

**Cobham plc**

Annual Report and Accounts 2013

**COBHAM**

The most important thing we build is trust



**Cobham protects lives and livelihoods with its differentiated technology and know-how, operating with a deep insight to customer needs and agility. The Group offers an innovative range of technologies and services to solve challenging problems across commercial, defence and security markets, from deep space to the depths of the ocean.**

**It has market leading positions in air-to-air refuelling; aviation services; audio, video and data communications, including satellite communications; defence electronics; life support; and mission equipment.**

**The most important thing Cobham builds is trust.**



**Front cover image**

Cobham's Distributed Antenna Systems (DAS) technology and wireless solutions for the public safety and cellular markets ensure that buildings and critical infrastructure have a fail-safe public safety communications system of the highest standard. The Burj Khalifa, Dubai, is one of the many pieces of infrastructure globally that benefit from Cobham's DAS technology.

**Inside front cover image**

Cobham provides governments globally with fixed and rotary wing services, including helicopter training, search and rescue, logistics and emergency medical services.

# Highlights of the Year

- Group revenue increased by 2%, with acquisitions trading ahead of plan
- Strong growth in commercial markets offset by continued weakness in defence/security markets resulted in 4% Group organic\* revenue decline
- Further progress in bringing more balance to the portfolio, with commercial 35% (2012: 31%) of Group revenue, and good progress with strategic objectives
- Incremental savings in Excellence in Delivery well ahead of plan, with site integrations being accelerated
- Group's PV investment\* increased to 6.2% (2012: 5.3%) of revenue, with focus on growth markets
- Recommended full year dividend increase of 10%, continuing the Group's long standing, progressive dividend policy

Dividend

**9.68p**  
(2012: 8.80p)

Total revenue

**£1,790m**  
(2012: £1,749m)

Earnings per Ordinary Share – underlying\*

**21.6p**  
(2012: 22.5p)

Earnings per Ordinary Share – basic

**10.7p**  
(2012: 16.0p)

\*For definitions, please refer to page 140.

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The Annual Report and Accounts contains certain forward looking statements with regard to the operations, performance and financial condition of the Group. By their nature, these statements involve uncertainty since future events and circumstances can cause results to differ from those anticipated. Nothing contained in this Annual Report and Accounts should be construed as a profit forecast.

You can view this Annual Report and Accounts online at [www.cobhaminvestors.com](http://www.cobhaminvestors.com)

# Group at a Glance

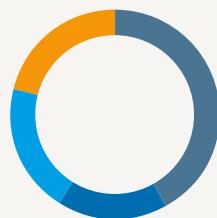
Cobham operates from 14 principal manufacturing locations, with nine in the USA, three in the UK and two in continental Europe, as well as satellite locations and sales offices across the world that provide a permanent presence in faster growth markets. In addition, Aviation Services operates from airport bases in Australia, the UK and elsewhere in the world.

## The Group in 2013

The Group leverages its innovative technology, know-how and understanding of customer needs to build and maintain leading positions in the second and third tiers of the global defence/security and commercial aerospace, marine and land markets.

Revenue

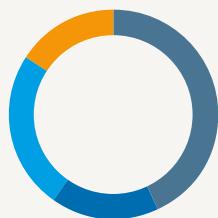
£1,790m



Aerospace and Security	42%
Defence Systems	17%
Mission Systems	20%
Aviation Services	21%

Trading profit

£318m



Aerospace and Security	44%
Defence Systems	15%
Mission Systems	25%
Aviation Services	16%

Divisional percentages for revenue and trading profit exclude non-core activities, head office results and eliminations:  
see note 4 on page 90

## Aerospace and Security (CAS)

See page 14



Provides aircraft and in-building communication equipment, law enforcement and national security monitoring solutions, and satellite communication equipment for land, sea and air applications.

## Defence Systems (CDS)

See page 16



Provides critical technology for network centric operations, moving information around the digital battlefield with customised and off-the-shelf solutions for people and systems to communicate on land, sea and in the air.

### Operating locations

United States, United Kingdom, Denmark, France, South Africa, Finland and Sweden

### Operating locations

United States and Mexico

### Revenue

£744m

(2012: £697m)

### Trading profit

£132m

(2012: £149m)

### Revenue

£309m

(2012: £323m)

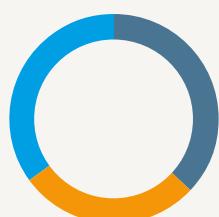
### Trading profit

£47m

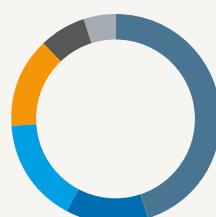
(2012: £45m)

## Rebalancing the portfolio for sustainable organic revenue growth

### Markets



### Geography



### Mission Systems (CMS)



Provides safety and survival systems for extreme environments, nose-to-tail refuelling systems and wing-tip to wing-tip mission systems for fast jets, transport aircraft and rotorcraft, and provides remote controlled robots and fully equipped bomb disposal vehicles for homeland security and military applications.

See page 18

### Aviation Services (CAvS)



Delivers outsourced aviation services for military and civil customers worldwide through military training, special mission flight operations, outsourced commercial aviation and aircraft engineering.

#### Operating locations

United States, United Kingdom and Germany

#### Revenue

**£358m**  
(2012: £373m)

#### Trading profit

**£74m**  
(2012: £81m)

#### Operating locations

Australia and United Kingdom

#### Revenue

**£365m**  
(2012: £327m)

#### Trading profit

**£48m**  
(2012: £38m)

## What we Do

Our technology and know-how based business model enables us to consistently deliver strong trading margins, long term growth and consistently high operating cash flow conversion.

Investment in differentiated and specialist technologies contributes to our market leading positions and strong trading margins. The combination of our margins and our relatively low capital requirements enables us to generate consistently good levels of cash.

Trading margin

17.7%  
(2012: 19.0%)

Free cash flow  
(after restructuring)

£155m  
(2012: £241m)

Leading positions  
in our markets

Investment in high  
value-add technology  
and know-how

1

2

4

3

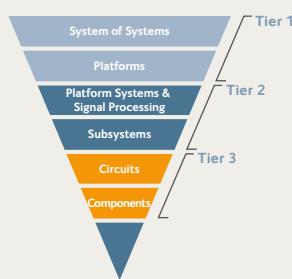
Understanding  
of and response  
to customer  
needs

Programme management  
and operational excellence

Leverage of  
existing technology,  
products and services  
into new markets

## 1 Leading positions in our markets

Cobham operates in specialist technology markets at the tier two (subsystems) and tier three (components) segments, supplying to a blue chip customer base. Its market leading positions enable Cobham to optimise its return on investment, so it can continue to invest in technology and in skills and capabilities as well as pay an increasing dividend to shareholders.



### Cobham in action

Cobham has built on its strong position in the commercial slip ring market for wind turbines by commencing additional operations at its Prescott, Arizona manufacturing facility. This facility is starting to supply US customers with products made in-country, which is leading to further market penetration of the wind turbine market.

See page 10 for more information.

## 2 Investment in high value-add technology and know-how

Private Venture (PV or company funded research and development – R&D) investment in the year increased to 6.2% (2012: 5.3%) of revenue. This is consistent with the previously announced plans to increase technology investment, closely aligning this to growth markets.

Total R&D investment, including customer funded projects, was up by 19% to £186m (2012: £156m) primarily due to the ongoing significant funded development activity on aerial refuelling programmes, which is expected to increase in 2014.

### PV investment

**£88m**  
(2012: £75m)

### Total R&D investment

**£186m**  
(2012: £156m)

### Cobham in action

Cobham's products are often smaller, lighter and use less power than competing technologies. This means that cost savings and operational benefits are generated for customers, together with a reduced impact on the environment through reduced fuel and energy consumption.

See page 9 for more information.

## 3 Leverage of existing technology, products and services into new markets

Cobham leverages its technology into new or adjacent commercial end markets, where there is strong customer demand. This is helping it to bring more balance to its portfolio and will enable it to grow revenue through business cycles.

During the year, Cobham has made progress towards this objective by growing its commercial revenue organically and through acquisitions.

### Revenue from commercial markets

**35%**  
(2012: 31%)

### Cobham in action

The new Solo7 ultra-miniature high quality wireless video encoder is based on defence/security technology and is now being sold into target broadcast markets. The product has already been used at the 2014 Sochi Winter Olympics.

See page 6 for more information.

## 4 Programme management and operational excellence

Programme management is a core competency focus for Cobham, which enables it to meet customer expectations and deliver growth. Considerable work has been undertaken to enhance functional excellence in project and programme management across the Group's diverse range of activities.

The transformational Excellence in Delivery (EiD) programme has continued to deliver further improvements to operational performance and customer delivery in Cobham's principal locations.

### Improvement in direct labour productivity since 2010

**40%**

### Cobham in action

EiD is reducing Cobham's physical footprint and thereby reducing its CO<sub>2</sub> emissions. Cobham continues to target reduced impacts on the environment from its products, facilities and supply chain.

### CO<sub>2</sub> emissions

**86.6 MWh/£m turnover**  
(2012: 87.2MWh/£m turnover)

See pages 9 and 35 for more information.

## Investing in skills and expertise

The delivery of Cobham's strategy depends on the right skills and capabilities being in place in the business. Cobham has increased its investment significantly in learning and development to further build the essential skills and capabilities that are critical to the delivery of future growth.

See page 8 for more information.

**366 employees**

**1,473 hours**

Employee training completed in the first three months on the new online Learning and Development Centre.

# Chairman's Statement



**"There has been considerable focus on the drive towards sustainable organic revenue and profit growth"**

## Overview

It has been a year of significant activity for Cobham. The Board has continued to give considerable focus to the Group's strategic objectives, which underpin the drive towards sustainable organic revenue and profit growth and increasing shareholder value.

The Group's transformational EiD programme has enabled us to streamline and simplify the business and is achieving significant efficiency savings by reducing costs through an extensive site integration and rationalisation programme. In part, as we guided in 2012, we are using these savings to increase our investment in the business, as part of our focus on generating revenue growth.

EiD has continued to deliver improvements in operational performance and customer delivery through implementation of a standard operating framework across Cobham's principal locations. With this first phase largely complete, the programme is moving into a continuous improvement phase that will not only sustain the progress already made but also drive further performance improvements. Operational excellence is essential to enable the Group to meet or, wherever possible, exceed customer expectations as the foundation for the delivery of sustainable organic revenue and profit growth.

We have increased our investment in the business, linking this more closely to market opportunities and the needs of our customers. We have leading positions in attractive technology-led markets and we aim to grow market share and revenue by investing in new or improved products, which are often smaller, lighter and less power consumptive than legacy products.

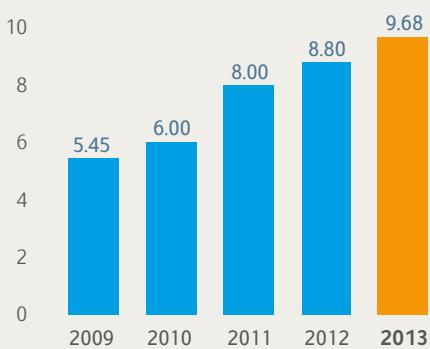
Furthermore, we also leverage our core suite of technologies into new commercial and geographic markets where suitable opportunities can be identified. This is aligned with our strategic objective of bringing more balance to the portfolio, so that the Group remains exposed to faster growth markets. The shift in the portfolio is also being achieved through carefully selected acquisitions, with two businesses with

### Full year dividend

**9.68p** +10%  
(2012: 8.80p)

### 13% CAGR over ten years

pence



highly complementary technology and know-how purchased in the year, also reinforcing our market positions.

None of this is possible without the right skills and capabilities in the business. We have therefore increased our investment in our people in recent years, and we are linking our workforce requirements more closely to the business planning process, reinvigorating our approach to training and development and strengthening key management capabilities within the business. The Board is also mindful of the ageing demographics within the aerospace and defence industry and so we are gradually increasing the number of university graduates in the business, with a focus on science and engineering, and we are increasing the number of apprentices we recruit from schools.

A strong and effective governance framework is essential in enabling the achievement of the Group's strategic objectives. Good progress has been made in this area in 2013, in particular in enhancing the Group's programme management processes and introducing new procedures aimed at improving allocation of PV expenditure to targeted commercial opportunities.

The Group strives for the highest standards possible in setting its ethics and compliance rules, and at all times to comply with all laws and regulations that apply in the jurisdictions in which it operates. It is therefore very disappointing for me to have to tell you about a potential issue with sales practices in a small business unit supplying products into Asia. This issue was identified internally and elevated through Cobham's reporting lines, in accordance with our ethics policy and training. After an initial internal investigation, we made a voluntary disclosure to the US Department of Justice (DoJ) on 24 February 2014. The investigation into this issue is ongoing and Cobham continues to co-operate fully with the DoJ.

### **The Board**

We welcomed Simon Nicholls to the Board as Chief Financial Officer on 1 May 2013. Simon joined us from Senior plc, a FTSE250 international group manufacturing engineered products for aerospace, defence and industrial applications. In his previous role as Group Finance Director at Senior, Simon played a key role in the strategic evolution and growth of the business and his experience of financial leadership will make him pivotal to the delivery of our strategic objectives.

Simon replaced Warren Tucker, who stood down after ten years service as Chief Financial Officer. The Board would like to thank Warren for his vision and enormous contribution to the Group over this time.

We also welcomed to the Board on 1 May 2013 Jonathan Flint as a Non-executive Director. Jonathan is Chief Executive of Oxford Instruments plc, a leading provider of high technology tools and systems for research and industry, where he continues to deliver strong growth and shareholder value in technology-led markets around the world.

Marcus Beresford, Non-executive and Senior Independent Director, stood down from the Board at the conclusion of the 2013 Annual General Meeting. The Board is grateful to Marcus for his dedicated service over nine years and his invaluable contribution to Cobham during that time. With his departure, Michael Wareing has taken on the role of Senior Independent Director.

John Patterson, Non-executive Director and the Chairman of the Remuneration Committee, will stand down from the Board at the conclusion of the 2014 Annual General Meeting. The Board is grateful for his significant contribution and support over the last nine years. Alison Wood will assume the role of Chair of the Remuneration Committee following his departure.

### **Dividend**

The Board is recommending a final dividend for 2013 of 7.04p (2012: 6.40p). This, together with the interim dividend of 2.64p (2012: 2.40p), will result in a total dividend per share for 2013 of 9.68p (2012: 8.80p), an increase of 10% on the prior year.

The Board is proud of Cobham's long record of delivering a progressive dividend to our shareholders. The dividend has been increased consecutively for the last 43 years, an enduring track record that only a handful of other companies can match. This has been made possible in part due to Cobham's cash generative business model, its differentiated positions in attractive technology markets and its prudent investment in acquisitions. Following investment in the business, we will continue to prioritise increasing the dividend payment in line with the long standing, progressive dividend policy.

### **Outlook**

Cobham has delivered full year results in line with its guidance, in what remains a challenging US defence/security market. It has made good progress in the year against its strategic objectives, including increased technology and other organic investments, and accelerated benefits from the operational excellence programme. It is now realigning its organisational structure to enable the next stage of development.

Trading conditions in the US defence/security market are likely to remain challenging in 2014 with potentially significant foreign currency headwinds and continued pressure on US defence/security investment accounts. However, the Group anticipates that its strong and growing positions in attractive commercial markets and the generally positive prospects for its non-US defence/security markets will partially offset this, and Cobham continues to plan for Group organic revenue to decline by low-to-mid single digits in 2014. Cobham will continue to take further actions as appropriate to substantially mitigate the impact of this organic decline.

Cobham has innovative technology and know-how supported by market leading positions, which allows it to leverage across its markets. As a result the Board continues to anticipate that it will deliver mid-single digit organic revenue growth from 2015.

Cobham benefits from a cash generative business model and a strong balance sheet, which enables it to maintain its long standing policy of a 10% progressive annual dividend increase.



