



**QinetiQ Group Plc  
FY2019 Preliminary  
Results**

Thursday, 23 May 2019

**Steve Wadey**

I would also like to thank our board members that have joined us here this morning. Welcome, Mark and James. I want to start by mentioning this picture. This is our state-of-the-art control room at our test range in Scotland, delivered through the long-term partnering agreement with the UK MOD, known as the LTPA. Last week, this control room was in action for NATO's live fire exercise, known as Formidable Shield 19, involving 13 nations, to test and train their operational readiness against the world's most demanding sea skimming and ballistic missile threats.

This picture is symbolic of the signature of the £1.3 billion contract amendment to the LTPA, the most significant milestone in QinetiQ's history since privatization, enabling us to modernise our core capabilities and secure a record order book of more than £3 billion. The LTPA now positions us as a world leader in the generation and assurance of defense and security capability at a national level and provides a strong platform for growth from the UK and international customers to deliver enhanced returns for our shareholders.

So, let's look at the agenda for this morning. I'll start by giving you the headlines. David will provide a commentary on our financial results. I'll come back and give you a strategic update, and then we will open up for any questions.

So, let's start with the headlines. This has been an excellent year, with strong operational performance. Orders are up 32 %, with a record high-quality backlog of £3.1 billion. Revenue is up 9 %, 8 % on an organic basis. We overcame strong profit headwinds by controlling our cost base and returned to organic profit growth, up 3 % after adjusting for no-recurring items. Cash performance remained strong, with 102 % cash conversion pre-Capex, and returns are healthy with EPS up 2 %, and a 5 % increase in the full-year dividend.

Our growth has been driven through disciplined execution of our strategy. Our largest achievement was signing the £1.3 billion LTPA contract that I mentioned a few moments ago. We improved our business maturity and won five major competitive long-term contracts in the UK, US, and Canada. We enhanced our training offering with the acquisition of EIS Aircraft Operations in Germany and made a strategic investment in Inzpire in the UK.

Over the past three years, we have grown the international share of our group revenue from 21% to 30% and engaged our employees in driving our strategy with a new all-employee bonus to align employee and shareholder interests by incentivising profitable growth. Looking forward, we start FY20 in a healthy position, with 74 % of our revenue under contract, up from 69 % last year. And our key priorities for the coming year are to maintain our strong operational performance through disciplined, good execution, program delivery, and control of our cost base; deliver the first year of the amended LTPA contract and develop growth opportunities; build on the success of our competitive wins and pursue our campaign-based approach globally; and continue our program of investment to maximize returns and drive sustainable, profitable growth. In summary, our growth strategy is delivering, and we are therefore maintaining expectations for group performance.

I'll now pass over to David to take you through the financial highlights.

David Smith:

Thank you, Steve, and good morning, everybody. I am going to begin with a summary of our financial performance for the year before going into more detail on the drivers.

As Steve mentioned, we delivered another strong year of financial performance. We have increased our revenue by 9 % to 911 million, and by 8 % on an organic basis. And we have delivered underlying profit growth of 1 % to 123.9 million. That was assisted by about 7 million of non-recurring trading items. I note in the prior year we benefited from around 9 million of non-recurring trading items. So, overall, we delivered a strong result.

We have also delivered a strong 28 % organic growth and order intake -- 32 % overall. And including the LTPA amendment, we have attained a record order backlog of £3.1 billion. And we have maintained strong discipline on cash, with 102 % underlying cash conversion before Capex.

Our underlying EPS rose to 19.7pence. I am proposing a full-year dividend of 6.6 pence, which is an increase of 5 % on the prior year, and in line with our progressive dividend policy.

So, starting with revenue, we've made really good progress in EMEA services, with 4 % organic revenue growth and a 22 % organic growth in global products. And combined, that gave us an overall organic revenue growth of 8 % in the period, which follows on from 3 % the prior year. And it's our third consecutive year of revenue growth.

Our acquisition of EIS and investment into Inzpire contributed another 15 million of revenue, resulting in reported revenue growth of 9 %. While it is not presented here, we are also making good progress against our strategy of becoming a more international business. We now generate 30 % of our revenue outside of the UK, which is up from 27 % a year ago and 21 % three years ago.

So, turning to the order intake, we made really strong progress on orders, with 28 % organic and 30 % overall growth. The main driver of our orders growth for the period was in EMEA services, which grew organically by £157 million, due both to secure long -- large, multi-year contracts as well as growth in smaller-value contracts.

In global products, orders are up about £10 million. And the acquisition of EIS and investment into Inzpire contributed a further £23 million of inorganic orders to the reported number. We have very good visibility at the start of Fiscal 20, with 74 % revenue cover for the year, which is compared to 69 % at the same time last year.

So, turning to operating profit, as I have already said, overall reported profit was up 1 %, and 3 % on an organic basis, excluding the impacts of non-recurring trading items, the acquisitions, and FX.

In the prior period, there were non-recurring items amounting to around £9 million. In this period, the one-time net benefits were lower, at £7 million.

In EMEA services, as we have been describing for a couple of years, we offset around £5 million of SSRO headwinds with £6.6 million in revenue growth and efficiency savings. And it is worth nothing that we successfully offset around £10 million of SSRO profit headwind over the past three years.

