QinetiQ Group plc

For release at 0700 hours on 26 May 2016

Creating the conditions for growth

QinetiQ, a leading science and engineering company operating primarily in the defence, security and aerospace markets, today publishes its full year results for the year to 31 March 2016.

	2016	2015
Business Performance – continuing operations[+]		
Orders	**£659.8m**	£613.6m
Revenue	**£755.7m**	£763.8m
Underlying operating profit*	**£108.9m**	£111.3m
Underlying operating margin*	**14.4%**	14.6%
Underlying profit before tax*	**£108.7m**	£107.8m
Underlying earnings per share*	**16.3p**	15.2p
Underlying net cash flow from operations (post capex)*	**£103.6m**	£114.9m
Underlying cash conversion ratio*	**96%**	103%
Net cash	**£274.5m**	£195.5m
Full year dividend per share	**5.7p**	5.4p
Statutory Reporting		
Operating profit from continuing operations	**£75.3m**	£109.5m
Profit attributable to shareholders	**£106.1m**	£104.7m
Total earnings per share	**18.1p**	16.6p

[+]The Group completed the sale of US Services on 23 May 2014. Total Group performance in 2015 included approximately two months contribution from US Services. 2015 continuing operations (above) comprise EMEA Services and Global Products but exclude US Services. The statutory reporting summary above includes the effect of specific adjusting items and discontinued operations as defined in note 1 and as outlined in note 3.

Headlines

- Solid operating performance in FY16
  - 8% increase in orders due to a multi-year contract renewal
  - Stable revenue and profitability with continued high cash conversion
  - Disposal of non-core Cyveillance business for net disposal proceeds of £22m
  - 6% increase in the full year dividend; £47m remaining of share buyback programme
- Focus on delivery of FY17
  - Markets continue to be challenging with some de-scoping and delay to orders
  - 74% of FY17 revenue under contract, broadly consistent with previous year (77%)
  - Board expectations for Group performance in FY17 remain unchanged
- Creating the conditions for growth
  - Set out vision and strategy
  - Reorganised the company
  - Launched a transformation programme to improve customer focus and competitiveness

Steve Wadey, Chief Executive Officer said: *"Last year we delivered a solid operating performance in challenging markets. The expertise of our scientists and engineers is well matched to emerging themes in global markets. We are capable of more. I have set out our vision and strategy, reorganised the company and launched a transformation programme. These changes are creating the conditions for growth."*
ENDS

* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary.

Other information

There will be a presentation of the preliminary annual results to analysts at 0900 hours UK time on 26 May 2016 in the Milton Suite, The Grange Hotel – St Pauls, 10 Godliman Street, London EC4V 5AJ. Registration for the webcast is available at: www.QinetiQ.com/investors where the presentation will also be available. An audiocast of the event will be available on +44 (0)20 3059 8125 (confirmation: QinetiQ).

About QinetiQ:

Listed on the London Stock Exchange (LSE: QQ.L), QinetiQ is a leading science and engineering company operating primarily in the defence, security and aerospace markets. Our customers are predominantly government organisations, including defence departments, as well as international customers in other targeted sectors. See www.QinetiQ.com | www.QinetiQ-blogs.com | @QinetiQ.

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Group overview

Orders grew 8% to £659.8m (2015: £613.6m), due to the award of a £153m five-year renewal from the UK Ministry of Defence (MOD) for aircraft engineering support, partially offset by some de-scoping and delays to orders in a challenging market environment. At the beginning of the new financial year, 74% of the Group's FY17 revenue was under contract, compared with 77% a year ago.

Revenue was £755.7m (2015: £763.8m), down 1% on an organic basis after adjusting for foreign exchange movements and the divestment of the non-core Cyveillance business in December 2015 for net disposal proceeds of £22m.

Underlying operating profit* was £108.9m (2015: £111.3m). Growth in EMEA Services, which benefited from a credit of approximately £3m due to the resolution of a historical overseas exposure, was offset by a reduction in Global Products, impacted by a reduction in income from the oil and gas sector and the completion of certain programmes in the prior year.

Underlying profit before tax* increased 1% to £108.7m (2015: £107.8m) with underlying net finance costs* falling to £0.2m (2015: £3.5m) as a result of the early repayment of the private placement debt in the prior year. Underlying earnings per share* for the continuing Group increased 7% to 16.3p (2015: 15.2p), benefiting from the higher underlying profit before tax* and reduced share count as a result of the Group buying back shares. Basic earnings per share for the total Group (including approximately two months of US Services in 2015) were 18.1p (2015: 16.6p per share).

Specific adjusting items, shown in the 'middle column', at the profit after tax level amounted to a total credit of £10.2m (FY15 credit: £8.0m). They included a profit of £16.2m recognised on the disposal of Cyveillance, a £7.5m gain following the closure of certain US Services warranty issues and a £31.9m impairment of US goodwill. There was also a net tax credit of £21.2m which includes the impact of the statutory change to the research and development tax credits regime offset by the associated surrender of previously capitalised tax losses and other non-recurring deferred tax movements. The prior year statutory operating profit included a profit of £15.9m recognised on the disposal of US Services, a £25.2m credit in respect of the capitalisation of a proportion of the Group's unused tax losses and a one-off accelerated interest cost of £28.8m associated with the early repayment of the private placement debt.

Underlying operating cash conversion* remained strong at 96% (2015: 103%), delivering an underlying cash flow from continuing operations* of £103.6m (2015: £114.9m). At 31 March 2016, the Group had £274.5m net cash, compared to £195.5m net cash at 31 March 2015 and £181.5m at 30 September 2015. The increase was primarily due to the Cyveillance disposal proceeds and net tax receipts of £27.9m (2015: £8.8m).

Priorities for capital allocation are:
1. Organic investment complemented by bolt-on acquisitions where there is a strong strategic fit,
2. The maintenance of balance sheet strength,
3. A progressive dividend, and
4. The return of excess cash to shareholders.

A £150m share buyback was initiated on 28 May 2014 following the US Services disposal and completed by 30 September 2015 with 72.5m shares purchased in total. An additional £50m share repurchase was announced in November 2015 to be executed over 12 months, of which £47m remains to be completed.

The Board proposes a final dividend of 3.8p (2015: 3.6p) making the full year dividend 5.7p (2015: 5.4p). Subject to approval at the Annual General Meeting, the final dividend will be paid on 2 September 2016 to shareholders on the register at 5 August 2016. The full year dividend represents an increase of 6% reflecting the Group's progressive dividend policy.

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Trading environment

QinetiQ is a leading science and engineering company operating primarily in the defence, security and aerospace markets.

UK

Alignment with UK defence customers

In the financial year to 31 March 2016, 67% (2015: 67%) of QinetiQ Group revenue was generated from the MOD in addition to 3% (2015: 3%) from other UK Government Departments. We are the UK's leading provider of test and evaluation (T&E) services across all military domains and the majority of equipment programmes. We generate more than £300m per year from T&E, underpinned by the Long Term Partnering Agreement (LTPA) which has delivered an improved service and significant savings for the MOD over the last 13 years. We estimate the UK T&E market is double this size and the addressable market worldwide is much greater. Leading the UK T&E enterprise by working in partnership with Government and prime contractors is a strategic priority for QinetiQ. In addition, we remain a market leader in research and advice in specialist areas such as C4ISR (Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance), weapons and energetics, cyber security and procurement advisory services.

Within the MOD, the main customers for our services are the MOD's procurement function DE&S (Defence Equipment and Support), the Defence Science and Technology Laboratory (Dstl) and the Front Line Commands (Navy, Army, Air and Joint Forces), whose influence on future capabilities has increased in recent years. Our businesses are aligned closely to these Commands and are well placed to help them with their growing procurement responsibilities. In particular, Joint Forces Command, with its own procurement arm and multi-billion pound budget, provides a focused channel for our Cyber, Information & Training business.

The UK Government's Strategic Defence and Security Review (SDSR) was published on 23 November 2015. Its publication has helped to clarify the UK's capability priorities, but it will take time before its impact on the associated allocation of the UK defence budget is clear.

Delivering more for less

As part of the SDSR, the MOD has declared plans to address important capability gaps such as maritime surveillance (through the purchase of nine new aircraft) and combat air numbers (by extending the life of Typhoon aircraft that have been in service for some time). These plans will require immediate savings to be made elsewhere in the 'defence enterprise' to fund them, with the UK Government looking to achieve a 30% reduction in MOD civilian staff and in 'built' estate and to deliver £11bn of savings from defence and security budgets over the next four years.

The introduction of new capabilities, and in particular extending the life of existing capabilities, provides QinetiQ with opportunities to deliver engineering, test and evaluation services. The savings programmes could also provide further opportunities for outsourcing, along with increased MOD presence on our sites. There is likely to be increasing competition, but QinetiQ is well positioned due to its strong record in delivering improved services combined with significant savings (ie more for less) for customers.

MOD spending on science and technology will continue to be protected at 1.2% of the defence budget with an increased emphasis on disruptive technologies and innovation, and a move away from some more traditional research programmes. Space, cyber security and cryptography are among the priorities, areas in which QinetiQ has recognised expertise.

The Single Source Regulations Office (SSRO) is now fully established as the independent regulator for single-source defence contracts driving greater transparency that will help demonstrate the value for money the Government derives from Qualifying Defence Contracts (QDCs). The SSRO has confirmed the baseline profit rate for new single source defence contracts is 8.95% for FY17 (10.6% in FY16) and that over the course of FY17 it will consult again and develop the methodology for calculating the baseline profit rate in future years, potentially introducing multiple profit rates. This baseline rate acts as the starting point for agreeing the profit rates of new and renewed contracts, and suppliers can both under and over-perform the contracted rate depending on, for example, risk, capital servicing and project execution. Further updates and clarifications are expected to be published by the SSRO on other topics affecting QDCs, eg allowable costs.

Our combination of capabilities is unique in the UK and, consequently, approximately 70% of total EMEA Services revenue is derived from single source contracts, including the non-tasking element of the Long Term Partnering Agreement (LTPA). As we have said before, we anticipate that the majority of our single source revenue will fall under the regulations within approximately three years.

Global Markets

Our Global Products division has a significant US footprint, providing a route to the world's largest defence market and, in the financial year to 31 March 2016, 6% (2015: 6%) of QinetiQ Group revenue was generated from the US Department of Defense (DoD).

US defence market: a greater focus on innovation
In the US, the defence downturn is reaching the bottom of the cycle, with the President requesting continued increases to the defence budget and the budget for overseas contingency operations. A renewed commitment by US military customers to unmanned systems products is reflected in plans to award new competitive Programs of Record over the next two years to enhance and sustain the US unmanned systems capability as a funded capability in the DoD budget.

The President has requested an increased research and development (R&D) budget for defence which includes the Defense Innovation Initiative, also known as the Third Offset Strategy, "an ambitious effort to identify and invest in innovative ways to sustain and advance America's military dominance for the 21st Century." This initiative is expected to put new resources behind innovation and, in particular, R&D in technology to support and optimise the interaction between humans and machines. These initiatives align with a number of areas in which QinetiQ has distinctive strengths including sensor fusion, man-machine interfaces, autonomy, and unmanned vehicles.

Supporting defence modernisation in Australia
QinetiQ's third home market is Australia. The Australian Government is responding to the need to modernise its defence equipment and now plans to replace the majority of its platforms over the next 15 years, supported by an increase in defence expenditure to 2% of GDP. In line with the recommendations of its First Principles Review, in which our Australian business played a role, the Government is also pursuing a defence transformation programme similar to that which has been underway in the UK since the beginning of the decade.

Global investment in defence
Many of our unique capabilities are attractive to customers beyond the UK, US and Australia, and we have made it a strategic priority to develop new home markets through partnerships, and grow sales by exporting our products and services. For example, as the Canadian Government pursues similar defence transformation programmes to the UK, it values the advice, test and evaluation that we can provide in support of better procurement.

