

QINETIQ

Full-year results for the year ended 31st March 2020

Call Transcript

Thursday 21st May 2020

Key:

Steve Wadey – Chief Executive Officer
David Smith – Chief Financial Officer
Ian Brown – Group Head of Investor Relations

Ian Brown

Good morning everyone and welcome to our full-year results webcast. Thank you very much for taking the time to join us this morning. I'm Ian Brown, part of the investor relations team at QinetiQ. I'm joined this morning by Steve Wadey, our CEO, and David Smith, our CFO.

Before I hand over to Steve, I would like to point out a couple of things. Firstly given the circumstances this is very much a lockdown special. We are webcasting this ourselves without the usual extended team of experts we have to support us at the London Stock Exchange, so, I do hope you can see and hear us clearly.

Steve and David will present the results and an update on our strategy, during which your lines will be on mute. Thereafter there'll be an opportunity to ask questions for our covering analysts and investors.

When we get to the Q&A section of the presentation, to ask a question, you should see a raised hand button at the bottom of your screen, do please press that to ask a question, I will then ask your name and if I press the right button, unmute your line.

But please also make sure you've unmuted your own device, otherwise you won't be able to hear me. And with that I will hopefully hand over to Steve.

Steve Wadey

Great, thank you Ian, and good morning everybody and welcome, thank you for joining in these unprecedented times. And as Ian's just said, David and I will present our full-year results and also give you an insight into our strategic response to the COVID-19 crisis.

This picture shows one of our team supporting a national repatriation flight Boscombe Down in the UK and represents our brilliant men and women who are committed and passionate about their work.

I'd like to take this opportunity to thank them all for their outstanding contribution to our performance last year and their ability as they continue to deliver vital outputs for our customers throughout the crisis. Thank you, you're really doing a great job.

Our relentless focus on our customers has delivered our fourth year of growth, demonstrating that our strategy is working and we are well positioned for a new world.

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

So, let's start with the headlines, this has been an excellent year with strong operational performance and limited impact from the COVID-19 crisis. Orders are up 25%, maintaining good revenue visibility with a backlog of £3.1bn. Revenue is up 18%, 10% on an organic basis. Profit is up 7%, 2% on an organic basis.

Cash performance remains strong with 133% cash conversion pre-capex. EPS is up 2% and

as previously announced the Board has postponed the dividend decision and guidance until later in the year. These decisions weren't taken lightly and will be reviewed as soon as sensible to do so.

Our growth has been driven through disciplined execution of our growth strategy, we secured £168m of orders through the engineering delivery partner contract. We continue to demonstrate our improving business maturity, winning four major long-term contracts.

Our most significant achievement was completing the acquisition of MTEQ, more than doubling the size of our business in the US to 25% of the Group. We've grown the international share of revenue from 21% to 31% over four years.

We've improved our employee engagement score by 10%, as we continue to engage and incentivise our employees in driving our growth strategy. We enter FY21 in a strong position and we have driven a strategic response to the unfolding COVID-19 crisis.

Whilst it's too early to understand the impact on our group performance, our key priorities for the coming year are implementing the robust actions that we've already put in place to boost our resilience, partnering with our customers to continue delivering their evolving priorities, engaging our employees to adapt and learn from our response to the pandemic.

And, accelerating our focus and investment on critical capabilities to position us for a new world, driving medium to long-term growth and healthy returns for our shareholders. I'll now hand over to David for overview of our financial performance.

David Smith

Thank you, Steve, and good morning everybody. As usual, I'm going to begin with a summary of fiscal 20 financial performance, before going into more detail on the drivers. As Steve mentioned, our strategy is delivering with a strong performance, resulting in a fourth year of growth.

We've grown both EMEA Services and Global Products this year, increasing overall revenue by 8% to £1.1bn, and by 10% on an organic basis. We've delivered underlying operating profit growth of 7%, to £133m, and our margin at 12.4% is within our target range of 12-13%.

Underlying EPS rose 2% to 20.0p, despite an increase in our tax rate. And we have delivered a strong 19% organic growth in order intake, 25% overall. And including the LTPA amendments, our backlog now stands at £3.1bn. We have achieved strong cash conversion with 133% underlying cash conversation and our balance sheet remains very strong, with net cash of £85m.

We have seen some small effect from COVID-19 last year, which I'll come on to shortly. And as we've previously announced, due to the unprecedented nature of the COVID-19 situation and the Board's wish to adopt a prudent course of action to protect the long-term strength of the QinetiQ, it will postpone the decision on the proposal of the dividends until later in the year. So, across the board this was a strong performance in fiscal 20.

Going into some detail, I'm going to begin with our order performance, we made very strong progress on orders, with 19% organic and 25% overall growth. The main driver in the period was EMEA Services, which grew organically by £115m.

And that growth was driven by a combination of the £67m multiyear contract for the UK Robust Global Navigation System, or R-GNS, and £168m of orders under our engineering

delivery partner contract that was nearly £100m higher than last year.

In Global Products, orders grew by £34m, driven by the €75m ALTIUS contract for the European Space Agency. The acquisition of MTEQ and NSC and impacts of a full versus half year for our 2019 acquisitions contributed a further £48m towards this reporting period. And at the start of fiscal 21 we have good visibility with £850m of fiscal 21 revenue under contract.

So, turning to revenue, we made good progress in EMEA Services with 12% organic revenue growth and 5% organic growth in Global Products, combined this gave us organic revenue growth overall of 10% in the period. Our acquisitions of MTEQ and the full year of the 2019 acquisitions contributed a further £66m, giving us overall reported revenue growth of 18%.

And whilst not presented here, we continue to progress our strategy of becoming a more international business and we've grown international revenue to £333m, which now represents 31% of total revenue.

Turning to operating profit, overall reported profit was up 7% and 2% on an organic basis, excluding acquisitions. Within this there were some one-time net benefits amounting to £6m, driven by finalising a business rates agreement and cost recovery on a major contract. In the prior year, non-recurring items were £7m.

In EMEA Services profit grew by £3.3m on an organic basis, driven by revenue growth offset by lower non-recurring trading items. In Global Products we saw a small decrease in profit, driven by a loss in OptaSense of £2m, offset by growth in other businesses.

MTEQ and NSC and the impacts of a full year versus half year of trading for 2019 acquisitions contributed £5.8m inorganic profit and that resulted overall in a group margin of 12.4%, compared to 13.7% in the prior period.

And one of the drivers of this movement is the increasing contribution from EDP, which I'll explain in more detail shortly. So, overall a strong performance with organic growth across orders, revenue and operating profit.

So, turning now to the two divisions, for EMEA Services the chart shows a split by major business and by revenue for EMEA Services. The 25% increase in orders was primarily due to the key wins, which I've already mentioned, particularly R-GNS and EDP.