In global products, we saw a 7 % organic increase in profit. The acquisition of EIS and investment into Inzpire contributed a further £1.3 million over the four to five months of the

reported number. And that period saw increased investment in those businesses to support future growth.

So, overall -- excluding non-recurring items -- a good performance, with business growth and efficiencies more than offsetting the profit impact of single-source pricing.

So, turning more specifically to EMEA services, the chart here shows the split of major business revenue within the EMEA services segment. Revenue increased by 6 %, 4 % on an organic basis. And that was actually largely driven within our CIT business. The significant 50 % increase in orders was primarily due to some key order wins, including the £69 million related to the engineering delivery partner, which we delivered this past year, and £41 million for BATCIS.

Performance was particularly strong on smaller-value contracts, where we put real focus on improving our effectiveness here. They accounted for £115 million of the order growth, and in their nature, were mainly delivered in year.

Underlying operating profit increased by 2 %, assisted by non-recurring trading items of around £9 million and £1.3 million from EIS and Inzpire.

So, excluding the impacts of these non-recurring items, acquisitions, and FX, underlying operating profit grew by £1.4 million, a 2 % increase. And that was despite the SSRO headwinds. Total funded order of that log has increased significantly, following the strong orders performance and the signing of the LTPA agreement. We continue to benefit from good revenue visibility with 79 % of Fiscal 20 revenue under contract. Compared with 75 % at the start of the year. Turning next to global products. Here, the increase in orders was due to a contract to deliver the unmanned air system services to the Canadian armed forces, and also some growth from smaller contracts on QNA and QTS. Revenue is up 22 % organically, at £223 million. That was driven by new survivability contracts and robotics research work run by the US business and QTS target sales particularly to India.

Global products operating profit was up 7% on an organic basis, excluding around a £2 million charge on non-recurring and FX. So, this was driven by increased revenue in QTS and QNA, partially offset by some lower volume of high margin license income that we saw in the previous year.

We have 60% of global products Fiscal 20 revenue under contract as of the 1st of April, and that compares to 51% in the prior period. And that really reflects the fact that we have now got these key multi-year contracts secured over the last two years, which will provide more stability going forward.

Turning now to cash flow - overall, our operating cash conversion at 102 % before Capex was strong. We saw a further working capital unwind of just over £27 million, primarily due to higher receivables. Pensions outflow fell to £1.8 million, as we have ceased now the regular deficit repair contributions to the defined benefit pensions scheme.

And cash flow associated with Capex increased to £80 million, as we continue to invest in our LTPA contract. After Capex, we had net cash inflows of £45 million. So, it's worth emphasizing that, given the cash generative nature of our business, we expect to be able to fund that Capex and organic investment from those operating cash flows.

This next slide then presents the drivers of our movement in net cash during the period. So, in addition to the £45 million I have already taken you through, of operating cash flow after Capex, we had a £10 million tax payment and a small net interest inflow, resulting in a free cash flow of £35 million. The acquisition of EIS, and investment in Inzpire, and the repayment of a bank loan related to EIS resulted in an outflow of £81 million. And after the dividend and receipts from property disposals, we ended the cash -- the year with a net cash number of £188.5 million.

While it is not presented here, our pension remains in a very strong position -- particularly having recently completed a buy-in, which reduces risk on approximately one-third of the scheme. So, we have a pension surplus of £210 million net of deferred tax. Overall, with this net cash balance, the pension surplus, and the newly renegotiated committed facilities of £275 million, our balance sheet remains robust with the capacity to support future growth plans for the company.

So, having run through the Fiscal 19 performance -- and I wanted to explain more about the financial aspects of our strategy -- this slide, which I presented in November, illustrates how our capital allocation framework is working in practice. It gives a sense of how we are able to fund both the organic and inorganic investment in the business. Our strong balance sheet, plus the cash generation from the business, provides the flexibility to deploy capital, in terms of organic Capex, such as the LTPA contract investment and other commercial opportunities. And additionally, we are deploying capital and strategic opportunities, such as EIS and Inzpire, as well as our progressive dividend.

Underpinning the long-term sustainability of the business is the rigorous appraisal process we go through when making investment decisions. The first point is that we don't draw a distinction between organic and inorganic investment. We apply the same rigor to both. Secondly, we carefully evaluate the opportunity against a range of qualitative and quantitative factors, including a thorough consideration of the potential risks we face. On the quantitative side, we look at a range of return metrics and cash profiles. We take all of this and evaluate it against our risk adjusted cost of capital, ensuring that we deliver the right return versus the risk we are taking. This process was used on recent acquisitions, such as QTS, EIS, and Inzpire, as well as our considerations around the LTPA contract, and it's now standard practice for all major investments.

So, the third slide is new, and it's really describing the overall picture of our financial strategy, which is focused on long-term and sustainable revenue and profit growth to deliver value to our shareholders. We're doing this by continuing to grow our revenues in a disciplined and thoughtful way. Steve will cover this in some more detail, but the investments we're making are increasing our abilities to both win and deliver longer term and higher value contracts. That brings many benefits to QinetiQ, most notably increase visibility, but also the ability to win further add-on work from these programs. We are being very selective and thoughtful in our business winning, with all the opportunities going through a rigorous approval process; the key element being that we really understand our customer requirements and the risks and how we will mitigate those risks as we move to more output-based contracts.