In Sweden, where QinetiQ operates the Flight Physiological Test Centre for the Swedish defence department, the defence environment is similar, with budget pressures evident against a background of heightened security threats. Such pressures, on Sweden and other Northern European nations, can drive greater cooperation on specific programme opportunities and greater interdependency between allies in capability provision.

Further afield, in Turkey and the Middle East, budgets remain more robust, offering increased export opportunities for defence products and services, albeit these and other nations are determined to develop indigenous capability for both economic and sovereignty motives. This can provide seams of growth potential for QinetiQ's most distinctive capabilities but accessing these markets will require thoughtful partnering approaches and alignment with UK Government export initiatives.

Emerging themes in our markets

Increasing threats; reducing budgets
Looking across our home and overseas markets we see a number of key themes. Governments are having to respond to increasing security threats with reducing budgets. They need to deliver more with less. So not only are government customers seeking greater value for money from their suppliers, they are also looking for assistance in meeting their own 'efficiency' challenges. Companies like QinetiQ, with a track record of delivering improved productivity and innovation in products and services, are strongly positioned to help.

Innovation in equipment processes and approach
Most governments recognise that being efficient is not enough and they also need to innovate to respond to these fast evolving threats. They are seeking new approaches to innovation in both equipment and processes so that they can rapidly integrate new technologies into existing capabilities. Investing and applying our core competence for customer advantage in defence and commercial markets is a strategic priority for QinetiQ. Many customers are keen to capture the innovation that comes from universities and small and medium sized enterprises (SMEs) and are looking for assistance from organisations that can help them connect their supply chains. Similarly governments are promoting multilateral approaches to developing new capabilities, encouraging suppliers to cooperate internationally.

QinetiQ already delivers an 'innovation integrator' role, building networks of suppliers to bring together Government, industry, SMEs and academia in collaborating teams and thereby facilitating innovation at every stage of the procurement process. Our Cyber Information & Training (CIT) business, for example, is the MOD's leading supplier of C4ISR research, managing framework contracts for the MOD that involve more than 100 UK SMEs.

CEO appointment

Steve Wadey joined QinetiQ as Chief Executive Officer (CEO) on 27 April 2015. He was previously the Managing Director of MBDA UK and Technical Director for the MBDA Group. During the year he set out a vision and strategy for QinetiQ and launched a transformation programme for immediate implementation.

Vision and strategy

Responding decisively to the changing market environment

The world around us is changing. Customers are looking to achieve more with less and demanding better value for money. This requires greater efficiency, innovation and collaboration both domestically and with international partners. We recognise that staying the same will not be good enough in a changing world.

As a company we have a solid foundation to build on because our core competencies are well matched to emerging themes in our markets. We have considerable breadth and depth of knowledge and capability that we deliver for our customers, particularly in test and evaluation, and science and technology. Not only are our people critical to sovereign capability, we are also experienced in delivering more for less and responding to new challenges through innovation in services, products and business models. Last year our customer satisfaction scores remained strong at more than eight out of ten. Customers have requirements we can meet if we remain sufficiently agile and responsive to connect their requirements with the strength and depth of our core technical and engineering competencies.

Our vision and strategic priorities

We have established an ambitious vision that defines where we want to be in five to ten years' time, building on our strengths. Our vision is to be: "The chosen partner around the world for mission-critical solutions, innovating for our customers' advantage."

To realise our vision, we are implementing strategic priorities designed to grow the company by focusing on our primary UK customer, on international customers and on innovation.

UK – We will be a leader in defence test and evaluation by working in partnership with our UK customer and prime contractors. We intend to modernise the approach to test and evaluation in the UK, focused on introducing a more agile capability. By working in partnership with Government and other companies, we will help our customers save money. As threats change we need to ensure that our test and evaluation capabilities continue to enable our customers to develop next generation military equipment. For example, in October 2016, we will host a world-first Royal Navy trial which will demonstrate how autonomous systems can operate together as part of a naval fleet.

International – We will build an international company that delivers additional value to our customers by developing our home markets, creating new home markets and exporting. QinetiQ will become an international company, operating around the world. We will maintain a focus on our home markets (the US and Australia in addition to the UK) where we already have a presence and market share, develop new home markets through partnerships, and grow sales by exporting our products and services. For example, to win in an export market, rather than compete independently we have chosen to partner with BAE Systems, with the backing of the UK Government, for a competition in Chile to upgrade their Type 23 frigates. A 'Team UK' approach.

Innovation – We will invest in and apply our core competence for customer advantage in defence and commercial markets. QinetiQ will continue to innovate, focusing on markets where customers have a clear need for our skills, applying and carefully investing in our competencies to meet their needs. For example, as part of our new Internal Research and Development (IRAD) programme, we are funding projects to develop next generation approaches to test and evaluation services, robotics and OptaSense applications in the rail industry.

Transforming our way of working

We are embedding a new way of working to align the company with our strategy and ensure we are agile and responsive in meeting customer needs. We have also launched a transformation programme to deliver the key changes that we need to put in place as a company to achieve growth.

Delivering benefits to our key stakeholders

Although market headwinds are strong, by working together and encouraging our peoples' entrepreneurial spirit, we are creating a customer-focused, collaborative and competitive environment in order to deliver growth. Our customers will benefit through better products and services, increased responsiveness and improved value for money. Our employees will benefit through greater opportunities to work in integrated teams, utilising their expertise across multiple domains throughout QinetiQ. Over the medium term, we expect our shareholders to benefit through growth in quality earnings as we realise our vision and deliver our full potential.

Our transformation programme

We have launched a transformation programme to enhance customer focus, improve competitiveness and drive investment in sustainable growth.

Leadership and organisation

To respond to a changing market environment we have reorganised the company, establishing new businesses responsible for our customer relationships, contract delivery and securing orders jointly with Business Development. Enabling functions provide support, in particular the dynamic resourcing of people and assets from across QinetiQ. Our scientists, engineers and operations community will be transferred to the new structure during the year, supported by an effective sales and operational planning process, enabling us to resource as one company. By improving productivity there is the potential to deliver efficiencies that will provide better value for money for customers and headroom for careful investment.

The leadership team has been strengthened with the appointment of new Group Directors of Business Development and Human Resources, and a new CEO for OptaSense, all from outside QinetiQ. In addition, a new Managing Director International will join this summer.

Operational excellence

Our future success will be built on operational excellence – doing what we say we are going to do, and underpinned by continued operational and financial discipline. In addition to driving efficiency and productivity, we have established a technical excellence function to improve project delivery.

We are positioning QinetiQ for the future through an integrated business planning process, the output of which will be a robust plan. This is supported by a new approach to performance management which will ensure every employee across the company has clear objectives aligned to our strategy that support the effective delivery of our plan. We have also established a Leadership Community at QinetiQ for the first time, bringing together the top 100 leaders every month to ensure we are focused on our business performance.

Business winning

Customer requirements are not only changing, they are also getting more demanding. There is a need to improve our business winning skills in order to thrive in an increasingly challenging market, so we have instigated a programme to develop the skills of our sales teams, bringing in experienced hires where required. We also need to improve our knowledge of home and international markets; for example in August we appointed a new CEO for OptaSense who brings more than 20 years' experience of working in the oil and gas sector. We have launched a new process for bidding and winning strategically important corporate campaigns, making best use of the skills that are available across the company.

As part of the reorganisation of the company, we have created an International business to deliver our products and services in international markets. It incorporates businesses with a significant international footprint and/or those with international growth potential. Customers outside our home markets are unlikely to know QinetiQ, so we are also improving the visibility of our brand through targeted, cost effective marketing – particularly in European countries such as Belgium and Sweden where we already have a presence.

Investing in our future

We are driving savings through improved efficiencies and greater agility which will ensure we remain one step ahead of the competition and also create the headroom so that we can invest in our future. This will allow us to invest carefully in R&D, improve skills and processes, take and manage risk more effectively on our customers' behalf, and pursue campaigns to grow the company.

The key enabler to the themes across our markets is innovation, not just novel technologies but also innovation in products, services and business models. By working in partnership with our customers we can propose innovative solutions to meet their emerging needs. For example, the £153m contract renewal for aircraft engineering services represents a new way of doing business with MOD, under which we are measured and paid on results and outputs rather than inputs. Last summer, we launched a new Internal Research and Development (IRAD) programme for QinetiQ led by our Chief Technology Officer and guided by an Innovation Steering Board to ensure that projects are customer-driven and properly controlled. This programme will develop future products and services using investment funded through cost savings across the company. Current projects include OptaSense applications in the rail industry, next-generation robotics and test and evaluation services.

QinetiQ has considerable breadth and depth of technical expertise; we are working to integrate these core competencies and connect them with customer needs to win market share. The strength of our balance sheet and the cash generative nature of our portfolio enables us to invest in our core competencies such as T&E, with capital expenditure likely to increase further as we continue to invest in the LTPA and other long-term contracts.

Capital allocation

A key part of building for the future will be capital discipline. We intend to maintain our priorities for capital allocation with a focus on investment in creating the conditions for growth:

1. Invest in our organic capabilities, complemented by bolt-on acquisitions where there is a strong strategic fit;
2. Maintain the necessary balance sheet strength;
3. Provide a progressive dividend to shareholders;
4. Return excess cash to shareholders.

FY17 outlook

The UK Government's Strategic Defence and Security Review has brought clarity to key defence programmes but will require further savings to be delivered from ongoing defence transformation. This will provide future opportunities for EMEA Services to build on its strong record of delivering more for less, whilst recognising that in the short term there will continue to be uncertainty and the potential for interruptions to order flow. Although revenue under contract for FY17 is slightly below that of a year ago, the division's performance as a whole is expected to remain steady this year.

The Group's Global Products division has shorter order cycles than EMEA Services. At the beginning of the financial year, FY17 revenue under contract was slightly above that of a year ago, but the performance of Global Products remains dependent on the timing and shipment of key orders.

Overall, the Board's expectations for Group performance this financial year remain unchanged.

Operating review

EMEA Services

	2016 £m	2015 £m
Orders[(1)]	**495.4**	461.6
Revenue	**616.4**	625.6
Underlying operating profit*	**93.8**	93.0
Underlying operating margin*	**15.2%**	14.9%
Book to bill ratio[(1)]	**1.2x**	1.1x
Funded backlog[(1)]	**719.1**	678.6

(1) Excludes the £998m third-term of the LTPA contract.
B2B ratio is orders won divided by revenue recognised, excluding the LTPA contract.

Overview

EMEA Services combines world-leading expertise with unique facilities to provide technical assurance, test and evaluation and training services, underpinned by long-term contracts. The most significant of these is the Long Term Partnering Agreement (LTPA) for test, evaluation and training services which has delivered an improved service and significant savings for the MOD over the last 13 years. EMEA Services is also a market leader in research and advice in specialist areas such as C4ISR, weapons and energetics, cyber security and procurement advisory services.

Financial performance

Each of the core Air & Space, Maritime, Land & Weapons and Cyber, Information & Training businesses delivered a solid performance in 2016 despite the uncertainty resulting principally from the UK Strategic Defence and Security Review (SDSR) published in November 2015 and budgetary pressures.

Orders grew 7% to £495.4m (2015: £461.6m) driven by the timing of multi-year contract awards (including the £153m five-year UK MOD renewal for aircraft engineering services) with some continued de-scoping and delay to other orders in a challenging market environment.

Revenue was flat on an organic basis at constant exchange rates, after adjusting for the divestment of Cyveillance Inc, which was sold in December 2015 for net disposal proceeds of £22m. Cyveillance, which had revenues of $18m in FY15, is a former business unit of the US Services division, sold in May 2014, and more recently has been reported in EMEA Services. At the beginning of the new financial year, 77% of EMEA Services' FY17 revenue was under contract, compared with 80% at the beginning of the prior year.

