QinetiQ

QinetiQ Group plc

Interim Results for half year ended 30 September 2013

21 November 2013

QinetiQ

Agenda

1. Headlines
2. Financial overview
3. Business overview
4. Q&A

Headlines

- Overall mixed performance with many encouraging elements against a very strong comparator period
  - Robust performance in EMEA Services; encouraging orders with growing international element
  - US Services stabilising post restructuring; strategic review underway including market testing exercise
  - Sharp decrease in US conflict-related product sales and profits against record first half of last year
- Balance sheet strength achieved enhanced by ongoing high cash conversion
- Increase in interim dividend reflecting re-basing of last year's final dividend and confidence in strategy
- Maintaining guidance for full year despite challenging markets

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Financial overview

David Mellors
Chief Financial Officer

Summary financial headlines

	FY14 H1 £m	FY13 H1 £m
Revenue	**599.6**	685.5
Operating profit*	**59.2**	95.3
Operating margin*	**9.9%**	13.9%
Profit before tax*	**52.3**	85.8
Earnings per share* (pence)	**7.0**	10.5
Statutory earnings per share (pence)	**9.5**	9.9
Net cash from operations (post capex)*	**69.6**	95.7
Cash conversion (post capex)*	**118%**	101%
Net cash	**120.5**	21.5
Dividend (pence)	**1.4**	1.1

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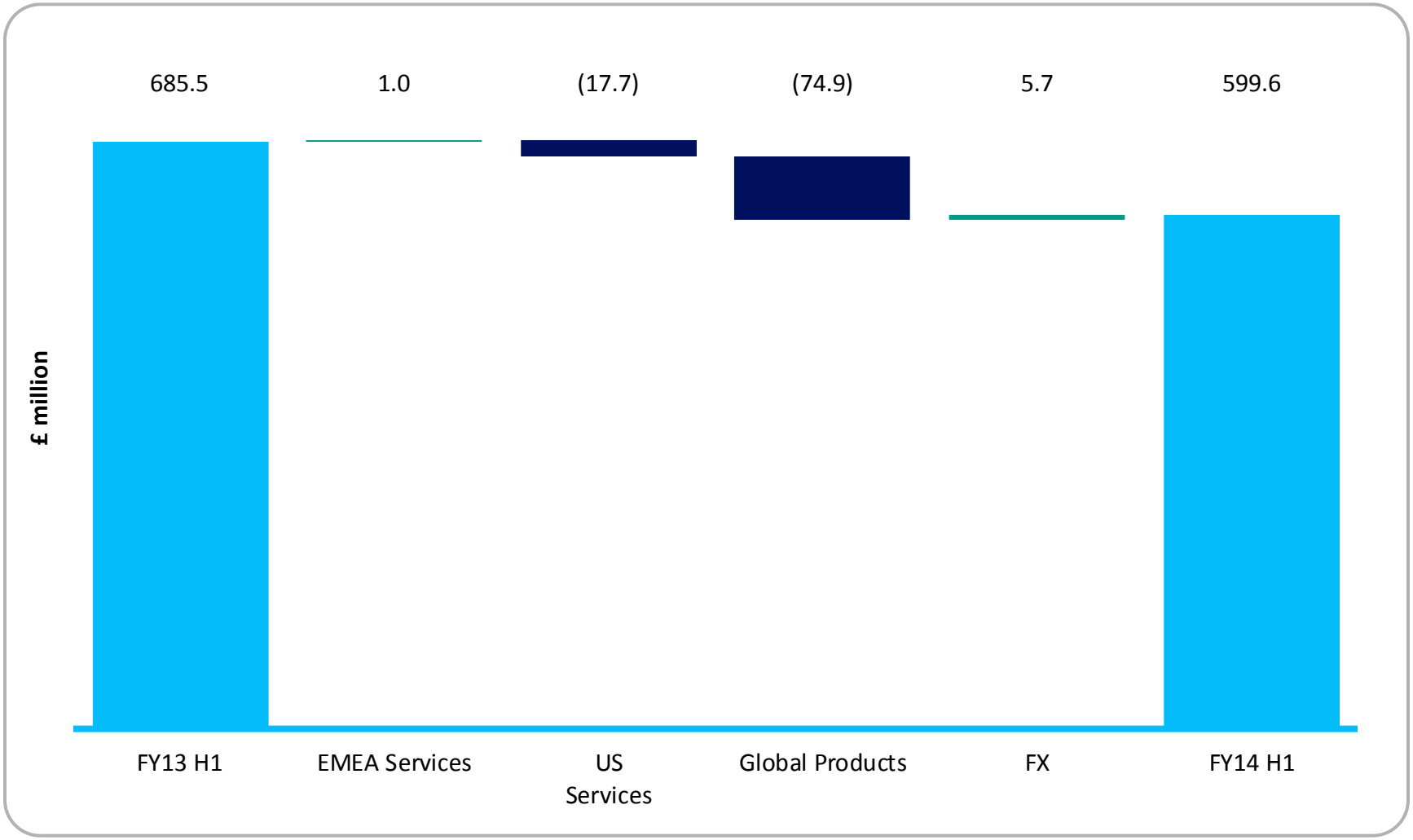
* Underlying performance as defined at appendix