We made further good progress on EDP with an additional £168m of orders and as a single-source contract, given its minimal capital requirements, the margin we made on EDP and other similar contracts is lower than our average group margin, but it remains well in line with defence industry more generally.

And the capital light model means we make an appropriate and attractive return on capital. We expect EDP to be a growth driver of our UK business in the medium to long-term.

Revenue increased by 16%, 12% on an organic basis, driven by new work through EDP and also on our BATCIS contract as well. And underlying operating profit increased by £3.8m with a resulting margin of 12.6%. Our total funded order backlog remains very strong following the good orders performance and we continue therefore to benefit from good revenue visibility, with £656m of our fiscal 21 revenue under contract, compared with £565m at the start of last year.

Turning now to Global Products, our Global Products division is a shorter cycle business than EMEA Services and performance varies more greatly due to the timing and mix of product sales. We've incorporated MTEQ now into our Global Products division and we're reporting this through QinetiQ, incorporating our US entity.

Turning to performance, order grew 25% in the period, 14% organically, driven by the Altius contract with the European Space Agency. Revenue was up 23%, 5% organically, driven by small robotics and upgrade kits in QinetiQ Inc. and continued growth in QinetiQ Target Systems.

Underlying operating profit was up 16%, assisted by £2.9m from the acquisition of MTEQ and good performance in QTS. With MTEQ's lower margin there was around a half a point dilution of Global Products' margin and about 0.1 or just over at the group level.

This will go to about half a point at the group level with a full-year contribution. We have £193m in Global Products fiscal 21 revenue under contract as of April 1, compared to £141m in the prior year.

Turning to cash flows, overall our operating cash conversion at 133% was strong. We saw very strong performance from working capital, particularly in the last few months of the year, supported by prompt customer payments. And that resulted in a working capital cash inflow of £2.5m.

Despite this strong performance, we do anticipate some of this unwinding. Cash flow associated with capex was £108m, as we continue to invest in our core contracts, such as LTPA and in our business. And after capex we had underlying net cash inflow of £70m.

It's worth re-emphasising what I've said before, that given the cash generative nature of the business we do expect to be able to fund organic investment from our operating cash flows.

On this next slide I've presented the movement in net cash. The fiscal 19 year end net cash position of £189m has been restated to reflect the adoption of IFRS 16 on leases, which reduced net cash by £28m. Net cash inflow from operations of £70m, I've already mentioned was partly offset by tax charges of £10m and a small interest charge. And that resulted in free cash flow of around £60m.

The acquisition of MTEQ and NSC resulted in an outflow of £90m with a further £8m outflow for associated transaction costs, the majority of which relates to MTEQ. After the dividend, this means the fiscal 19 final and fiscal 20 interim dividend, receipts from property disposals and payment of finance leases; we ended the year with net cash of £85m.

I now want to cover the trading impact and our liquidity position in light of COVID-19. Due to the uncertainty surrounding the resolution of national safeguarding measures and also the impact to customer budgets, we're adopting a cautious and prudent approach over the next few months.

We're doing this in order to maintain the strength of the business in the long-term interest of our employees, customers and shareholders. With a total order book of £3.1bn, we do enter this crisis from a position of strength. Our EMEA Services division benefits from long-term contracts, performing work that is critical to sovereign defence capabilities and to date has been less impacted by COVID-19.

While some trials actively has been delayed, this has largely been offset by the acceleration of work directly linked to the COVID-19 response. Although difficult to quantify the impact at

this stage, we do anticipate a further deferral of contracts and project delays due to difficulties with travelling logistics. And then medium-term potential project constraints.

The Global Products business operates on a shorter cycle and is therefore more exposed to cancellations, delays and deferrals of trial activity. The effects are more pronounced in some business areas than others, for example in QinetiQ target systems we've seen customers delay trial activity and reduce orders for targets, which has created the need to furlough staff at our Ashford manufacturing facility.

We have also been affected in our German business with reduced flying hours and as a result of this and some operating cost issues have taken a small €5m payment in goodwill, to reflect prospective margins and revenue. Our North American business, on the other hand, continues to see demand and delivery continue against robotic programmes of record, for instance.

Financially we enter fiscal 21 in a very strong position with overall liquidity of £360m, comprising the net cash of £85m supplemented by a £275m undrawn committed credit facility. And that has an option for maturity through to September 2025.

Overall our balance sheet therefore remains robust with the capacity to support our growth plans for the company and provide resilience in the COVID-19 crisis without having to raise any capital. The RCF was undrawn at year end, although we will probably use it partially to maintain a prudent level of available cash.

We're supported by a sustained negative working capital position and are taking prudent steps to minimise short-term cash outflows, including inventory management, receivables selection, etc.

Additionally we've put in place a series of actions, including temporary CEO/CFO and senior salary reductions and have reduced Board fees, reducing operating expenditure and deferring discretionary capital expenditure and the dividend decision deferral. Steve will put all of this into strategic context later.

By taking these prudent measures to preserve our balance sheet, we'll be well placed to emerge from this crisis in a position to continue accelerating our strategy, delivering both organic and inorganic growth in the mid to long-term.

So, turning now to technical factors, I'm just going to point out three here, our effective tax rate was 14%, that was up, and we anticipate this to continue to increase due to the greater proportion of international revenue and profit and the higher UK tax rates recently announced by the Chancellor.

We had a small cash inflow from working capital in the year, but at this stage, like our general outlook, we don't give detailed guidance on this, although an outflow wouldn't be unexpected. Capital expenditure is likely to remain similar to fiscal 20 in fiscal 21 at £70-100m range, as we continue to invest in our major contracts, although keeping under review discretionary capex in light of the crisis. In line with what I've said previously, we anticipate remaining in that range until fiscal 23 as we invest organically in the business.

So, finally, while we enter fiscal 21 from a position of strength, it really is too early to draw conclusions on the overall impact of COVID-19 to our business. At this stage we are planning for a range of outcomes, depending upon the duration and extent of measures, such as social distancing and potential budgetary pressures.

We'll provide further updates to the market as more clarity presents itself, both in terms of near-term trading and long-term trends. With the continued implementation of our strategy and investment, we are well placed to respond to changing customer requirements, delivering medium to long-term profitable growth. I'm now going to hand back to Steve to take you through our strategic priorities.

Steve Wadey

Thank you, David. The markets in which we operate are changing rapidly to deal with evolving threats, which will be accentuated by the COVID-19 crisis. In the UK, the defence and security review has been delayed, although we can expect priorities to change and pressures on budgets to intensify.