Underlying operating profit* increased 1% to £93.8m (2015: £93.0m) assisted by a credit of approximately £3m due to the resolution of a historical overseas exposure.

Year in review

Air & Space

With technology developments increasingly blurring boundaries between air and space systems, our Air & Space businesses were combined on 1 April 2016 to increase collaboration in our engineering capabilities to de-risk complex aerospace programmes.

The business is working in partnership with the MOD and the supply chain to implement a new model to transform the provision of aircraft test and evaluation. During the year, it was awarded two single source

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contract renewals under this new model, worth a combined £153m over five years, to deliver technical services to fast jets and heavy lift aircraft. This represents a new way of working under which we are measured and paid on results and outputs, not inputs, improving long-term planning, providing better visibility, and delivering considerable savings to the MOD. This award complements a £13m contract to assist the MOD in bringing the Delta Test variant of the A400M Atlas into UK service, and a £5m contract to evaluate flight control system upgrades to Boeing's Chinook helicopter.

In international markets, the Air & Space business was awarded a five-year extension to the contract under which it manages and assists in the delivery of training at the Swedish Flight Physiological Centre. It is also developing the gridded ion engine electric propulsion systems for the flight module to be used on the European Space Agency's BepiColombo mission to Mercury. Significant resources are being deployed by all parties to ensure the mission meets the planned launch date which has been deferred to 2018. The business delivers turnkey services for customers using Remotely Piloted Air Systems (RPAS) to meet growing demand particularly from international organisations such as the United Nations. Following the opening of the Snowdonia Aerospace Centre at Llanbedr in Wales, it successfully demonstrated the use of RPAS in tackling environmental issues in a project for the Welsh Government.

Maritime, Land & Weapons

The Maritime, Land & Weapons business was created on 1 April 2016 combining businesses with a strong focus on test and evaluation at a time when customers are increasingly undertaking more complex, multi-domain trials. The new business will deliver operational advantage to customers by providing independent research, evaluation and training services.

In the weapons domain, the business is a leading provider of independent research on weapons and energetics, coordinating the MOD's conventional weapons research programme through its leadership of the Weapons Science and Technology Centre. During the year it was also awarded a new research framework contract for trials, testing and analysis in cyber and electronic warfare, a five-year contract to provide advice to the MOD on military batteries and a four-year contract to provide advice to NATO, contracts which all demonstrate confidence in QinetiQ as a long-term partner. In addition to research and advice, core capabilities include test and evaluation, delivered mainly under the LTPA, and targets services. In October 2015, the business led a team from across QinetiQ to deliver an international at sea demonstration at the Hebrides range, the largest in Europe. The exercise attracted nine ships from eight nations, culminating in the first ever launch of a ballistic rocket into space from the UK and its subsequent engagement by an SM3 missile launched by a US guided missile destroyer. As a result, the business is now pursuing opportunities for further combat scenario training and inter-operability testing involving customers from many nations. It also undertook testing of the latest helicopter-borne Infra-Red Threat Warning System in live rocket and gunfire scenarios.

Sustaining and growing its core technical advice and design support services to the UK Royal Navy is a strategic priority for the Maritime Land & Weapons business, and during the year it was awarded a new contract to deliver acceptance trials for the four new MARS class tankers. The business also resolved urgent operational issues to enable ships to deploy and be effective in theatre including improving the hydrodynamic efficiency of Type 23 frigates by optimising the design of the propeller and hull, enabling the Royal Navy to realise potential fuel savings across its fleet. It also delivered a container-based combat system for close-in defence against Fast Inshore Attack Craft offering a new, flexible solution for the self-protection of support ships. The business is pursuing selected growth campaigns with a focus on emerging technologies such as autonomous systems. During the year, it won a number of autonomy-related contracts, including support to the Royal Navy to deliver the Unmanned Warrior exercise in October 2016 which will demonstrate the use of autonomous systems in a wide-range of scenarios. QinetiQ's role also includes the delivery of a containerised command system to control multiple unmanned systems.

Cyber, Information & Training (CIT)

The CIT business helps government and commercial customers respond to ever-evolving threats based on its expertise in training, secure communication networks and devices, intelligence gathering and surveillance sensors, and cyber security.

Although competition is fierce, the SDSR and the focus on counter-terrorism are likely to drive increases in budgets for C4ISR and cyber security. The CIT business is the MOD's leading supplier of C4ISR research, maintaining its research revenues during the year and winning new work to improve information systems for deployed headquarters. The business manages a network of more than 100 UK SMEs through these research framework contracts, fulfilling an 'innovation integrator' role that is becoming more and more important in defence and other sectors. Large framework contracts are being used increasingly for the delivery of technology services and during the year the business was awarded a position with Northrop Grumman on a seven year framework contract to deliver cyber security support to the UK Government. It also won a contract with Motorola Solutions to provide monitoring, assessment and assurance services in support of the delivery of the UK Emergency Services Network.

Outside its traditional markets, CIT is providing advice to regional and local government customers on innovation initiatives to support local business growth, and is delivering training and simulation services to customers in North America, Europe and the Middle East. Finally, the business is providing secure receiver processing for the encrypted Public Regulated Service (PRS) on the Galileo constellation of satellites – the European Union version of GPS which goes live in 2017. During the year it launched a new receiver that will utilise the PRS service for use by governments, the military and emergency services across Europe.

International

On 1 April 2016, a new International business was established incorporating businesses with a significant international footprint and those with international potential, as well as to manage other opportunities via our international offices. The business includes QinetiQ Australia as well as Advisory Services (previously known as Procurement Advisory Services).

The Australian business provides impartial advice and services predominately to government customers. This year, the business successfully agreed with the Australian Department of Defence, the renewal for up to 15 years of the Aircraft Structural Integrity (ASI) services contract for a minimum contract value of A$21m, which supports the airworthiness of military aircraft. This is one of two underpinning contracts for the Australian business, which position it well for 'strategic partner' style contracts that the Australian Government is using increasingly as it implements its recapitalisation and defence acquisition reform programmes.

Advisory Services helps customers deliver complex programmes by providing analytical services and the evidence required to make complex decisions. Building on its strong record in the UK, the business won a major contract to provide early stage advice and business case support to a Middle Eastern client for a complex engineering project.

Global Products

	2016 £m	2015 £m
Orders	**164.4**	152.0
Revenue	**139.3**	138.2
Underlying operating profit*	**15.1**	18.3
Underlying operating margin*	**10.8%**	13.2%
Book to bill ratio	**1.2x**	1.1x
Funded backlog	**139.1**	116.7

Overview

Global Products delivers innovative solutions to meet customer requirements and undertakes contract-funded research and development, developing intellectual property in partnership with key customers and through internal funding with potential for new revenue streams.

Financial performance

Orders grew 8% to £164.4m (2015: £152.0m) as a result of a new pipeline contract for OptaSense and due to improved order flow in QinetiQ North America. As a result, the Global Products division had 64% of its FY17 revenue already under contract at the beginning of the new financial year compared with 61% at the same time last year.

Revenue was up slightly to £139.3m (2015: £138.2m) as a result of currency movements, but underlying operating profit* fell to £15.1m (2015: £18.3m), impacted by a reduction in income from the oil and gas sector and the completion of certain programmes in the prior year. The underlying operating profit margin* was 10.8% (2015: 13.2%).

Year in review

QinetiQ North America

QinetiQ North America develops and produces innovative military protection products, specialising in unmanned systems, survivability and maritime systems, along with products in related commercial markets. The performance of this business improved in year as it continued to adapt to a defence funding environment that has shifted markedly from the overseas contingency operations associated with Iraq and Afghanistan. QinetiQ North America is the world's leading provider of military robots with employees centred in Massachusetts, Pennsylvania and Virginia. Activity in year focused on the reset and recapitalisation of robots previously used on operations and the upgrade of systems with new capabilities such as the detection of CBRNE (chemical, biological, radiological, nuclear and explosives). At the same time, the business is preparing for multi-year Programs of Record which will be funded out of the Department of Defense's base budget.

During the year the business announced a contract win valued at $16m from General Atomics in San Diego, California to deliver control hardware and software for the Electromagnetic Aircraft Launch System (EMALS) and the Advanced Arresting Gear (AAG) to be installed on the Navy's next aircraft carrier, the future John F. Kennedy (CVN 79). It was also awarded orders for survivability products for both US and international customers, with demand for air and ground armour increasing in year. In addition to product sales, QinetiQ North America is building on its base of contract-funded R&D projects to drive technology development, explore new customer problems and expand its competitive offerings.

* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary.

OptaSense

OptaSense is a Distributed Acoustic Sensing (DAS) business operating in multiple vertical markets. During the year, Jamie Pollard was appointed to be its CEO after more than 20 years running large global businesses within the oilfield services company Schlumberger. An OptaSense advisory board has also been established, comprising senior industry specialists to provide domain expertise in key target markets including Hansjorg Hess, a former Executive Director of Deutsche Bahn Netze. Although growth in the upstream oil and gas market has been constrained by the low oil price, the product development agreement with Shell continues to deliver significant technical progress and a fourth generation OptaSense system was launched in year. The business also signed a strategic marketing agreement with Weatherford, an oil and gas service company with a presence in every major oil and gas region of the world. The partnership will deliver enhanced data acquisition and monitoring of seismic activity, well construction, completion and fracture operations, and production flow.

OptaSense continues to make progress in infrastructure security, winning a contract with a partner to deliver the world's largest distributed fibre sensing project for the Trans-Anatolian Natural Gas Pipeline (TANAP) that runs from Azerbaijan, through Georgia and Turkey, to Europe. The total contract value is more than $30m, of which approximately half has been contracted with OptaSense, and will cover the protection of over 1,850km of pipeline. The business also won a contract to monitor a further 500km of gas pipeline in India. At the end of September, OptaSense successfully completed an 18-month development project with Deustche Bahn, which concluded that DAS technology has the potential to significantly reduce the cost of sensing in the rail industry. It also won a contract with a Class 1 US railroad operator to deliver a software platform in preparation for a wider rollout of DAS technology.

Space Products

QinetiQ's Space Products business, which provides satellites, payload instruments, sub-systems and ground station services, delivered several innovative projects during the year. In March, the European Space Agency's (ESA's) ExoMars mission was launched, containing QinetiQ's UHF transceiver which will transmit data from the lander on the planet's surface back to Earth via a satellite orbiting Mars. The project will pave the way for a second mission, recently rescheduled to 2020, in which a rover will spend six months analysing Mars's environment for signs of life. The business is currently developing the computer and avionics for ESA's Proba 3 satellites, to be launched in 2019 to study the Sun.

EMEA Products

EMEA Products provides research services and bespoke technological solutions developed from intellectual property spun out from EMEA Services. QinetiQ makes an important contribution to sovereign UK capability in advanced materials technology, and during the year it renewed a five-year, £10m contract to provide materials research and advice to the UK MOD. This capability underpins ongoing commercial relationships with EDF Energy for the development of stealth wind turbines. QinetiQ also became the first company accredited and authorised by the French Government to assess proposed wind farm impact on meteorological radars, in order to speed up planning applications. Other orders received in year included a contract with the US Defense Advanced Research Projects Agency (DARPA) to develop an electric hub-drive that will improve survivability and mobility of future military ground vehicles. The contract, worth $2m with an option for a further $3m, is part of DARPA's Ground X-Vehicle Technologies (GXV-T) programme.

Subsidiaries Boldon James and Commerce Decisions are reported in EMEA Products. Boldon James, which provides data classification solutions to large military and commercial organisations, had a strong year and should see further opportunities following changes to European Union regulations that introduce significant penalties for data classification leaks. Commerce Decisions renewed its agreement with the MOD for the provision of tender assessment and procurement support software. It also won the first contract through its Australian arm and was selected to deliver bid evaluation criteria for the Canadian Surface Combatant programme which will be used to assess warship designers and combat system integrators.