Revenue bridge



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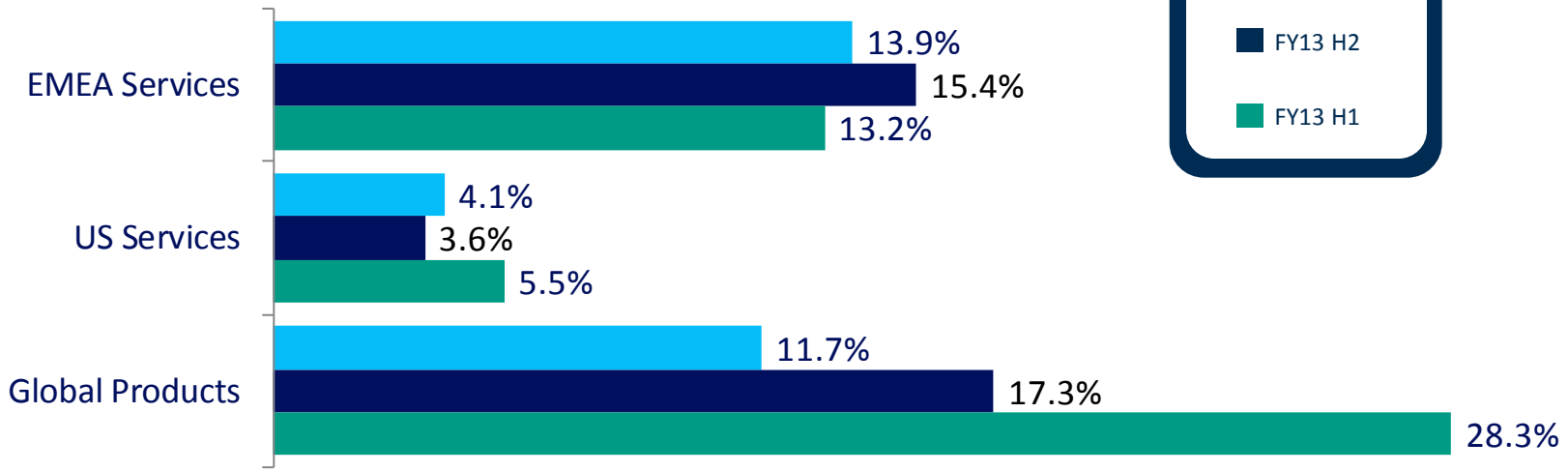
Segmental analysis of profit and margin

	Operating profit*		
	FY14 H1	FY13 H2	FY13 H1
	£m	£m	£m
EMEA Services	**40.3**	47.5	38.3
US Services	**9.4**	8.5	13.4
Global Products	**9.5**	17.4	43.6
Group	**59.2**	73.4	95.3



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* Underlying performance as defined at appendix

Specific adjusting items*

	FY14 H1 £m	FY13 H1 £m
Non-cash items		
Amortisation of acquired intangibles	**(5.6)**	(7.5)
Pension net finance expense	**(1.2)**	(0.8)
Items with cash impact		
Reduction in DB pension scheme liability	**31.1**	-
Pension mitigation costs	**(4.0)**	-
Gain on disposal of investment	**-**	2.5
Total specific adjusting items (pre-tax)	**20.3**	(5.8)