In the US, the drive for technological advantage continues to modernise capabilities across all domains. And the Presidential election will take place later this year.

In Australia, focus continues on the recapitalisation of major defence platforms and developing indigenous industrial capability, supported by a strong budget outlook.

Across all our markets competition is increasing and we're seeing a resurgence of national protectionism. The COVID-19 pandemic represents a strategic shock to both our financial and customer markets. Whilst we believe demand will remain robust over the long term, we also expect the crisis to drive fundamental changes to market dynamics.

A global recession will drive ever increasing pressure on budgets and threats will evolve to demand greater exploitation of digital technologies and the need for greater agility and pace in delivering solutions for our customers.

These changes reinforce my view that our inherent strengths and strategy are particularly well matched, enabling us to be agile and proactive to address both short-term challenges and pursuing medium to long-term growth.

As the scale of the COVID-19 pandemic became apparent, we rapidly established a strategic response to the crisis, adherent with our long-term strategy. Priority 1 is protecting the health and wellbeing of our employees and their families.

Whilst respecting national safeguarding measures, we've been agile in successfully mobilising the company to 80% working from home and 20% on site, based on physical need and or national security requirements. And we are rapidly learning from our response to the crisis to accelerate our digital transformation, establishing more flexible distributed teams as part of our new normal.

Priority 2 is continuing to deliver for our customers; we've provided direct support to fighting COVID-19 as well as manufacturing PPE for local health services. Feedback from our customers has been excellent and they're appreciative of our continued delivery of critical defence and security outputs. Our focus is now on partnering with our customer to tailor our approach to mission-led innovation as they reprioritise their needs.

Priority 3 is sustaining our company for the long term. As David mentioned, we've taken prudent actions to boost or resilience in the short term by managing cash outflows and reducing costs, including 250 of our senior leaders agreeing to a salary reduction, demonstrating their personal commitment to our company.

We've done this in a balanced way to enable us to continue investment in future capabilities

to drive medium to long-term growth. In summary, we have responded with agility, successfully mobilising the company to safely navigate the immediate challenges and ensuring we are ready to emerge as a stronger more vibrant company to drive medium to long-term growth.

In May 2016, I launched our vision-based strategy to address rapidly changing market dynamics and drive growth by transforming our customer focus and our competitiveness.

This strategy has delivered four successive years of growth and remains unchanged, with three priorities, leading and modernising UK Defence Test and Evaluation, building an international company and innovating for our customers' advantage.

Our strategy was developed to respond to budget pressures and is built upon a customer value proposition we call mission-led innovation, enabling agile capability development through co-creation of solutions to meet our customers' needs across the lifecycle.

Create it, developing cutting edge technology and rapidly turning it into capability. Test it, ensuring that capability will work when critically needed. Use it, ensuring our customers are trained and operationally ready.

Whilst I believe it's inevitable that our home country's response to the pandemic will increase pressure on budgets, I also believe there's an emerging sense that we're not spending enough on innovation, research and technology to keep ahead of our adversaries.

I'm therefore confident that our value proposition will have increasing resonance with our defence and security customers, delivering them better value for money and creating opportunities.

We've made great progress in building an integrated global defence and security company. Over the last four years we've grown our revenue by 42%, established an order book of more than £3bn and more than doubled our share of international revenue.

This growth has been driven by our strategy-led choices to build and leverage our capabilities across the group, underpinned by a clear capital allocation policy with rigorous financial discipline to deliver returns for our shareholders.

We've created a mindset of partnering and collaboration to focus on our customers' needs; we've upskilled our business, winning capability through recruitment and training, resulting in us consistently winning larger long-term programmes.

We've strengthened our capabilities by investing in six acquisitions. And, finally, our success has been underpinned by executing our programmes efficiently and delivering consistently for our customers.

With an addressable market of more than £8bn, we have significant potential. Key to our next phase of growth will be the continued disciplined execution of our strategy and maturing our high performance culture by focusing on engaging and incentivising our brilliant scientists and engineers to deliver our strategy and implementing our global operating model to coherently expand into our home and priority countries.

The first phase of our transformation and growth has been successful and we're well positioned and increasingly relevant for the future.

The first priority of our strategy is to lead and modernise UK Defence Test and Evaluation, ensuring capabilities we deliver through the long-term partnering agreement are relevant and

competitive to meet UK defence needs and be attractive to our international allies.

These capabilities are critical to defence and national security outputs and I'm really pleased that our teams have adapted well to maintain deliveries throughout the COVID-19 crisis. We have successfully delivered the first year of the £1.3bn LTPA amendment.

We're investing £190m with appropriate returns for our shareholders to modernise our ways of working and put in place new equipment and infrastructure to support larger and more complex trials and at the same time attract new work.

Feedback from our customers has been really excellent, as we undertake major enhancements whilst at the same time continue to support delivery of major defence programmes. Test and evaluation is an integrated and synergistic component of our value proposition and is at the centre of enabling agile development capability to counter evolving threats.

Modernising the LTPA is now delivering additional growth. The recent Commando Warrior exercise in Norway, experimenting with manned and unmanned teaming, strong demand from both UK and international customers for our state of the art and cost effective test air crew training programme.

And winning further upgrades to our air range capabilities to prepare for NATO's largest life-fire exercise in 2021. Modernising test and evaluation has and will continue to provide a strong platform for our growth.

Our second strategic priority is to build an international company by developing our three home countries, of UK, US and Australia, and creating new home countries in Canada, Germany and Belgium. In December we completed the acquisition of MTEQ in the US to accelerate our growth in the world's largest defence and security market.

We are now a leader in advance sensing, robotics and autonomy, critical to modern warfare. We have secured a new special security agreement with the US Government enabling collaboration across the group and underpinning our future growth.

In Australia we delivered a fifth successive record year of growth, we continue to expand into larger longer-term work packages as part of the major service provider role we secured with Nova Systems. And we have won our first contract to design and construct an unmanned air system test range, leveraging our capabilities and experience from the LTPA in the UK.

My long-term ambition remains to grow our international share of revenue to 50%. We've more than doubled our international revenue over the past four years, we're 25% now in the US. We have significant opportunity to drive further growth by implement our multi-domestic business model in our home and priority countries by leveraging our skills and knowledge across international borders.

And with more than 92% of our revenue delivered within our home and priority countries, our strategy remains resilient to the ongoing COVID-19 crisis. I'm pleased to day that as a result of our strategy we are successfully becoming a truly integrated global defence and security company, adding value to our customers.

Our third strategic priority is to focus on commercial and technical innovation. Our campaign-based approach has enabled us to win many larger long-term contracts. And I'm pleased to see that we are successfully delivering and growing them.