Complementing our growing top-line is a focus on delivering stable margins. As I have already mentioned, in EMEA services, the SSRO headwinds we faced over the last two or three years are abating. We are going to continue to invest to sustain our future growth. In global products, as we win more strategic longer term and higher value contracts, as well as increase our product portfolio, that will also improve the overall stability of margins. And we're going to

maintain our cost discipline as well.

Finally, we are going to ensure that this growth and investment will make and deliver the right and appropriate capital returns to our shareholders. And we will do this with a clear framework for evaluating opportunities and thoughtful use of the balance sheet I have already highlighted. Overall, I believe strongly that this financial strategy will deliver long-term profitable growth.

So, turning now to a few technical factors, I've updated these for the forecast for Fiscal 20. With a positive cash balance, our underlying net finance costs are expected to remain minimal. Our effective tax rate last year was 10.1 %, and we anticipate this to begin to increase a little in Fiscal 20, due to the greater proportion of international revenues. We now also expect the cash outflow to increase in Fiscal 20 as well.

We've seen a continued unwind of our negative working capital position, as anticipated, and that will continue, we think, into Fiscal 20, in the region of £20 to £30 million. And the pension deficit recovery payments have now ceased through Fiscal 20, although we will continue to see just over £2.5 million in respect to the asset-backed funding scheme that we do.

Capital expenditure is likely to remain similar to Fiscal 19, in the £80 to £100 million range, as we continue to invest in our major contracts. And as I said at the LTPA presentation forum, through 2022, it will be in the £70 to £100 million range.

So, finally, our outlook. Outlined here are the outlooks from the preliminary statements released this morning. Our focus remains on continued strong operational delivery while investing in our growth strategy. In Fiscal 20, we anticipate delivering mid-single digit revenue growth, including some further organic revenue progression. We're maintaining expectations for group performance in Fiscal 20, excluding non-recurring trading items, with revenue growth at a stable margin, resulting in continued operating profit progress.

So, thank you. I'll now hand back to Steve.

Steve Wadey:

Thank you, David. So, the pace in the world around us continues to increase. Political uncertainty, security threats, economic pressure, technological change. The companies that proactively understand and respond to these dynamics are the companies that will do well. Three years ago, this is why I launched our vision-based strategy, to drive growth by transforming our customer focus and our competitiveness. And as a direct result, we are successfully growing in an uncertain world.

Three years on, our vision and strategy remain the same. My ambition is to build an integrated global defense and security company that is a world leader in its selected markets, leveraging its skills and capabilities across the group to grow. To realize this ambition, we have simplified and clarified our unique value proposition. We enable our customers to generate and assure their defense and security capability at a national level.

In simple terms, not only can we develop cutting-edge technology and turn it into capability; we can also tell you if that capability will work when it's critically needed and ensure you are trained and operationally ready. In essence, we work with our customers to create it, test it, and use it. A simple strategy underpinned by a clear value proposition provides us with greater focus for our investment choices, and creates value for our customers, and returns for our shareholders.

We've made great progress over the last three years. We've grown the company revenue by 21 %, with the international share of revenue increasing by to 30 %. And by focusing on our delivery of performance and cost base, we've overcome strong profit headwinds and returned to organic profit growth. We are coherently growing into our addressable market worth more than £8 billion per annum as illustrated in the graphic. We've established three joint ventures in the Middle East; made four strategic acquisitions to strengthen our capabilities; won five major long-term programs in significant growth areas; and finally, we secured the modernised LTPA contract.

I'd like to take this movement to thank our brilliant men and women who are committed and passionate about the work that they do for our customers, and their outstanding contribution to the performance that we have achieved over the last three years. Creating a high-performance culture is critical to ensure our growth strategy is both sustainable and profitable. And the key changes that we've made include robust strategic business planning to drive short-term decisions coherent with our long-term plan for growth; rigorous financial discipline to investment choices in core capabilities and acquisitions; stronger leadership and management capability fit for a growing company; building more capable business winning teams, with 60 % now new to the company; and greater discipline in program execution and focus on cost efficiencies.

Our continued success is underpinned by engaging our people in driving our strategy. This is why I've introduced a new app-based employee feedback tool to empower local teams to improve performance supported by a new all-employee bonus to align employee and shareholder interests by incentivizing and rewarding profitable growth.

The first part of our strategy is to lead and modernise UK defense test and evaluation. When we launched our strategy in 2016, my objective was to ensure that the capabilities that we delivered through the LTPA were relevant and competitive for future UK defense needs, as well as being attractive to international allies. The highlight of the year was securing the £1.3 billion amendment to the LTPA, building upon the £1 billion amendment that we signed in 2016.

We will invest a further £190 million, with appropriate returns to our shareholders, to modernise our ways of working infrastructure and equipment, ensuring our T&E capabilities enable the delivery of UK MOD's major programs, such as the Queen Elizabeth Class aircraft carriers, Dreadnought submarines, and future combat aircraft. Fundamental to this agreement is that we are changing the whole LTPA contract to be output-based, providing us with improved operational and commercial flexibility, to drive efficiency, and keeping us relevant, and giving us a platform for future growth.

