**40.1**	1,204	38.0	37.9

	Millions	**Millions**	Millions	Millions
Weighted average number of shares used in calculating basic earnings per share	**3,161**	**3,161**	3,165	3,165
Incremental shares in respect of employee share schemes		**10**		10
Weighted average number of shares used in calculating diluted earnings per share		**3,171**		3,175

1. The tax impact is calculated using the underlying effective tax rate, excluding research and development expenditure credits and adjustment of tax provisions, of 21% (2014 19%).

6. Retirement benefit obligations

	UK £m	US and other £m	Total £m
Total IAS 19 deficit at 1 January 2015	(6,066)	(746)	(6,812)
Actual return on assets excluding amounts included in interest expense	(335)	(198)	(533)
Decrease in liabilities due to changes in financial assumptions	1,348	202	1,550
Decrease in liabilities due to changes in demographic assumptions	–	29	29
Experience gains/(losses)	224	(4)	220
Additional contributions in excess of service cost	177	–	177
Recurring contributions in excess of service cost	44	53	97
Past service cost – plan amendments	(10)	–	(10)
Settlements	–	4	4
Net interest expense	(206)	(32)	(238)
Foreign exchange adjustments	–	(40)	(40)
Movement in US healthcare schemes	–	2	2
Total IAS 19 deficit at 31 December 2015	**(4,824)**	**(730)**	**(5,554)**
Allocated to equity accounted investments and other participating employers	1,053	–	1,053
Group's share of IAS 19 deficit excluding Group's share of amounts allocated to equity accounted investments and other participating employers at 31 December 2015	**(3,771)**	**(730)**	**(4,501)**
Represented by:			
Retirement benefit surpluses	120	73	193
Retirement benefit obligations	(3,891)	(803)	(4,694)
	(3,771)	**(730)**	**(4,501)**

Certain of the Group's equity accounted investments participate in the Group's defined benefit schemes as well as Airbus SAS (Airbus), the Group's share of which was disposed of in 2006. As these schemes are multi-employer schemes, the Group has allocated a share of the IAS 19 pension deficit to its equity accounted investments and other participating employers.

In December 2015, BAE Systems, Airbus and the scheme trustees agreed to work towards the creation of a separate Airbus section of the BAE Systems Pension Scheme (Main Scheme) in 2016 with the allocation of the deficit to the BAE Systems and Airbus sections based on each member's last employer. This allocation methodology is considered to represent a better estimate of the deficit allocation than the relative payroll contributions of active members and has been reflected in the allocation of the IAS 19 pension deficit in the Main Scheme at 31 December 2015. The impact of this change on the amounts allocated at 31 December 2015 is an increase of £187m (£153m post-tax) in the Group's share of the reported IAS 19 deficit. Currently, in the event that an employer who participates in the Group's pension schemes fails or cannot be compelled to fulfil its obligations as a participating employer, the remaining participating employers are obliged to collectively take on its obligations. The Group considers the likelihood of this event arising as remote. However, following the creation of an Airbus section of the Main Scheme, the Group's obligation in respect of Airbus is expected to be removed.

With the exception of the allocation of the Main Scheme deficit to Airbus, the deficit allocation method for other employers of the Main Scheme and for all other schemes is based on the relative payroll contributions of active members, which is consistent with prior years and is intended to reflect a reasonable approximation of the share of the deficit.

Funding

The majority of the UK and US defined benefit pension schemes are funded by the Group's subsidiaries, equity accounted investments and other participating employers. The individual pension schemes' funding requirements are based on actuarial measurement frameworks set out in their funding policies.

For funding valuation purposes, pension scheme assets are included at market value, whilst the liabilities are determined based on prudent assumptions set by the trustees following consultation with scheme actuaries.

The separate actuarial valuations for funding purposes include assumptions which differ from the actuarial assumptions used for IAS 19 accounting purposes. The latest valuations of the Main Scheme and BAE Systems 2000 Pension Plan were performed as at 31 March 2014 and showed a funding deficit of £2.6bn. The total net funding deficit in respect of all of the UK schemes was £2.7bn. Deficit recovery plans agreed with the trustees of the relevant schemes run until 2026.

The results of future triennial valuations and associated funding requirements will be impacted by the future performance of investment markets, and interest and inflation rates.

The total Group contributions made to the defined benefit schemes in the year ended 31 December 2015 were £438m (2014 £548m) excluding those amounts allocated to equity accounted investments and participating employers of £98m (2014 £92m). This includes additional contributions of £33m into the UK schemes relating to the share buyback programme (2014 £108m).

In 2016, the Group expects to make contributions at a similar level to the recurring contributions and deficit funding as made in 2015.