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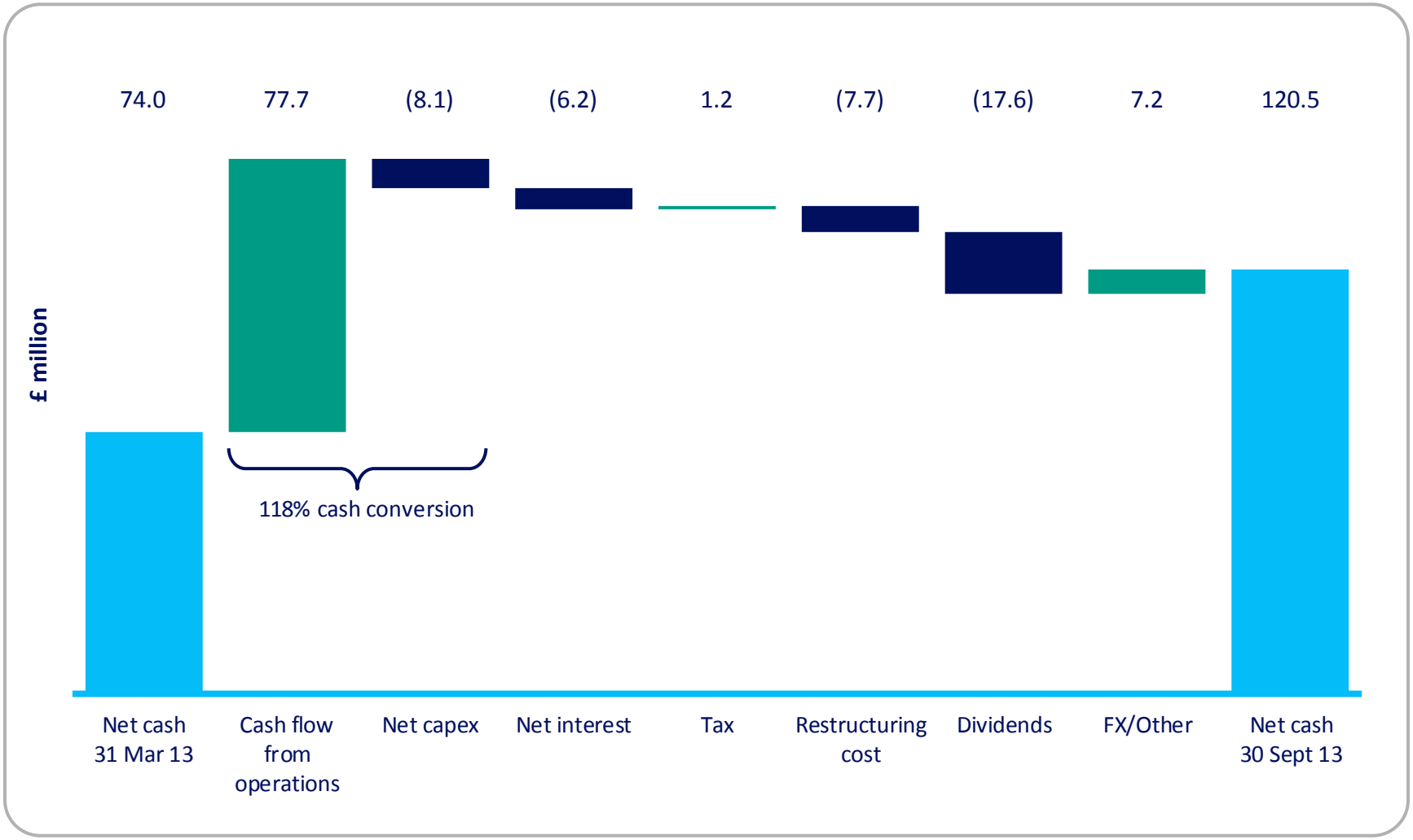
* Specific items adjusted in arriving at underlying performance as defined in appendix

Movements in net cash



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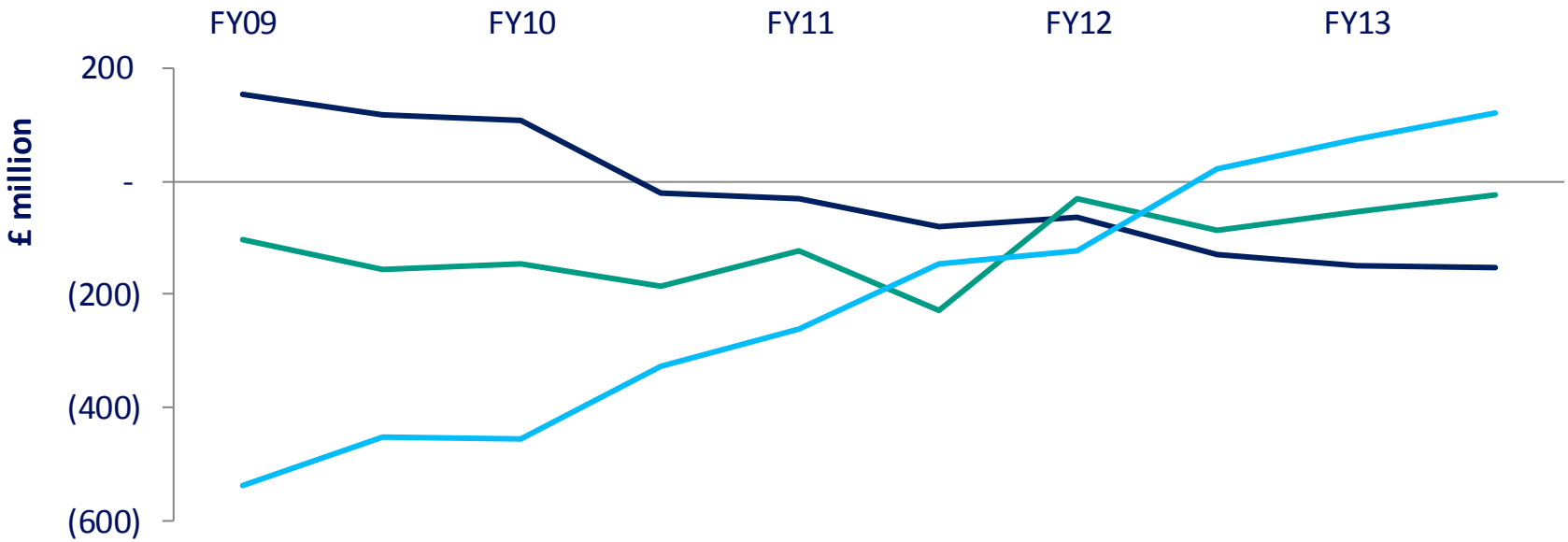
Strong balance sheet achieved