Our focus is now on disciplined execution of the contract. Our investment in the December 2016 amendment has already made great progress. Modernisation of our air range continues to plan, enabling us to build a more complex and realistic exercises with more demanding threats. And the new test aircraft training service is operational, attracting international customers from Australia, Netherlands, Switzerland, and Singapore.

I'm now going to show you a short film that brings to life how our investment in test aircraft training has modernised the Empire Test Pilots' School, known as ETPS, and is already delivering benefits.

[Video Plays]

Steve Wadey

So, carrying the modernised LTPA contract positions, QinetiQ is a world-leader in the generation insurance of defense and security capability, and strengthens our foundation as the UK's leading provider of research, development, and test and evaluation, known as RDT&E. While the LTPA contract will deliver appropriate returns, in its own right, we have the opportunity to enhance returns by attracting additional customers.

Firstly, our objective is to increase our UK RDT&E market share by focusing on enabling the delivery of MOD's major programs, to attract further work from both MOD and industrial customers. Secondly, we will leverage the strengths of the LTPA to grow into near-adjacent markets, attracting international customers, to use our T&E capabilities, expanding the use of our T&E capabilities into training, and working with international customers to develop their indigenous T&E capabilities.

My long-term ambition remains to grow the company to a 50/50 UK international mix, over the next five to 10 years. And securing the LTPA is a major milestone towards realising this ambition and provides us with a strong platform for growth.

Our second strategic priority is to build an integrated global defense and security company by developing our three home countries, of the UK, US, and Australia; creating new home countries; and driving exports. Our business in the United States is performing well, winning significant orders in the rapidly-expanding area of robotic and autonomous systems, including two major programs of record, and continues to deliver, across its portfolio, survivability products, maritime systems, and Talon ground robots.

In Australia, we continue to expand into larger engineering services programs, as part of the major support partner role we secured with Nova Systems at the end of FY18. And, after three years of all this growth, we achieved another year or record order intake, breaking through the \$100 million mark for the first time.

We have a strategic objective to create a new home country in Canada. I'm, therefore, delighted that we've won a \$51 million order with the Canadian Armed Forces, a brilliant example of our strategy in action, leveraging the acquisition of QinetiQ target systems, known as QTS, with our group wide capabilities. This film explains how we won the program and the capability that it delivers for our customers.

[video plays]

Steve Wadey:

We've made significant progress to becoming an integrated global defense and security company, increasing our international share of revenue to 30%. The key drivers were strong organic growth in the US and Australia, supported by our joint ventures in the Middle East, and strong export performance driven by QTS, which achieved 44% revenue growth compared to the prior year.

During the year, we strengthened our training capabilities to a strategic investment in Inzpire in the UK and the acquisition of AIS aircraft operations, now known as QinetiQ Germany. I'm pleased with both of these businesses, which are complementary to our existing capabilities.

And we're investing in them to realize significant growth potential, in both UK and international training markets.

As I said earlier, my ambition remains to grow out international share of revenue to 50 %. We'll accelerate our growth by investing in our home countries and selected priority countries to drive further organic growth through campaigns, exports, and our joint ventures, leveraging our strategic acquisitions, and the modernised LTPA, to maximize the return from these investments and pursuing further complementary acquisitions.

Our third strategic priority is to focus on commercial and technical innovation. Over the last three years, we've been pursuing a campaign-based approach to win a number of larger, longer-term opportunities based on major government-funded programs and strategic partnering. As you can see, we have won four of the opportunities, as well as the win in Canada that I described earlier.

Winning these larger, longer-term programs marks a step change in our business maturity and has enabled us to deliver organic revenue growth. For example, the BATCIS contract has been the primary driver for our cyber information and training business, delivering 20 % growth. Please note that the figures in the table are indicative of customer budgets for a total program and revenue will only be realized as they are contracted and delivered.

Whilst I'm delighted with our progress, we need to learn from both successes and losses to build further momentum and win high-valued programs with a balanced risk approach. A brilliant example of leveraging both our commercial and technical innovation is winning the US Army's Ground Robotics program, known as CRS(I). Here's a short film to bring CRS(I) to life.

[video plays]

In the second half of the year, we secured £69 million of initial contracts and delivered engineering services for our customers through building and leading an ecosystem based off of the capability of more than 120 SMEs and prime contractors across the UK, winning these longer-term programs is underpinned by our technical innovation. Over the last year, we invested £26 million, which has directly supported our competitive wins, as well as developing the next generation of products and services to position ourselves from medium to long-term growth.

This investment is not about technology for technology's sake. Therefore, I am pleased to see that we are generating returns from this investment with first contract awards for a number of new products, such as the Rattler supersonic target, Bracer secured satellite communication system, and our Obsidian Counter-UAV radar.

Later this year, we will be holding another investor seminar focused on innovation and explaining how we create disruptive next generation services and products through rapid experimentation and exploitation of commercial technology; co-creation of solutions with our customers, academia, and industry; and developing commercial models, ultimately, how we create more value for our customers and our shareholders. Thus, we've made great progress across all fronts of our strategy. There's much more to come.

So, how do we plan to strengthen our strategy and deliver sustainable, profitable growth? Having matured our business-winning capability, we will focus on long-term opportunities to

drive organic revenue growth into our £8 billion addressable market. To do this, we are evolving our campaign-based approach to be truly global across both defense and security markets, by leveraging our skills and our technical capabilities across the group.