**John Devaney**  
Chairman  
5 March 2014

# Chief Executive Officer's Statement



**"We are transforming the Group's operational performance and customer delivery through our Excellence in Delivery programme"**

## Strategy

Last year, I set out the Group's strategy which is to leverage its innovative technology, know-how and understanding of customer needs to build and maintain leading positions in the second and third tiers of the global defence/security and commercial land, marine and aerospace markets. This enables Cobham to generate sustainable top and bottom line growth, relative to the markets in which we operate, while consistently generating good free cash flow, thereby creating shareholder value.

As a Group, we have invested significantly in the development of our strategy during the year and we are making tangible progress towards achieving our objectives and we anticipate a return to mid-single digit organic revenue growth from 2015.

## Strategic Overview

Our seven strategic priorities will enable us to return to sustainable growth. They focus on:

1. Innovation with insight
2. Focus on components and subsystems
3. Leverage our technology
4. Focus on M&A
5. Operational excellence
6. Programme execution
7. Invest in skills and capabilities

This will enable us to:

**Deliver growth – Generate free cash flow**  
**– Create shareholder value**

See page 12 for more information

## Investment in management capabilities

We have increased investment in the year to achieve the objective of enhancing the skills and capabilities of our employees, who are critical to the delivery of future growth. As part of this investment, we are implementing a strategic workforce plan, have commenced deployment of an integrated talent management programme and are continuing to invest in an online learning and development centre.

Programme management is a core competency focus which enables us to meet customer expectations and deliver growth. Considerable work has been undertaken to enhance functional excellence in project and programme management across the Group's diverse range of customer and internally funded activities, together with an increased focus on lifecycle management.

To enable the next stage of our strategic development and to make further progress towards achieving sustainable growth, we have undertaken a review of our structure. We will be retaining our four previously reported Divisions, now calling them Sectors, and these will be Communications and Connectivity (previously Aerospace and Security), US Defence Electronics, Mission Systems and Aviation Services. Within this structure, we will consolidate our three separate Special Security

Agreements into one, with all classified US Government work being carried out within US Defence Electronics. This consolidation requires the transfer of some business units from Communications and Connectivity to US Defence Electronics. There are no changes to the other two Sectors. We will reflect these changes in our reported results, commencing with our 2014 interims.

We are also strengthening our senior management and reporting structure to support the continuing transformation. This includes the appointment of a Chief Operating Officer (COO) who will be given direct responsibility for some key Group-wide functions as well as direct responsibility for Communications and Connectivity and Mission Systems.

### **Technology investment**

We have significantly increased PV investment to 6.2% (2012: 5.3%) of Group revenue. This is consistent with our previously announced plans to increase investment in our markets where there are good growth opportunities.

As part of this, we have increased technology investment in SATCOM product development, relating to the new Inmarsat Global Xpress (GX) satellite constellation, with global coverage expected by the end of 2014. Within Antenna Systems, a revolutionary next generation Distributed Antenna System (DAS) platform, 'idDAS', has been launched. idDAS is the first major DAS platform that provides the ability to dynamically shift capacity around an 'in-building' facility on demand.

We have also increased PV investment in Cobham Defence Systems in a range of critical defence/security technologies, including components and subsystems for next generation radar, electronic warfare and electronic attack applications, where there is an identified customer need and funding.

Total R&D investment, including customer funded projects, was up 19% to £186m (2012: £156m). The increased level of customer funding is primarily due to the ongoing significant funded development activity on aerial refuelling programmes, which is expected to increase in 2014.

### **Operational excellence**

Our transformational EiD programme has continued to deliver critical improvements to operational performance and customer delivery. EiD has three components: the integration and rationalisation of operating sites into a set of principal locations; the implementation of a standard operating framework designed to drive operational excellence and establish a culture of continuous improvement; and the implementation of a standard ERP system.

Given the challenging conditions the Group is continuing to face in its US defence/security market, we have worked hard to accelerate the benefits of the integration and downsizing activities. A number of satellite facilities have been integrated or rationalised during the year and, in total, we have now rationalised 27 sites since the beginning of 2010. This has significantly reduced the cost base of the Group. We are using the savings generated in part to fund increased investment in our business, to help deliver sustainable organic growth. EiD has also simplified the Group's operating structure and enhanced our flexibility and scalability.

Work has now been completed, as planned, in the principal locations on implementing the production, supply chain and engineering standard operating frameworks. Since the programme started, it has delivered significant improvements in the principal locations across a range of operational and customer metrics including on time delivery, quality and an improvement in direct labour productivity of 40%.

With centrally driven implementation activities largely finished, we are now focusing on actions to ensure that the significant progress that has been made to date is sustained, and that a culture of continuous improvement is embedded across the business to drive further improvements.

Work on the ERP system, also a major contributor to sustaining the operating and customer benefits of the standard operating framework, has continued.

Largely driven by the significant acceleration of integration activity, we have achieved £28m of year-on-year efficiency savings during 2013, well ahead of the £19m guidance. This brings the total annualised benefits to £76m since the programme began in 2010. The success in reducing costs means that we now expect EiD will generate £105m of annualised efficiency benefits by 2015, which is an increase of £5m on the previous guidance and this will be achieved one year earlier than planned. We expect to be able to achieve this within the existing budget, which is £191m over the programme life. EiD costs in the year were £56m, reflecting the acceleration of activity.

### **Capital allocation and mergers and acquisitions**

We continue to prioritise investment for organic growth, followed by our long standing, progressive dividend policy. After this, we use the significant free cash flows generated and the strong balance sheet to acquire businesses that are complementary to, and reinforce, our differentiated technology and know-how and market positions. During the year, we invested over £150m in acquisitions: primarily Axell in May for up to £85m, including contingent consideration, and in July the £74m acquisition of the outstanding 50% stake in FBH, our helicopter joint venture. We remain focused on bringing more balance to the portfolio and we will achieve this through a rigorous and disciplined approach to investment.

### **Conclusion**

We remain convinced that the successful pursuit of these objectives is key to the ongoing health of the business. Accordingly, we intend to maintain our strategic focus on executing our key priorities. This is especially important as conditions in the US defence/security market are likely to remain challenging in 2014. We remain confident that this will enable us to develop the capabilities, processes and people that we need to meet the Board's growth expectations and deliver increasing value for Cobham's shareholders and other stakeholders.

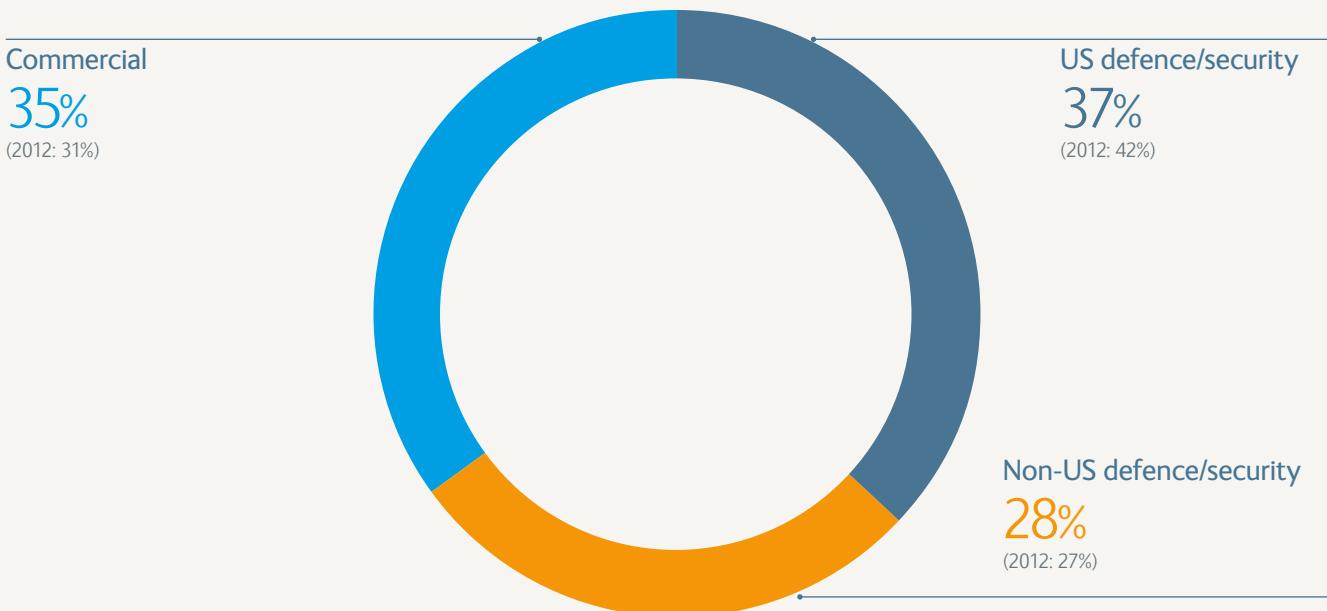


**Bob Murphy**  
Chief Executive Officer  
5 March 2014

# Our Markets

**The Group operates in three end markets: US defence/security, non-US defence/security and commercial, which comprises specialist aerospace, marine and land markets.**

## The Group operates in three market segments



### Competitive position within our markets

During the year, the Group has continued to make progress in bringing more balance to the revenue derived from its end markets, with the proportion generated from commercial markets increasing to 35% (2012: 31%). This has increased due to a combination of organic growth and acquisitions. These acquisitions have brought complementary technology and capability to the Group in predominantly commercial markets.

The Group has market leading positions and a portfolio of attractive technologies which can be leveraged across defence/security and commercial customers.

Within the US defence/security market, the Group is well positioned on high priority new platforms, including the KC-46 aerial refuelling tanker, the F-35 Joint Strike Fighter, and on a

number of ballistic missile defence programmes. It is also well positioned to benefit from upgrade programmes where it partners with a number of different system integrators to supply key components and subsystems, including on a variety of high priority next generation radar and electronic warfare programmes.

Cobham's technology and know-how are also highly relevant to non-US defence/security markets, where there are opportunities to benefit from significant platform/programme export orders won by larger defence companies and also from selling products and services direct to end customers. The Group has strong positions on a number of defence/security platforms with good export potential in markets outside of the US, including the European

A400M and Brazilian KC-390 aerial refuelling tankers, the Eurofighter Typhoon and the Swedish Gripen fighter aircraft.

The Group has strong technology and know-how positions in a number of aerospace and aviation markets, including large transport, regional and business jets, helicopters and smaller aircraft. It has technology positions with manufacturers such as Boeing, Airbus, Airbus Helicopters and Bombardier, as well as airline customers.

In addition to aerospace, it also has positions in the SATCOM market, where it is a leader in the marine market, and in a number of commercial land markets.

Achieving further balance across the portfolio remains a strategic objective for the Group.



### US defence/security market

Conditions in the US defence/security market in 2013 were challenging, as expected, and are likely to remain so for the foreseeable future. The Bipartisan Budget Act of 2013 has brought increased certainty to the level of US Federal spending in 2014 and 2015 and partial relief from the full impact of budget cuts mandated under the Budget Control Act of 2011.

However, ongoing pressure is still expected on the US Department of Defense investment accounts, as the bulk of the relief funding is likely to be used to reduce the backlog in training, maintenance and the readiness of the armed forces, rather than for investment in capabilities. The Group also remains cautious on medium-term prospects in this market as, based on previous down-cycles, the investment accounts may continue to drift lower, before reaching their cyclical trough.

Notwithstanding these market challenges, Cobham continues to believe that its differentiated technology and know-how, with its focus on improving communications, enhancing mobility and keeping people safe in harsh environments, remain aligned with the customers' priorities.



### Non-US defence/security markets

Demand conditions in defence/security markets outside of the US have remained subdued in Europe but there are sizeable and growing opportunities elsewhere in the world. The Group believes that overall prospects in these markets remain good, with growth being driven by regional procurement priorities and a variety of security concerns including border security, piracy, drug trafficking and terrorism.

Overall, the Group anticipates that demand in accessible non-US defence/security markets is likely to be aligned with the ongoing shift in spending away from the flat or lower growth budgets in Europe, to increasing budgets in the Middle East, Asia and other faster growth economies. The Group remains well positioned to capitalise on this trend.

Cobham's Aviation Services business has significantly enhanced its existing capabilities during the year through the acquisition of FB Heliservices (FBH), which has added rotary to its existing fixed wing capability in markets including the Middle East and the Caribbean. Going forward, this market is expected to continue to benefit from a trend towards increased outsourcing.



### Commercial markets

Cobham's differentiated technology and know-how are also used in attractive commercial markets, where it has strong and growing positions. The Group's primary commercial markets are those in specialist aviation in Australia, the marine SATCOM market, land markets globally and a range of other aerospace markets including large transport aircraft, regional and business jets, helicopters and smaller aircraft, as well as land markets globally.

Growth in Cobham's Aviation Services business in Australia is linked to the long term growth in demand for natural resources. The Group has made good progress during the year in this market, winning some significant long term orders in Australia.

Demand in other commercial markets has also increased strongly, driven by factors including aircraft production rates, a desire for increased bandwidth on air and marine platforms, and demand for smaller and lighter products which drive operational efficiency and fuel savings. The Group also benefits from an increasing desire for communication in locations that lack effective terrestrial communications and from increasingly stringent safety requirements.

### US defence/security market

Aligned to the customers' priorities



Total 37%

CAS	11%
CDS	16%
CMS	10%

### Non-US defence/security markets

Sizeable and growing opportunities across the globe

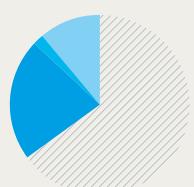


Total 28%

CAS	9%
CDS	1%
CMS	8%
CAvS	10%

### Commercial markets

Leverage technology and know-how into attractive markets



Total 35%

CAS	22%
CMS	2%
CAvS	11%

# Our Strategy and Key Performance Indicators

**Delivering on our seven strategic priorities enables us to generate sustainable top and bottom line growth, relative to the markets in which we operate, while consistently generating good free cash flow and creating shareholder value.**

## Our strategic priorities focus on

1. <b>Innovation with insight</b>	2. <b>Focus on components and subsystems</b>	3. <b>Leverage our technology</b>	4. <b>Focus on M&amp;A</b>
Improve understanding of our markets and customers' future needs, aligning PV investments with these priorities.	Remain focused on the second and third tiers of global defence/security markets, and commercial aerospace, marine and land markets.	Identify adjacent markets where our existing technology and know-how can be leveraged to meet the needs of new customers.	Use mergers and acquisitions to shift the emphasis of the portfolio ahead of market movements to remain exposed to faster growing markets.
<b>Why this is important:</b> Our differentiated technology and know-how are a key competitive advantage in our markets. Having a thorough understanding of market opportunities and our customers' future needs optimises our ability to closely align our technology investments to customer requirements.	<b>Why this is important:</b> Our innovative technology and know-how are focused on tier two (subsystems) and tier three (components) segments of our markets, where we have a competitive edge. This enables us to provide comprehensive solutions for our customers' complex technology problems.	<b>Why this is important:</b> Accessing adjacent commercial markets allows us to leverage our existing technology and know-how, thereby increasing revenue and shareholder returns. This also brings more balance to our portfolio and enables us to provide sustainable growth through business cycles.	<b>Why this is important:</b> Utilising our strong free cash flow and the Group's balance sheet, we acquire businesses that are complementary to, and reinforce, our differentiated technology and know-how. We achieve this through a rigorous and disciplined approach to investment. Our strategic objective is to use M&A to bring more balance to the portfolio.
Group PV investment  Target: 6% <b>6.2%</b> (2012: 5.3%)	Group organic revenue growth  Target: mid-single digit organic revenue growth from 2015 <b>(4)%</b> (2012: (1)%)	During the year, we invested over £150m in acquisitions, primarily Axell for up to £85m, including contingent consideration, and the £74m acquisition of the outstanding 50% stake in FBH, the helicopter joint venture. These acquisitions bring differentiated and complementary technology and know-how in growing and attractive markets.	See page 9 for more information.