The Group incurred a charge of £140m (2014 £125m) in relation to defined contribution schemes for employees.

Principal actuarial assumptions

The assumptions used are estimates chosen from a range of possible actuarial assumptions which, due to the long-term nature of the obligation covered, may not necessarily occur in practice.

	UK			US		
	2015	2014	2013	**2015**	2014	2013
Financial assumptions						
Discount rate (%)	**3.9**	3.6	4.5	**4.5**	4.1	4.9
Inflation (%)	**3.2**	3.2	3.4	**n/a**	n/a	n/a
Rate of increase in salaries (%)	**3.2**	3.2	3.4	**n/a**	n/a	n/a
Rate of increase in deferred pensions (%)	**2.3/3.2**	2.3/3.2	2.5/3.4	**n/a**	n/a	n/a
Rate of increase in pensions in payment (%)	**1.8 – 3.6**	1.8 – 3.6	1.9 – 3.7	**n/a**	n/a	n/a
Demographic assumptions						
Life expectancy of a male currently aged 65 (years)	**87 – 89**	87 – 89	87 – 89	**87**	87	84
Life expectancy of a female currently aged 65 (years)	**89 – 90**	89 – 90	89 – 90	**89**	89	86
Life expectancy of a male currently aged 45 (years)	**89 – 91**	89 – 91	88 – 90	**87**	87	84
Life expectancy of a female currently aged 45 (years)	**91 – 92**	91 – 92	91 – 92	**89**	89	86

Sensitivity analysis
The sensitivity information has been derived using scenario analysis from the actuarial assumptions as at 31 December 2015 and keeping all other assumptions the same.

Financial assumptions
Changes in the following financial assumptions would have the following effect on the defined benefit pension obligation before allocation to equity accounted investments and other participating employers:

	(Increase)/ decrease £bn
Discount rate:	
0.1 percentage point increase	0.5
0.1 percentage point decrease	(0.5)
Inflation:	
0.1 percentage point increase	(0.5)
0.1 percentage point decrease	0.5

The sensitivity analysis does not allow for the impact of the Group's risk management activities in respect of interest rate and inflation risk on the valuation of the assets. Across all of its pension schemes, the Group is hedged against approximately 35% and 40% of interest rate and inflation risk, respectively, measured relative to the funding liabilities. The Group's US schemes are not indexed with inflation.

The sensitivity of the valuation of the liabilities to changes in the inflation assumption presented above assumes that a 0.1 percentage point change to expectations of future inflation results in a 0.1 percentage point change to all inflation-related assumptions (rate of increase in salaries, rate of increase in deferred pensions and rate of increase in pensions in payment) used to value the liabilities. However, upper and lower limits exist on the majority of inflation-related benefits such that a change in expectations of future inflation may not have the same impact on the inflation-related benefits, and hence will result in a smaller change to the valuation of the liabilities. Accordingly, extrapolation of the above results beyond the specific sensitivity figures shown may not be appropriate. To illustrate this, the (increase)/decrease in the defined benefit pension obligation resulting from larger changes in the inflation assumption would be as follows:

	(Increase)/ decrease £bn
Inflation:	
0.5 percentage point increase	(1.6)
0.5 percentage point decrease	1.6
1.0 percentage point increase	(3.2)
1.0 percentage point decrease	3.0

Demographic assumptions
Changes in the life expectancy assumption, including the benefit of longevity swap arrangements, would have the following effect on the total IAS 19 deficit:

	(Increase)/ decrease £bn
Life expectancy:	
One-year increase	(0.9)
One-year decrease	0.9

7. Equity dividends

	2015 £m	2014 £m
Prior year final 12.3p dividend per ordinary share paid in the year (2014 12.1p)	**389**	383
Interim 8.4p dividend per ordinary share paid in the year (2014 8.2p)	**266**	259
	655	642

After the balance sheet date, the directors proposed a final dividend of 12.5p per ordinary share. The dividend, which is subject to shareholder approval, will be paid on 1 June 2016 to shareholders registered on 22 April 2016. The ex-dividend date is 21 April 2016.

Shareholders who do not at present participate in the Company's Dividend Reinvestment Plan and wish to receive the final dividend in shares rather than cash should complete a mandate form for the Dividend Reinvestment Plan and return it to the registrars no later than 10 May 2016.

8. Acquisition and disposal of subsidiaries

Subsidiaries acquired during 2015

In June, the Group completed the acquisition of Eclipse Electronic Systems, Inc., a provider of advanced Intelligence, Surveillance and Reconnaissance products and services, for cash consideration of $8m (£5m).

Subsidiaries disposed of during 2015

In April, the Group completed the sale of its 75% holding in BAE Systems Land Systems South Africa (Pty) Limited for cash consideration of 655 million Rand (£36m).