We've ordered a backlog of more than £3 billion. We will continue to be disciplined in delivering our commitments to our shareholders and our customers. Our markets remain highly-competitive. Therefore, to ensure that our revenue growth is converted to profit growth, we'll maintain good control of our cost space through productivity and efficiency improvements and continue to improve the effectiveness of our bidding and contract execution through discipline, program, and risk management.

Investment remains central to our growth strategy. Over the last three years, our investment choices, whether organic or inorganic, have been strategy-led to integrate and strengthen our value proposition. And these choices have been, and will continue to be, underpinned by the rigorous financial discipline that David described earlier. By strengthening our strategy and maintaining our operational performance, we will continue to convert revenue growth into sustainable profit growth at stable margins, thereby increasing returns to our shareholders.

So, in summary, our strategy is delivering. And I'm delighted that we've delivered three years of growth. This has been an excellent year, with strong operational performance. We achieved 9 % revenue growth and 3 % organic profit growth, offsetting strong profit headwinds through focus on our cost space. And we secured the modernised LTPA contract through to 2028, the most significant milestone on QinetiQ's history since privatisation, delivering a record order book of £3.1 billion and providing a strong platform for growth.

Our strategy has enabled us to grow in an uncertain world and improve our company maturity. We've demonstrated our commercial acumen through five major competitive wins and increased the international share of revenue from 21 % to 30 % over the past three years. And we are building momentum towards being an integrated global defense and security company to drive further growth.

Through disciplined execution of our strategy, we will see growing revenue at stable margins deliver increased profit and returns to our shareholders. This will be achieved by leveraging our strengths across the group into our £8 billion addressable market, continuing investment in or people, technology, systems, and infrastructure, and maintaining strong operational performance.

Overall, I'm really pleased. We've delivered an excellent year. And we're well-positioned for sustainable profitable growth in the years ahead.

Now, finally, I'd like to thank Mark Elliott, our current chair. He'll be retiring at the AGM in July. This is Mark's last results presentation. So, on behalf of the board, and on behalf of all of our employees, I'd like to publicly thank him for overseeing the turnaround phase, which rescued QinetiQ and the first three years of growth. And I'd also like to personally thank him for his support over the past four years. Thank you, Mark.

So, David and I would now be happy to take any questions.

Charlotte Keyworth [Barclays]:

Charlotte Keyworth from Barclays. I've got three questions for you. First is on the EPS piece, which is great. You've offset about 5 million EBIT headwind from SSRO. How much of that would you characterise as cost-driven versus revenue-driven profit? Perhaps you could give us a bit more detail on the activities that you've undertaken to achieve that. Secondly, we're seeing very, very punchy global products topline growth here. What's the medium-term outlook for this division? How excited should we be about it? Perhaps you could give us some commentary around the end market. And then just as a follow on, you're guiding to flat margins in that division and I understood that won with a lot of operational drop through for the investments that you're making this year, so the growth, what is it? And should we think about that as an inlying investment -- I'm sorry, and end year investment or will it continue?

And then finally, one for David, just given the great outlook.

David Smith:

Sure. Of course.

Do you want me to start? I've got hundreds of questions. And, what's the right level of -- what's the right cash position for -- on the balance sheet for QinetiQ going forward? I mean this the business clearly in a great space? And then obviously to follow onto that is, you know, how would you characterize --

Okay. I'll stop. How would you characterize the valuation environment for acquisition targets at the moment? I'll stop there. Thank you.

Steve Wadey:

Can I suggest that -- David, could you maybe take number one and three so EPS and flat margins. I'll talk about global products. And then maybe we'll come back to cash valuations --

David Smith:

Okay. I think, you know, clearly our revenue growth has delivered some improvement. And if you just cast your mind back to our profit chart, we delivered around £7 million in EMEA services of revenue and efficiency improvements. Per year, it's roughly half and half between the delivery of revenue growth and efficiency improvements. And the efficiency improvements really are right across the business. As Steve mentioned, you know, we have put more focus over the last year in how we're utilising our people. How we make sure that they have the right tools to build, to deliver properly to customers. And we're making investments in some of those areas as well. And certainly, you know, that's -- that's an area that's received focus. And basically, what it enables us to do is to deliver our contracted customer activities at a high margin at the end of the day. So, you know, it's something that we'll continue a real focus as we increase our ability, I think, as a business to operationally deliver. I think we are rightly proud of the revenue growth, and the fact that we've been able to deliver that with profit growth this year, is down to a much stronger focus, I think, around operational delivery right across the business. I think that sort of answers that question.

Steve Wadey:

On global products, Charlotte, I mean, I think it's an important question, and certainly, if you look back in our history, global products has been particularly lumpy in responding to operational tempo. I think there are three main points that I'd bring out looking to medium and long-term on global products.

First of all, in the last three years, our structure has really expanded the portfolio to having a more diverse portfolio, particularly if you look at robots now. You have growing demand for unmanned target systems. I think that expansion of the product portfolio starts to reduce the volatility that you may have seen in the past.