In the UK we secured £168m of new orders through the engineering delivery partner highlighting our success of our commercial innovation. In the US we've won the Robotic Combat Vehicle Light programme to integrate unmanned vehicles into ground combat operations. Finally, in Belgium, we are growing our space business winning a €75m contract to design and build the, actually the Altius satellite for the European Space Agency.

This year we've matured our campaign based approach to focus on long-term global opportunities aligned with our value proposition. Having established clear roadmaps to expand into our addressable market we're winning critical building-block opportunities and investing in complimentary capabilities such as land domain training through the acquisition of NSC.

As I mentioned earlier, the COVID-19 crisis is accelerating the need for mission-led innovation. We're well positioned to do this by leveraging our current framework contracts and investing in current and future global capabilities. Our approach to technical and commercial innovation enables us to co-create solutions with our customers, to put technology into the hands of the war fighter at pace, mission-led innovation in action underpinning our next phase of growth.

The world has changed significantly due to the strategic shock of COVID-19. In the short term we do anticipate a global recession causing budget pressures to increase for our customers, however, we remain confident that our markets will adapt and provide opportunity for growth in the medium to long term.

We must use this year to make ourselves even more relevant to emerging defence and security needs by developing new digital services to drive creativity and solutions at lower cost for our customer and strengthening our technological capabilities and skills to deliver mission-led innovation to counter evolving threats.

Learning from our response to the pandemic we will also accelerate our transformation to find more innovative ways to deliver for our customers by embracing distributive working to increase our productivity, maturing our skills and processes to improve our performance and capturing new market opportunities by investing in our core capabilities and global collaboration.

Of course this year will be challenging, I'm confident that we have the right strategy to be agile and proactive to changing market dynamics and enable our next phase of sustainable growth.

So, in summary, our strategy is delivering, and I'm delighted that we've achieved four years of growth, this has been an excellent year with strong operational performance despite the limited impact of COVID-19 at the end of the year. We achieved 18% revenue growth and 7% profit growth, 2% on an organic basis. We've maintained a healthy order book at £3.1bn, providing good revenue visibility.

And our most significant milestone was completing the acquisition of MTEQ in the US providing a strong platform to grow in the world's largest defence and security market. We've adopted a strategic response to the unfolding COVID-19 crisis with record order intake, organic profit growth and net cash on the balance sheet, we enter the year in a strong position.

It's too early to understand the impact on our group performance this year we're implementing robust actions to boost our resilience to the immediate challenges of the crisis,

and are accelerating our focus and investment on critical capabilities to enable us to emerge from the crisis as a stronger more agile company.

Our strategy has enabled us to successfully grow in an uncertain world over the last four years by adding value to our customers. Whilst the world has changed around us, our strategy is unchanged and is more relevant than ever to meet the needs of our customers in this new world.

Focussing on delivering mission lead innovation to meet evolving threats, leveraging our strengths across the group into our £8bn addressable market and continuing to invest and build a truly integrated global defence and security company to drive medium to long-term growth and healthy returns for our shareholders. David and I would now be happy to take any questions, thank you.

Ian Brown

Thanks Steve. So, if you'd like to ask a question please press the raise hand button at the bottom of your screen, I will then announce your name and unmute line. I think the first question is coming from Richard Page, so Richard, I'm going to unlock your line now. Richard, hopefully you should now be in the call.

Richard Paige (Numis)

Morning all. A few questions if I may, please. First of all, on the LTPA, we're obviously in this two-year transition period, to the new way of working, how should we expect to see that work its way through in terms of what we see on our side of the fence in the financials, please?

And secondly, is there any update you can provide on capex you've spent thus far and leveraging of that in terms of new customer wins or growth within that? And secondly on that capex side, just, you've obviously said within the COVID environment you want to maintain flexibility, what flexibility do you have in that £70-100m of capex guidance with regard to what you're committed to spending?

And then, just a second part on the cyber business, obviously grown very strongly within EMEA Services, helped by acquisitions, could you just quantify the, sort of, level of organic growth that business is delivering and obviously, and the opportunities within that as well, please?

Steve Wadey

Great, thanks Richard. Well, if I start off just describing maybe generally how we got on with the LTPA, you said the first year, and some of the capex investments, and I'll ask David put that, the financial questions that you're asking, then maybe go on to flexibility and the organic growth. So, I mean, really, as I present it, I mean the LTPA, you know, has gone considerably well, very well, in the first year.

As you said, it's a two-year transition, we've been delivering all of the outputs in parallel with transition, but then we've been working and partnering with our customers to establish new ways of working, change infrastructure and build new capabilities fit for future.

We've had a brilliant programme with some tough milestones, it's a two-year programme and every single one of the milestones this year we've hit on or ahead of schedule to full customer satisfaction. So, the programme, we're absolutely on track to complete the full operational capability or the full set of exchanges by the end of next year.

In terms of the type of investment, we've been putting investment into a whole range of capabilities across the entire LTPA, from building new infrastructure, new buildings, new control rooms, also some new technology in terms of how data would be processed and shared with our ranges but also with our partners.

New radars and new telemetry to support advanced trials, so there's a whole range, there's no one project really to, sort of, pull out, much like the first LTPA contract where it's very much around your test aircrew training, as an example. So, a whole range of projects where the capital has been going in.

So, very successful, excellent feedback from the customer and it absolutely has already been positioning us in winning business. And you may have noted in the presentation I gave three examples of new business that we're winning through the LTPA, now the LTPA is not just about test activity, it also undertakes experimentation and it undertakes training.

So, the example that I shared about Norway, where we were doing experimentation that is using LTPA capabilities and people within that contract to take unmanned capability and experiment with some of those over in Norway, a hugely successful trial and more of those experimental capabilities offering in growth as we see that end to end capability through the LTPA.

And the other one that I would choose is the series of trials called, formidable shield, and we're winning new business, upgrading target capability, the ability to process large missile capability, as well as putting in additional infrastructure to support more complex trials.

You know, all of those changes are going on right now, I've seen photographs this week of physical changes that's going on in the Hebrides and all of that is preparing for next year's suite of trials and they are tangible elements of growth that are occurring from the LTPA. Because we've been far more focussed on the customer need.

You're looking at the UK customer, international allies, making sure that we're preparing the ground, excuse the pun, to make sure that we're fit to attract this new work. But now I'll pass over to David to put that into the financial terms that you asked for, Richard.

David Smith

Yes, I mean, I think fiscal 20 for us was a bit of a hybrid year, because we were still spending on the air range modernisation and just got air crew training projects from three years ago, so beginning to ramp up on the new LTPA projects. This year and the next two years will really be the peak of our spending on the LTPA.