	FY09 £m	FY10 £m	FY11 £m	FY12 £m	FY13 £m	FY14 H1 £m
Working capital	154.0	107.2	(30.7)	(62.7)	(148.3)	**(151.5)**
Retirement benefit obligation (pre-tax)	(105.2)	(147.3)	(124.6)	(31.5)	(54.1)	**(24.8)**
Net (debt) / cash	(537.9)	(457.4)	(260.9)	(122.2)	74.0	**120.5**

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Business overview

Leo Quinn
Chief Executive Officer

Portfolio roles

EMEA Services

- Highly differentiated; high barriers to entry
- IP generation
- Long-term contracts
- Cash generation underpins progressive dividend policy

US Services

- Performance stabilising post restructuring
- Strong capabilities and market positions
- Good range of contract vehicles
- Strategic review will determine path to maximum value

Global Products

- Sharp decline in US OCO budget but market will re-set
- Diversifying product portfolio; moving beyond defence
- OptaSense® oil and gas business model maturing
- Portfolio option value

Each division has a specific role to play

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Market environment

US

- Delays and indecision
- October shutdown – further interruptions
- Drawdown post Afghanistan and “pacific pivot”
- Defence budget will re-base over time with focus on protecting the war-fighter

UK

- Focus on financial stability
- Defence transformation a priority
- Responsibility shifting to frontline / single service commands
- Growing maritime budget; “Successor” programme etc

International

- International requirement for independent advice and assurance

Changing nature of market presents opportunities for the ‘Core’

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Organic-Plus – growing and diversifying the 'Core'

Is it real, can we win, is it worth it?

Core	Explore	Test for Value
Maximise c90% of revenue	**Scale** c8% of revenue	**Maintain the rigour** c2% of revenue
EMEA Services: Weapons, Air, Maritime, C4ISR, Acquisition Services	• International ranges • Protective monitoring • UAS Services • Training and Simulation	• International procurement advice • Smart metering assurance
US Services: Aerospace Ops; Mission & Defense Solutions	• Cyveillance®	
Global Products • TALON® • Q-Net® • LAST® Armor	• OptaSense® • Robotic applique kits and controllers • Space products	• ALARM™ • E-X-Drive® • Integrated Warrior System™ • MEWS™ • Power Line Sensors

Achieved important strategic milestones for 'Explore'

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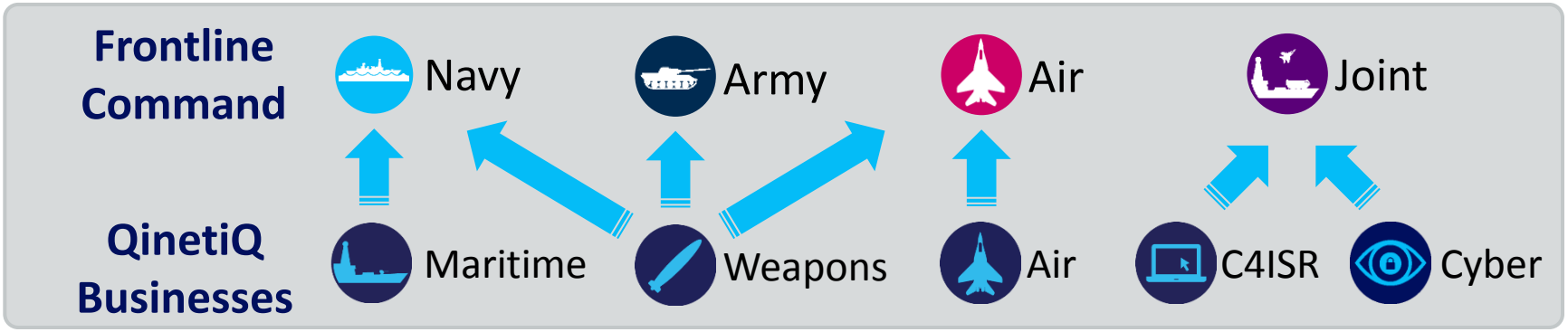
EMEA Services – progress in period