Financial items

Net finance costs

Net finance costs were £1.3m (2015: £4.1m) benefiting from the repayment of private placement debt in the prior year. The underlying net finance costs* were £0.2m (2015: £3.5m), with an additional £1.1m (2015: £0.6m) in respect of the pension net finance expense reported within specific adjusting items*.

Taxation

The effective tax rate of 11.8% (2015: 10.9%) continues to be below the UK statutory rate, primarily as a result of the benefit of research and development tax relief in the UK. The effective tax rate is expected to remain below the UK statutory rate in the medium term, subject to the impact of any tax legislation changes, the geographic mix of profits and the assumption that the benefit of net R&D tax relief retained by the Group remains in the tax line.

UK Group companies have now elected to obtain tax benefits in respect of allowable R&D expenditure through the R&D Expenditure Credit (RDEC) process rather than through the previous treatment as a super-deduction in the tax computations. This election was made retrospectively back to 1 April 2013 and the incremental impact on the tax expense for the years ending 31 March 2014 and 31 March 2015 has been reported in the current year as a specific adjusting item. The change of regime results in the utilisation of previously capitalised UK trading losses and the associated deferred tax asset has been charged to the income statement with other non-recurring deferred tax movements (see note 8) also as specific adjusting items. Deferred tax has been calculated using the enacted future statutory tax rates.

At 31 March 2016 the Group had unused tax losses of £154.8m (2015: £291.6m) which are potentially available for offset against future profits. £26.1m of these losses are time limited of which £6.3m will expire in 2034 and £19.8m will expire in 2035. Certain UK tax losses had been recognised on the balance sheet as at 31 March 2015 as a deferred tax asset of £25.2m. As noted above, those tax losses have now been utilised following the election into the RDEC regime. No deferred tax asset is recognised in respect of the remaining tax losses due to uncertainty over the timing and extent of their utilisation.

The current tax liability is £39.9m as at 31 March 2016 (31 March 2015: £15.3m). The increase in the liability is primarily due to a potential tax liability crystallising in the US following a court decision in respect of taxes payable in respect of the Group's acquisition of Dominion Technology Resources, Inc. in 2008. An insurance policy was taken out by the Group at the point of acquisition and if, subject to an appeal, the court's decision is final then the funds required to settle this dispute will be provided by the insurers and an escrow account funded by the vendors. Hence, an offsetting receivable is reported on the balance sheet as at 31 March 2016 (included within trade and other receivables).

Earnings per share

Underlying basic earnings per share* for the continuing Group were 16.3p (2015: 15.2p) benefiting from the higher profit before tax and the reduced share count, as a result of the Group buying back shares. Basic earnings per share for the total Group were 18.1p (2015: 16.6p per share). The average number of shares in issue during the year, as used in the basic earnings per share calculations, was 587.0m (2015: 630.9m) net of Treasury shares, and there were 586.7m shares in issue at the year end.

* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary.

Dividend

The Board proposes a final dividend of 3.8p (2015: 3.6p) making the full year dividend 5.7p (2015: 5.4p). Subject to approval at the Annual General Meeting, the final dividend will be paid on 2 September 2016 to shareholders on the register at 5 August 2016. The full year dividend represents an increase of 6% reflecting the Group's progressive dividend policy.

Cash flow, net cash and liquidity

The Group's cash flow from operations before cash flows in respect of specific adjusting items but after capital expenditure was £103.6m (2015: £114.9m). Underlying operating cash conversion* remained strong at 96% (2015: 103%).

At 31 March 2016 net cash was £274.5m (2015: £195.5m), reflecting continued strong operating cash performance, £22m Cyveillance disposal proceeds and non-recurring net tax receipts totalling £28m relating to the impact of the regime change to R&D tax credits and the associated surrender of UK trading losses. Total committed facilities available to the Group at year end, consisting solely of a revolving credit facility which is currently undrawn, amounted to £235.6m (2015: £233.3m).

A £150m share buyback was initiated on 28 May 2014 following the US Services disposal and completed by 30 September 2015 with 72.5m shares purchased in total. An additional £50m share repurchase was announced in November 2015 to be executed over 12 months, of which £47m remains to be completed.

Foreign exchange

The Group's income and expenditure is largely settled in the functional currency of the relevant Group entity, mainly Sterling or US Dollar. The Group has a policy in place to hedge all material transaction exposure at the point of commitment to the underlying transaction. Uncommitted future transactions are not routinely hedged. The Group continues its practice of not hedging income statement translation exposure.

The principal exchange rates affecting the Group were the Sterling to US Dollar exchange rate and the Sterling to Australian Dollar rate.

	12 months to 31 March 2016	**12 months to 31 March 2015**
£/US$ - opening	1.49	1.67
£/US$ - average	1.50	1.63
£/US$ - closing	1.44	1.49
£/A$ - opening	1.95	1.80
£/A$ - average	2.05	1.85
£/A$ - closing	1.87	1.95

Pensions

The net pension liability under IAS 19, before adjusting for deferred tax, was £37.7m (31 March 2015: £39.4m; 30 September 2015: £20.4m). The market value of the assets at 31 March 2016 was £1,410.4m (2015: £1,454.6m) and the present value of scheme liabilities was £1,448.1m (2015: £1,494.0m). The decrease in the net pension deficit is primarily driven by cash contributions into the Scheme, partially offset by a net actuarial loss arising from changes to financial assumptions.

* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary.

The key assumptions used in the IAS 19 valuation of the scheme were:

Assumption	**31 March 2016**	**31 March 2015**
Discount rate	3.4%	3.2%
CPI Inflation	2.1%	2.1%
Life expectancy - male (currently aged 40)	91	91
Life expectancy - female (currently aged 40)	93	93

Each assumption is selected by the Group in consultation with the Company actuary and takes account of industry practice amongst comparator listed companies. The sensitivity of each of the key assumptions is shown in the table below.

Assumption	Change in assumption	Indicative effect on scheme liabilities (before deferred tax)
Discount rate	Increase / decrease by 0.1%	Decrease / increase by £27.0m
Inflation	Increase / decrease by 0.1%	Increase / decrease by £25.0m
Life expectancy	Increase by 1 year	Increase by £36.0m

The latest triennial valuation of the scheme, on a funding basis, was a net surplus of £31.0m as at 30 June 2014, although if a funding valuation was carried out today the valuation could be a net deficit and may differ materially from the IAS19 accounting valuation of deficit due to the inherent methodology differences. There has been no change to the cash contributions required under the recovery plan, which continues to require £13m of company contributions per annum until 31 March 2018.

Principal risks and uncertainties

The Group continues to be exposed to a number of risks and uncertainties which management continue to assess, manage and mitigate to minimise their potential impact on the reported performance of the Group. An explanation of these risks, together with details of risk management and mitigation, can be found in the annual report which is available for download at https://www.qinetiq.com/investors/Pages/default.aspx. A summary of the significant risks and uncertainties is set out below:

- Reduction in government defence and security spending;
- Complex market characteristics including a changing regulatory environment for single source contracts;
- A material element of the Group's revenue and operating profit is derived from one customer (the UK MOD), governed by complex pricing requirements;
- A high proportion of the Group's revenue is derived from fixed price contracts that would be adversely impacted by increases in costs;
- Change in the timing of orders receipts;
- Policies or attitudes may change towards Organisational Conflicts of Interest (OCI);
- A material element of the Group's revenue and operating profit is derived from one contract;
- Losing key capability and competencies through failure to recruit and retain employees;
- Failure of information technology systems and breaches of data security;
- Inherent risks from trading in a global marketplace;
- Failure to comply with laws and regulations, particularly trading restrictions and export controls;
- Tax liabilities may change as a result of changes in tax legislation;
- Financial position of the defined benefit pension scheme.

Consolidated income statement

for the year ended 31 March

all figures in £ million	Note	**2016** Underlying	**2016** Specific adjusting items*	**2016** Total	2015 Underlying	2015 Specific adjusting items*	2015 Total
Revenue	2	**755.7**	**–**	**755.7**	763.8	–	763.8
Operating costs excluding depreciation, amortisation and impairment		**(630.5)**	**0.3**	**(630.2)**	(636.9)	1.0	(635.9)
Other income		**9.5**	**–**	**9.5**	7.6	–	7.6
EBITDA (earnings before interest, tax, depreciation and amortisation)		**134.7**	**0.3**	**135.0**	134.5	1.0	135.5
Depreciation and impairment of property, plant and equipment	3	**(23.0)**	**–**	**(23.0)**	(21.7)	–	(21.7)
Impairment of goodwill		**–**	**(31.9)**	**(31.9)**	–	–	–
Amortisation and impairment of intangible assets		**(2.8)**	**(2.0)**	**(4.8)**	(1.5)	(2.8)	(4.3)
Operating profit/(loss)		**108.9**	**(33.6)**	**75.3**	111.3	(1.8)	109.5
Gain on business divestments	6	**–**	**16.2**	**16.2**	–	–	–
Finance income	7	**1.0**	**–**	**1.0**	1.3	–	1.3
Finance expense	7	**(1.2)**	**(1.1)**	**(2.3)**	(4.8)	(0.6)	(5.4)
Profit/(loss) before tax	3	**108.7**	**(18.5)**	**90.2**	107.8	(2.4)	105.4
Taxation (expense)/income	8	**(12.8)**	**21.2**	**8.4**	(11.8)	23.8	12.0
Profit for the year from continuing operations		**95.9**	**2.7**	**98.6**	96.0	21.4	117.4
Discontinued operations							
Profit/(loss) before tax – discontinued operations		**–**	**7.5**	**7.5**	1.2	(13.7)	(12.5)
Tax in respect of discontinued operations		**–**	**–**	**–**	(0.5)	0.3	(0.2)
Profit/(loss) for the year from discontinued operations		**–**	**7.5**	**7.5**	0.7	(13.4)	(12.7)
Profit for the year attributable to equity shareholders		**95.9**	**10.2**	**106.1**	96.7	8.0	104.7
Earnings per share							
Basic – continuing operations	10	**16.3p**		**16.8p**	15.2p		18.6p
Basic – total Group	10	**16.3p**		**18.1p**	15.3p		16.6p
Diluted – continuing operations	10	**16.2p**		**16.7p**	15.1p		18.5p
Diluted – total Group	10	**16.2p**		**18.0p**	15.2p		16.5p

* For details of 'specific adjusting items' refer to note 3.