So, to your question about flexibility around capex, that is somewhat limited by the need to make sure that we continue to meet the modernisation objectives that we've set out in the LTPA. But we are looking for areas where we may be able to move some money around to reduce the upfront cash flow.

And that's why I've given a slightly bigger range on capex of £70-100m this year. I think you asked a question also on the cyber business, didn't you, we actually saw some good growth in our cyber business last year, there was a whole series of projects that we won, the R-GNS contract, the BATCIS contract that we have won the previous year and some other projects as well.

And I think the number was in the £40-50m range of growth in our cyber intelligence business last year, so we actually did see some really good growth in that business and

we're very pleased with the improvement that.

Ian Brown

Thank you. I think the next question comes from Charlotte Keyworth. Charlotte, I'm going to unmute your line right now.

Charlotte Keyworth (Barclays)

Morning gents, So, I've got three questions, the first one, I just wanted to touch on margins as we start to operate under a new world order. You mentioned COVID-19 impact on QTS demand, which is a strong contributor for the Global Products.

And then when I think about EMEA Services, I just wonder longer-term if SSRO margins might start feeling some pressure on things like benchmarking or in a global recession or margins on a global basket of products, sorry of companies. So, what's giving you confidence you can maintain a medium-term guidance of 12 to 13% at the group level? That's the first question.

The second is on the capital for allocation, you're in cash conservation mode, as is everyone at the moment, but given free cash was quite nicely ahead at the full year, and you've obviously got your net cash position, my question is how active do you expect to be on the future acquisition activity, given a recessionary environment might provide some nice opportunities for you?

And then finally, just following up on the earlier capex comments and looking ahead, you've announced deferrals to discretionary spends, but will retain LTPA customer capex, I think it's fair, most of us have probably modelled a nice role-off the 2023 LTPA, so my question is, what explicitly are you deferring for now, what's the impact on programmes and growth by doing so and should we therefore expect some catch-up spend in 2023 as a result? Thank you.

Steve Wadey

Okay, thanks Charlotte. I'll take the second question about capital allocation and acquisition and then I'll ask David to talk a little bit about margins and capex requests. First of all, I'd like to just, sort of, step back, Charlotte, what I've tried really tried to express today is that we have had a robust strategy that's been operating in a challenging world over the last four years and we've taken very deliberate and focussed business choices to make changes in the business and invest in areas where we could see great growth.

And I think that's been really successful over the last four years and as part of that strategy, as you pointed out, we had a very clear capital allocation policy where the number one was investment in organic growth and acquisitions that were appropriate and complementary.

As I've said, the strategy has not changed, the world around us has changed, but the strategy has not changed. And as you've just said, our medium to long-term guidance is very much about continuing on our growth trajectory. But we need to be wise and prudent in the circumstances that we find ourselves.

And that's why we've taken the various actions that we've described in the presentation. And therefore the answer to your question is, the strategy is not changed, but we're in a situation where we've got short-term pressures and the word that connects those is balance.

We just need to be really balanced and thoughtful, so we absolutely will right now keep our

eye on the world of M&A and when and if appropriate we see something that is absolutely on point with our strategy and it's consistent and not going to cause us undue concern or risk in the short or medium term, then I could see that we could proceed.

But it's very much about being intelligent, being thought through, being strategy led, making sure that we get the balance between the short-term environment that we find ourselves in and the continuing with the strategy. So, that's how I would think about, your answer to the question of capital allocation. I'll now ask David to talk about margins and also the capex profile going forward.

David Smith

So, let me put the margin question in context, because clearly if you go back two, three, four years, we were seeing margins in the 14, almost 15% range. And we were very clear last year that, we thought very hard about this, and what we're trying to do is grow our top line revenue in the medium to long term, but keep margins in a 12 to 13% bracket, which is a challenging bracket.

It is above the average for the defence industry and we recognise that it is a challenging number, but we still think it's a realistic objective to be setting out. Now there are some things in the short term, I mentioned a couple of them, the growth of the EDP contract is a challenge for internal sales, although obviously not for internal capital.

MTEQ in the next two or three years as we transition their business model is going to be a dilutive effect on margins. But also we see other areas that we're trying to grow, I've mentioned some of the areas, like the cyber information business, there should be some good opportunities to grow that business.

As we've already set out two or three years ago, building on the core LTPA structure to bring in additional work from international customers into the LTPA business is another area.

So, this is a portfolio mix and we're trying to balance some of the pressures that we see and again the opportunities that we can see developing where hopefully we can bring to bear any capability and skill in our margin business. You're right, the thing that probably no one has factored in yet is, is there going to be an impact on the SSRO base of defence profitability, you could well be right that we might see that as an additional headwind over the next two or three years.

I don't think anybody really knows the answer to that. I wouldn't want to back away from what we're trying to do, which I'll just repeat again, increase our top line, maintain sustainable margins in that 12 to 13% range and deliver a good return on capital for our investors.

Ian Brown

Does that answer your question, Charlotte?

Charlotte Keyworth (Barclays)

Yes, it does, thank you. And then just the capex at the end in terms of the...

David Smith

You're right, if we do defer some expenditure out of this year it is likely that that will get picked in 22 and 23, so it may get a bit more spread. We're not going to change the total

capex, but we're looking at whether certain internal projects, projects upgrading buildings, might be an example where it's not quite so time critical, that we can defer.

There are other things that are very time critical, we've got a lot of work going on, on digitising ranges for instance, that we think we might want to accelerate that. So, there's again a portfolio balance that we'll have the right conversation with our customers around to make sure that we're continuing to meet their priorities and their commitments, to see if we can find a different solution to the portfolio that's not capex investment.

Ian Brown

Great. The next question comes from Chris Leonard at Credit Suisse. Chris, hopefully you are on the line with us.

Chris Leonard (Credit Suisse)

Yes, hi, morning guys. I hope you can hear me.

Steve Wadey

Yes, we can, Chris.

Chris Leonard (Credit Suisse)

Brilliant. Just two questions from me if I may please. Staying on EMEA Services and looking at EDP where you've seen a lot of growth over the last two years, I think I'm right in saying that the order intake you've had is maybe £240m over the first two-ish years of the contract and that's a ten year contract, from memory.

With the scope you seem to be around a billion plus. Does that still stand now or are you maybe thinking your run rate has been good and that could trend higher in terms of an outlook in the medium term?

And then the second question, turning towards Global Products, US robotics programme of records that you have and this year you've stated that small robotics have helped growth in Global Products.

I'm just wondering if you can give any more visibility on what the bill rates could be going forward after the initial phase for CRS(I) and similarly actually to the new contract on RCV, just giving us a pipeline of how that could develop please.

Steve Wadey

Maybe I can just pick up the business context on both of those, Chris, and then maybe David can add a couple of financial points on that.