5. Operational excellence	6. Programme execution	7. Invest in skills and capabilities	Key Performance Indicators
<p>Drive a culture of continuous improvement from an integrated, streamlined business through Excellence in Delivery.</p> <p><b>Why this is important:</b> Alongside financial benefits, EiD has delivered a number of significant operating and customer benefits, including improved productivity, shortened manufacturing lead times and improved levels of quality. It has resulted in a simpler, more scalable business and a sharper focus on the customer, with enhanced internal communication and collaboration.</p> <p>Operational excellence is one of a number of tools with which we drive, improve and monitor our health &amp; safety performance.</p> <p><b>Staff safety – major accident incident rate*</b> </p> <p>Target: zero</p> <p><b>326</b> (2012: 666) * Per 100,000 employees</p> <p>See pages 9 and 34 for more information.</p>	<p>Improve programme execution across customer and PV funded projects to achieve sector leading customer delivery and operational performance.</p> <p><b>Why this is important:</b> Programme management is a core competency focus and enables us to meet customer expectations and deliver growth.</p> <p>We have undertaken considerable work to enhance functional excellence in project and programme management across the diverse range of customer and internally funded activities, together with an increased focus on lifecycle management.</p> <p>See page 8 for more information.</p>	<p>Ensure the right capabilities are in place in changing markets by increasing investment to build essential skills and capabilities.</p> <p><b>Why this is important:</b> The delivery of our strategy depends on the right people, skills and capabilities being in place. We have continued to increase our investment in learning and development to build the essential skills and capabilities from which to drive future growth, by attracting, training and retaining the best talent.</p> <p><b>Voluntary staff turnover</b> </p> <p>Target: &lt;10%</p> <p><b>6.9%</b> (2012: 8.7%)</p> <p>See pages 8 and 30 for more information.</p>	<p>Cobham's progress is monitored with a score card of financial and non-financial metrics. The following are considered the most important:</p> <p>Underlying EPS growth  </p> <p>Target: high single digit</p> <p><b>(4)%</b> (2012: 3%)</p> <p>See page 24 for more information</p> <p>Operating cash conversion  </p> <p>Target: &gt;80%</p> <p><b>85%</b> (2012: 104%)</p> <p>See page 24 for more information</p> <p>Return on invested capital </p> <p>Target: &gt;10%</p> <p><b>15.3%</b> (2012: 18.1%)</p> <p>For definitions, see page 140.</p>

 Key performance indicator used by management.  
 Used as a measure for determining executive remuneration.

## Aerospace and Security

Provides aircraft and in-building communication equipment, law enforcement and national security monitoring solutions, and satellite communication equipment for land, sea and air applications.

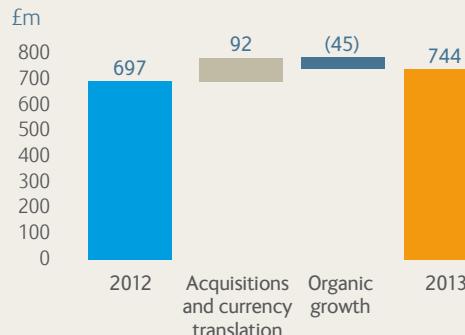
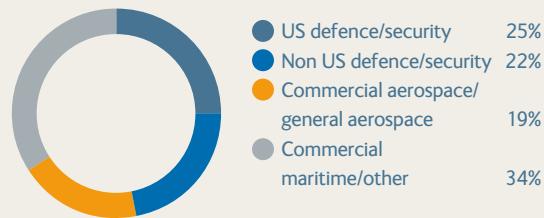
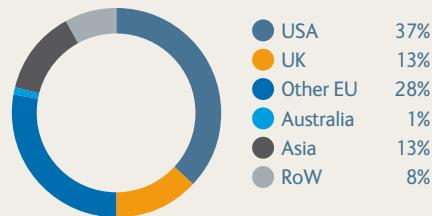


The quality, reliability and innovation demonstrated across SAILOR and SeaTel maritime based SATCOM systems, combined with a worldwide network of service facilities, ensure that Cobham Aerospace and Security meets the communication requirements of any vessel or fleet, regardless of size, application or location.

**Revenue**

Total revenue increased by £47m, or 7%, and at constant exchange rates increased by £34m, or 5%, primarily due to the 2013 acquisition of Axell and the full year impact of the 2012 Thrane & Thrane acquisition.

There was a good performance in commercial markets with revenue 6% higher, although this was offset by lower defence/security revenue resulting in a 6% decline in organic revenue.

**Divisional revenue****Divisional trading margin****Revenue by market****Revenue by geography****Other performance highlights**

- Strong revenue growth from commercial aircraft manufacturers, including first deliveries of radio communication and other products for the new Airbus A350 aircraft, which is due to enter service in the second half of 2014;
- First significant revenue generated for the hand-held 'Minehound' product for humanitarian mine clearance applications, partially offsetting lower counter-IED revenue in defence/security markets;
- Demand for the new land based Explorer 700 SATCOM terminal, offering high data rate capability, with first deliveries in 2013;
- The planned integration of the Axell acquisition has been completed and the business has performed above expectations, including securing orders to equip stadia in Brazil for the football World Cup and for the Olympics.



Development aircraft MSN3's first flight was in June 2013 with the A350 XWB entry into service expected in the second half of 2014. The A350 aircraft has a number of Cobham Aerospace and Security communication products, including SATCOM antennas and its radio and audio integrated management system.

## Defence Systems

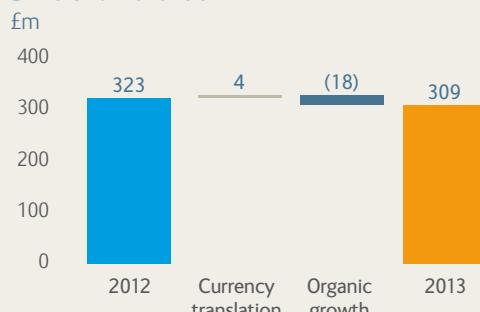
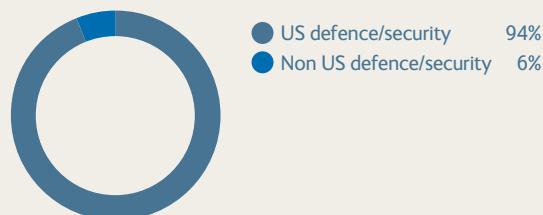
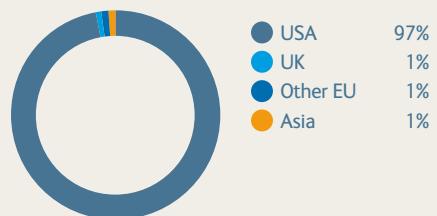
**Provides critical technology for network centric operations, moving information around the digital battlefield with customised and off-the-shelf solutions for people and systems to communicate on land, sea and air.**

Cobham Defence Systems supplies critical electronics on the standard missile which is used for ballistic missile defence, with Cobham Aerospace and Security also providing major radio frequency and microwave assemblies for the associated Aegis surveillance and fire control radar system.



**Revenue**

Total revenue fell by £14m, or 4%, and at constant translation exchange rates organic revenue was down by £18m, an organic decline of 5%. This was driven principally by reduced US defence/security spending, with the division adversely impacted by lower revenue from some land based programmes and from missile guidance systems.

**Divisional revenue****Divisional trading margin****Revenue by market****Revenue by geography**

For information on the calculation of geographic and market revenue, please see page 140.

**Other performance highlights**

- Increasing shipments of microelectronic assemblies for proprietary electronic intelligence programmes, with a strong backlog supporting continuation of revenue through to 2015;
- Award of a development contract for a major subsystem on the Air and Missile Defense Radar. This new programme upgrades the US Navy ship-board missile defense radar, with development activity continuing to 2015 and first production the following year;
- The Predator Unmanned Aerial Vehicle (UAV) successfully demonstrated a 'sense and avoid' capability utilising Cobham AESA radar panels. This capability is crucial in enabling the US Federal Aviation Administration to allow UAV access into non-segregated US airspace;
- The AMRAAM 'D' missile is nearing successful completion of its operational evaluation. Full rate production of this latest version will follow, with Cobham's content set to triple.

The Active Electronically Scanned Array (AESA) radar is the next generation of radar technology. Cobham Defence Systems has key components and subsystems for future AESA upgrades of the F-16 fighter aircraft.



## Mission Systems

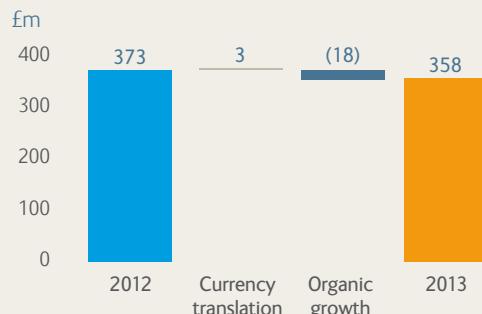
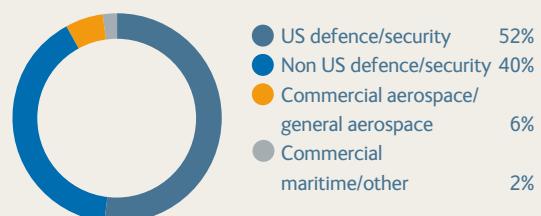
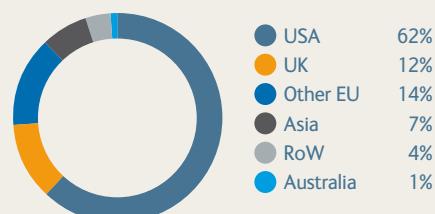
**Provides safety and survival systems for extreme environments, nose-to-tail refuelling systems and wing-tip to wing-tip mission systems for fast jets, transport aircraft and rotorcraft, and provides remote controlled robots and fully equipped bomb disposal vehicles for homeland security and military applications.**

Cobham supplies aerial refuelling equipment to every major tanker programme, including the Lockheed Martin C-130, Airbus Military A300MRTT, A400M, Boeing KC-46 and Embraer KC-390 aircraft. The UK's Voyager programme, which utilises the A330MRTT aircraft, was formally released to service in August 2013.



**Revenue**

Total revenue was £15m or 4% lower, and at constant translation exchange rates fell by £18m, an organic decline of 5%. The principal driver of this was in the US, where there was reduced revenue in the short cycle life support products. This decrease was partially offset by an increase in non-US defence/security revenue, principally relating to oxygen products and advanced bomb disposal robots. Also, in the UK there was significant revenue from the initial provision of aerial refuelling spares to the FSTA programme. This partially offset the one-off revenue milestone in 2012.

**Divisional revenue****Divisional trading margin****Revenue by market****Revenue by geography**

For information on the calculation of geographic and market revenue, please see page 140

**Other performance highlights**

- Significant revenue from the initial provisioning of aerial refuelling spares to support the UK's growing FSTA fleet;
- Increased revenue from advanced bomb disposal robots for homeland security applications, with a growing pipeline of future prospects in Europe and the Middle East;
- Deliveries of aircraft oxygen systems commenced for export to the Indian, Brazilian, Korean and Turkish military trainer aircraft programmes, along with Royal Saudi Air Force F-15 fighter aircraft. Shipments are expected to continue over the next five years;
- Qualification of Mobile Aircrew Restraint Systems and Water Actuated Release Systems for helicopters. These products protect crews from injury or death and will provide a significant revenue stream over the next five years.



The first major international order for the Cobham PHANTOM Jump Bottle System was received in late 2013, representing the next generation in military parachutist oxygen equipment. Cobham Mission Systems utilises state of the art material technology, expertise and knowledge to ensure this complex breathing system is perfectly suited to the high altitudes and harsh environments experienced by the military.

## Aviation Services

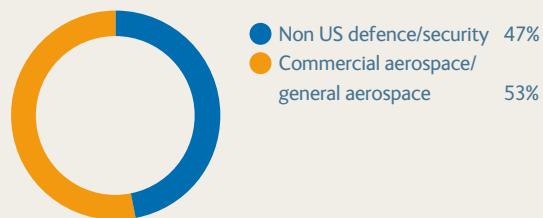
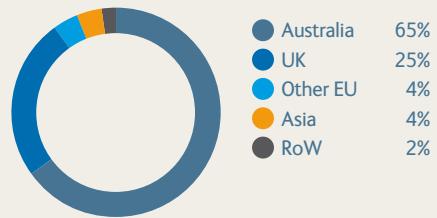
**Delivers outsourced aviation services for military and civil customers worldwide through military training, special mission flight operations, outsourced commercial aviation and aircraft engineering.**



In 2013, the UK Ministry of Defence awarded Aviation Services a five year base contract extension worth £165m through to 2019 for essential operational readiness training. Cobham has extensive understanding of front-line needs and technology know-how, providing training to service personnel operating platforms including some of the UK's most modern equipment, such as the Eurofighter Typhoon aircraft and Type 45 Destroyer.

**Revenue**

Total revenue increased by £38m due to organic growth of 3% and the FBH acquisition, which was completed in the year. This was partly offset by an adverse translation impact from the Australian dollar.

**Divisional revenue****Divisional trading margin****Revenue by market****Revenue by geography****Other performance highlights**

- Three of five additional B717 aircraft under contract for QantasLink have now entered service with the remaining two to commence operations in the first half of 2014;
- Modification of five Dash 8 surveillance aircraft for Australian Customs and Border Protection Command was completed enabling search and rescue operations as part of the Sentinel contract;
- Modification and mobilisation of three aircraft to provide ongoing support to the Ok Tedi mine in Papua New Guinea until 2019;
- FB Heliservices' transition into Cobham Helicopter Services has progressed well. Business development activities are focused on Helicopter Services' existing international footprint, with its training and support contract in Trinidad and Tobago expanded from the beginning of 2014.



During 2013, Cobham Aviation Services was awarded an AUS\$150m scope expansion to its current Boeing 717 (B717) regional QantasLink contract. This sees the fleet of B717s operated by Cobham increase from 13 to 18 aircraft and the establishment of new operating bases in Australia.



**“Cobham has delivered full year results in line with its guidance, in what has remained a challenging US defence/security market”**

## Highlights

- Group revenue increased by 2%, with acquisitions trading ahead of plan
- Incremental savings in Excellence in Delivery well ahead of plan, with site integrations being accelerated
- Technology investment increased 19% to £186m, including customer funded projects
- Solid operating cash conversion of 85%

## Summary of underlying results

£m	2013	(as restated)
Revenue	<b>1,790</b>	1,749
Trading profit	<b>318</b>	332
<i>Trading margin</i>	<b>17.7%</b>	19.0%
Underlying net finance expense	<b>(30)</b>	(32)
Underlying profit before tax	<b>288</b>	300
Underlying tax	<b>(57)</b>	(58)
<i>Underlying tax rate</i>	<b>20.0%</b>	20.0%
Underlying profit after tax	<b>231</b>	242
Weighted average number of shares (millions)	<b>1,069</b>	1,075
Underlying EPS (pence)	<b>21.6</b>	22.5

### Results

#### Orders

At the year end, the Group's order book was £2.27bn (2012: £2.40bn). At constant translation exchange rates, and after adjusting for the impact of the 2013 acquisitions, the Group's order book was 4% lower than the prior year, in part driven by the US defence/security exposed businesses. Group order intake in the year was £1,670m (2012: £1,656m).

The Group's book-to-bill ratio in the year was 0.93 times (2012: 0.95 times). The overall book-to-bill ratios in Cobham's long and short cycle businesses were both broadly in line with these trends.

Book-to-bill in the largely commercial SATCOM business reflected the anticipated flat revenue profile, ahead of the GX satellite constellation achieving global coverage by the end of 2014.