Consolidated statement of comprehensive income

for the year ended 31 March

all figures in £ million	2016	2015
Profit for the year	**106.1**	104.7
Items that will not be reclassified to profit or loss:		
Actuarial loss recognised in defined benefit pension schemes	**(10.6)**	(24.5)
Tax on items that will not be reclassified to profit and loss	**2.1**	5.1
Total items that will not be reclassified to profit or loss	**(8.5)**	(19.4)
Items that may be reclassified to profit or loss:		
Foreign currency translation differences for foreign operations	**3.2**	11.0
Recycling of currency translation differences to the income statement on disposal of foreign subsidiary	**1.7**	(40.9)
Decrease in fair value of hedging derivatives	**(0.1)**	(0.1)
Reclassification of hedging derivatives to the income statement	**–**	0.1
Fair value (losses)/gains on available-for-sale investments	**(0.6)**	0.2
Total items that may be reclassified to profit or loss	**4.2**	(29.7)
Other comprehensive expense for the year, net of tax	**(4.3)**	(49.1)
Total comprehensive income for the year	**101.8**	55.6

Consolidated statement of changes in equity

for the year ended 31 March

all figures in £ million	Issued share capital	Capital redemption reserve	Share premium	Hedge reserve	Translation reserve	Retained earnings	Total	Non-controlling interest	Total equity
At 1 April 2015	**6.1**	**40.4**	**147.6**	**0.1**	**(6.8)**	**110.6**	**298.0**	**0.1**	**298.1**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**106.1**	**106.1**	**0.1**	**106.2**
Other comprehensive income/ (expense) for the year, net of tax	**–**	**–**	**–**	**(0.1)**	**4.9**	**(9.1)**	**(4.3)**	**–**	**(4.3)**
Purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(0.7)**	**(0.7)**	**–**	**(0.7)**
Purchase and cancellation of shares	**(0.2)**	**0.2**	**–**	**–**	**–**	**(46.9)**	**(46.9)**	**–**	**(46.9)**
Share-based payments	**–**	**–**	**–**	**–**	**–**	**4.7**	**4.7**	**–**	**4.7**
Dividends	**–**	**–**	**–**	**–**	**–**	**(32.3)**	**(32.3)**	**–**	**(32.3)**
At 31 March 2016	**5.9**	**40.6**	**147.6**	**–**	**(1.9)**	**132.4**	**324.6**	**0.2**	**324.8**
At 1 April 2014	6.6	39.9	147.6	0.1	23.1	160.7	378.0	0.1	378.1
Profit for the year	–	–	–	–	–	104.7	104.7	–	104.7
Other comprehensive expense for the year, net of tax	–	–	–	–	(29.9)	(19.2)	(49.1)	–	(49.1)
Purchase of own shares	–	–	–	–	–	(0.6)	(0.6)	–	(0.6)
Share-based payments settlement	–	–	–	–	–	0.6	0.6	–	0.6
Purchase and cancellation of shares	(0.5)	0.5	–	–	–	(107.1)	(107.1)	–	(107.1)
Share-based payments	–	–	–	–	–	3.2	3.2	–	3.2
Dividends	–	–	–	–	–	(31.7)	(31.7)	–	(31.7)
At 31 March 2015	6.1	40.4	147.6	0.1	(6.8)	110.6	298.0	0.1	298.1

Consolidated balance sheet

as at 31 March

all figures in £ million	Note	2016	2015
Non-current assets			
Goodwill	11	**73.1**	107.2
Intangible assets		**8.3**	15.3
Property, plant and equipment		**233.4**	229.6
Other financial assets		**0.6**	0.9
Investments		**0.9**	0.4
Deferred tax		**4.1**	12.9
		320.4	366.3
Current assets			
Inventories		**19.0**	18.5
Other financial assets		**10.8**	12.3
Trade and other receivables		**156.2**	159.2
Investments		**1.7**	2.3
Cash and cash equivalents		**263.5**	184.3
		451.2	376.6
Total assets		**771.6**	742.9
Current liabilities			
Trade and other payables		**(338.7)**	(352.3)
Current tax		**(39.9)**	(15.3)
Provisions		**(5.3)**	(3.0)
Other financial liabilities		**(0.2)**	(1.9)
		(384.1)	(372.5)
Non-current liabilities			
Retirement benefit obligation	13	**(37.7)**	(39.4)
Provisions		**(13.8)**	(22.4)
Other financial liabilities		**(0.2)**	(0.1)
Other payables		**(11.0)**	(10.4)
		(62.7)	(72.3)
Total liabilities		**(446.8)**	(444.8)
Net assets		**324.8**	298.1
Capital and reserves			
Ordinary shares		**5.9**	6.1
Capital redemption reserve		**40.6**	40.4
Share premium account		**147.6**	147.6
Hedging and translation reserve		**(1.9)**	(6.7)
Retained earnings		**132.4**	110.6
Capital and reserves attributable to shareholders of the parent company		**324.6**	298.0
Non-controlling interest		**0.2**	0.1
Total shareholders' funds		**324.8**	298.1

Consolidated cash flow statement

for the year ended 31 March

all figures in £ million	Note	**2016**	2015
Net cash inflow from continuing operations before cash flows in respect of specific adjusting items		**133.4**	143.9
Net cash outflow relating to restructuring		–	(0.6)
Disposal-related pension contribution		–	(6.0)
Cash generated from discontinued operations		–	1.8
Cash inflow from operations		**133.4**	139.1
Tax received		**27.9**	8.8
Interest received		**0.9**	1.0
Interest paid		**(0.6)**	(36.4)
Net cash inflow from operating activities		**161.6**	112.5
Purchases of intangible assets		**(1.6)**	(4.2)
Purchases of property, plant and equipment		**(28.6)**	(24.8)
Proceeds from sale of property, plant and equipment		**0.4**	–
Investment in available for sale investments		–	(10.0)
Acquisition of business		**(0.6)**	(3.7)
Sale of investment in subsidiary		**28.0**	79.6
Net cash (outflow)/inflow from investing activities		**(2.4)**	36.9
Repayment of bank borrowings		–	(147.1)
Payment of bank loan arrangement fee		–	(1.3)
Purchase of own shares		**(48.6)**	(106.8)
Dividends paid to shareholders		**(32.3)**	(31.7)
Capital element of finance lease rental payments		**(1.4)**	(2.8)
Capital element of finance lease rental receipts		**1.5**	3.0
Net cash outflow from financing activities		**(80.8)**	(286.7)
Increase/(decrease) in cash and cash equivalents		**78.4**	(137.3)
Effect of foreign exchange changes on cash and cash equivalents		**0.8**	0.4
Cash and cash equivalents at beginning of year		**184.3**	322.2
Cash and cash equivalents disposed		–	(1.0)
Cash and cash equivalents at end of year	12	**263.5**	184.3

Reconciliation of movement in net cash

for the year ended 31 March

all figures in £ million	Note	**2016**	2015
Increase/(decrease) in cash and cash equivalents in the year		**78.4**	(137.3)
Add back net cash flows not impacting net cash - repayment of bank loans and fees		–	148.4
Add back net cash flows not impacting net cash - investments		–	10.0
Add back net cash flows not impacting net cash - other		**(0.1)**	(0.2)
Change in net cash resulting from cash flows		**78.3**	20.9
Cash and cash equivalents disposed		–	(1.0)
Other movements including foreign exchange		**0.7**	5.1
Movement in net cash in the year		**79.0**	25.0
Net cash at beginning of year		**195.5**	170.5
Net cash at end of year	12	**274.5**	195.5

1. Significant accounting policies

Accounting policies

The following accounting policies have been applied consistently to all periods presented in dealing with items that are considered material in relation to the Group's financial statements. In the income statement, the Group presents specific adjusting items separately. In the judgement of the Directors, for the reader to obtain a proper understanding of the financial information, specific adjusting items need to be disclosed separately because of their size and nature.

Specific adjusting items include:

- amortisation of intangible assets arising from acquisitions;
- pension net finance expense;
- gains/losses on business divestments and disposal of property and investments;
- impairment of goodwill and other intangible assets;
- one-off recovery of research and development tax credits and associated write-off of deferred tax asset in respect of tax losses; and
- significant non-recurring deferred tax movements.

Basis of preparation

The financial information in this preliminary announcement has been extracted from the Group's consolidated financial statements for the year ended 31 March 2016. The Group's financial statements have been prepared on a going concern basis and in accordance with International Financial Reporting Standards as adopted by the EU ('IFRS') and the Companies Act 2006 applicable to companies reporting under IFRS.

The financial information included within the preliminary announcement has been prepared using accounting policies consistent with International Financial Reporting Standards (IFRSs) as endorsed by the European Union. The accounting policies followed are the same as those published by the Group within its Annual Report for the year ended 31 March 2016 which is available on the Group's website, www.QinetiQ.com subject to the changes noted below. The preliminary announcement was approved by the Board of Directors on 26 May 2016. The financial information in this preliminary announcement does not constitute the statutory accounts of QinetiQ Group plc ('the Company') within the meaning of section 435 of the Act.

The statutory accounts for 2016 were approved by the Board of Directors on 26 May 2016 and will be delivered to the Registrar of Companies following the Company's Annual General Meeting on 20 July 2016. The financial information for 2015 is derived from the statutory accounts for 2015 which have been delivered to the Registrar of Companies. The auditors have reported on the 2016 and 2015 accounts. The reports were (i) unqualified; (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report; and (iii) did not contain a statement under section 498 (2) or (3) of the Companies Act 2006.

Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiary undertakings to 31 March 2016. The purchase method of accounting has been adopted. Those subsidiary undertakings acquired or disposed of in the period are included in the consolidated income statement from the date control is obtained to the date that control is lost (usually on acquisition and disposal respectively). An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. This is the IFRS 10 definition of "control".

The Group comprises certain entities that are operated under the management of a Proxy Board. Details of the Proxy Board arrangements and the powers of the proxy holders and QinetiQ management are set out in the Corporate Governance section of the Annual Report. IFRS 10 is the accounting standard now applicable in respect of consolidation of entities. This does not specifically deal with proxy situations. However, having considered the terms of the proxy agreement, the Directors consider that the Group meets the requirements of IFRS 10 in respect of control over such affected entities and, therefore, consolidates these entities in the consolidated accounts.

An associate is an undertaking over which the Group exercises significant influence, usually from 20%-50% of the equity voting rights, in respect of financial and operating policy. A joint venture is an undertaking over which the Group exercises joint control. Associates and joint ventures are accounted for using the equity method from the date of acquisition to the date of disposal. The Group's investments in associates and joint ventures are held at cost including goodwill on acquisition and any post-acquisition changes in the Group's share of the net assets of the associate less any impairment to the recoverable amount. Where an associate or joint venture has net liabilities, full provision is made for the Group's share of liabilities where there is a constructive or legal obligation to provide additional funding to the associate or joint venture.

The financial statements of subsidiaries, joint ventures and associates are adjusted where necessary to ensure compliance with Group accounting policies.

On consolidation, all intra-Group income, expenses and balances are eliminated.

Recent accounting developments

Developments adopted by the Group in 2016

The following UK GAAP and EU-endorsed Standards and amendments, improvements and interpretations of published standards are effective for accounting periods beginning on or after 1 January 2015 and have been adopted with no material impact on the Group's financial statements:

FRS 100, 101 and 102
FRS 100, 101 and 102 all fall under the new UK GAAP regime. FRS 100 sets out the application of financial reporting requirements in the UK and Republic of Ireland and FRS 101, known as 'IFRS with reduced disclosures' outlines the reduced disclosure framework available for use by qualifying entities choosing to follow the principles of IFRS but under the umbrella of UK GAAP. FRS 102 is applicable in the UK and Republic of Ireland and is known as the 'new UK GAAP'. FRS 102 follows more closely the principles of existing UK GAAP with some exceptions. The mandatory effective date for the new framework of reporting is for accounting periods beginning on or after 1 January 2015. QinetiQ had the choice between applying either full IFRS, or a choice of either FRS 101, or FRS 102 to its subsidiary entities. The two latter options both fall under UK GAAP and either may therefore be applied to subsidiary entities on an entity by entity basis. The Group has adopted the UK GAAP option as of 1 April 2015.

IAS 19 Employee Benefits – amendment to clarify requirement that relate to how contributions from employees or third parties that are linked to service should be attributed to periods of service.

Annual improvement 2010-2012 cycle:
IFRS 2 Share-based Payment – amendment to the definitions of 'vesting condition' and 'market condition' and adds definitions for 'performance condition' and 'service condition'.
IFRS 3 Business Combinations – amendment to clarify that contingent consideration that is classified as an asset or liability shall be measured at fair value at each reporting date.
IFRS 8 Operating Segments – two amendments relating to disclosure requirements on application of aggregation criteria and reconciliation of assets.
IFRS 13 Fair Value Measurement – amendment related to short-term receivables and payables with no stated interest rate.
IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets – amendment clarifying that under the revaluation method, accumulated depreciation should be restated on a proportionate basis.
IFRS 24 Related Party Disclosures – clarification that an entity providing key management personnel services to the reporting entity or to the parent of the reporting entity is a related party of reporting entity.