First of all, I'm pleased that you've brought up Engineering Delivery Partner because I remember when I introduced it, it felt a little bit maybe ethereal to a number of people in the market and was it really going to be this programme that was going to add substantial value to QinetiQ. And I think now seeing the track record of EDP, and your question illustrates it, people are now really starting to sit up and question what impact it could be.

I go back to my opening phrase when we signed the contract in October the year before last. I do believe that EDP will have the same level of impact and significance in QinetiQ in the long term the LTPA has. I think it absolutely will be a billion pound plus programme.

The difference is that we see the revenue and the benefit of that programme coming through

in individual tasking contracts rather than being contracted as one large fixed price programme. So the nature of contracting is different but the value will be similar in that sense.

I also think it's worth just stepping back, particularly when we're in a COVID crisis and I've been talking about the pressures on customers' budgets.

EDP was a brilliant example of the first phase of our strategy where we deliberately engaged and partnered with our customers and co-created a commercial and technical solution which was there to deliver savings and help them accelerate or have high confidence in the delivery of their programmes, and that's what it's absolutely done.

So it's not purely about measuring it from a financial point of view. Our customers are genuinely seeing benefits of that commercial approach. And it's one of the programmes that we have integrated and managed the largest supply chain, bringing the best of British contracting to bear and deliver value for the customer.

So it's a really good example of, yes, something that is going to grow and add value which I think will be quite significant to the company in the long term.

But it's also a brilliant example of our strategy actually in the last few years which is also going to be the type of commercial innovation that we can lean in and support our customers over the coming weeks, months and years as they deal with their budget pressures that are going to come as a result of the pandemic. So I think it's a really good example to have brought into the conversation.

In terms of US robotics, I think that our performance on US robotics is strategically going very well. The team in Boston have done very well winning several programmes of records over the last couple of years, positioning ourselves not just in small robots but in medium size ground robots.

And the recent win on the robotic combat vehicle light programme, which is a demonstration phase. We need to be clear that it's a demonstration phase. It's a great example of our innovation in robotics and autonomy being judged by our customer.

That is a couple of years demonstration programme. It's doing something very new and different in the field of ground robotics. And the US Army will judge in a couple of years' time whether that programme will go ahead into a major production programme.

Clearly there is no commitment to that at this point in time but we're in the box seats. We're the only contracted company that's part of that RCV demonstrator. We're leaning into that programme, we're innovating, we're focusing on the war fighters' needs and we look forward to the competition in two years' time.

The other thing I would want to add on US robotics is not just thinking about US robotics as a standalone capability. The whole reason why we acquired MTEQ in the US is that the synergy between robotics, autonomy and sensing provides a huge opportunity in the field of modern warfare. That's why we invested in the MTEQ acquisition.

That's why Mary Williams, our President, they're working with Jeff Yorsz, the President of the team in Boston. The two of them are now integrating that business to really build a solid platform in the US to add even more value to the US war fighter.

And that's why we've also engaged with brilliant support from the US government the

establishment of a special security agreement, an SSA that will allow us to collaborate across the Group in a controlled manner to share technology and leverage capabilities to support further growth in the US.

So we're really, really pleased with what's going on in the US and in fact it's probably the biggest story that I want to convey of the success of last year. David, maybe you can come back and add a bit of colour on the numbers for Chris.

David Smith

Yes, I think on EDP we were very pleased with the progress last year because it's accelerated quicker than we might have been able to expect. The adoption across a wide range of MOD customers has been very strong.

I think people are seeing it's a very flexible way of procuring engineering services into a whole series of different requirements that are needed across a wide range of activities. So we've got the adoption now.

I think probably on the orders, I don't think we'll increase so much from where we are today. The revenue can still ramp up some more as we obviously start delivering on those orders.

But the key thing for us is actually to continue the trend of moving away from shorter term work into longer term contracting and making sure that as we do that we're really adding value and taking costs out.

That's the whole theory of what we're trying to do, rather than a plethora of very small short-term contracts, actually trying to move this onto a more sustainable basis where we can provide the right capability and skills over a period of time and take costs out for the customer.

There is still more work to be done in that area. And that by the way also helps us improve our own marginal businesses as well as we do that because we can provide higher added value services as well.

So there's a win-win there for the customer to take costs out and us as well, and something that we're trying to pursue.

On US robotics, I think in this particular calendar year, I'm talking about fiscal 21, we're still really in the early phases. It's more going to be 22 and 23 when we start seeing a ramp up in production volumes on CRS(I) and the RCV-light programme that Steve mentioned is a year, maybe 18 months behind that.

But we're making good progress on most of those and equally on RCV-light for instance we're already seeing synergies between the business that is based in Boston and our new acquisition in MTEQ in terms of providing sensor solutions into that overall package.

It's proving the theory that robotics or autonomy and sensing is a very integrated suite that we can offer to the customers and provide better solutions and we can provide those on a comprehensive basis rather than an individual basis.

Ian Brown

Does that answer your questions, Chris?

Chris Leonard (Credit Suisse)

Yes, very much so. Thanks for the detailed answers. That's really clear. Thanks guys.

Ian Brown

Thanks, Chris. So I think the final question comes from Andrew Gollan at Berenberg. Andrew, I'm un-muting your line now. Can you hear us?

Andrew Gollan (Berenberg)

Yes, hi guys. I've got a couple of questions on the COVID impacts. So firstly on the revenue side, the disruption effects that you've seen have really picked up post year-end.

I understand there's lack of visibility going forward but is there anything you can say on the shortfall impacts so far, say in the first six weeks, the revenue impact compared to expectations in April for example as we, I guess, peaked out on these impacts?

To follow on from that, is there any sign of recovery in customers' behaviour? Maybe as the world looks to open up again, any signs of that? Any potential to catch up or is it just a blip or just lost revenues? That was the revenue side.

On the cost side, as far as cost actions, as far as I can see it's the salary cuts and the pay freezes, presumably a temporary effect linked to the revenue impact. Are there any structural changes to costs that need to be made as part of the strategy or aligning strategy to customers that are going to have less cash? So that's the cost question.

And the last question is on working capital. In the presentation you talked about accelerated payments boosting the working capital number. Just some colour on that really; where did that come from? Is that a UK thing or is it US? Is it anything to do with progress payments picked up in the US or...? If it's UK, it's the first I've heard of any acceleration from the MOD.

Steve Wadey

Thank you, Andrew. So the first one on revenue, maybe I could just make a couple of comments on that and I'll link then into our cost actions. And then David, maybe you can bring those together in answering Andrew's last one.

First of all, in terms of where, and I think David was clear in his presentation, where we have seen impact has been around activity that's been directly impacted by cross-border implications where travel restrictions or customer reprioritisation has affected revenue.