	FY14 H1 £m	FY13 H1 £m
Orders†	**217.5**	201.2
Revenue	**289.9**	289.6
Underlying Operating Profit*	**40.3**	38.3
Underlying Operating Profit Margin*	**13.9%**	13.2%
Book to Bill Ratio†	**1.1x**	1.0x
Funded Backlog†	**662.2**	639.6

- Robust performance
- 8% increase in orders; strong pipeline
- De-layered to increase accountability and agility; reduces costs
- Support to defence transformation
- Businesses aligned with frontline commands



Strong defensible base – capable of growth

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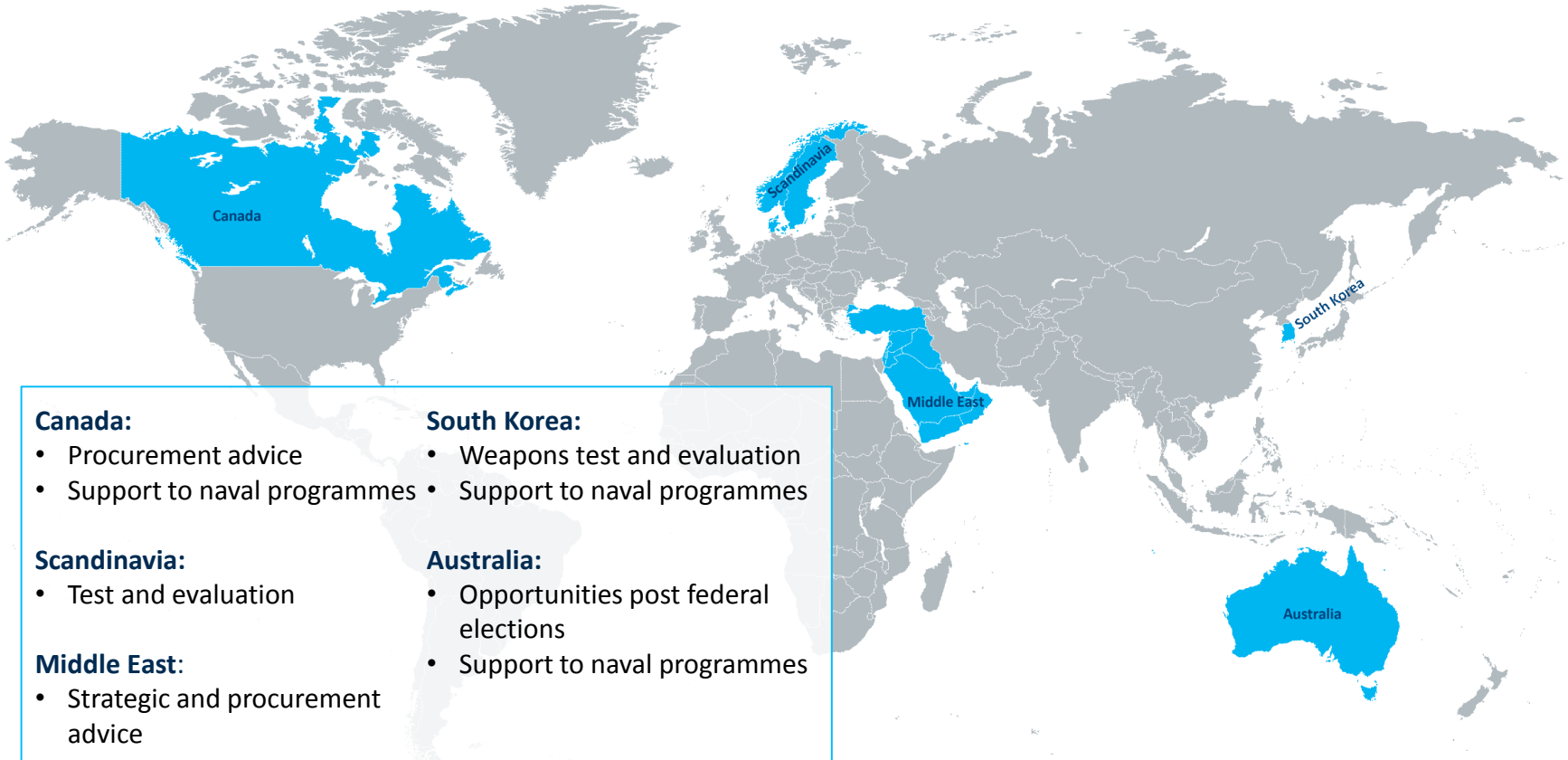
* Underlying performance as defined at appendix