Annual improvement 2011-2013 cycle:
IFRS 1 First-time Adoption of IFRS - amendment relating to first-time application of IFRS.
IFRS 3 Business Combinations – amendment clarifying that IFRS 3 excludes from its scope the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself.
IAS 40 Investment Property – amendment clarifying the interrelationship of IFRS 3 and IAS 40 when classifying property as investment property or owner-occupied property.

Developments expected in future periods of which the impact is being assessed
IFRS 15 Revenue from Contracts with Customers: The final Standard was published in May 2014 and the IASB has taken the decision to defer the effective date of IFRS 15 to 1 January 2018 i.e. FY19 for QinetiQ. The new Standard introduces a five-step model to the principle of revenue recognition. Briefly, the framework includes identifying the contract with the customer, identifying the performance obligations in the contract, determining the transaction price, allocating the transaction price to the performance obligations in the contract and recognising revenue when (or as) the entity satisfies a performance obligation. QinetiQ is currently undertaking an assessment of the impact of the new standard. Typical issues to be analysed on a contract-by-contract basis include whether the current methodology for recognising revenue over time remains appropriate, the treatment of contract modifications, variable consideration, determination and distinction of performance obligations, collectability and licences (list not exhaustive). QinetiQ is also undertaking an analysis of the transitional guidance which allows for two different approaches; the retrospective method (with optional practical expedients) or the cumulative effect method. Under the retrospective method, QinetiQ would need to restate prior year comparatives and recognise the cumulative effect of applying the new standard in equity at the start of the earliest presented comparative period. Under the cumulative method, QinetiQ would apply the new standard as of the date of initial application, with no restatement of comparative period amounts. It would record the cumulative effect of initially applying the new standard – which would affect revenue and costs – as an adjustment to the opening balance of equity at the date of initial application. Under the cumulative effect method, the provisions of the new standard apply only to contracts that are open (i.e. not complete) under previous GAAP at the date of initial application.

IFRS 16 Leases: The final Standard was published in January 2016. Under the new Standard, companies will recognise new assets and liabilities, bringing added transparency to the balance sheet. IFRS 16 eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Instead, there is a single, on-balance sheet accounting model that is similar to current finance lease accounting. Lessor accounting remains similar to current practice – i.e. lessors continue to classify leases as finance and operating leases. The Standard will be effective from 1 January 2019 i.e. FY20 for QinetiQ subject to EU endorsement.

IFRS 9 Financial Instruments: This new Standard on accounting for financial instruments will replace IAS 39 Financial Instruments: Recognition and Measurement. This Standard has not yet been endorsed by the EU. It is expected to come into effect for accounting periods beginning on or after 1 January 2018.

Developments expected in future periods with no material impact on the Group's financial statements
The Directors anticipate that the adoption of the following new, revised, amended and improved published standards and interpretations, which were in issue at the date of authorisation of these financial statements, will have no material impact on the financial statements of the Group when they become applicable in future periods:

- IFRS 14 'Regulatory Deferral Accounts';
- Amendments to IFRS 9, 10 and 11; and
- Amendments to IAS 1, 7, 9, 12, 15, 27, 36 and 38.

2. Segmental analysis

Operating segments
For the year ended 31 March

all figures in £ million	Note	**2016**		2015	
		Revenue	**Operating profit**	Revenue	Operating profit
EMEA Services		**616.4**	**93.8**	625.6	93.0
Global Products		**139.3**	**15.1**	138.2	18.3
Total operating segments		**755.7**	**108.9**	763.8	111.3
Operating profit before specific adjusting items[1] – underlying operating profit			**108.9**		111.3
Specific adjusting items:					
Restructuring			–		1.0
Profit on disposal of property			**0.3**		–
Impairment of goodwill			**(31.9)**		–
Amortisation of intangible assets arising from acquisitions			**(2.0)**		(2.8)
Operating profit			**75.3**		109.5
Gain on business divestments	6		**16.2**		–
Net finance expense	7		**(1.3)**		(4.1)
Profit before tax			**90.2**		105.4
Taxation income	8		**8.4**		12.0
Profit for the year from continuing operations			**98.6**		117.4
Discontinued operations					
Profit/(loss) from discontinued operations, net of tax	4		**7.5**		(12.7)
Profit for the period attributable to equity shareholders			**106.1**		104.7

[1] The measure of profit presented to the chief operating decision maker is underlying operating profit (as defined in glossary).

3. Profit before tax

The following items have been charged in arriving at profit before tax for continuing operations:

all figures in £ million	2016	2015
Depreciation of property, plant and equipment:		
Owned assets: depreciation	**(23.4)**	(20.7)
Owned assets: impairment reversal/(charge)	**0.4**	(1.0)
Foreign exchange gain/(loss)	**0.2**	(0.3)
Research and development expenditure – customer funded contracts	**(277.6)**	(285.8)
Research and development expenditure – Group funded	**(23.2)**	(20.8)

Specific adjusting items

In the income statement, the Group presents specific adjusting items separately. In the judgement of the Directors, for the reader to obtain a proper understanding of the financial information, specific adjusting items need to be disclosed separately because of their size and nature. Underlying measures of performance exclude specific adjusting items. The following specific adjusting items have been (charged)/credited in arriving at profit before tax:

all figures in £ million		2016	2015
Profit on disposal of property		**0.3**	–
Reversal of unutilised restructuring provisions		**–**	1.0
Specific adjusting items before amortisation, depreciation and impairment		**0.3**	1.0
Impairment of goodwill		**(31.9)**	–
Amortisation of intangible assets arising from acquisition		**(2.0)**	(2.8)
Specific adjusting items operating loss		**(33.6)**	(1.8)
Gain on business divestments	6	**16.2**	–
Defined benefit pension scheme net finance expense		**(1.1)**	(0.6)
Specific adjusting items loss before tax – continuing operations		**(18.5)**	(2.4)
Profit on disposal of subsidiary – before accelerated interest expense	4	**7.5**	15.9
Loss on disposal of subsidiary – accelerated interest expense	4	**–**	(28.8)
Profit/(loss) on disposal of subsidiary	4	**7.5**	(12.9)
Amortisation of intangible assets arising from acquisition		**–**	(0.8)
Specific adjusting items profit/(loss) before tax – discontinued operations		**7.5**	(13.7)
Total specific adjusting items loss before tax		**(11.0)**	(16.1)
Specific adjusting items – tax (continuing operations)	8	**21.2**	23.8
Specific adjusting items – tax (discontinued operations)		**–**	0.3
Total specific adjusting items profit after tax		**10.2**	8.0

Reconciliation of underlying profit for the year to total profit for the year

all figures in £ million	2016	2015
Underlying profit after tax – total Group	**95.9**	96.7
Total specific adjusting items profit after tax (see above)	**10.2**	8.0
Total profit for the year attributable to equity shareholders	**106.1**	104.7

4. Discontinued operations

In the prior year, on 23 May 2014, the Group completed its sale of the US Services division, comprising QinetiQ North America Inc. and its subsidiaries. The Circular seeking shareholder approval for the sale of the US Services division specified that the proceeds would be applied in settling the remaining private placement ('PP') debt of $248m which was put in place to finance the acquisitions of the US Services business. Accordingly, the penalty of £28.8m incurred on the early redemption of the PP is considered to be inextricably linked to the sale of that business and was, therefore, disclosed as an adjustment to the loss on its sale rather than as a finance expense.

Net cash inflow in respect of this transaction was £78.6m in the year to 31 March 2015, with a further £28.8m outflow in respect of the associated PP early redemption expense. Additional deferred consideration, the earn-out, was payable on a sliding scale between zero and $50m based on gross profit generated by the disposed business in the financial year to 31 March 2015. Actual gross profit delivered by the disposed business resulted in deferred consideration of £6.2m (in line with expectations and matching the prior year book value of deferred consideration receivable) becoming due, which was paid in full in the year to 31 March 2016.

In the current year an income statement impact of this transaction occurred from the release of opening warranty and indemnity liabilities following expiry of the contractual warranty clauses and an assessed remote possibility of claims under the extant indemnity clauses of the sale agreement.

a) Results of discontinued operations

all figures in £ million	**2016**	2015
Revenue	–	55.7
Operating costs excluding depreciation, amortisation and impairment	–	(54.2)
EBITDA (earnings before interest, tax, depreciation and amortisation)	–	1.5
Depreciation, amortisation and impairment of assets	–	(0.3)
Underlying operating profit	–	1.2
Amortisation of intangible assets arising from acquisitions	–	(0.8)
Operating profit	–	0.4
Finance expense	–	–
Profit before tax	–	0.4
Taxation expense	–	(0.2)
Results from operating activities, net of tax	–	0.2
Profit on sale of discontinued operations – before accelerated interest costs	**7.5**	15.9
Loss on sale of discontinued operations – accelerated interest costs	–	(28.8)
Profit/(loss) for the period	**7.5**	(12.7)
Basic gain/(loss) per share	**1.3p**	(2.0)p
Diluted gain/(loss) per share	**1.3p**	(2.0)p

b) Cash flows from discontinued operations

all figures in £ million	**2016**	2015
Net cash from operating activities	–	1.8
Net cash inflow for the year from the disposed entity	–	1.8
Cash outflow in respect of accelerated interest expense – included within 'Interest paid'	–	(28.8)
Net cash outflow related to discontinued operations	–	(27.0)

c) Effect of disposal on the financial position of the Group

all figures in £ million	**2016**	2015
Consideration received (net of transaction costs), satisfied in cash	**6.2**	79.6
Cash and cash equivalents disposed	–	(1.0)
Net cash inflow in the year	**6.2**	78.6

5. Business combinations

The Group made two acquisitions in the prior year to 31 March 2015: SR2020 and Redfern Integrated Optics Inc. Consideration (of £0.4m) for the acquisition of SR2020 was paid in full in the prior year and no further payments, or adjustments to the assets acquired, were made in the year to 31 March 2016. The total consideration for the acquisition of Redfern Integrated Optics Inc. was £3.9m, of which £3.3m was paid in the prior year. The remaining consideration of £0.6m was paid in the current year.

6. Gain on business divestments – continuing operations

For the year ended 31 March

all figures in £ million	**2016**	2015
Gain on business divestments	**16.2**	–

The gain on business divestments relates to the sale of the Cyveillance business on 11 December 2015 for consideration before costs of $34.1m and a gain on disposal of £16.2m. There is no deferred consideration receivable.