## Revenue

### Analysis of Group revenue (£m)

2012	FX translation	Acquisitions	Organic growth	2013
1,749	7	103	(69)	1,790

Total Group revenue increased 2% to £1,790m (2012: £1,749m), primarily due to the positive impacts of the 2013 acquisitions of Axell and FBH and the additional part year contribution from Thrane & Thrane, which was acquired in June 2012. Revenue from these acquisitions was, in part, offset by the divestment of the non-core emergency locator beacons businesses in 2012. There was also a favourable net foreign exchange translation impact, driven by a slight strengthening of the US dollar.

Group organic revenue in 2013 declined by 4% overall, compared to the prior year. Growth in the Group's commercial markets was strong at 7% with a good performance in Aviation Services and increasing revenue from radio and audio products, antennas and SATCOM products as large transport aircraft production volumes continued to increase.

US defence/security organic revenue was 11% lower with a significant decline in short cycle land revenue, particularly surveillance and tracking and locating products, Life Support products and counter-IED (improvised explosive device) products.

Non-US defence/security organic revenue fell by 5%, including lower revenue from the UK FSTA programme.

### Technology investment

The Group's PV investment increased in the year to £88m (2012: £75m), representing 6.2% (2012: 5.3%) of revenue. This is consistent with Cobham's previously announced plans to increase technology investment in its markets, closely aligning it to growth opportunities.

### Organic revenue growth

#### Defence/Security

**(9)%**  
(2012: (2)%)

#### Commercial

**7%**  
(2012: 2%)

#### Group

**(4)%**  
(2012: (1)%)

Total R&D investment, which includes PV investment and customer funded projects, was up by 19% to £186m (2012: £156m). The increased level of customer funding is primarily due to the ongoing significant funded development activity on aerial refuelling programmes, which is expected to increase in 2014.

### Trading profit

Group trading profit was £318m (2012: £332m). The reduction in trading profit relates primarily to the impact of the decline in revenue from short cycle US defence/security exposed businesses, most notably in the Group's Tactical Communications and Surveillance business. Total trading profit included the contributions from the Axell and FBH acquisitions in 2013, as well as the additional part year contribution from the 2012 Thrane & Thrane SATCOM acquisition. These positive contributions were partly offset by the negative impact of the divestment of the non-core emergency locator beacons businesses in 2012.

The Group's trading margin in 2013 was 17.7% (2012: 19.0%). Within this, the trading margin in organic operations fell by 0.9 percentage points. This was principally due to a combination of lower sales volumes in US defence/security businesses, increased technology and other organic investments in the business in line with the Group's strategy, and a change in the portfolio mix. These factors were partially offset by the favourable impact of EiD efficiencies. In addition, the Group's 2013 and 2012 acquisitions reduced the Group's trading margin by 0.4 percentage points.

Group statutory operating profit was lower at £159m (2012: £237m). In addition to the factors above, this was driven by higher EiD costs of £56m (2012: £38m), increased amortisation of intangible assets arising on acquisitions of £104m (2012: £69m) and a goodwill impairment charge of £63m (2012: £nil) on the Tactical Communications and Surveillance business, which experienced a significant revenue decline in the year, particularly in the US. The principal item partially offsetting the above was a gain of £62m (2012: £1m) on the revaluation of the existing equity interest in FBH, which arose at the time the Group acquired the outstanding 50% stake of the joint venture.

### Underlying net finance expense and underlying profit before tax

The Group's underlying net finance expense was £30m (2012: £32m). The net interest expense on cash and debt holdings was slightly lower at £27m (2012: £29m), partly due to the mix of fixed and floating debt in the year, offsetting higher debt levels in the second half from acquisitions and adverse foreign exchange movements. There was a non-cash net finance charge from pension schemes of £3m (2012: £3m).

In 2014, the Group's non-cash net finance charge from pension schemes is expected to be £4m.

The Group's underlying profit before taxation was £288m (2012: £300m).

# Financial Review continued

## Reconciliation of underlying profit

£m	2013	2012 (as restated)
<b>Trading profit is calculated as follows:</b>		
Results before joint ventures	<b>156</b>	230
Share of post-tax results of joint ventures and associates	<b>3</b>	7
<b>Operating profit</b>	<b>159</b>	237
Adjusted to exclude:		
Business restructuring – Excellence in Delivery	<b>56</b>	38
Movements in non-hedge accounted derivative financial instruments	<b>(2)</b>	(11)
Amortisation of intangible assets arising on business combinations	<b>104</b>	69
Impairment of goodwill	<b>63</b>	–
Revaluation gain arising on equity interests in FBH (2012: Thrane & Thrane)	<b>(62)</b>	(1)
Total operating reconciling items	<b>159</b>	95
<b>Trading profit</b>	<b>318</b>	332
<b>Underlying profit before tax is calculated as follows:</b>		
Profit before taxation	<b>127</b>	204
Total operating reconciling items as above	<b>156</b>	95
Unwinding of acquisition related discounting	<b>2</b>	1
<b>Underlying profit before taxation</b>	<b>288</b>	300
Taxation charge on underlying profit	<b>(57)</b>	(58)
<b>Underlying profit after taxation</b>	<b>231</b>	242
<b>Underlying EPS (pence)</b>	<b>21.6</b>	22.5

## Taxation

The Group's underlying tax rate is unchanged at 20.0% (2012: 20.0%), from an underlying tax charge of £57m (2012: £58m). The rate is calculated by taking the underlying tax charge and dividing it by the underlying profit before tax of £288m (2012: £300m), excluding the £3m (2012: £7m) share of post-tax results of joint ventures.

## Earnings per Share (EPS)

Underlying EPS at 21.6p (2012: 22.5p) was 4% lower at constant translation exchange rates, consistent with the Group's trading profit performance.

Basic EPS was 10.7p (2012: 16.0p).

## Cash flow

Operating cash flow, which is stated after net capital expenditure but before net interest and tax payments, was £269m (2012: £339m). The operating cash conversion rate (which is calculated by dividing operating cash flow by the Group's trading profit, excluding its share of the post-tax profits of joint ventures) was solid at 85% (2012: 104%).

Cash conversion was adversely impacted by a £32m outflow (2012: £25m inflow) in working capital in the year, which was driven by an increase in trade and other receivables. This in part reflected strong trading in December and, encouragingly, the Group's days sales outstanding remained broadly consistent with the prior year. Overall, inventory movements had no impact on cash flow, with a number of sites achieving year-on-year inventory reductions. However, this was offset by an increase in work-in-progress relating to funded aerial refuelling programmes in development. In addition, inventory increased due to the acquisitions in the year.

Capital expenditure was broadly consistent with the previous year at £61m (2012: £63m).

The Group generated £155m (2012: £241m) of free cash flow. This is stated after £51m (2012: £32m) of EID payments, net interest payments of £29m (2012: £29m) and £38m (2012: £45m) of tax payments. Dividend receipts from joint ventures fell to £4m (2012: £8m), following the Group taking full control of the FBH joint venture during the year.

Out of free cash flow, the Group paid dividends of £97m (2012: £93m) and invested a net £152m (2012: £275m) in acquisitions, primarily the acquisitions of Axell and FBH and an investment in the FSTA consortium.

## Dividends

The Board is recommending a final dividend for 2013 of 7.04p (2012: 6.40p). This, together with the interim dividend of 2.64p (2012: 2.40p), will result in a total dividend per share for 2013 of 9.68p (2012: 8.80p), an increase of 10% on the prior year, in line with the Group's long standing progressive dividend policy.

The shares will be traded ex dividend on 30 April 2014. The dividend will be payable on 30 May 2014 to all holders on the register at 2 May 2014, subject to shareholder approval.

## Treasury

The Group's treasury activities are managed centrally by the Group Treasury function, which reports to the Chief Financial Officer. The Treasury function operates within written policies and delegation levels that have been approved by the Board. It is the Group's policy that trading in financial instruments is used for financial risk management purposes only.

## Cash flow

£m	2013	2012 (as restated)
Trading profit (excluding joint ventures)	<b>315</b>	325
Depreciation, amortisation and other items	<b>61</b>	66
Pension contributions in excess of service and administration cost	<b>(14)</b>	(14)
(Increase)/decrease in working capital	<b>(32)</b>	25
Net capital expenditure	<b>(61)</b>	(63)
<b>Operating cash flow</b>	<b>269</b>	339
<i>Operating cash flow/trading profit (excluding joint ventures)</i>	<b>85%</b>	104%
Net interest paid	<b>(29)</b>	(29)
Taxation paid	<b>(38)</b>	(45)
Dividends received from joint ventures	<b>4</b>	8
<b>Free cash flow before restructuring costs</b>	<b>206</b>	273
Restructuring costs – EID	<b>(51)</b>	(32)
<b>Free cash flow</b>	<b>155</b>	241
Dividends paid	<b>(97)</b>	(93)
Acquisition payments less divestment proceeds, other related costs and loans to joint ventures	<b>(152)</b>	(275)
Net purchase of treasury shares	<b>(2)</b>	(19)
Exchange movements	<b>3</b>	18
<b>Increase in net debt</b>	<b>(93)</b>	(128)

## Debt and financing

At the year end, net debt, which comprises short term cash balances and fixed term borrowings, increased to £453m (2012: £360m). It is the Group's policy to hold a significant proportion of its borrowings in foreign currency, principally US dollars, as a natural hedge against assets and earnings denominated in those currencies, which gave rise to modest exchange rate movements at the year end of £3m (2012: £18m).

The Group has a strong balance sheet, with year end net debt/EBITDA ratio of 1.2 times, as defined under the Group's debt covenants, and interest cover of 11.9 times. Under the terms of these borrowing facilities, it is required to maintain its ratio of net debt/EBITDA at or below 3.5 times and its interest cover ratio at or above 3.0 times, and so the Group remains well within the limits contained within its debt covenant agreements.

For covenant purposes, net debt is typically expressed at average foreign exchange translation rates. EBITA, EBITDA and net interest numbers include pro forma adjustments for joint venture interests, acquisitions and disposals.

## Maturity profile of Group's outstanding debt facilities



Included within net debt are pound sterling and US dollar cash deposits, as well as borrowings which are primarily denominated in US dollars and which are held for the reasons described in the section on foreign exchange below. At 31 December 2013, the Group held total cash and short term bank deposits, all with an original maturity of three months or less, of £201m (31 December 2012: £264m).

The Group's principal borrowings include:

- A US\$360m multi-currency credit agreement, of which US\$90m expires in October 2016 and US\$270m which expires in October 2018. Interest is payable at the applicable benchmark rate of the drawn currencies plus margin, of which US\$343m had been drawn down under this agreement at the year end;
- A EUR70m loan agreement which expires in June 2017. Interest is payable at the applicable benchmark rate of the drawn currencies plus margin, of which EUR44m had been drawn down under this agreement at the year end;
- A DKK525m multi-currency credit agreement which expires in October 2017. Interest is payable at the applicable benchmark rate of the drawn currencies plus margin, of which DKK472m had been drawn down under this agreement at the year end;
- US\$359m of senior notes maturing in tranches in 2014, 2016, 2019 and 2020 with an average coupon of 6.25%; and
- US\$155m of senior notes maturing in 2017 and 2018, with an interest rate at the applicable LIBOR rate plus margin.

## Debt covenants

	Dec 2013	Dec 2012
Net debt (£m) – balance sheet	<b>(453)</b>	(360)
Net debt (£m) – average rate	<b>(480)</b>	(371)
EBITDA (£m)	<b>395</b>	408
Net debt to EBITDA (not to exceed 3.5 times)	<b>1.2</b>	0.9
EBITA (£m)	<b>322</b>	348
Net interest (£m)	<b>27</b>	30
Interest cover (to exceed 3 times)	<b>11.9</b>	11.6

# Financial Review continued

There were no significant movements in the Group's debt or facilities during the year. However, in February 2014, the Group agreed an AUS\$90m multi-currency revolving credit agreement maturing in 2018. Interest is payable on the basis of a margin over the applicable benchmark.

Further details on the Group's borrowings are given in note 19 to the Group Financial Statements.

## Foreign exchange

	2013	2012
Income statement – average rate		
US\$/£	<b>1.57</b>	1.58
AUS\$/£	<b>1.62</b>	1.53
EUR/£	<b>1.18</b>	1.23
DKK/£	<b>8.79</b>	9.18
Balance sheet – closing rate		
US\$/£	<b>1.66</b>	1.63
AUS\$/£	<b>1.85</b>	1.57
EUR/£	<b>1.20</b>	1.23
DKK/£	<b>8.97</b>	9.20

The Group's aim is to reduce, or eliminate whenever practical, foreign exchange transaction risk, of which the pound sterling/US dollar exchange rate is the most important. This is primarily because many global aerospace and defence contracts are denominated in US dollars.

Additionally, foreign exchange translation exposure arises on the earnings of operating companies largely based in the US, Europe and Australia. These are partially offset by foreign currency –

principally US dollar – denominated interest costs as the Group generally funds the acquisition of overseas companies using borrowings denominated in the same currency, which provides partial hedging of currency denominated profits.

The Group considers that the US dollar, the Australian dollar, the euro and the Danish krone are its most important foreign currencies. After taking into account the partial hedging of the Group's foreign exchange translation exposure within the income statement, a combined 10 cent movement in the average rate over one year for these currencies would result in a £10m impact on Group profit before tax. The Group estimates that the US dollar would account for approximately half of this movement.

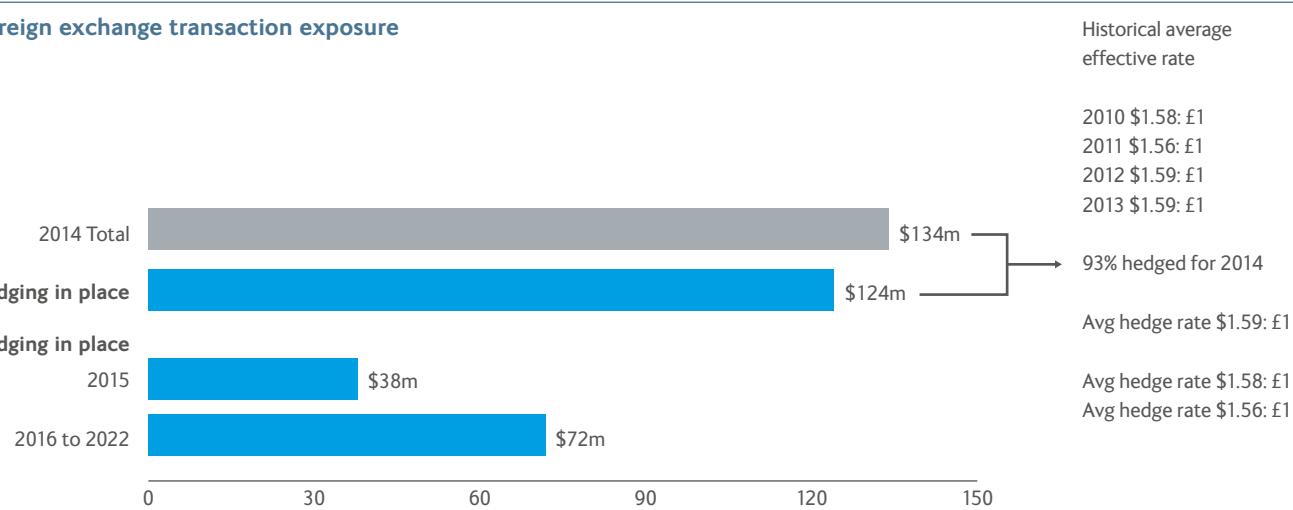
All foreign exchange hedging transactions are approved under delegated authority from the Board. A number of financial instruments are used to manage transactional foreign exchange exposure, such as forward rate contracts. The Group has a policy of hedging at least 80% of estimated transactional exposure for the next 12 months, a proportion of exposures between 12 and 36 months and firm exposures on long term contracts. Details of the most significant of these instruments are described in notes 23 and 25 of the notes to the Group Financial Statements.

Some 93% of the Group's anticipated exposure to the pound sterling/US dollar exchange rate movements is hedged for 2014 at an average rate of US\$1.59.