† Excludes the third term £998m renewal of the LTPA contract. Book to Bill ratio is orders won divided by revenue recognised excluding the LTPA contract

EMEA Services – international demand



Canada:
- Procurement advice
- Support to naval programmes

Scandinavia:
- Test and evaluation

Middle East:
- Strategic and procurement advice

South Korea:
- Weapons test and evaluation
- Support to naval programmes

Australia:
- Opportunities post federal elections
- Support to naval programmes

EMEA Services model – transferable to other countries

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US Services – progress in period

	FY14 H1	FY13 H1
	£m	£m
Orders	**247.7**	283.5
Revenue	**228.7**	241.6
Underlying Operating Profit*	**9.4**	13.4
Underlying Operating Profit Margin*	**4.1%**	5.5%
Book to Bill Ratio	**1.1x**	1.2x
Funded Backlog	**209.3**	243.8

- Tough markets – lack of visibility
- Stabilising performance post restructuring
- Circa $1bn bid pipeline
- Strong capabilities and market positions:
  - NASA opportunities
  - Growing intelligence revenues
  - Strong maritime contract base
- Strategic review ongoing, including market testing

Cyveillance® (not in strategic review)

- Open source threat intelligence and remediation
- Market c$300m; under 10% penetration
- Double-digit growth; profitable
- 24x7 response centre opened Sep 13
- Threat increasing – "hactivism", DOS attacks
- Growth strategy based on repeatable services

Strategic review will determine path to maximum value

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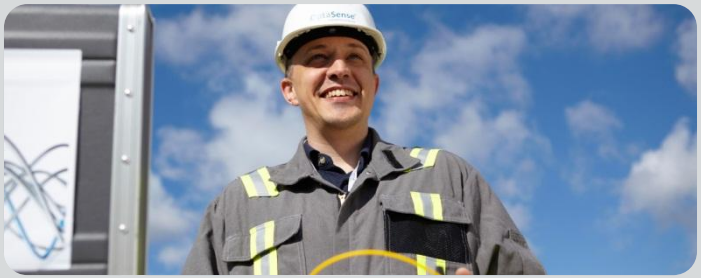
* Underlying performance as defined at appendix

Global Products – progress in period

	FY14 H1	FY13 H1
	£m	£m
Orders	**68.5**	120.5
Revenue	**81.0**	154.3
Underlying Operating Profit*	**9.5**	43.6
Underlying Operating Profit Margin*	**11.7%**	28.3%
Book to Bill Ratio	**0.8x**	0.8x
Funded Backlog	**94.5**	124.6

- Lumpy revenue profile
- $18m Q-Net® order
- New international markets, eg $28m TALON® to Iraq and Pakistan
- Growing contribution from new products, eg £4m MEWS™ order, E-X-Drive®, ALARM™
- Moving beyond defence – eg power line sensors, Space - Proba V, OptaSense®

OptaSense® *bespoke fibre sensing*



- IP portfolio progressing through to grant
- Business model clarified for oil field services
- Substantive progress in proving our solution in each vertical market – oil and gas, subsea, pipelines, rail, roads, borders

Encouraging progress in broadening the portfolio beyond defence

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* Underlying performance as defined at appendix

Outlook for FY14

- Although the short-term range of possible outcomes remains wider than usual, particularly in Global Products, the Board is maintaining its expectations for overall Group performance in the current year absent any material changes in customer requirements.

- Over the medium term, our confidence that our 'Core' businesses and newer growth opportunities will drive a sustainable increase in earnings is reflected in the increased interim dividend.

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Organic-Plus – reshaping QinetiQ

- Mixed performance with many encouraging elements
- Strong EMEA core business
- Organic-Plus programme developing momentum
- Balance sheet strength achieved

Committed to actions which drive value

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Questions

Download our iPad app from the App Store or scan the QR code

Appendices

Definitions

- Underlying performance is stated before
  - Amortisation of intangibles arising from acquisitions;
  - Reduction in liability arising on pension scheme closure;
  - Pension scheme closure costs;
  - Pension net finance expense;
  - Gains on disposal of investments;
  - Restructuring costs; and
  - Tax effect of the above.
- Organic growth
  - Is calculated at constant foreign exchange rates, adjusting the comparatives to incorporate the results of acquired entities and excluding the results for any disposals for the same duration of ownership as the current period.