7. Finance income and expense – continuing operations

For the year ended 31 March

all figures in £ million	**2016**	2015
Receivable on bank deposits	**1.0**	1.1
Finance lease income	**–**	0.2
Finance income	**1.0**	1.3
Amortisation of recapitalisation fee	**(0.3)**	(0.7)
Payable on bank loans and overdrafts	**(0.6)**	(0.9)
Payable on US Dollar private placement debt	**–**	(2.6)
Finance lease expense	**–**	(0.2)
Unwinding of discount on financial liabilities	**(0.3)**	(0.4)
Finance expense before specific adjusting items	**(1.2)**	(4.8)
Specific adjusting items:		
Defined benefit pension scheme net finance expense	**(1.1)**	(0.6)
Total finance expense	**(2.3)**	(5.4)
Net finance expense	**(1.3)**	(4.1)

8. Taxation – continuing operations

all figures in £ million	2016 Underlying*	2016 Specific adjusting items*	2016 Total	2015 Underlying*	2015 Specific adjusting items*	2015 Total
Analysis of charge						
Current UK tax expense/(income)	**2.2**	**(35.6)**	**(33.4)**	0.5	–	0.5
Overseas corporation tax						
Current year	**2.4**	–	**2.4**	1.4	(0.5)	0.9
Adjustment for prior year	–	–	–	(1.0)	0.6	(0.4)
Current tax expense/(income)	**4.6**	**(35.6)**	**(31.0)**	0.9	0.1	1.0
Deferred tax expense/(income)	**7.7**	**20.0**	**27.7**	11.3	(22.9)	(11.6)
Deferred tax impact of change in rates	**(0.2)**	–	**(0.2)**	(0.4)	–	(0.4)
Deferred tax in respect of prior years	**0.7**	**(5.6)**	**(4.9)**	–	(1.0)	(1.0)
Deferred tax expense/(income)	**8.2**	**14.4**	**22.6**	10.9	(23.9)	(13.0)
Taxation expense/(income) – continuing operations	**12.8**	**(21.2)**	**(8.4)**	11.8	(23.8)	(12.0)
Factors affecting tax charge/(credit) in year						
Principal factors reducing the Group's current year tax charge below the UK statutory rate are explained below:						
Profit/(loss) before tax	**108.7**	**(18.5)**	**90.2**	107.8	(2.4)	105.4
Tax on profit/(loss) before tax at 20% (2015: 21%)	**21.7**	**(3.7)**	**18.0**	22.6	(0.5)	22.1
Effect of:						
Expenses not deductible for tax purposes and non-taxable items	**3.7**	**4.5**	**8.2**	(7.9)	1.7	(6.2)
Research and development credits/reliefs	**(13.7)**	**(36.8)**	**(50.5)**	(10.7)	–	(10.7)
Tax in respect of an FY09 US acquisition – payable to the tax authorities	**16.2**	–	**16.2**	–	–	–
Tax in respect of an FY09 US acquisition – recoverable from insurers	**(16.2)**	–	**(16.2)**	–	–	–
Utilisation/(recognition) of deferred tax asset in respect of UK trading losses	–	**25.2**	**25.2**	–	(25.2)	(25.2)
Current tax losses for which no deferred tax asset was recognised	–	–	–	6.9	–	6.9
Deferred tax impact of change in rates	**(0.2)**	–	**(0.2)**	(0.4)	–	(0.4)
Deferred tax in respect of prior years	**0.7**	**(5.6)**	**(4.9)**	0.9	–	0.9
Other deferred tax movements	–	**(4.8)**	**(4.8)**	–	–	–
Effect of different rates in overseas jurisdictions	**0.6**	–	**0.6**	0.4	0.2	0.6
Taxation expense/(income) - continuing operations	**12.8**	**(21.2)**	**(8.4)**	11.8	(23.8)	(12.0)
Effective tax rate	**11.8%**		**(9.3%)**	10.9%		(11.4%)

* Definitions of underlying measures of performance and specific adjusting items can be found in the glossary.

UK Group companies have now elected to obtain tax benefits in respect of allowable R&D expenditure through the R&D Expenditure Credit ('RDEC') process rather than through the previous treatment as a super-deduction in the tax computations. This election was made retrospectively back to 1 April 2013 and the incremental impact on the tax expense for the years ending 31 March 2014 and 31 March 2015 has been reported in the current year as a specific adjusting item. The change of regime results in the utilisation of previously capitalised UK trading losses and the associated deferred tax asset has been written off in the current year, also reported as a specific adjusting item. Other deferred tax movements include the effect of changes in estimates in respect of the apportionment of book values between qualifying and non-qualifying property, plant and equipment.

Deferred tax has been calculated using the enacted future statutory tax rates.

At 31 March 2016 the Group had unused tax losses of £154.8m (2015: £291.6m) which are available for offset against future profits. £26.1m of these losses are time limited of which £6.3m will expire in 2034 and £19.8m will expire in 2035. Certain UK tax losses had been recognised on the balance sheet as at 31 March 2015 as a deferred tax asset of £25.2m. As noted above those tax losses have now been utilised following the election into the RDEC regime. No deferred tax asset is recognised in respect of the remaining tax losses due to uncertainty over the timing and extent of their utilisation.

Factors affecting future tax charges

The effective tax rate continues to be below the UK statutory rate, primarily as a result of the benefit of research and development tax relief in the UK. The effective tax rate is expected to remain below the UK statutory rate in the medium term, subject to the impact of any tax legislation changes, the geographic mix of profits and the assumption that the benefit of net R&D tax relief retained by the Group remains in the tax line. Future recognition of unrecognised tax losses will also affect future tax charges.

9. Dividends

An analysis of the dividends paid and proposed in respect of the years ended 31 March 2016 and 2015 is provided below:

	Pence per share	£m	Date paid/ payable
Interim 2016	**1.9**	**11.1**	**Feb 2016**
Final 2016 (proposed)	**3.8**	**21.6**	**Sept 2016**
Total for the year ended 31 March 2016	**5.7**	**32.7**	
Interim 2015	1.8	11.1	Feb 2015
Final 2015	3.6	21.2	Sept 2015
Total for the year ended 31 March 2015	5.4	32.3	

The Directors propose a final dividend of 3.8p (2015: 3.6p) per share. The dividend, which is subject to shareholder approval, will be paid on 2 September 2016. The ex-dividend date is 4 August 2016 and the record date is 5 August 2016.

10. Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to equity shareholders by the weighted average number of ordinary shares in issue during the year. The weighted average number of shares used excludes those shares bought by the Group and held as own shares. For diluted earnings per share the weighted average number of shares in issue is adjusted to assume conversion of all potentially dilutive ordinary shares arising from unvested share-based awards including share options.

For the year ended 31 March		2016	2015
Weighted average number of shares	Million	**587.0**	630.9
Effect of dilutive securities	Million	**3.7**	3.7
Diluted number of shares	Million	**590.7**	634.6

Underlying basic earnings per share figures are presented below, in addition to the basic and diluted earnings per share, because the Directors consider this gives a more relevant indication of underlying business performance and reflects the adjustments to basic earnings per share for the impact of specific adjusting items (see note 3) and tax thereon.

Underlying EPS – continuing operations

For the year ended 31 March		2016	2015
Profit attributable to equity shareholders	£ million	**98.6**	117.4
Remove loss after tax in respect of specific adjusting items*	£ million	**(2.7)**	(21.4)
Underlying profit after taxation	**£ million**	**95.9**	96.0
Weighted average number of shares	Million	**587.0**	630.9
Underlying basic EPS – continuing operations	**Pence**	**16.3**	15.2
Diluted number of shares	Million	**590.7**	634.6
Underlying diluted EPS – continuing operations	**Pence**	**16.2**	15.1

Underlying EPS – total Group

For the year ended 31 March		2016	2015
Profit attributable to equity shareholders	£ million	**106.1**	104.7
Remove loss after tax in respect of specific adjusting items*	£ million	**(10.2)**	(8.0)
Underlying profit after taxation	**£ million**	**95.9**	96.7
Weighted average number of shares	Million	**587.0**	630.9
Underlying basic EPS – total Group	**Pence**	**16.3**	15.3
Diluted number of shares	Million	**590.7**	634.6
Underlying diluted EPS – continuing operations	**Pence**	**16.2**	15.2

Basic and diluted EPS – continuing operations

For the year ended 31 March		**2016**	2015
Profit attributable to equity shareholders	£ million	**98.6**	117.4
Weighted average number of shares	Million	**587.0**	630.9
Basic EPS – continuing operations	**Pence**	**16.8**	18.6
Diluted number of shares	Million	**590.7**	634.6
Diluted EPS – continuing operations	**Pence**	**16.7**	18.5

Basic and diluted EPS – total Group

For the year ended 31 March		**2016**	2015
Profit attributable to equity shareholders	£ million	**106.1**	104.7
Weighted average number of shares	Million	**587.0**	630.9
Basic EPS – total Group	**Pence**	**18.1**	16.6
Diluted number of shares	Million	**590.7**	634.6
Diluted EPS – total Group	**Pence**	**18.0**	16.5

* For details of 'specific adjusting items' refer to note 3.

11. Goodwill

all figures in £ million	**2016**	2015
Cost		
At 1 April	**183.3**	541.4
Acquisitions	–	0.1
Disposals	**(16.2)**	(370.1)
Foreign exchange	**4.4**	11.9
At 31 March	**171.5**	183.3
Impairment		
At 1 April	**(76.1)**	(400.1)
Disposals	**11.0**	328.9
Impairment	**(31.9)**	–
Foreign exchange	**(1.4)**	(4.9)
At 31 March	**(98.4)**	(76.1)
Net book value at 31 March	**73.1**	107.2

Goodwill as at 31 March 2016 was allocated across various cash generating units (CGUs) in the following segments: EMEA Services (two) and Global Products (two). Goodwill previously allocated to an EMEA Services CGU (the Cyveillance business) of £5.2m was written off in the year on disposal of that CGU.

Goodwill is attributable to the excess of consideration over the fair value of net assets acquired and includes expected synergies, future growth prospects and employee knowledge, expertise and security clearances. The Group tests each CGU for impairment annually, or more frequently if there are indications that goodwill might be impaired.

Impairment testing is dependent on management's estimates and judgments, particularly as they relate to the forecasting of future cash flows, the discount rates selected and expected long-term growth rates. Significant headroom exists in all CGUs with the exception of US Global Products, discussed below, and management considers that there are no likely variations in the key assumptions which would lead to an impairment being recognised in any of the other CGUs.

Key assumptions

Cash flows

The value-in-use calculations generally use discounted future cash flows based on financial plans approved by the Board covering a two-year period. Discounted cash flows for the US Global Products CGU were based on a Board-approved three-year plan, reflecting increases in revenue from new product lines. Cash flows for periods beyond these periods are extrapolated based on the last year of the plans, with a terminal growth-rate assumption applied.

Terminal growth rates

The specific plans for each of the CGUs have been extrapolated using a terminal growth rate of 2.0% – 2.4% (2015: 2.0% – 3.0%). The US Global Products terminal growth rate was 2.4% (2015: 3.0%). Growth rates are based on management's estimates which take into consideration the long-term nature of the industry in which the CGUs operate and external forecasts as to the likely growth of the industry in the longer term.

Discount rates

The Group's weighted average cost of capital was used as a basis in determining the discount rate to be applied, adjusted for risks specific to the market characteristics of CGUs as appropriate on a pre-tax basis. This is considered to appropriately estimate a market participant discount rate. The pre-tax discount rates applied for the two EMEA Services CGUs were 11.7% and 14.7%, for the UK Global Products CGU was 11.7% and for the US Global Products CGU was 11.3%.

Sensitivity analysis shows that the value of the terminal year cash flow, the discount rate and the terminal growth rates have a significant impact on the value of the discounted cash flow.

Significant CGUs

US Global Products

The carrying value of the goodwill for the US Global Products CGU as at 31 March 2016 was £37.9m (2015: £67.2m). The decrease results from an impairment of £31.9m in the year following a reduction in the value in use, calculated using the assumptions noted above. The impairment is primarily due to the combined impact of changes to the discount rate and terminal growth rate. Sensitivity analysis has been undertaken to assess the impact of changes to the key assumptions. Applying a sensitivity to remove new product growth would increase the impairment by £4.5m. Alternatively, increasing the discount rate by 1% would increase the impairment by £6.0m and reducing the terminal growth rate by 1% would increase the impairment by £5.3m. The carrying value of net operating assets as at 31 March 2016 was £82.8m.

Other CGUs

The UK Global Products CGU and the two individual CGUs within EMEA Services all have significant headroom. An increase in the discount rate or a decrease in the terminal growth rate by 1% would not cause the net operating assets to exceed their recoverable amount. The carrying value of goodwill for the UK Global Products CGU as at 31 March 2016 was £5.5m (2015: £5.2m). The carrying values of goodwill for the two EMEA Services CGUs as at 31 March 2016 were £27.5m and £2.2m (2015: £27.5m and £2.1m). The Directors have not identified any other likely changes in other significant assumptions between 31 March 2016 and the signing of the financial statements that would cause the carrying value of the recognised goodwill to exceed its recoverable amount.