## Interest rates

The Group has various long and short term borrowings at both fixed and floating rates of interest. The Group continually monitors its exposure to movements in interest rates to bring greater stability and certainty to borrowing costs, with the policy being to assess

## Foreign exchange transaction exposure



the proportion of borrowings that are fixed and floating in the context of prevailing market conditions.

Note 25 to the Group Financial Statements gives more details on the financial risks facing the Group.

#### **Retirement obligations**

The Group operates a number of defined benefit schemes, the most significant being the Cobham Pension Plan (CPP). At 31 December 2013, the estimated deficit for accounting purposes between the value of the defined benefit schemes' assets and the present value of the future liabilities was £87m before deferred tax (2012: £73m).

The principal movements in the deficit before tax during the year were as follows:

	£m
Pension deficit at 1 January 2013	<b>(73)</b>
Interest charge	(3)
Actuarial loss relating to buy-in	(39)
Other actuarial gains	13
Net employer funding	15
<b>Pension deficit at 31 December 2013</b>	<b>(87)</b>

The principal movement in the pension deficit in the year was the £39m actuarial loss, relating to the CPP buy-in arrangement. Further details of this buy-in are set out below.

Other actuarial gains of £13m comprised:

- Strong investment returns on Scheme assets in the year;
- A gain from the triennial assessment of the personal demographics of Scheme members;
- These were partially offset by an increase in the assumed rate of salary rises (based on inflation), which increases the Scheme liabilities.

The £15m reduction in the deficit from net employer funding relates to employer contributions made in the year in excess of the Scheme service costs and administrative expenses.

During the year, the liabilities relating to the past service of CPP pensioners were subject to a buy-in arrangement whereby the CPP transferred assets in exchange for an insurance policy. This has eliminated the Group's exposure to interest, inflation and longevity risks associated with liabilities amounting to £242m. Following the de-risking activity carried out in 2011 on other, smaller Group schemes, 42% of total defined benefit pension liabilities are covered by insurance policies at the year end.

The Group's defined benefit pension schemes have been closed to new entrants since 2003, with alternative defined contribution schemes offered in all cases. Cobham remains committed to the support of the legacy defined benefit pension schemes within the Group and continues to work with the trustees of those schemes to ensure that net deficit issues are managed appropriately.

Further details on the Group's retirement benefit schemes, the primary assumptions, the amounts recognised in operating profit and the changes in value of defined benefit schemes during the year are given in note 24 to the Group Financial Statements.

#### **Going concern**

The Group's business activities, together with factors likely to affect its future development, performance and position, are set out in the Business overview on pages 2 to 21 and the principal risks on pages 28 to 31. In addition, notes 23 and 25 of the notes to the Group Financial Statements include the Group's objectives, policies and processes for managing its capital, financial risk management, details of financial instruments and hedging activities and its exposure to credit, liquidity and other risks.

The Group has considerable financial resources together with long term contracts with a number of customers across different geographic areas. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully.

Accordingly, after making enquiries, the Directors have formed a judgement at the time of approving the financial statements that it is their expectation that the Company and the Group as a whole have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Group and Parent Company Financial Statements.

The Strategic Report on pages 2 to 35 has been approved by the Board of Directors and signed on its behalf by:

**Simon Nicholls**  
**Chief Financial Officer**  
5 March 2014

# Principal Risks

## 2013 saw the further enhancement of the risk management process

The Board sets the policy for managing risks and recognises the importance of identifying, actively monitoring, mitigating and managing, as appropriate, the full range of financial and non-financial risks facing the business. By regularly reviewing the risk appetite of the business, the Board ensures that the Group's risk exposure remains appropriate at any point in the economic cycle and links effectively into the management of its strategic objectives. The Board has ultimate accountability for risk management systems and controls, with the Risk Committee responsible for overseeing execution of risk management processes and procedures throughout the Group. The Audit Committee has delegated responsibility for monitoring and reviewing the effectiveness of the system. More details on the role of the Audit Committee in this regard are set out on pages 44 to 47.

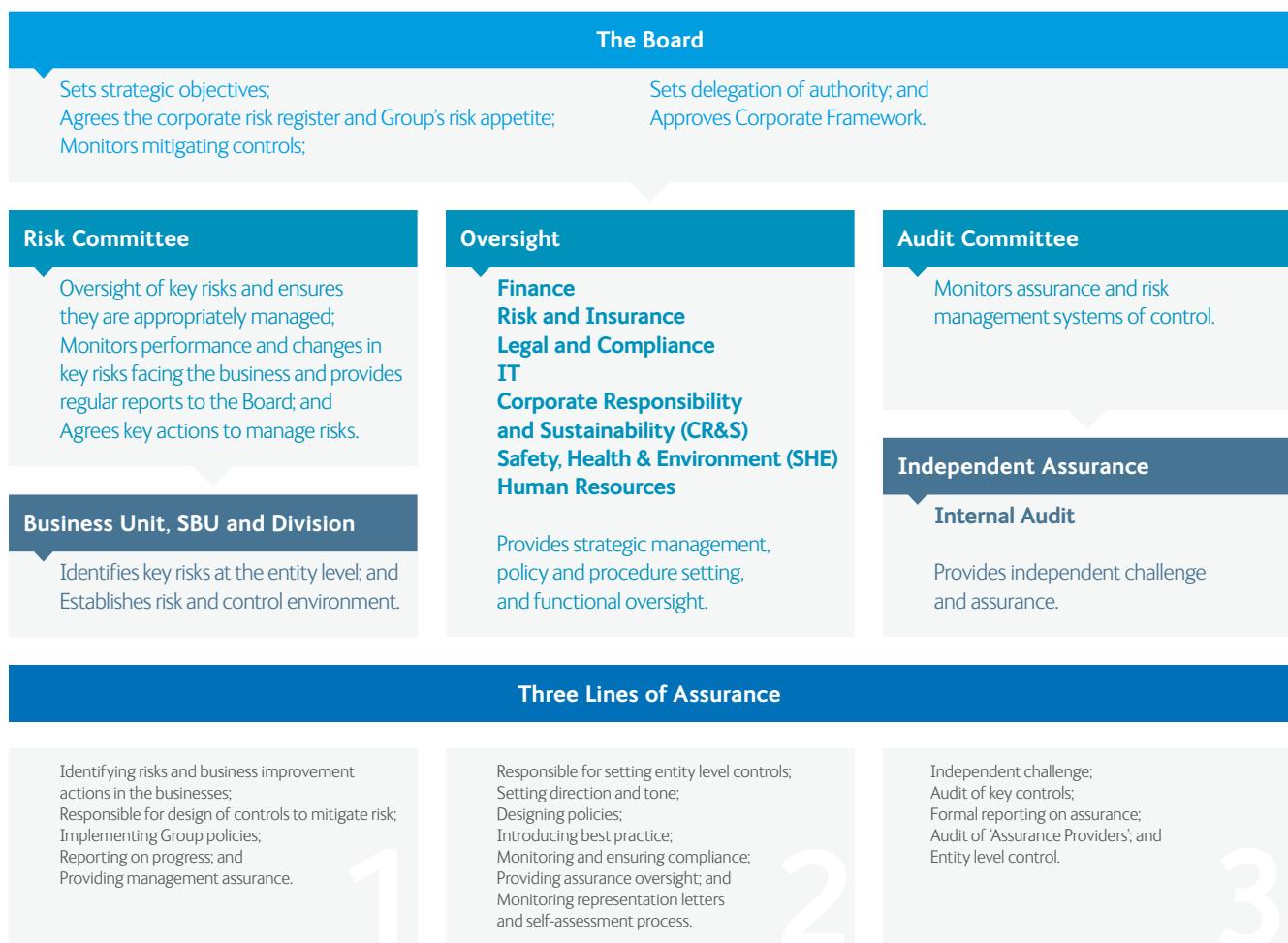
The process for monitoring and controlling risk, illustrated below, emphasises continuous evaluation and monitoring by Division Presidents, together with their respective management teams, including business unit management and functional management. The risk framework is structured to ensure that risks are identified promptly, mitigated and managed appropriately and that actions are undertaken that ensure alignment of performance with the Group's Strategic Plan.

The Group manages risk by operating a 'Three Lines of Assurance' risk and control model. The first line lies with operational management implementing and maintaining effective internal controls and risk management procedures. They are supported by a number of oversight functions which form the second line. Internal Audit is the third line, trusted with reviewing

controls and risk management processes and procedures, identifying areas for improvement and reporting to senior management and the Audit Committee. Due to its independence and objectivity, Internal Audit is able to provide reliable assurance on the effectiveness of the overall governance, risk management and internal control processes. In addition to considering the Group's Internal Audit advice, the Audit Committee takes account of the views of our independent External Audit team.

A description of the principal risks in the context of Cobham's operations, together with a description of the potential impact on the Group if unaddressed, and an outline of the actions taken to mitigate them, are set out on pages 29 to 31. The risks are not intended to be in any particular order.

## How we monitor and control risk



**1**

## Deterioration in the macroeconomic environment adversely impacting our markets

► Risk

The Group's revenue is derived from global defence/security and commercial markets. The level and type of spending is dependent on a complex mix of macroeconomic, fiscal and strategic defence and security imperatives.

► Impact

Changes in government spending could lead to programme terminations or delays, or changes in market growth.

Deterioration in demand affecting short cycle business or a fundamental shift in how customers procure products or services could have an adverse effect on the Group's future results.

► Mitigation

A review of near and long term market trends is conducted as part of the Group's strategic planning process to ensure that actual and anticipated impacts from macroeconomic environment risks are managed effectively.

Increased emphasis on identifying adjacent markets in which the Group's proven and transferable technologies can be applied.

The Group is seeking more balance in its portfolio between its defence/security and commercial markets, so it can grow through economic cycles.

The successful completion of the EiD programme together with a culture of continuous improvement will enable the Group to have sector leading operating performance, while reducing costs. This will enable it to remain competitive in the face of volume declines or price pressures and retain flexibility to adjust the cost base appropriately to changing market conditions.

Regular review of market demand data, re-forecasting and adjusting planning in line with market demand.

**2**

## Failure to execute on agreed strategy to return to sustainable organic revenue growth

► Risk

The Group's ability to generate organic revenue and associated profit growth consistently is the key driver of value creation.

► Impact

Failure to grow leads to an impaired competitive position, reduced trading margins and a declining return on invested capital.

The Group will experience reputational damage and a reduced ability to invest for future growth.

► Mitigation

Effective strategic planning, maintain robust and dynamic strategic thinking processes to ensure the Group is exposed to growth markets through the economic cycle.

Continued focus on and investment in programme management to ensure customer expectations are met underpins the Group's ability to grow.

Appropriate investment in future technologies aligned to identified market growth areas.

The Group remains focused on continuous improvement across all operations, including EiD, programme management, business development, functional excellence and strategic workforce planning.

# Principal Risks continued

**3**

## Failure to identify and execute value creating M&A to supplement organic growth

### ► Risk

Underpinning the Group's Strategic Plan is the identification of appropriate acquisition targets and the subsequent execution of value creating transactions.

**4**

## Inability to attract, retain and develop the best talent, leading to a shortage of key skills

### ► Risk

The success of the Group's strategy is dependent on its ability to attract and retain talent and skills.

**5**

## Contract risk and execution

### ► Risk

The Group designs, develops and delivers products and services that are often customised, utilising complex technologies, under fixed price contracts that are sometimes long term in nature. This gives rise to the risks of failure to execute the contract profitably, the supply of a defective or delayed product, the incurrence of other contractually related liabilities, or damage to reputation and commercial relationships.

### ► Impact

Failure to complete appropriate transactions impacts the Group's ability to generate shareholder value.

### ► Impact

Lacking all the skills necessary to execute on growth plans and deliver key customer programmes leads to reduced customer confidence in the Group and a degraded financial outlook.

### ► Impact

Failure by Cobham to execute or deliver a contract gives rise to increased programme costs, contract penalties, litigation and other financial liabilities, reduced future profitability and reputational risk.

Poor operational performance could also lead to customers withholding new and existing business from the Group.

### ► Mitigation

The implementation of rigorous M&A disciplines, aligned with the Group's strategic planning process, improves the ability to successfully execute transactions.

The Group has a rigorous post-acquisition review process to ensure that targeted returns are achieved and lessons learnt shared.

The Group continually monitors whether it has capable resources in place to manage M&A projects from origination to integration.

The Group's capital allocation strategy includes a willingness to return capital to investors, in the absence of value enhancing acquisitions.

### ► Mitigation

The Group is implementing a Strategic Workforce Plan, aligned with the Group's overall strategy, to ensure it has the right people with the right skills in the right place.

It has established an integrated management training and appraisal programme.

The Group is expanding its graduate recruitment and apprenticeships programmes.

The Group is committed to providing its employees with a safe working environment.

### ► Mitigation

A thorough review of the business case and terms and conditions, and subsequent variations, prior to signing ensures contract provisions and risks are fairly allocated between parties.

The Group has established an EVP, Life Cycle Management (LCM) and Programme Management position, to ensure its key contract and programme management policies and procedures are applied consistently and appropriately across all areas of the business, and to provide increased focus on improvements to its programme management and LCM capabilities.

Monthly reporting of progress against agreed improvement actions on LCM to the Group Executive, and semi-annually to the Audit Committee.

**6**

## Long term contract exposures to inflation, currency and commodity pricing fluctuations

► Risk

The Group's financial results are dependent on managing macro financial risks, including inflation, currency and commodity.

► Impact

Failure to manage financial risks can impact operating profit through higher costs or lower revenue and result in the Group failing to meet its financial results forecast.

► Mitigation

Currency risks are considered as part of the bid approval process on large contracts. Cobham puts currency or other hedges in place for at least 80% of estimated transactional exposure for a rolling 12 months, a proportion of exposures between 12 and 36 months and firm exposures on long term contracts.

The Group sources and manufactures in local currency whenever practicable.

The Group manages inflation and commodity pricing risks through appropriate contractual terms, with suppliers contracted on an equivalent basis to match residual risks where possible.

Minimum/maximum supplier prices are stipulated where possible to avoid unlimited exposure, when there is a risk that costs inflate ahead of revenue. Fixed price quotes are avoided for commodity related costs.

**7**

## Significant business interruption

► Risk

The Group's business could be impacted by natural disasters affecting its operational locations, by IT systems failures or by cyber attack, rendering critical systems unworkable.

► Impact

Unscheduled interruption to business activities would result in reduced profits, loss of customer satisfaction, potential cost outlays, and reputational impact.

► Mitigation

The Group maintains major incident and IT failure business continuity plans. All employees are trained in the relevant procedures.

IT security and capability are continually monitored and strengthened when needed.

The Group works closely with insurers to ensure operating infrastructure and processes include robust risk improvement activities.

**8**

## Failure to comply with laws, regulations and restrictions

► Risk

Cobham operates in a highly regulated environment and is subject to the laws, regulations and restrictions of many jurisdictions, including those of the US, the UK and other countries.

These include anti-bribery provisions, import and export controls, and government contracting rules.

► Impact

Sanctions for failure by the Group, or its sales intermediaries, or others acting on its behalf to comply with these laws, regulations and restrictions could include fines, penalties, legal claims, suspension or debarment of the Group from future government contracts for a period of time, as well as having an impact on the Group's reputation. Such sanctions could have an impact on the Group's financial position and future operations.

► Mitigation

Cobham continues to drive a culture that ensures that safety, ethics and integrity are embodied in all that it does.

Policies and procedures are included in the Group's Corporate Framework, which is regularly reviewed and audited, including procedures related to the use of sales and marketing representatives, anti-bribery and anti-corruption, gifts and hospitality, whistleblowing and investigation of ethics and compliance concerns.

Mandatory training is undertaken on a variety of compliance related subjects, including US Government contracting, anti-bribery and corruption.