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Detailed income statement

	FY14 H1 £m	FY13 H1 £m
Revenue	**599.6**	685.5
Underlying operating profit*	**59.2**	95.3
Net finance expense	**(6.9)**	(9.5)
Underlying profit before tax*	**52.3**	85.8
Amortisation and impairment of acquisition-related intangibles	**(5.6)**	(7.5)
Pension net finance expense	**(1.2)**	(0.8)
Gain on disposal of investment	**-**	2.5
Pension mitigation costs	**(4.0)**	-
Reduction in DB pension scheme liability	**31.1**	-
Statutory profit before tax	**72.6**	80.0
Taxation	**(10.5)**	(15.5)
Statutory profit after tax attributable to equity shareholders	**62.1**	64.5

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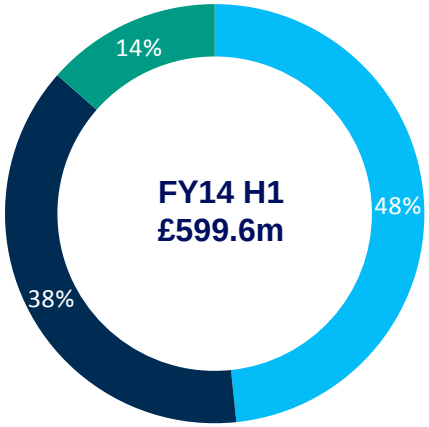
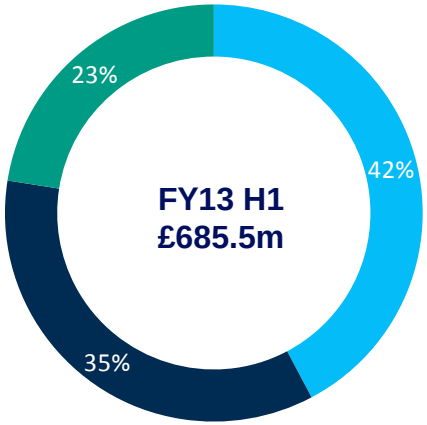
* Underlying performance as defined at appendix

Revenue by sector and customer

Revenue by sector (%)

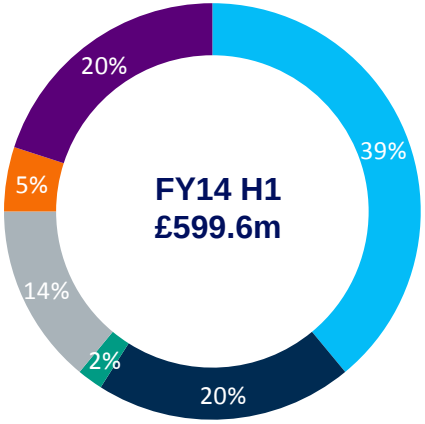


- EMEA Services
- US Services
- Global Products

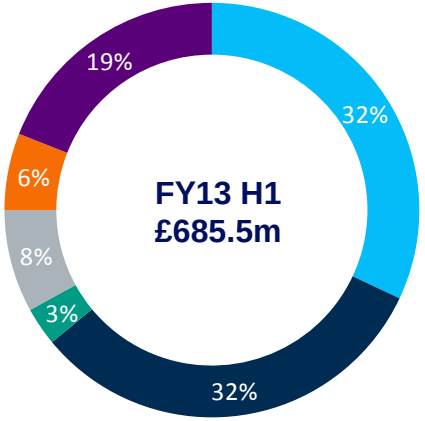


- EMEA Services
- US Services
- Global Products

Revenue by customer (%)



- MOD
- DoD
- DHS
- NASA
- Commercial Defence
- Civil/Other Government agencies



- MOD
- DoD
- DHS
- NASA
- Commercial Defence
- Civil/Other Government agencies

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Taxation

	FY14 H1 £m	FY13 H1 £m
Underlying tax charge*	**(6.7)**	(17.4)
Tax on non-recurring items	**(3.8)**	1.9
Headline tax charge	**(10.5)**	(15.5)
Underlying tax rate*	**12.8%**	20.3%

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* Underlying performance as defined at appendix

Balance sheet

	30 September 2013 £m	31 March 2013 £m
Goodwill	**274.1**	290.4
Intangible assets	**50.0**	57.8
Property, plant and equipment	**233.6**	241.4
Working capital	**(151.5)**	(148.3)
Retirement benefit obligation (net of tax)	**(20.3)**	(40.4)
Other assets and liabilities	**(32.7)**	(36.4)
Net cash	**120.5**	74.0
Net assets	**473.7**	438.5