12. Net cash

As at 31 March

	2016			2015		
all figures in £ million	**Assets**	**Liabilities**	**Net**	Assets	Liabilities	Net
Current financial assets/(liabilities)						
Deferred financing costs	**0.3**	**–**	**0.3**	0.3	–	0.3
Borrowings	**0.3**	**–**	**0.3**	0.3	–	0.3
Available for sale investment	**9.9**	**–**	**9.9**	10.0	–	10.0
Derivative financial instruments	**0.6**	**(0.2)**	**0.4**	0.5	(0.5)	–
Finance lease debtor/(creditor)	**–**	**–**	**–**	1.5	(1.4)	0.1
Total current financial assets/(liabilities)	**10.8**	**(0.2)**	**10.6**	12.3	(1.9)	10.4
Non-current assets/(liabilities)						
Deferred financing costs	**0.5**	**–**	**0.5**	0.8	–	0.8
Borrowings	**0.5**	**–**	**0.5**	0.8	–	0.8
Derivative financial instruments	**0.1**	**(0.2)**	**(0.1)**	0.1	(0.1)	–
Total non-current financial assets/(liabilities)	**0.6**	**(0.2)**	**0.4**	0.9	(0.1)	0.8
Cash	**68.4**	**–**	**68.4**	41.6	–	41.6
Cash equivalents	**195.1**	**–**	**195.1**	142.7	–	142.7
Total cash and cash equivalents	**263.5**	**–**	**263.5**	184.3	–	184.3
Total net cash as defined by the Group			**274.5**			195.5

At 31 March 2016 £1.6m (2015: £1.3m) of cash was held by the Group's captive insurance subsidiary, including £0.1m (2015: £0.1m) that was restricted in its use.

Reconciliation of net cash flow to movement in net cash

all figures in £ million	2016	2015
Increase/(decrease) in cash and cash equivalents in the year	**78.4**	(137.3)
Repayment of US$ private placement notes	–	147.1
Outflow in respect of purchase of available for sale investment	–	10.0
Payment of bank loan arrangement fee	–	1.3
Capital element of finance lease payments	**1.4**	2.8
Capital element of finance lease receipts	**(1.5)**	(3.0)
Change in net cash as defined by the Group resulting from cash flows	**78.3**	20.9
Cash and cash equivalents disposed	–	(1.0)
Amortisation of deferred financing costs	**(0.3)**	(0.7)
Finance lease receivables	–	0.3
Finance lease payables	–	(0.2)
Foreign exchange and other non-cash movements	**1.0**	5.7
In–year movement in net cash as defined by the Group	**79.0**	25.0
Net cash as defined by the Group at the beginning of the year	**195.5**	170.5
Net cash as defined by the Group at the end of the year	**274.5**	195.5
Less: other financial assets and liabilities	**(11.0)**	(11.2)
Total cash and cash equivalents	**263.5**	184.3

13. Post-retirement benefits

The Scheme is a final salary plan, which provides benefits to members in the form of a guaranteed level of pension payable for life. The level of benefits provided depends on the members' length of service and their final pensionable earnings at closure to future accrual. In the Scheme, pensions in payment are generally updated in line with the Consumer Price Index (CPI).

The fair value of the QinetiQ Pension Scheme assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the Scheme's liabilities, which are derived from cash flow projections over long periods, and thus inherently uncertain, were:

all figures in £ million	2016	2015
Equities - quoted	**347.9**	447.2
Equities - unquoted	**66.1**	70.0
LDI investment[1]	**362.8**	323.4
Corporate bonds	**314.2**	311.4
Alternative bonds[2]	**176.6**	176.3
Property	**126.6**	113.4
Cash and other	**16.2**	12.9
Total market value of assets	**1,410.4**	1,454.6
Present value of Scheme liabilities	**(1,448.1)**	(1,494.0)
Net pension liability before deferred tax	**(37.7)**	(39.4)
Deferred tax asset	**1.5**	1.6
Net pension liability after deferred tax	**(36.2)**	(37.8)

[1] The Scheme has assets invested in a Liability Driven Investment portfolio. As at 31 March 2016 this hedges against 40% of the interest rate and 100% of the inflation rate risk, as measured on the Trustee's gilt-funding basis.
[2] Includes allocations to high-yield bonds, secured loans and emerging market debt.

Changes to the fair value of Scheme assets

all figures in £ million	2016	2015
Opening fair value of Scheme assets	**1,454.6**	1,304.6
Interest income on Scheme assets	**46.3**	53.9
Re-measurement (loss)/gain on Scheme assets	**(75.8)**	116.3
Contributions by the employer	**14.6**	9.2
Net benefits paid out and transfers	**(28.1)**	(28.1)
Administrative expenses	**(1.2)**	(1.3)
Closing fair value of Scheme assets	**1,410.4**	1,454.6

Changes to the present value of the defined benefit obligation

all figures in £ million	**2016**	2015
Opening defined benefit obligation	**(1,494.0)**	(1,326.8)
Interest cost	**(47.4)**	(54.5)
Actuarial gain/(loss) on Scheme liabilities based on:		
Change in financial assumptions	**40.4**	(128.3)
Experience gains	**24.8**	7.8
Change in demographic assumptions	**–**	(20.3)
Net benefits paid out and transfers	**28.1**	28.1
Closing defined benefit obligation	**(1,448.1)**	(1,494.0)

Total expense recognised in the income statement

all figures in £ million	**2016**	2015
Net interest on the net defined benefit liability	**1.1**	0.6
Administrative expenses	**1.2**	1.3
Total expense recognised in the income statement (gross of deferred tax)	**2.3**	1.9

Assumptions

The major assumptions used in IAS19 valuation of the Scheme were:

	2016	**2015**
Discount rate applied to Scheme liabilities	**3.4%**	**3.2%**
CPI inflation assumption	**2.1%**	**2.1%**
Assumed life expectancies in years:		
Future male pensioners (currently aged 60)	**89**	**88**
Future female pensioners (currently aged 60)	**91**	**91**
Future male pensioners (currently aged 40)	**91**	**91**
Future female pensioners (currently aged 40)	**93**	**93**

14. Contingent liabilities and assets

Subsidiary undertakings within the Group have given unsecured guarantees of £32.8m at 31 March 2016 (2015: £36.2m) in the ordinary course of business.

The Company has on occasion been required to take legal action to protect its intellectual property rights, to enforce commercial contracts or otherwise and similarly to defend itself against proceedings brought by other parties. Provisions are made for the expected costs associated with such matters, based on past experience of similar items and other known factors, taking into account professional advice received, and represent management's best estimate of the likely outcome. The timing of utilisation of these provisions is uncertain pending the outcome of various court proceedings and negotiations. However, no provision is made for proceedings which have been or might be brought by other parties unless management, taking into account professional advice received, assesses that it is more likely than not that such proceedings may be successful. Contingent liabilities associated with such proceedings have been identified but the Directors are of the opinion that any associated claims that might be brought can be resisted successfully and therefore the possibility of any outflow in settlement is assessed as remote.

The Group has not recognised contingent amounts receivable relating to the Chertsey property which was disposed of during 2004 or the Fort Halstead property disposed of in September 2005. Additional consideration is potentially due on the purchasers obtaining additional planning consents, with the quantum dependent on the scope of the consent achieved.

The Group has also not recognised contingent amounts receivable relating to property impairments in prior years that may potentially be recovered from the MOD. Recovery is subject to future negotiations. It is not considered practicable to calculate the value of this contingent asset.

15. Cash flows from operations

For the year ended 31 March

all figures in £ million	2016	2015
Profit after tax for the year	**106.1**	104.7
Adjustments for:		
Taxation income	**(8.4)**	(11.8)
Net finance costs	**1.3**	4.1
(Profit)/loss on business divestments and disposal of investments	**(23.7)**	12.9
Reversal of unutilised restructuring provisions	**–**	(1.0)
Amortisation and impairment of purchased or internally developed intangible assets	**2.8**	1.5
Amortisation of intangible assets arising from acquisitions	**2.0**	3.6
Impairment of goodwill	**31.9**	–
Depreciation and impairment of property, plant and equipment	**23.0**	22.0
Loss on disposal of property, plant and equipment	**1.2**	1.2
Share of post-tax (profit)/loss of equity accounted entities	**(0.5)**	0.1
Share-based payments charge	**4.7**	3.6
Changes in retirement benefit obligations	**(13.4)**	(7.9)
Net movement in provisions	**(0.3)**	(1.6)
	126.7	131.4
(Increase)/decrease in inventories	**(0.2)**	2.6
Decrease in receivables	**13.8**	27.3
Decrease in payables	**(6.9)**	(22.2)
Changes in working capital	**6.7**	7.7
Cash generated from operations	**133.4**	139.1
Add back: cash outflow relating to restructuring	**–**	0.6
Add back: disposal-related pension contribution	**–**	6.0
Less: cash generated from discontinued operations	**–**	(1.8)
Net cash flow from operations before specific adjusting items	**133.4**	143.9

Reconciliation of net cash flow from operations before specific adjusting items to underlying operating cash flow

all figures in £ million	2016	2015
Net cash flow from operations before specific adjusting items	**133.4**	143.9
Purchases of intangible assets	**(1.6)**	(4.2)
Purchases of property, plant and equipment	**(28.6)**	(24.8)
Proceeds from sale of property, plant and equipment	**0.4**	–
Underlying operating cash flow	**103.6**	114.9

Glossary

Book to bill ratio	Ratio of funded orders received in the year to revenue for the year, adjusted to exclude revenue from the 25-year LTPA contract
C4ISR	Command, control, communications, computers, intelligence, surveillance and reconnaissance
CPI	Consumer Price Index
DE&S	MOD's Defence, Equipment and Support organisation
EBITDA	Earnings before interest, tax, depreciation and amortisation
EPS	Earnings per share
Funded backlog	The expected future value of revenue from contractually committed and funded customer orders (excluding the £998m third-term re-pricing of the LTPA contract)
IAS	International Accounting Standards
IFRS	International Financial Reporting Standards
LTPA	Long Term Partnering Agreement – 25-year contract established in 2003 to manage the MOD's test and evaluation ranges
MOD	UK Ministry of Defence
Organic growth	The level of year-on-year growth, expressed as a percentage, calculated at constant foreign exchange rates, adjusting comparatives to incorporate the results of acquired entities but excluding the results for any disposals or discontinued operations for the same duration of ownership as the current period
Specific adjusting items	Amortisation of intangible assets arising from acquisitions; impairment of goodwill and intangible assets; gains/losses on business divestments and disposal of property and investments; net pension finance expense; net restructuring charges/ recoveries; tax on the preceding items; one-off recovery of research and development tax credits and associated write-off of tax losses; and other significant non-recurring deferred tax movements
SDSR	Strategic Defence and Security Review
SSRO	Single Source Regulations Office
UK GAAP	UK Generally Accepted Accounting Practice
Underlying basic earnings per share	Basic earnings per share as adjusted to exclude 'specific adjusting items'
Underlying effective tax rate	The tax charge for the year excluding the tax impact of 'specific adjusting items' expressed as a percentage of underlying profit before tax
Underlying net cash from operations (post capex)	Net cash inflow from operations before cash flows of specific adjusting items less net cash outflow on purchase/sale of intangible assets and property, plant and equipment
Underlying net finance costs	Net finance costs excluding net pension finance costs
Underlying operating cash conversion	The ratio of underlying net cash from operations (post capex) to underlying operating profit excluding share of post-tax result of equity-accounted joint ventures and associates
Underlying operating margin	Underlying operating profit expressed as a percentage of revenue
Underlying operating profit	Operating profit as adjusted to exclude 'specific adjusting items'
Underlying profit before tax	Profit before tax as adjusted to exclude 'specific adjusting items'