David mentioned in his presentation some of the trials activity and some of that impacted the year end, and there has been some continuity of similar levels in terms of coming into April.

In terms of signs of recovery, there are two points that I would make. Even in the last week we have seen some trials that were either delayed or deferred by customers in March, this week they've started to rebook them.

I know that that's a very small example but it is an example of green shoots of where we have seen some impact that some customers themselves have started to work through the impacts of the crisis. They're starting to adapt and work through ways that they need to re-plan their activities.

So it's the nature of that type of activity where we're seeing the impact. And yes, we have seen some green shoots in some cases where customers have re-planned.

I'd like to take the opportunity to reinforce the statistic that I put into the presentation because we have had some commentary that says that our international growth strategy is flawed in a COVID-19 situation.

We've got a strategy that has three home countries, UK, US and Australia, three priority countries, Canada, Germany and Belgium, and 92% of our revenue last year was delivered within those six countries, not subject to cross-border trade.

I think that should give a great confidence to those of you who are looking at the risk and resilience level of the company.

We're not, in contrast to some other businesses, a business that is very dependent on elements of civil aviation or commercial aerospace. And equally we're not a heavy manufacturing export driven business.

The majority of our revenue is delivered from within each of those six nations, and I think that builds some level of resilience that we are focused on. The nature of our business is also far more about science and technology, research and development within those nations.

You would have seen even commentary yesterday, I think the Science Minister was talking about that innovators are going to be key to recovery.

I think if you connect my answer to Chris' question about EDP and the profile of our company, that's why from a medium to long-term point of view, yes, we'll see what level of impact we have this year but we absolutely have the same strategy and we'll accelerate the transformation that gives us confidence in our medium to long-term strategy.

In terms of your question about cost actions, they were very strategic, very thought through.

We wanted to make sure that they were not only going to give us additional resilience to boost us to weather whatever storm the COVID crisis could throw at us, but they were done in a fair, balanced and proportionate way across all of our stakeholder groups, whether that's shareholders, customers or employees to ride through that storm and come out as a stronger company.

I do think there will be, and we haven't done them all yet, I think there will be some levels of structural change. During the course of the presentation I mentioned that we are accelerating our transformation. I'll just give you one example about what I mean by that.

We very well adopted home-working and we're going through a process now of defining what we call our new normal. We expect some level of distributed home and on-site working, maybe even in a blended way, being part of our new normal, being a permanent feature.

That could significantly affect, as an example, the real estate, the permanent real estate of this company on an ongoing basis. That could be a structural cost change that we make in our business, and equally David, on a previous question, talked about areas of capital that we're going to have to invest in and maybe accelerate.

Digital transformation is just one of those examples where, and already we've actually approved an acceleration of our digital transformation programme, all the way through from not just focusing on core communication tools to enable that more distributed working, but also collaboration tools, internally as a company, with industry, and with our customers so that we can provide that innovation and that service with digital services in a different way.

I think these things over time, and we don't have all of the answers, Andrew, will create some structural change in our culture space but I would say very much in a positive way. It actually becomes a platform to propel us into our next phase of sustainable growth. So, David.

David Smith

Yes, I'll be a bit specific about your first question because you did ask... I think in March and April we've seen low to mid-single digit millions of impact, so they are relatively small in terms of our overall revenue.

Some of those things are just going to be deferrals that we'll come back to in the year.

And indeed I mentioned I think in my presentation that we have temporarily shut the Ashford manufacturing facility for QTS. We will have to restart that probably in the next month because we do have an order book and we're going to have to restart that and we're just judging the right time to do that.

The working capital actually is the UK MOD and I'll give them some credit. I think they've been pretty responsive because they know, I think, that it's very important to keep cash flowing to us in these circumstances because equally we've been paying our own SMEs more quickly as well to avoid any risk really in the supply chain.

So they were pretty prompt in paying at the end of March and that's continued during April, and we are returning that in terms of making sure that we pay our own suppliers as much as possible as well.

I think that is a general Defence thing. I don't think we're unusual. I think that's happening through our Defence peers as well.

Steve Wadey

Does that answer your questions, Andrew?

Andrew Gollan (Berenberg)

Yes, very much so. I appreciate the detail. Thank you.

Ian Brown

Good. So I think that concludes the questions, Steve.

Steve Wadey

Okay, we'll just maybe wait if there are any last minute questions from anyone, any raised hands, Ian.

Ian Brown

Yes, there's a question from Alex Savvides. Alex, I'm going to un-mute your line now.

Alex Savvides (JO Hambro)

Hi guys. Good morning. I just had a quick question about the dividend deferral decision. I just wanted to understand that in a bit more detail. What are you looking for to make you think about that dividend coming back? And is that the dividend will come back I think in absolute terms at the same level? I just wanted to hear your thinking around that. Thank you.

Steve Wadey

I think I said it in the presentation but I'd really like to reinforce it. The decision wasn't taken lightly, Alex. It really wasn't. And it was something that we deliberated on with the whole board.

We just really feel that we're in a global crisis and it is unprecedented. We just don't know, all of us in the world, exactly how this crisis will unfold. And therefore we've really lent in as a business and I just referred to taking fair, balanced and prudent, or proportionate actions across all of our stakeholder groups.

The board took that decision to postpone the dividend decision until later in the year, giving the same in terms of guidance for the year. It's part of that prudence in the short-term, just to build resilience for whatever will occur in the coming weeks and months.

Very much as a business we have your interests at the top of our minds. We will continuously review the situation and we'll look for the trends and we'll get to the position, and as soon as it's sensible to do so we'll review that decision and determine what we take forward in terms of any dividend.

That's really the background to it. I'll maybe just ask David to bring a little bit more colour to it, Alex.

David Smith

Alex, this is clearly a difficult decision and we're trying to make sure that the actions we take really balance right across what we're asking from employees and what we're asking from shareholders to maintain the strength of the company.

We will evaluate this continuously. We had a discussion at a recent board meeting and I'm sure we'll have further discussions at the next board meetings as well to make sure that we're doing the right thing.

We're conscious of the fact that we need to make sure that over time we give the right return to shareholders but at the present, given the uncertainty, we think it is the prudent and the wise thing to do to hold onto that cash for the moment until it's clearer what the outcome is going to be, if it's going to be more long-lasting or shorter term.

We just don't really know and I don't think anybody knows to be quite honest, and therefore it's the right thing to be doing over the next few months.

Steve Wadey

And the only additional point, Alex, and I come back to the phrase that when we created the strategic response framework which I presented, the overall guiding principles are very much about this fair, balanced and proportionate response across all stakeholders.