# Corporate Responsibility and Sustainability

**Cobham's approach to Corporate Responsibility and Sustainability is designed to engender trust with its key stakeholders and ensure that the Company thrives over the long term.**

## Approach

Cobham believes that acting responsibly and sustainably aligns with its business strategy and creates value for all key stakeholders. The Group's strategy is to make Corporate Responsibility and Sustainability (CR&S) part of everything it does by:

1. Pursuing the highest ethical standards in all aspects of its business;
2. Building a culture in which talented employees can succeed and are rewarded;
3. Providing a safe working environment;
4. Managing the environmental impacts of the Group's products, services and operations.

CR&S covers issues identified by internal and external stakeholders (shareholders, business partners, regulators, industry bodies, employees and communities) that support or limit the Group's ability to execute its strategy and protect its reputation.

The CEO has overall responsibility for the Group's approach. He is supported by the CR&S Committee, which he chairs, in ensuring that appropriate policies, monitoring and operational systems are in place to achieve the Group's objectives. The CEO updates the Board on CR&S matters. The Board in turn assesses the significance of environmental, social and corporate governance risks and opportunities to the Group's Strategic Plan.

There is strong alignment between the Group's CR&S focus and its strategic priorities. Refer to page 12 for more details on these.

CR&S	Strategic priorities						
	1	2	3	4	5	6	7
Business ethics and compliance	•	•	•	•	•	•	•
Sustainable supply chain		•		•	•	•	•
Talent management		•	•	•	•	•	•
Diversity and inclusion	•	•	•		•	•	•
Health and safety	•		•		•	•	•
Environmental sustainability	•	•	•	•	•	•	•

Each of the focus areas are discussed in more detail below.

## Objectives and performance

**Business ethics and compliance**

**Strengthen the Group's ethics and compliance processes to ensure that employees have clear guidance to support them in making ethical decisions**

**Business ethics  
KPI:**

**100%**

of employees have completed the Code of Business Conduct training  
(2012: 99%)

Non-compliance with governmental regulations is recognised as one of Cobham's principal risks. For more detail on how this risk is being managed, see risk eight on page 31.

Cobham pursues the highest ethical standards in all aspects of its business through its ethics and compliance programme, overseen by the Business Ethics and Compliance Committee. This creates the knowledge, structures and processes to drive a culture of integrity and ethical behaviour.

The ethics and compliance programme is supported by mandatory annual training for all employees.

The Code of Business Conduct (the Code) is the cornerstone of Cobham's approach to ethics and compliance and is made available to all employees in the Group's key languages. A number of other policies support the Code in driving a culture of safety, ethics and integrity to help Cobham face the risks posed by the markets in which it operates, both sector and geographic.

The Code sets out the Group's expectations – and advice – on ethical behaviour and how to deal with possible breaches. Cobham fosters an open reporting culture reinforced by an independent third party ethics helpline.

Key supporting policies include the Anti-Bribery and Anti-Corruption (ABAC) Policy. This sets out the policy of zero tolerance towards bribery and corruption with further direction on gifts, hospitality and the use of sales intermediaries.

### Sustainable supply chain

#### Develop a responsible and sustainable supply chain that prioritises and mitigates material ethical, environmental and community risks

The Group has a number of controls and processes to mitigate issues (including human rights) that may arise in regard to the supply chain, most notably in connection with principal risk seven. Refer to page 31 for more details.

The Group outsources an increasingly significant proportion of component manufacture to suppliers, and then assembles and tests finished products in-house. Recognising the various issues that may arise, Cobham's strategy is for its supply chain to be responsible and sustainable, which also includes having regard to human rights considerations. To achieve this, Cobham has developed, in support of the Code, a Responsible Supply Chain Management Policy (RSCM), setting out its expectations for suppliers to have effective ethical, environmental and community risk management systems appropriate for the nature and scale of their business. This addresses those risks most likely to impact suppliers' ability to meet Cobham's needs.

Cobham has rolled out the RSCM policy and approach to its principal locations and is providing training and support on prioritising risks for key spend categories.

Specifically, Cobham has developed a process to report on conflict minerals present in its products to those customers required to disclose under US legislation and in anticipation of similar EU legislation, which is likely to impact Cobham directly.

Moving forward, Cobham will continue to implement its responsible supply chain management policy through training and assessment of its principal locations.

### Talent management

#### Continue to ensure the Group has the right people with the right skills to execute its strategy

##### Talent management

KPI:

**6.9%**  
voluntary staff turnover  
(2012: 8.7%)

Employee retention and development are recognised as one of the Group's principal risks. For more details on how we are managing this, see risk four on page 30.

As a high-tech engineering and service group, Cobham continues to require the highest calibre functional expertise and future leadership to deliver its business strategy. Attracting and retaining the very best is an increasing challenge as the number of science and engineering graduates is declining. A dedicated Cobham resourcing team has

increased awareness of the Cobham employer brand (Innovators with Insight) in the recruitment marketplace.

The Group's strategic high potential talent development programmes range from entry level (apprentices and graduates) to senior and functional experts aimed at developing a robust internal talent pipeline. The programmes all include rigorous assessments to ensure Cobham accesses the brightest and best individuals. Apprentice and graduate schemes commence with placement based roles to blend on-the-job training and project activity with formal learning. Many of Cobham's UK apprentices achieve recognition through national award programmes. The graduate programme aims to attract high potential individuals from targeted universities within priority disciplines.

Cobham has invested in the development of an online Learning and Development Centre (LDC). The centre provides blended learning activities that are linked to Cobham's defined competencies. During 2013, a total of 1,473 hours of learning was completed by 366 employees within the first three months of the LDC launch. A certified management programme was developed and piloted through the LDC in 2013. This will produce a consistent standard and approach to line management across the Group.

Cobham is implementing a strategic workforce planning process that will allow the business to better plan its resourcing requirements. During 2013, the Group developed a global view of its workforce by functional area and by location.

Moving forward, Cobham is planning to further expand its graduate development programme into Denmark and South Africa, utilise the strategic workforce planning data to assess its workforce requirements against business activity over the next five years, and launch its certified management programme globally.



High performing apprentices

Cobham has once again been successful in the Brathay Apprentice Challenge, reaching the 2013 finals. Cobham's apprentices regularly receive a variety of external awards for both team and individual achievements: in 2013, 27% of the apprentice population received such recognition, improving on the 8% in 2012.

# Corporate Responsibility and Sustainability continued

## Diversity and inclusion

### Benchmark the Group's diversity and inclusion against publicly available data for its comparator group

The Group is committed to equal opportunities for all its employees and aims to ensure the workplace is free from discrimination. Recruitment, selection and career development are based on competence and job requirements, irrespective of race, sex, sexual preference, religion or disability. With regard to employees who become disabled, the policy is to take all reasonable steps, including retraining, to ensure that they can remain in employment wherever practicable.

A lack of diversity and an inability to attract and retain the best talent are risks to the Group; refer to principal risk four on page 30.

Cobham has been monitoring its gender, age and ethnic diversity since 2008. In 2013, it reviewed its diversity and benchmarked itself against industry peers using publicly available data. The results showed that Cobham generally equals or exceeds them. Overall, the Group trend over the past five years has been that the percentage of women in the total workforce and in management positions has marginally declined, although recent graduate recruitment includes an increasing intake of women.

## Diversity and inclusion KPI:

13%  
female senior managers\*  
(2012: 11%)

11%  
women on the Board  
(2012: 11%)

9%  
female senior managers\*\*  
(2012: 7%)

27%  
female employees  
in the Group  
(2012: 27%)

\* Legal definition (Directors of legal entities)

\*\* Cobham's definition (Vice Presidents and above)

## Health and safety

### Continue to embed health and safety into the Group's core business processes

## Health and safety KPI:

326  
major accident incidence rate\*

(2012: 666)

\* Per 100,000 employees

Cobham is committed to providing its employees with a safe working environment and considers it key to talent retention and recruitment. Cobham addresses workplace safety, health and environment (SHE) together through the Code and SHE policy. The Group is committed to creating a culture in which all employees take responsibility for themselves, their fellow workers, contractors, visitors and the general public.

The policy is implemented through a standardised management approach. All business units are required to achieve at least a basic level of performance and follow a programme of continuous improvement. Assurance is obtained through independent peer reviews and external audits.

Progress is monitored through an Executive-led steering committee, which reports to the Group Executive and Board Audit Committee. SHE considerations are integrated into the annual strategic planning and standardised business integration processes.

A review of the way in which the Group resources SHE was undertaken in 2013 and, as a result of this review, actions will be taken to strengthen the SHE function over the coming years.



SHP-IOSH awards finalist

Cobham Antenna Systems in Marlow, UK was a finalist in the prestigious Institute of Occupational Safety and Health Awards for Safety in Manufacturing following the success of a zero harm initiative that has improved the site's SHE culture.

**Environmental sustainability****Reduce the Group's environmental impacts and mitigate the environment's impact on the Group**

**Greenhouse gas emissions**  
**KPI:**

**51 tonnes**

Total Scope 1 carbon dioxide equivalent per £m turnover\*  
(2012: 54 tCO<sub>2</sub>e/£m)

**27 tonnes**

Total Scope 2 carbon dioxide equivalent per £m turnover\*  
(2012: 30 tCO<sub>2</sub>e/£m)

**228 tonnes**

Total Scope 3 carbon dioxide equivalent per £m turnover\*  
(2012: 214 tCO<sub>2</sub>e/£m)

\* Scope one, two and three are further explained within the Directors' Report, page 66.

The Group has a number of mitigating actions in place to reduce the risks associated with environmental sustainability. See principal risk seven on page 31.

Cobham's SHE policy sets out its commitment to environmental sustainability through product stewardship (from resource extraction to end-of-life), resource efficiency and climate change initiatives. With respect to the environment, Cobham's aim is to continuously improve its resource efficiency (raw materials, energy and natural resources) and reduce its use of hazardous substances wherever possible.

Cobham often designs products which are smaller, lighter and less power consumptive than competitors' products. In doing so, it has an opportunity to generate significant benefits for its customers and the environment. This objective is being built into the principal locations' standardised design review processes.

Hazardous Materials legislation is having an increasing impact on industry by phasing out certain materials at a pace quicker than viable alternatives can be identified, tested and certified for use. Cobham is actively monitoring the impacts of this legislation and engaging regulators to develop suitable solutions through its industry association memberships.

Climate change is affecting the Group's regulatory regime and operations to varying degrees based on geography and market. The principal impacts relate to product, facility and supply chain resilience. The majority (84%) of Cobham's direct Scope 1 and 95% of Cobham's indirect scope 3 greenhouse gas emissions come from aviation fuel consumption in the Aviation Services business.

As Aviation Services successfully grows, by operating more aircraft or achieving higher utilisation of the existing fleet, energy consumption will also increase. Management of the Group's aviation and non-aviation emissions are therefore separated. Aviation fuel use intensity (fuel burn per operational flying hour for all aircraft) is now reported in addition to facility energy use intensity. Details of the Group's greenhouse gas emissions data are included on page 66 of the Directors' Report.

Moving forward, Cobham will continue to target reduced impacts from its products, facilities and supply chain on the environment and to manage the impact of the environment on the Group.



Facility resilience award

Cobham and its insurers, FM Global, have won an Insurance Partnership of the Year award from Continuity, Insurance and Risk magazine.

Over the past eight years, Cobham and FM Global have been working together to ensure the Group's principal locations reach and maintain the coveted Highly Protected Risk status through compliance with FM Global standards.

This level of business continuity management enables our principal locations to mitigate the risks associated with adverse weather events such as flooding.

► Further detail on Cobham's CR&S approach, objectives and performance is available at [www.cobhamsustainability.com](http://www.cobhamsustainability.com).

# Board of Directors



1. J Devaney

**Non-executive Chairman**  
**BEng, CEng, FIMechE, FIEE**  
Age 66

**Appointed:** Director February 2010,  
Chairman May 2010

**Skills and experience:** John's executive career was built in engineering companies within the Verity Group. John has previously served as Non-executive Director of Northern Rock Asset Management (between 2007 and 2010) and Chairman of Marconi plc, later renamed Telent. He was President of Perkins Engines in the mid-1980s, and he went on to be President of Kelsey-Hayes, the automotive components manufacturer. He was subsequently Chief Executive of Eastern Electricity, the largest regional electricity company in the UK at the time. Following its acquisition by Hanson, he was appointed Executive Chairman of Hanson. John retired from his role as Non-executive Chairman of National Express Group plc on 31 January 2013.

**External appointments:** Non-executive Chairman of NATS, the National Air Traffic Services.

**Committee membership:** Chairman of the Nomination Committee.



2. R (Bob) Murphy

**Chief Executive Officer, Executive Director**  
Age 56

**Appointed:** June 2012

**Skills and experience:** Bob was with BAE Systems for 13 years from 1999, serving as a member of the Executive Committee of BAE Systems plc as Executive Vice President for the global operations of the Product Sectors business for BAE Systems, Inc. including its Electronic Systems, Land & Armaments and Platform Solutions sectors. He has also held a number of other senior operational and financial roles with BAE Systems. Prior to this, Bob spent 18 years with General Electric where he held numerous financial leadership positions, culminating in his role as CFO of the military engines operation of the GE Aircraft Engines Group. Previously, Bob has served on the Board of Trustees for the US National Defense Industrial Association and the Board of Visitors for the Clark School of Engineering at the University of Maryland.

**External appointments:** None.

**Committee membership:** Executive Directors Committee.



3. S Nicholls

**Chief Financial Officer, Executive Director**  
**BSc (Hons), ACA**  
Age 49

**Appointed:** May 2013

**Skills and experience:** Simon was CFO of Senior plc, the FTSE 250 international manufacturing group providing engineered products for aerospace, defence and commercial industrial applications, a position he held from 2008. Previously, Simon was CFO of Hanson North America and prior to that he was Financial Controller for Hanson plc for three years. Simon spent nine years with Price Waterhouse, now PwC, in the UK and Canada, and four years working in senior financial positions. Simon served as a Non-executive Director of AIM listed Hamworthy plc from September 2011 until its takeover in February 2012. Simon is a Chartered Accountant, holding a Bachelor of Science degree in Mathematics, Operational Research, Statistics and Economics from the University of Warwick.

**External appointments:** None.

**Committee membership:** Executive Directors Committee.

## Independent Directors



4. M Wareing

**Senior Independent Non-executive Director**  
**CMG, FCA, FCCA, MCSI**  
Age 60

**Appointed:** December 2010

**Skills and experience:** Michael worked for KPMG from 1973 until 2009 when he retired. Between 2005 and 2009, he was International Chief Executive Officer, KPMG, Chairman, KPMG International Executive Team, and Chairman, KPMG Iberoamerica Board. He was formerly the Prime Minister's Envoy for Reconstruction in Southern Iraq.

**External appointments:** Non-executive Director and Chairman of the Audit Committee of Wolseley plc and Senior Independent Non-executive Director and Chairman of the Audit Committee of Intertek Group plc. Economic Development Adviser to the Government of Afghanistan.

**Committee membership:** Chairman of the Audit Committee and member of the Nomination Committee.



5. J Patterson

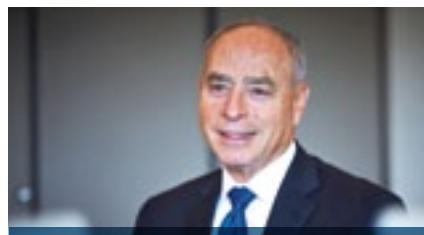
**Independent Non-executive Director**  
**CBE, MBChB, FRCP, FMed Sci**  
Age 66

**Appointed:** November 2005

**Skills and experience:** John qualified in medicine in 1971 and obtained a Membership (now Fellowship) of the Royal College of Physicians in 1974. He joined ICI (now AstraZeneca) in 1975 and in December 2004 was appointed to the main Board as Executive Director responsible for development. He retired as a Director of ICI in March 2009. He is a former President of the Association of the British Pharmaceutical Industry, a former Non-executive Director of Amersham plc and a former member of the supervisory Board of the UK Medicines Control Agency.