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Cash conversion

	FY14 H1 £m	FY13 H1 £m
Underlying operating profit*	**59.2**	95.3
Share of JVs & associates	**-**	(0.1)
Operating profit before JVs & associates*	**59.2**	95.2
Cash flow from operations*	**77.7**	106.1
Net capex	**(8.1)**	(10.4)
Net cash flow from operations post capex	**69.6**	95.7
Cash conversion %*	**118%**	101%
Net interest paid	**(6.2)**	(29.3)
Taxation	**1.2**	2.0
Free cash flow*	**64.6**	68.4

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* Underlying performance as defined at appendix

Movements in net cash / (debt)

	FY14 H1 £m	FY13 H1 £m
Free cash flow	**64.6**	68.4
Net restructuring (outflow)/inflow	**(7.7)**	64.9
Sale of investment	**-**	3.4
Dividends	**(17.6)**	(13.0)
Purchase of own shares	**(0.2)**	(0.2)
Other	**0.1**	19.3
Change in net cash/debt before FX	**39.2**	142.8
FX translation impact	**7.3**	0.9
Change in net cash/debt	**46.5**	143.7
Opening net cash/(debt) - 1 April	**74.0**	(122.2)
Closing net cash - 30 September	**120.5**	21.5

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Defined benefit pension scheme – IAS 19 balance sheet position

	FY14 H1 £m	FY13 £m
Market value of assets	**1,261.7**	1,256.5
Present value of scheme liabilities	**(1,286.5)**	(1,310.6)
Net pension liability before deferred tax	**(24.8)**	(54.1)
Deferred tax asset	**4.5**	13.7
Net pension liability	**(20.3)**	(40.4)

Assumptions	**FY14 H1 %**	FY13 %
Discount rate	**4.4%**	4.4%
Inflation (CPI)	**2.6%**	2.7%

Sensitivity of deficit to main assumptions:

Assumption	**Change in assumption**	**Sensitivity**
Discount rate	Increase / decrease by 0.1%	Decrease / increase by £26m
Inflation	Increase / decrease by 0.1%	Increase / decrease by £26m
Salary increase	Increase / decrease by 0.1%	Increase / decrease by £26m
Life expectancy	Increase by 1 year	Increase by £28m

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Credit and debt facilities

	Maturity date	Denomination	Value in denomination	Value £m
Revolving Credit Facility	February 2016	£m	118.0	118.0
Revolving Credit Facility	February 2016	$m	250.0	154.5
Private Placement	February 2016	$m	43.0	26.6
Private Placement	December 2016	$m	48.0	29.7
Private Placement	February 2019	$m	157.0	97.2
Total Committed Facilities				**426.0**

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Employee numbers

	30 September 2013	31 March 2013
EMEA Services	**5,296**	5,145
US Services	**3,021**	3,350
Global Products	**793**	1,003
Total	**9,110**	9,498

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This document contains certain forward-looking statements relating to the business, financial performance and results of the Company and/or the industry in which it operates. Actual results, levels of activity, performance, achievements and events are most likely to vary materially from those implied by the forward-looking statements. The forward-looking statements concern future circumstances and results and other statements that are not historical facts, sometimes identified by the words 'believes',' expects', 'predicts', 'intends', 'projects', 'plans', 'estimates', 'aims', 'foresees', 'anticipates', targets', 'goals', 'due', 'could', 'may','should', and similar expressions. These forward-looking statements include, without limitation, statements regarding the Company's future financial position, income growth, impairment charges, business strategy, projected levels of growth in the relevant markets, projected costs, estimates of capital expenditures, and plans and objectives for future operations. Nothing in this document should be regarded as a profit forecast.

The forward-looking statements, including assumptions, opinions and views of the Company or cited from third party sources, contained in this Results Announcement are solely opinions and forecasts which are uncertain and subject to risks. Although the Company believes that the expectations reflected in these forward-looking statements are reasonable, it can give no assurance that these expectations will prove to be correct. Actual results may differ materially from those expressed or implied by these forward-looking statements. A number of factors could cause actual events to differ significantly. These factors include, but are not limited to:

Defence budgets which are subject to review and change from time to time and the level of available funding open to private contractors in the United Kingdom and United States;

The winning of new business or retention of previous business through a competitive bidding process;

The level of pension liability the Company accrues, given market conditions and actuarial factors;

Material adverse changes in economic conditions in the markets served by the Company; and

Future regulatory actions and conditions in the Company's operating areas, including competition from others.

Most of these factors are difficult to predict accurately and are generally beyond the control of the Company. Any forward-looking statements made by, or on behalf of the Company, speak only as of the date they are made. Save as required by law, the Company will not publicly release the results of any revisions to any forward-looking statements in this document that may occur due to any change in the Directors' expectations or to reflect events or circumstances after the date of this document.

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