	£m	£m
Cash consideration		36
Transaction costs paid		(2)
Cash proceeds		**34**
Net assets disposed:		
Intangible assets	(19)	
Property, plant and equipment	(9)	
Inventories	(7)	
Trade and other receivables	(9)	
Deferred tax assets	(3)	
Cash and cash equivalents	(13)	
Trade and other payables	8	
Deferred tax liabilities	2	
Provisions	6	
		(44)
Non-controlling interest disposed		6
Cumulative currency translation loss		(20)
Loss on disposal of businesses		**(24)**

Subsidiaries acquired during 2014

In 2014, the Group acquired Perimeter Internetworking Corp., trading as SilverSky; an additional 59% shareholding in Saudi Development and Training Company; and Signal Innovations Group, Inc. For all acquisitions made during 2014, there were no adjustments made in 2015 to the provisional fair values.

9. Fair value measurement

Fair value of financial instruments
Certain of the Group's financial instruments are held at fair value.

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the balance sheet date.

The fair values of financial instruments held at fair value have been determined based on available market information at the balance sheet date, and the valuation methodologies listed below:

– the fair values of forward foreign exchange contracts are calculated by discounting the contracted forward values and translating at the appropriate balance sheet rates;

– the fair values of both interest rate and cross-currency swaps are calculated by discounting expected future principal and interest cash flows and translating at the appropriate balance sheet rates; and

– the fair values of loans and overdrafts have been estimated by discounting the future cash flows to net present values using appropriate market-based interest rates prevailing at 31 December.

Due to the variability of the valuation factors, the fair values presented at 31 December may not be indicative of the amounts the Group would expect to realise in the current market environment.

Fair value hierarchy
The fair value measurement hierarchy is as follows:

– Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities;

– Level 2 – Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

– Level 3 – Inputs for the asset or liability that are not based on observable market data (i.e. unobservable inputs).

Carrying amounts and fair values of certain financial instruments

	2015		2014	
	Carrying amount £m	**Fair value £m**	Carrying amount £m	Fair value £m
Financial instruments measured at fair value:				
Non-current				
Available-for-sale financial assets	**6**	**6**	7	7
Other receivables[1]	**234**	**234**	238	238
Other financial assets	**107**	**107**	38	38
Other financial liabilities	**(72)**	**(72)**	(79)	(79)
Loans	**(346)**	**(346)**	(325)	(325)
Trade and other payables[1]	**(264)**	**(264)**	(262)	(262)
Current				
Other financial assets	**105**	**105**	46	46
Other financial liabilities	**(130)**	**(130)**	(107)	(107)
Financial instruments not measured at fair value:				
Non-current				
Loans	**(3,429)**	**(3,704)**	(2,543)	(2,900)
Current				
Cash and cash equivalents	**2,537**	**2,537**	2,308	2,308
Loans and overdrafts	**(237)**	**(241)**	(482)	(494)

1. Represents US deferred compensation plan assets and liabilities.

All of the financial assets and liabilities measured at fair value are classified as level 2 using the fair value hierarchy. There were no transfers between levels during the year.

Financial assets and liabilities in the Group's consolidated balance sheet are either held at fair value or their carrying value approximates to fair value, with the exception of loans, most of which are held at amortised cost.

The fair value of total loans and overdrafts estimated using market prices at 31 December 2015 is £4,291m (2014 £3,719m).

10. Related party transactions

Transactions occur with the equity accounted investments in the normal course of business, are priced on an arm's-length basis and settled on normal trade terms. The more significant transactions are disclosed below:

	Year ended 31 December 2015 £m	Year ended 31 December 2014 £m
Sales to related parties	**1,602**	1,229
Purchases from related parties	**379**	209

	31 December 2015 £m	31 December 2014 £m
Amounts owed by related parties	**75**	92
Amounts owed to related parties	**446**	494

11. Annual General Meeting

This year's Annual General Meeting will be held on 4 May 2016. Details of the resolutions to be proposed at that meeting will be included in the notice of Annual General Meeting that will be sent to shareholders at the end of March 2016.

12. Other information

The financial information for the year ended 31 December 2015 contained in this preliminary announcement was approved by the Board on 17 February 2016. This announcement does not constitute statutory accounts of the Company within the meaning of Section 435 of the Companies Act 2006, but is derived from those accounts.

Statutory accounts for the year ended 31 December 2014 have been delivered to the Registrar of Companies. Statutory accounts for the year ended 31 December 2015 will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

The auditors have reported on those accounts. Their reports were not qualified, did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report, and did not contain a statement under Section 498 (2) or (3) of the Companies Act 2006.