And of course we've put them in and they've had impact on all of our stakeholders and we understand that. And of course what we don't know is the unfolding impact of the crisis which is why we've taken them to boost resilience. But of course we'll want to remove these as quickly as we can.

So we'll look at how the situation unfolds, we'll look at our performance, we'll look for more of those green shoots.

And I can assure you that I've got exactly the same question from 250 leaders that have

personally volunteered to sacrifice their salary as a demonstration of commitment to not only the company but to you as shareholders to help the company ride through this storm as quickly as possible and get back onto the trajectory that we were on.

So we fully understand your question, fully understand the importance but...

Alex Savvides (JO Hambro)

Can I just ask one more? Let's say things carry on in the same vein where you're not seeing a material impact from the pandemic, would the intention be to make the deferred...

Let's say it comes back after the interims, would it be that you pay the deferred final and then pay the interim dividend as normal, i.e. you go back to paying roughly 38 million growing at 3% to 5% or 4% to 6% annually? Is that what we're looking at?

I'm just nervous of a back door cut here that was unnecessary to use the cash for other things undefined.

David Smith

Alex, we're not trying to do that. We're trying to find the right way through the next six to 12 months. Clearly at some stage we want to get back onto the trajectory that we were on anyway for the dividend.

How we exactly handle that in terms of final, full year, interim, I think it's actually a bit of detailed point. The quantum is what we need to decide and the quantum is really going to be about how we see the cash outflows going in the business over the next six to 12 months.

It's just too early to say because we don't really understand fully what the revenue impact is going to be for the business and we just need some more time to be able to assess that.

Steve Wadey

We'll look at it regularly and see how the situation unfolds. We understand the question you're asking and we'll take a fair and balanced judgement at the right time. It's at the top of the minds of the board, I can assure you, Alex.

Alex Savvides (JO Hambro)

Okay. One other question, I don't know if it got asked because my computer crashed halfway through the Q&A. The EIS write-down in Germany, was that just the auditors taking quite an aggressive approach? Can you just explain a little bit more about what drove that write-down please?

David Smith

No, it wasn't the auditors. We proposed that. I had another look at the business plan for EIS, or for what we now call QinetiQ Germany, and they've been impacted over the last year or more recently by some reduced flying hours, that's one of the COVID effects we're seeing, and some additional costs in some of the programmes.

We've therefore just taken a more prudent view of how we see them recovering from that over the next two to three years. We do this annual goodwill test and in anticipation of that we've taken a more prudent view of the business and therefore that's sadly been like a bit of a mechanical effect in terms of the goodwill assessment.

And what we've therefore written off is the mechanical answer of that question, but it was

proactive from me and the management team. Obviously it's been heavily reviewed by the auditors but it wasn't their instigation.

Alex Savvides (JO Hambro)

Is there a long-term impairment to the business case for owning that asset and growing it, and using it to grow a position in Germany? I'm a little bit confused as to maybe a bit of a reduction in scope of a current contract or a couple of contracts?

David Smith

There's still a lot of growth in the plan but probably not so much as we had planned last year and therefore may have taken a more conservative view about the pace of that growth.

Alex Savvides (JO Hambro)

Okay. Just a final one from me then, EDP, the way I understand it you stand in the middle really, so you allocate and control the spend to some degree. I guess it depends on where that spend is. But then you have the ability to allocate it to yourselves where you can supply the service.

So in trying to understand how we should think about the margin, can you try and maybe give us an indication of...

Let's say we have a run rate of £100m a year of revenues from that contract at some point, I don't know what you did last year, what percentage do you think would be fulfilled by QinetiQ businesses, services and what percentages would be external third party?

And what would the margins be on... Would they be materially different?

Steve Wadey

So first of all let's clarify how the model works. The Engineering Delivery Partner programme, we're the prime, we have a consortium and we manage a complete ecosystem of supply chain across the UK.

So as a prime we have effectively a programme management office with key partners and the customer is involved.

We're engaging the customer in terms of what tasks they need to perform to deliver various outputs, whether it's saving money in certain programmes or delivering timeliness of their in-service dates. And that team jointly develops industrial teams to deliver each of those tasks.

So they're not all individual packets that are just determined to be allocated as such to individual companies. They're integrated packages of work which will have multiple companies involved in them.

It's true to say that some of those packages of work may not involve our own engineering and science capability but many of them do, and that's very much driven by the best skills, the best capabilities across the entire supply chain.

So very much similar to, in some ways, what you might see in a normal major procurement programme where an integrated industrial team puts together to deliver to the programme.

In terms of the revenue type mix and margin, David, maybe I could ask you to answer that.

David Smith

Yes and there are different models within EDP that I won't go into too much complexity about. But really depending on the level of value added there are different charge rates. As things get increasingly complex over the longer period then the margins increase, so that work compared to shorter term, just pure, almost like a cost plus delivery piece of work.

So as I mentioned earlier, we are consistently trying to move this onto the longer term, A, because it delivers better cost savings for the customer, but secondly from our own point of view it improves margins.

I think we deliver, and I'm just trying to remember the number, I think it's between 25 and 30% at the moment, but the work is in that kind of range. And the rest is coming from the rest of the supply chain, our two other partners and over 100 other people in the supply chain.

We book the revenue and we get a margin depending on our own work plus also some margin on work that's done by other people. So it is a mix in terms of the results in our books.

Alex Savvides (JO Hambro)

What's the target? Is it similar to the LTPA where historically there's a base rate, it's defined and then you have an ability to outperform that base rate through outperformance?

Is it similar to that, that you can guide to a base rate expectation but there's going to be a range that is basically above that base rate depending on the split that we've talked about, how much is delivered internally and then based on the delivery of the contracts and how well you deliver them? Is that fair?

So if I was to throw some numbers out, a base of six and an upside to nine, ten, is that how you can think about it?

David Smith

So the numbers are probably in that kind of range, yes. And you're absolutely right, there's always going to be an incentive to take cost out as you actually implement the project. But that's in everybody's interest that we do that.

These things are individually contracted and therefore I think pretty well every case has its own little nuances to it. But we're not talking about double digit margins here and the range that you've indicated is probably fair over the portfolio.

But how we do within that does depend on how we manage to mix the portfolio and try and drive up higher value added work to that portfolio.

Alex Savvides (JO Hambro)

Understood. Okay, that's all. Thank you.

Steve Wadey

Great. Thank you, Alex.

Ian Brown

It looks as though there are not further questions, Steve, at this time.

Steve Wadey

Okay, great. Well, thank you everybody for joining. If you do have any follow-up questions then please send them through to Ian and we'll pick them up offline. So thank you very much and appreciate you taking the time to join us. Thank you, bye.