The second driver really, for us, will be that we've migrated a number of our product programs onto -- sorry, onto longer term programs. They're winning programs like CRIS(I), winning programs like the OFS autonomy program winning some of our major export, multi-air programs in our target business. You know, this moves us into a more stable position of longer-term programs.

And thirdly, I only briefly mentioned it, we're looking ahead at the cycle beyond and the cycle beyond that. Therefore, we're having far more proactive investments in next generation products and not just robotics and targets, but other elements where we might expand our portfolio. So, I really -- part of our strategy is to reduce that volatility. Of course, if there were to be a major conflict demand on products, then you might get spikes. But what we're trying to get to is a much longer term diverse portfolio and thinking ahead of the cycles of product development so we can see that medium term sustainable growth. That's how we're focusing on global products.

Do you want to come back to cash, David?

David Smith:

Well just picking up on your margin questions, as well.

So, if you stick on nonrecurring items, we delivered just under 13 % growth margin. Slightly lower in EMEA Services, slightly higher than that on Global Products. And my guidance would be that's about what we ought to be able to deliver this year. And essentially, you know, it is a business that's undergoing change. We're putting in place some longer-term contracts. And those contracts provide a very solid foundation. But the real critical thing is we need to be able to add onto those contracts as well. I described in the LTPA presentation how the core contract provides a good level of return. But the opportunity is then to enhance that experience attracting additional business, and that actually applies in other areas as well. So, there is a tension here between, you know, still the -- the sort of the regulatory commercial pressure which is probably having a downward pressure on margins and finding new areas of business where we can increase margins to keep that stability.

The international business is also an area where, you know, we've already described it. It's been good growth, and we intend to continue to grow that. And that does require some investment as we do that. And that's certainly an area that probably, just for the moment, is not contributing at the same margin level as the rest of the business. But we would hope to get that business to that place over the next couple of years. So, it is a factor, though, the business is changing in nature. But I think if we can deliver that change and grow with a stable overall margin picture, that will be a good achievement.

You asked about our cash position, and what the kind of high level of cash. Well, it's a very difficult question for a finance director to answer because as much as possible [unintelligible]. The answer -- but clearly. We said two things that I think are very important. Firstly, we completely agree and are trying to make sure that we can invest organically in the business from within the cash flow that we generate as of operations, and we certainly did that last year,

and we intend to do that this year as well. But we do need the fire power to go beyond that in terms of the acquisitive side of the business. And last year, we used basically £60 million, and I think the year before it's about £60 -- I'm sorry, £80 million of cash. The year before about £60. So, we certainly have the fire power. There's no reason why the business cannot operate on net debt basis at all. And I think over the next two to four years we would continue to drive the acquisition strategy in the right way from the strategic point of view and from financial returns, and we may well end up in a net debt position. But we are trying to make sure that we take various positions in a very reasoned and thoughtful way.

In terms of valuation environment, that is difficult. I would say. And certainly, you know, I think I said before, you don't buy every company you look at. For some reasons, they don't make strategic sense when you're taking a real deep look at it. But equally the valuation environment, particularly, in the US is a quite tough environment, and you know, we have to make sure that we keep faithful, I think, to what we're trying to do, which is to deliver the right long-term capital appreciation for shareholders and make sure anything that we buy will do that for us. So, we definitely won't get carried away on pricing valuation on the acquisition side.

Rami Myerson [Investec]:

Good morning,. Rami from Investec. Starting with revenue growth. You got into mentioning a little digit organic revenue growth based on I think probably about £25 to £30 million of revenue growth should come from the acquisitions you made and prior fiscal year. It's just a slow down to low single digit organic revenue growth and not struggle to solve that with the good order book, with the order coverage -- the order intake. Is it just [unintelligible] or is there some reason why you expect the growth to slow down so drastically?

The second one is on the margins, and part of the question recurring/nonrecurring. This is the second year in a row where you've had some marginal recurring benefits. I'm just curious what your expectations are for FY20. And more important, if you are moving into a period of consistent organic growth, and if so headwinds are subsiding, why are you not more optimistic on margin expansion, and what is holding you back, given all this operation improvement from delivering margins that are higher? It may be a question more for Steve relating to ASDOT what comes next after that contract was cancelled how does it inspire and contribute to the group without ASDOT, and maybe EIS, are you starting to realize some of the synergies that you expect from that business with some of these international customers you talked about, the US Air Force being a potential customer, potentially selling services into the German military. Thank you.

Steve Wadey:

Okay. If I may, I might take the second and third one around margins. Give me an opportunity to say something that leads back to Charlotte as well and then maybe David you can add to that and do revenue and I'll come back --

David Smith:

Yeah.

Steve Wadey:

And EIS. I think as -- as David was trying to explain to Charlotte, we've really transitioned the business over the last three-four years. We guided -- I remember in our first results, we guided that we would come down from the margins that were 15 plus % at the time.

And we've transitioned to, you know, a stable margin rate that is commensurate with the market sectors that we're operating in for the cycle of this type of business. And excluding those non-recurring items, I think we've been, you know, really clear today that we see driving the top line and maintaining that stability -- the margins ultimately, you know, passing through to enhancement.

And I think the recurring items that you mentioned are a feature of transitioning a business portfolio. I mean, we've gone through a number of strategic changes around, you know, the LTPA as an example. And as part of going through that transition, it has triggered those non-recurring items. So, certainly, as we come out of that stability -- out of that transition phase, we will probably expect, you know, the level of non-recurring items to subside.