**External appointments:** Non-executive Director of Ferring Holding SA.

**Committee membership:** Chairman of the Remuneration Committee and a member of the Nomination Committee.



6. M Ronald

**Independent Non-executive Director**  
**CBE, BA, BScEE, MScEE**  
Age 72

**Appointed:** January 2007

**Skills and experience:** Mark was, until his retirement at the end of 2006, Chief Operating Officer of BAE Systems plc and Chief Executive Officer of BAE Systems, Inc., its wholly-owned US subsidiary. Previously, he was Vice-President, Programme Management with Litton Industries and Chief Operating Officer of AEL Industries. Mark was a Non-executive Director of ATK Inc.

**External appointments:** Non-executive Director of Beechcraft Holdings LLC and Aeroflex Holdings, Inc., senior adviser of Veritas Capital LLC and a management consultant.

**Committee membership:** Member of the Nomination and Remuneration Committees.

## Independent Directors continued



**7. M Hagee**

**Independent Non-executive Director**  
Age 69

**Appointed:** December 2008

**Skills and experience:** Mike served in the US Marine Corps for almost 39 years ending his career in 2007 as Commandant of the Marine Corps and a member of the Joint Chiefs of Staff. His numerous military assignments included Commanding General, 1st Marine Expeditionary Force, Deputy Director of Operations at the US European Command and Executive Assistant to the Director of Central Intelligence. He also served in a number of diplomatic missions including the presidential diplomatic mission to Somalia.

**External appointments:** President and CEO of the Admiral Nimitz Foundation in Fredericksburg, Texas, US, Co-Chairman of the National Security Advisory Council for the Center of US Global Engagement and US Global Leadership Campaign, Non-executive Director of SGI Corp., Kaseman LLC, DynCorp International Inc. and Freedom Group Inc., and Outside Director on the Government Security Committee of the Special Security Agreement of TE SubCom, a TE Connectivity Limited company.

**Committee membership:** Member of the Audit and Nomination Committees.



**8. A Wood**

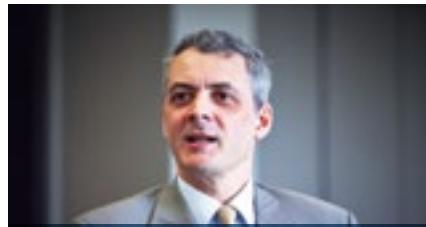
**Independent Non-executive Director**  
MA, MBA  
Age 50

**Appointed:** July 2011

**Skills and experience:** Alison is currently engaged with a mix of not for profit and non-executive activities. She was formerly Global Director Corporate Development & Strategy for National Grid plc. Previously, she was Group Strategic Development Director for BAE Systems plc responsible for corporate strategy, mergers and acquisitions and strategic business development across the UK and US. She has held three previous Non-executive Directorships: BTG plc from 2004 to 2008, THUS plc from 2007 to 2008 and GCHQ from 2009 to 2011.

**External appointments:** Chairman of Aerospace, Aviation and Defence Knowledge Transfer Network. Appointed Non-executive Director and Senior Independent Director of e2v technologies plc, 17 July 2013. Appointed Non-executive Director of Costain plc, 1 February 2014 and will become Chair of their Remuneration Committee from 1 April 2014.

**Committee membership:** Member of the Remuneration and Nomination Committees.



**9. D (Jonathan) Flint**

**Independent Non-executive Director**  
CBE, MBA, BSc, FREng, FInstP  
Age 53

**Appointed:** May 2013

**Skills and experience:** Jonathan is currently Chief Executive of Oxford Instruments plc, a leading provider of high technology tools and systems for research and industry, a position he has held since 2005. Prior to this, he was the UK Managing Director of Vislink plc and has also held management positions with BAE Systems and GEC Marconi Avionics. A physics graduate from Imperial College London, Jonathan was made a CBE in 2012.

**External appointments:** Chief Executive of Oxford Instruments plc. Jonathan was appointed as a Non-executive Director of Andor Technology plc, in January 2014.

**Committee membership:** Member of the Audit and Nomination Committees.

## Board meeting attendance for 2013

	Number of meetings attended/held
J Devaney	9/9
R Murphy	9/9
S Nicholls <sup>1</sup>	5/5
W Tucker <sup>2</sup>	4/4
M Beresford <sup>3</sup>	4/4
M Hagee	9/9
J Patterson	9/9
M Ronald	9/9
M Wareing <sup>4</sup>	8/9
A Wood	9/9
D Flint <sup>5</sup>	5/5

<sup>1</sup> S Nicholls appointed on 1 May 2013.

<sup>2</sup> W Tucker retired from the Board on 1 May 2013.

<sup>3</sup> M Beresford retired from the Board on 25 April 2013.

<sup>4</sup> M Wareing had been hospitalised before the February meeting, which he could not attend.

<sup>5</sup> D Flint appointed on 1 May 2013.

## STRUCTURE OF THE REPORT

The section that follows on corporate governance is intended to give shareholders a clear and comprehensive picture of the Group's governance arrangements and how they operated during the year. Page 39 sets out details of the areas of the Board's focus during the year, while descriptions of how the Group complied with each Principle and Provision of the UK Corporate Governance Code are set out on pages 68 and 69.

# Corporate Governance Report

This part of the Annual Report and Accounts, together with the Directors' Remuneration Report set out on pages 48 to 63, describes how the Company has applied and complied with the principles contained in the UK Corporate Governance Code published in September 2012 (the Code). The Code is published by the Financial Reporting Council and is available from its website [www.frc.org.uk](http://www.frc.org.uk). A high level summary of our compliance with the Code is shown on pages 68 and 69.

## Statement of compliance with the provisions of the Code

The Ordinary Shares are listed on the London Stock Exchange. In accordance with the Listing Rules of the UK Listing Authority, the Company confirms that, throughout the year ended 31 December 2013 and at the date of this Annual Report and Accounts, it was compliant with the provisions of the Code.

## Share capital

Details of the share capital of the Company and the powers of the Directors in relation to allotment, issue and market purchase of shares are given in the Directors' Report on page 64.

## The Board composition

The Board comprises a Non-executive Chairman (John Devaney), a CEO (Bob Murphy), a CFO (Simon Nicholls) and six other Non-executive Directors of whom Mike Wareing is the Senior Independent Director. All Non-executive Directors are considered to be independent and the Chairman was considered to be independent on appointment. They all held office throughout the year except Simon Nicholls and Jonathan Flint, who both joined the Board on 1 May 2013. Warren Tucker, the former CFO, stood down from the Board on 1 May 2013. Marcus Beresford stood down from the Board, having completed nine years as a Non-executive Director, at the conclusion of the 2013 AGM.

Biographies of the Directors, giving details of their experience and other significant commitments, are set out on pages 36 and 37. The wide ranging experience and backgrounds of the Non-executive Directors enable them to support, debate and constructively challenge management in relation to both the development of strategy and the performance of the Group. The attendance of Directors at Board meetings is set out on page 37 and attendance at principal Board committee meetings as members of such committees during the year is set out in the reports from each committee on pages 42, 44 and 48.

Non-executive Directors are appointed for specified terms of three years, which can be extended by agreement provided that the individual's performance continues to be effective. The rules for the appointment and replacement of Directors are set out in the Company's Articles of Association (the Articles), copies of which can be obtained from Companies House in the UK or by contacting the Company Secretary. Changes to the Articles must be approved by shareholders passing a special resolution. The Directors and the Company (in the latter case by ordinary resolution) may appoint a person who is willing to act as a Director, either to fill a vacancy or as an additional Director.

All Non-executives have confirmed they have sufficient time to meet their time commitments to the Group. Copies of their appointment letters are available on request to the Company Secretary and will be available for inspection at the AGM.

In accordance with the Code, which recommends that all Directors of FTSE350 companies seek re-election by shareholders on an annual basis, all Directors currently in office will retire and seek re-election at the AGM. In addition, Simon Nicholls and Jonathan Flint, who were appointed to the Board on 1 May 2013, are seeking election by shareholders at the 2014 AGM for the first time.

The Board has set out in the circular a resolution to elect Simon Nicholls as an Executive Director and Jonathan Flint as a Non-executive Director and explains why it believes they should be elected. The Chairman confirms to shareholders when proposing election or re-appointment that the individual's performance continues to be effective and that the individual continues to demonstrate commitment to the role. Non-executive Directors are subject to Companies Act provisions relating to the removal of a Director.

The Chairman is, among other things, responsible for chairing Board meetings and leading the Board. The CEO's responsibilities include development and implementation of the Group's strategy, operational performance and corporate social responsibility. He also focuses on long term growth and development of the Group, its people and customer relationships. The Board's policy is that the roles of Chairman and CEO should be performed by different people.

The Senior Independent Director's responsibilities include the provision of an additional channel of communication between the Chairman and the Non-executive Directors. He also provides another point of contact for shareholders if they have concerns that communication through the normal channels of Chairman, CEO or CFO has failed to resolve, or where these contacts are inappropriate.

Marcus Beresford stood down as Non-executive Director and Senior Independent Director at the conclusion of the 2013 AGM. The role of Senior Independent Director was assumed by Michael Wareing following Marcus' retirement.

## The Board and its proceedings



Dear Shareholder

As I mention in my Chairman's Statement earlier in this report, 2013 has been a year of significant activity. The Board has been busy refining the strategic objectives and ensuring the structure is in place to position the business to achieve the Group's Strategic Plan.

EiD is transitioning to continuous improvement initiatives and the streamlining of business operations continues.

The key focus for the Board during 2013 has been supporting the Executive Directors, both of whom are relatively new to the Group, to put in place the strategic enablers needed to achieve the Group's Strategic Plan. This has involved revisiting the constitution of the senior management team with more emphasis placed on customer relationships, operational excellence and the development of our talent.

Our markets in 2014 will continue to challenge and we will continue to work hard to respond to those challenges. I trust we can rely on your support for the foreseeable future.

**J Devaney**  
Chairman

### Overview

#### Role and focus

The Board's main duties are to:

- Lead the Group with a view to the creation of strong, sustainable financial performance and long term shareholder value;
- Review and agree Group strategy;
- Ensure that the necessary resources are in place;
- Monitor management performance; and
- Supervise the conduct of the Group's activities within a framework of prudent and effective internal controls.

#### Highlights of 2013

- The Board and senior management devoted additional time to the further development of the Group's strategy;
- Talent and succession planning has been high on the agenda, with various initiatives implemented to ensure we have the right resources to deliver our strategic objectives;
- Approved the acquisition of the Axell and FB Helservices groups of companies;
- Overseen the search and appointment of a new CFO;
- Overseen the restructuring of the senior management group;
- Evaluated and approved six large bid submissions above authority limits delegated to the Executive Directors outside of the regular Board meeting agenda; and
- Monitored the progression of the EiD programme and approved the transition to a continuous improvement initiative, with resource within the business to progress this further.

#### Priorities for 2014

- Review performance against agreed strategic enablers;
- Continued focus on market evaluation and strategic development;
- Continued rebalance of the portfolio towards the commercial market; and
- Oversight of Strategic Workforce Plan and organisational realignment.

Board meetings, scheduled in accordance with the annual timetable, take place five times a year on a face to face basis, four times a year by telephone and otherwise as required. There is contact between meetings to progress the Group's business as required. Meetings were held at the head office in Wimborne, at the Company's London office and at an international operational location (Exeter in the US). In addition, the Senior Independent Director held a meeting with the Non-executives in the absence of the Chairman to appraise the Chairman's performance. The Chairman has held meetings with the Non-executives in the absence of the Executive Directors.

The Board's role is to lead the Group with a view to the creation of strong, sustainable financial performance and long term shareholder value.

The Board has adopted a schedule of matters reserved for its specific approval. The schedule provides the framework for those decisions which can be made by the Board and those which can be delegated either to committees or otherwise. Among the key matters on which the Board alone may make decisions are the Group's business strategy, its five year plan, its consolidated budget, Group policies, dividends, acquisitions and disposals, and all appointments to and removals from

# Corporate Governance Report continued

Evaluation year	Observations	Actions taken
2012	The risk management process needs to be strengthened with clear delineation between the work of the Risk and Audit Committees and the Board.	The Risk Committee was strengthened during 2013 with the membership expanded to include the Group Executive. The risk appetite statement was considered, approved and published during the year.
	More rigour should be placed around paper compilation and submission.	The substance of reports was improved and a standard reporting format adopted, introducing a more timely and efficient process.
	Senior management objectives need to be visible to the Board to support talent and succession planning.	Objectives for the Group Executive were presented to the Board for review. Opportunities for the Board to meet members of the Cobham high potential programme will continue to be pursued.
2013	Members of the Group Executive should be provided with opportunities to present to the Board on their areas of the business to provide more exposure to the Board members.	Presentations from the Group Executive to be built into the Board Work Plan for 2014.
	Continued development of the strategic planning process.	A two day Board meeting in 2014 has been added to the Board schedule, with the business of that meeting devoted purely to strategy. Ongoing strategic updates form part of the rolling Board agenda.

the Board. Authority is delegated to management on a structured basis in accordance with the provisions of the Corporate Framework ensuring that proper management oversight exists at the appropriate level. Matters delegated in this way include, within defined parameters, the approval of bids and contracts, capital expenditures and financing arrangements.

The Board has adopted procedures relating to the conduct of its business, including the timely provision of information, and the Company Secretary is responsible for ensuring that these are observed and for advising the Board on corporate governance matters. The Company Secretary is appointed, and can only be removed, by the Board.

If a Director were to have a concern which cannot be resolved, it would be recorded in the Board minutes. On resignation, Non-executive Directors are invited to provide a written statement to the Chairman for circulation to the Board if they have concerns. No such statements were made during 2013.

All potential situational and transactional conflicts of interest are disclosed, noted and authorised. Procedures are in place and operating effectively to keep such disclosures up to date.

## Performance evaluation

The Board conducts an evaluation of its activities on an annual basis. During 2013, the Board and its committees undertook an internal evaluation. The evaluation included the circulation of a questionnaire. The Board considered the output and has approved an action plan to address issues arising.

A table of actions instigated by this and the previous performance evaluation is included above.

## Financial reporting

In the Directors' view, the Annual Report and Accounts for 2013, together with the interim management statements, the interim report and other reports made during the year, present a fair, balanced and understandable assessment of the Group's position and prospects.

The Directors have adopted the going concern basis in preparing the Annual Report and Accounts as stated in the Financial Review on page 27.

## Shareholder relations

A summary of the 2013 activity by our Investor Relations team is shown below.



\*Interim Management Statement is a short quarterly update on the Group's trading, significant events and financial position.

A full programme of engagement with investors and analysts, both in the UK and overseas, is undertaken each year by the CEO, CFO and Director of Investor Relations, including presentations, industry exhibitions, roadshows and site visits. Site visits are hosted by senior members of management within the business units and are intended to give investors detailed insight and access to the business' operations.

The Board is accountable to shareholders for the performance and activities of the Group and engages in regular dialogue with them. During the year, the CEO and the CFO held regular meetings with shareholders to discuss information made public by the Group. A wide range of business and corporate governance topics were discussed with institutional investors during the year as part of the investor relations programme. These included Cobham's overall performance, the Group's markets, particularly with respect to the development of the US Department of Defense budgets, progress on the Group's EID programme, progress against the Group's strategic objectives, changes in senior management and cash deployment including dividends, share buy-backs and mergers and acquisitions.

The Non-executive Chairman and the Senior Independent Director are available to meet with major shareholders at any time. The Chairman met with four of the top five shareholders during October 2013 and gave them an opportunity to raise any concerns they had with communications, ethics and/or governance. In summary, those met raised no concerns and were very pleased with business performance. The Chairman of the Remuneration Committee also consulted with major shareholders during the year with regards to executive remuneration arrangements.