But it's normal business. You know, there will always be, from time to time, those that we've probably have just been through a heightened period of them because of the significant change in strategy and transition of the business.

But I think, you know, we're now in a strong position as we've shared. We really think that the margin, excluding non-return -- non-recurring, is right for our sector and our focus now is about driving the revenue growth, maintaining good discipline around execution, efficiency, cost control and that will drive profit growth.

That's slightly expanding also. My prospective on Charlotte's question. And I think that that includes you taking into account the SSRO position. You know, securing the LTPA, you know, through to 2028. It's a very large percentage of our backlog now. And, therefore, it gives us that stable base, you know, to drive forward at that stable margin.

So, I think that's two and three. David, on revenue growth.

David Smith:

And just one thing on recurring items. You know, I'm under no obligation from an accounting point of view to talk about recurring items, but I think it's important to the transparency that we do that. So, we set our precedent a couple of years back and I think, you know, I'm trying to make sure that we continue that. But as Steve said, it would make my life a lot easier if we didn't have to, but we do.

So, there we go.

In terms of revenue growth, I mean, you're right. There will be a contribution from acquisitions. It's more like £15 than £25 in terms of the -- the increment because we saw £10 million in last year's number. So, that takes us to about 25. And I think we will see stronger growth in global products this year.

We've got the Canadian contract which will begin to start delivering again. It's clearly we've got continued growth through expanding the QTS portfolio. We've got QNA in terms of ramping up following CRS(I) So, there will be above single digit -- or above mid-single digit growth in global products.

But I think -- we think the outlook for services is probably more stable this year when we exclude the contribution from the two acquisitions. And, you know, hopefully we're going to do better

than that. I'm not -- we're certainly not trying to cap it at some level, but we're trying to be realistic, I think. The -- having won a lot of business, we've now got a very important delivery phase particularly with the LTPA. So, you know, we're guiding to that as we think a sensible position on revenue growth for this year.

And then picking up on your last two questions. Obviously, on the specific of the ASDOT program, I mean, you know as well, it's being cancelled. And in terms of the specific of that program, we're waiting for the customer to give us guidance about how they wish to, you know, take that program forward.

But if I could expand your point more generally about training, we absolutely -- as stated by our strategy -- training is a growth area of opportunity for us. If we look at our experience and our skill set, you know, areas of simulation, synthetics, blending, live and synthetic training, you know. And some of the technology and people-based aspects of training is one of our core strengths. And that's what we were bringing to Cobham ASDOT team.

And we would expect however, that program evolves there is an enduring need here for good, operational training in a high [unintelligible], you know, environment which align with our strengths.

So as the future of the program evolves, if so, we will look to engage. I think we come back to our inherent strength in training. And some of the areas of investment that we're putting in bringing new technology is where we would see opportunity to engage going forward.

I'd also add to that, your comment about Inzpire. You know, so Inzpire bring a complementary capability. Obviously, very deeply embedded with the customer and very much looking at the effectiveness of operational training direct with frontline commands. And you may well be right that that can bring an opportunity depending on how, you know, the program evolves in the months and years ahead.

But one thing that we are working very closely with Inzpire on is some international opportunities. That's where we originally, you know, looked for the growth by combining our experience and growing experience in international markets, with some of their very close, you know, operational frontline command engagements that they've got and how we can leverage that in key countries.

In terms of EIS, we're very pleased with the EIS business. I mean, clearly, it's a short period, since we've been under full ownership. And we're integrating that. We've really looked at some of the longer term growth potentials. Potential areas in -- in not just airborne training, but in special mission and flying test bed capability. There are three areas where we see, you know, growth not just in Germany but trying to leverage that capability in other areas around the world.

And, therefore, we've already taken some positive investment decisions to yield those growth opportunities. So, its early days, but we're very pleased with it and we see growth potential.

And one specific that you read in the detail of the statement, which is being an internal synergy that we've been able to bring some of their experience actually into the long-term partnering agreement and use some of their skills and capabilities, you know, to support us on maritime clearance to support trials activity. So, we are already starting to see synergies, but I'd say it's very early days with the growth potential that we see in the medium and long term.

Male Speaker:

Maybe just a [unintelligible] on German customer. Have you had any -- what's the engagement level with the German MOD at the moment?

Male Speaker:

It's very good. You know, we have a very good reputation as a business in Germany. We've also recently held a bit of a showcase where we've started to expose to the German customer, you know, a whole range of other capabilities that the group has, which it can bring to their -- through what is now QinetiQ Germany. So our engagement is -- our reputation is good, and our engagement is good.

Male Speaker:

Thanks.

Chris Leonard [Credit Suisse]:

I'm Chris Leonard from Credit Suisse. Global products. Looking at the Rattler targets. What sort of opportunities do we see here? Because I think you've previously stated it is around a 50 % lower price point potentially verses US peers with a similar offering.

So, just trying to scope what we can see there. And in line with that, we've seen new orders coming through for the global products division over the last year, year and a half. And I suppose adding to what Charlotte's been asking, can we see a midterm margin getting back to around 15 %? Do you think that would be sustainable given the further orders coming through the business?

And then, lastly, you might have already mentioned it, but Australia -- what sort of organic growth did we do there this year? And, equally, can you just update us on the opportunities there for test and evaluation over the next year or of two years if you could please? Thanks.

Steve Wadey:

Okay. I'll take the first one, and then maybe, David, you do margin and I'll come back with Australia.

So, Rattler, I'm pleased you brought it out as one of the products that we mention in here. We launched the internal research and development for the Rattler product probably only -- probably only about 12 months ago.

And so, we've been very quick to turn that into first contract. And it probably requires us to step back and think about why we are investing in Rattler. And it comes back to our value proposition, you know, of create it, test it, use it.

We see very significant growth in, you know, all of our forces needing to really test and train their capabilities against the most, you know, demanding threats. And when you do that you need to represent those threats in the most cost-effective way. And to your point, what we -- we're trying to do with Rattler, find a very disruptive way of representing a very high-speed target at low costs. And that was the innovation that we brought into the Rattler design, and that's why -- and it does that -- and that's why, within, you know, 12, 13 months, we've been able to secure first contract award.

And if I link it to the formidable shield exercises that I mentioned right at the start of the

presentation, you know, that's a NATO-led activity. You know, the US government leads the engagement with us. They have already committed to come back to our test range on a multi-year basis, and we're in long-term discussions about how we increase, you know, the intensity and the challenge of the threat environment that we pose to those NATO forces. And therefore, seeing Rattler, you know, go under contract very quickly, we will see Rattler, you know, coming into those types of exercises. So, the, you know, the nations that we're working with can really test and train against the most demanding threats.

So, we would expect to see, you know, expansion, you know, of that product, and contribution, you know, in the medium and long-term. And maybe, also, to you know -- Charlotte's point, "That's what I would call the next generation of low-cost supersonic target." We're also working on the generation after next, and that's long-term strategic thinking about customer trends. You know, how we're going to create value not just in the short-term, but medium and long-term. Back to margins again, David.

David Smith:

Yeah, I think -- I mean, you're right that last year, we did have a 15 % margin on global products. This year, we're -- we adjust to a non-recurring. It was, I think, 13.2 or 13.3, something like that. I've looked back over the last five years, and actually, that's about the average of the last five years. So, I actually think, probably, 13 to 14 % is the right margin range for global products going forward. But clearly, you know, there is the opportunity, always, in global products, that we can overachieve on volume because of the drop-through to do better. And clearly, that will be the intent.

You asked about Australia, also. You know, Australia was an interesting case last year. They didn't see a lot of revenue growth, but actually, we did see some good orders growth in Australia. We were disappointed -- Steve had the slide -- at not winning a quite an important contract opportunity we saw for us on [unintelligible] infrastructure in Australia. And we think we lost it fairly narrowly, but we did lose it. So, that was unfortunate.

But there's still a lot of things that the Australia business are looking at for how to develop the business. So, it's still absolutely a focus, in terms of growing that business over the long-term. But -- and particularly, into areas that are more below the line in terms of not being so much consulting and advisory work, but actually looking at areas where we can get involved in operational activities, as well. And if I expand on that around Australia, and maybe, I sort of link into what we've been calling our campaign-based approach -- so, it was three years ago that we introduced the campaign-based approach. And if you remember how I described it, I was trying to change the company from being, you know, transactional and responding to requirements, to a company that understood, you know, market trends, customer needs, you know, shaped and engaged its customers and then, positioned itself to win those contracts.

And that campaign-based approach was also supported by the investment in our business development capability and our engagement with our customers. And it's been three years of work, investing and relentlessly pursuing that campaign-based approach, that has resulted to the five major competitive wins that you've seen, that we've reported. So, just think about that cycle. And it's three years of work to have got to winning those larger, long-term contracts.

We also pointed to, in the presentation, that we will be maturing and evolving that approach to what we're calling, you know, taking the approach global. You know, and that's, you know -- and I would immediately put that in the time frame of five to 10 years. You know, this is where

we're now really raising our sights as a company, you know, not just thinking about, "What is it we're trying to do this year," or even in the next one to five years. How are we positioning this company, you know, to be a global leader in these selected markets on a five to 10-year basis?

And you know, we're doing that by focusing on particular areas where we believe that we can specialize and be a world leader. You know, the obvious one of those is the one that you've mentioned, test and evaluation. I mean, what we're doing, you know, here, with the Ministry of Defense, you know, is going to be world-class, you know? And several nations that we're focused on, equally, will want to modernise, you know, modern methods, digital technologies about how they create, test, and use, you know, their defense capabilities.

And then, we have a very clear focus that is a geographic focus. So, we have our home countries: UK, US, and Australia. So, you know, Australia will continue to be a very long-term focus for us in those areas of expertise that we see. We're also looking at how we can build new home countries. That takes us to Canada -- that's why the Canadian win. You know, we -- okay, we've got a great reputation and position in Canada, but this takes us to a new level. You know, and secondly, Germany, which we just talked about.

You know, and therefore, I think -- being very clear that we have a very long-term ambition in focused areas of expertise, in clear focus of geography -- it gives us that long-term potential.

Male Speaker:

Okay, well thank you very much, and we'll be around for any questions later if you wish to follow-up. So, thank you. Thank you for your time.

[end of transcript]