Presentations were given on the day of the announcement of the interim and preliminary results. The presentations were accompanied by a live webcast for shareholders unable to attend in person. Copies of the associated presentation materials, together with webcasts, can be accessed at [www.cobhaminvestors.com](http://www.cobhaminvestors.com). Presentations are conducted in accordance with the FCA's Disclosure Rules on the dissemination of inside information.

The Board receives a report from the CFO at each of its meetings on investor relations generally, including significant changes to shareholdings, meetings with and feedback from shareholders and research published on the Group. The Board also received an independent report during the year outlining how institutional

investors regard the Group, its strategy, markets, businesses, financial position, capital allocation, governance, communications, valuation and investment standing.

Communication with shareholders also takes place via RNS announcements, the Group's website, the Annual Report and Accounts, the interim management statements and the AGM. The AGM is attended by all Directors and shareholders have the opportunity to question the Board on its stewardship of the Group and to meet the Directors informally. The results of the votes on the resolutions proposed at the AGM are published on the Group's website at [www.cobhaminvestors.com](http://www.cobhaminvestors.com).

### **Responsibility statements**

Statements relating to the responsibilities of the Directors are on page 67 and those relating to the auditors are on pages 73 and 126.

The Board is supported in its work by a number of committees. The Company Secretary acts as secretary to all Board committees. Committee chairmen provide oral reports on the work undertaken by their committees at the following Board meeting. Information relating to the Nomination and Audit Committees appears below and the activities of the Remuneration Committee are described in the Directors' Remuneration Report on pages 48 to 63. All Board committees are provided with sufficient resources to undertake their duties.

The other principal Board committee is the Executive Directors Committee. The Executive Directors are members of this Committee under the chairmanship of the CEO. The purpose is to assist the CEO in the performance of his duties and its terms of reference include establishing and implementing internal policies, systems and controls to ensure that potential inside information is communicated to it, considered, verified and released to the market where required, the discharge of obligations arising under the Company's share plans, the determination of the remuneration of the Non-executive Directors, the approval of banking facilities and the approval of bids and contracts. This Committee met on 28 occasions during the year and, in addition, as required to respond to business needs and market conditions.

The Group Executive Committee and the other principal management committees are shown in the table below.

Board of Directors							
Audit Committee	Nomination Committee	Remuneration Committee	Executive Directors Committee				
The Board is ultimately responsible for corporate governance and the Group's system of internal control, with day to day responsibility resting with management.	Group Executive (incorporating the Risk Committee)						
	Contract Bid Approval	Merger & Acquisitions	Corporate Responsibility & Sustainability	Business Ethics & Compliance	Internal Audit Sub-committee	Talent Board	Safety, Health & Environment

● Principal Board Committees

● Management Committees

# Corporate Governance Report continued

## Nomination Committee



Dear Shareholder

A key focus during 2013 has been the appointment of two Directors, one Executive, one Non-executive. Both of these appointments were managed in conjunction with Korn/Ferry Whitehead Mann, recruitment consultants who have signed up to the voluntary Code of Conduct for executive search firms. Korn/Ferry provided a shortlist of candidates for these roles. The shortlisted candidates were interviewed by myself and separately by Mike Wareing, Alison Wood and John Patterson before meeting the Executive Directors.

As mentioned last year, a fresh look at talent and succession further down the management chain has been undertaken during the year and significant progress made, which has been described in the talent management section of the CR&S report on page 33.

A handwritten signature in black ink, appearing to read "J Devaney".

**J Devaney**  
Nomination Committee Chairman

### Overview

#### Membership and attendance

	Number of meetings attended/held
J Devaney (Chairman)	4/4
M Beresford <sup>1</sup>	2/2
D Flint <sup>2</sup>	2/2
M Hagee	4/4
J Patterson	4/4
M Ronald	4/4
M Wareing <sup>3</sup>	3/4
A Wood	4/4

<sup>1</sup> M Beresford retired from the Board (and hence the Nomination Committee) on 25 April 2013.

<sup>2</sup> D Flint joined the Nomination Committee on joining the Board on 1 May 2013.

<sup>3</sup> M Wareing had been hospitalised before the February meeting, which he could not attend.

#### Other attendees

CEO, by invitation.

#### Role and focus

The Nomination Committee's main duties are to:

- Review the structure, size and composition of the Board; and
- Consider succession planning for Directors and other senior executives.

#### Highlights of 2013

- Evaluated the balance of skills, knowledge and experience of the Board;
- Considered external appointments to subsidiary boards;
- Considered succession planning to ensure the Group is well positioned for the future;
- Conducted a thorough and comprehensive search for two new Non-executive Directors, one yet to be appointed; and
- Conducted an effectiveness review.

#### Priorities for 2014

- Conclude Non-executive Director search to replace John Patterson who will stand down at the conclusion of the 2014 AGM.

The Committee's terms of reference, which were reviewed during the year, are available on the Company's website at [www.cobhaminvestors.com](http://www.cobhaminvestors.com) or on application to the Company Secretary.

The Committee is cognisant of the need for diversity, including gender diversity, when considering the composition of the Board. In recruiting for Board roles, targets have been set around ensuring a proportion of female applicants are included in the candidate pool for Non-executive Director positions. For the recent recruitment, the profile has included the requirement for a diverse geographical background and commercial market experience. Elsewhere in the business, diversity in the workforce is taken very seriously and a full report on current strategy is set out in the diversity and inclusion section in the CR&S report on page 34.

The current Board composition, in relation to the Non-executive Directors, as of 31 December 2013, is set out in the table below identifying the skills and experience of the Board members.

#### Succession planning

Succession planning takes place at Board and senior management level on a regular basis to ensure that the Group is managed by executives with the necessary skills, experience and knowledge. The Board has a role to play in overseeing the development of management resources in the Group. Specifically, the Board wants to see depth and quality in management and robust processes are in place to help the Board in this task.

Succession planning for Non-executive Directors is based on maintaining a depth of knowledge and experience on the Board. The Nomination Committee actively manages Non-executive Director succession, having regard to anticipated retirement dates for existing Directors, and initiates focused searches for Non-executive Directors as positions are required.

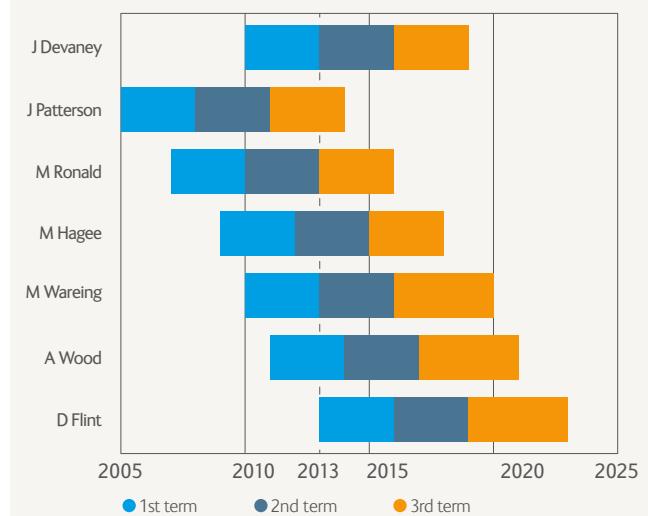
The current Board composition in relation to the Non-executive Directors, as of 31 December 2013, in terms of length of service and current term is shown diagrammatically in the table adjacent.

#### Directors' professional development

On appointment, Directors undertake a structured induction programme, in the course of which they receive information about the operations and activities of the Group, the role of the Board and the matters reserved for its decision, the Group's corporate governance practices and procedures and their duties, responsibilities and obligations as Directors of a listed public limited company. This is supplemented by visits to key locations and meetings with, and presentations by, senior executives.

Training for Directors is available as required and is provided mainly by means of external courses, internal computer based training, briefing from specific consultants or in-house presentations. In addition, Directors' knowledge of the legal and regulatory environment is updated through the provision of information by the Group's advisers and by means of regular updates from the Company Secretary and the legal team.

#### Board succession planning



	Independence	Years with Cobham	Skills			Experience						
			Leadership	Strategy	UK Corporate Governance	Corporate	Engineering	Defence	Finance	US Market	UK Listings	HR
J Devaney	●	3	●	●	●	●	●	●	●	●	●	
R Murphy	●	1	●	●	●	●	●	●	●	●	●	●
S Nicholls	●	0	●	●	●	●	●	●	●	●	●	
D Flint	●	0	●	●	●	●	●	●	●	●	●	
M Hagee	●	5	●	●			●			●		
J Patterson	●	8	●	●	●	●				●	●	●
M Ronald	●	7	●	●		●	●	●		●	●	
M Wareing	●	3	●	●	●	●	●	●	●	●	●	
A Wood	●	2	●	●	●	●	●	●		●	●	

# Corporate Governance Report continued

## Audit Committee



Dear Shareholder

It has been yet another busy year for the Audit Committee and much has been reviewed and reported from across the Group.

We have kept abreast of the ongoing consultations on audit reform and implemented new processes and reporting to deal with the revised Code requirements and narrative reporting.

We welcome the Competition Commission decision to delay their conclusions on audit tendering until the outcome of the European Commission work is known. Further comment on the tendering of the external audit is made below.

Each member of the Committee brings relevant skills and experience at a senior executive level and the appointment of Jonathan Flint broadens the scope of expertise of the Committee. I currently chair the Audit Committee of two other FTSE companies and was the International Chief Executive of KPMG until I retired in September 2009. This provides the Board with assurance that the Audit Committee meets the Code requirements that at least one member of the Committee has significant, recent and relevant financial experience. The key skills and experience of each member of the Committee are shown on page 43.

A handwritten signature in black ink, appearing to read "M Wareing".

**M Wareing**  
Audit Committee Chairman

### Overview

#### Membership and attendance

	Number of meetings attended/held
M Wareing (Chairman) <sup>1</sup>	4/5
M Beresford <sup>2</sup>	2/2
D Flint <sup>3</sup>	3/3
M Hagee	5/5

<sup>1</sup> M Wareing had been hospitalised before the February meeting, which he could not attend.

<sup>2</sup> M Beresford retired from the Board (and hence the Audit Committee) on 25 April 2013.

<sup>3</sup> D Flint joined the Audit Committee on joining the Board on 1 May 2013.

#### Other attendees

Individuals who attended and received papers for each Audit Committee meeting included:

- Chairman (papers received and attends by invitation);
- CEO (papers received and attends by invitation);
- CFO;
- Group Director of Financial Control;
- Head of Internal Audit;
- Company Secretary or her representative; and
- Senior representatives of the Company's external auditors.

Other senior executives were also invited to certain meetings to present and discuss specific items. The Committee periodically meets separately with the Head of Internal Audit and the external auditors without the presence of executive management and also separately with the CFO.

#### Role and focus

The Audit Committee's main duties are to:

- Monitor the integrity of the Group's Financial Statements and any formal announcements relating to its financial performance, reviewing accounting policies used and judgements applied;
- Consider the effectiveness of the Group's internal control systems;
- Consider the effectiveness of the Group's risk management procedures;
- Monitor and review the effectiveness of the Group's internal audit activities;
- Make recommendations as to the appointment, remuneration and terms of engagement of the external auditors;
- Monitor and review the external auditors' independence (including the provision of non-audit services) and objectivity and the effectiveness of the audit process;
- Review arrangements by which the Group's employees may confidentially raise concerns about possible improprieties;
- Provide assurance to the Board on whether the Annual Report and Accounts for 2013 was fair, balanced and understandable; and
- Report to the Board on how it has discharged its responsibilities.

**Highlights of 2013**

- Monitored and contributed to the debate on external audit tendering/rotation led by the UK Financial Reporting Council (FRC), UK Competition Commission and the European Commission, and considered the impact on the Group;
- Considered how to adapt procedures and implemented new processes to provide advice to the Board on whether the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides all information necessary to a shareholder to assess the Group's performance, business model and strategy; and
- Greater scrutiny given to the Group's LCM process, EiD controls and IT controls, including cyber risk.

**Priorities for 2014**

- Continued oversight of the impact of the defence market uncertainty on the financial position of the Group;
- Continued monitoring of the external audit tendering/rotation debate and consideration of the Group's audit tender timetable as appropriate; and
- Continued focus on the Group's governance framework including LCM, EiD, IT controls and risk management processes.

**Allocation of time spent during the year**

Set out in the table and the narrative below is a summary of matters considered by the Committee during 2013. Key issues covered by the Committee are reported to the subsequent meeting of the Board and all Board members have access to copies of the minutes of each meeting.

	Feb	Apr	Jul	Nov	Dec
<b>Financial reporting and significant financial judgements</b>					
Full year results and associated announcements	•				
Half year results and associated announcements		•			
<b>External audit</b>					
Auditors' full year report to the Committee	•				
Independence review of external auditor	•				
Effectiveness review of external auditor	•				
Review of engagement letter		•			
Appointment recommendation to the Board	•				
Auditors' half year report to the Committee		•			
Annual external audit plan		•		•	
Chairman's approval of non-audit fees	•	•		•	
Review of audit and non-audit fees		•			
<b>Internal audit</b>					
Effectiveness review of internal audit	•				
Internal audit report to the Committee	•		•		
<b>Risk management</b>					
Fraud and whistleblowing report	•		•		
Risk management report to the Committee	•		•		
Review of the risk sections of the Annual Report	•				
Review of risk management framework	•				
Annual review of internal controls					•
<b>Other</b>					
Updates on accounting and corporate governance developments					•
Terms of reference review					•
Review of effectiveness of the Committee					•
LCM review	•		•		

# Corporate Governance Report continued

## Risk management and internal controls

The Board is responsible for the oversight and application of the Group's risk management and internal control systems, the aim of which is to manage risks that are significant to the fulfilment of the Group's business objectives and to contribute to the safeguarding of shareholders' investment and the Group's assets. The Board receives reports on a regular basis from the Audit Committee in relation to the effectiveness of the Group's system of internal control and has, accordingly, reviewed the effectiveness of the Group's system of internal control in respect of 2013. The review covered all material controls, including financial, operational and compliance controls and risk management systems and is designed to give assurance that the day to day risk management and internal control policies and procedures, which are embedded in the business, have operated effectively in the review period. The principal elements, which are split into three lines of assurance, are outlined in the diagram shown on page 28. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

Risk management is an integral part of the system of internal control. Division Presidents are required to ensure that appropriate processes, including the maintenance of business unit and divisional risk registers, exist to identify and manage risks and to regularly carry out formal risk assessments. The Risk Committee undertakes a top level review of significant risks and the CEO reports regularly to the Board on their mitigation.

The latest Principal Risks and the risk management process are highlighted on pages 28 to 31.

The Group operates under a system of internal controls which has been developed and refined over time to meet its needs and the risks and opportunities to which it is exposed. This includes a strategic planning process involving the preparation of the Strategic Plan, a comprehensive budgeting system with an annual budget which is approved by the Board, the regular revision of financial forecasts for the year, the monitoring of financial performance and the appropriate delegation of authorities to operational management. Delegations and other operational controls are contained in the Corporate Framework and the Group Finance Manual. Specifically with regard to the financial reporting process and the preparation of the Group Financial Statements, the system includes an annual and semi-annual representation letter from all business units. Included in those letters are written acknowledgements that financial reporting is based upon reliable data and that the results are properly stated in accordance with Group policies.

The Committee believes that the current arrangements comprising the half yearly risk assessment process, a rotational programme of internal financial and other control reviews by the internal audit function, other experienced internal teams, external experts and business reviews carried out by the CEO and CFO and a process of self-assessment of internal financial controls by all business units provide appropriate coverage of the Group's activities. Where weaknesses have been identified, plans for remedying them are developed and progress monitored.

## Cobham Code of Business Conduct violations and fraud

The CR&S section of this report, on pages 32 to 35, contains details of the Cobham Code of Business Conduct and the mechanisms, including those maintained by independent third parties, by which suspected violations of the Code are raised and independently investigated. The Audit Committee received reports providing details of these cases, their outcome, and any corrective actions taken. The reports also included details on anonymous reporting rates and the duration of the investigations. In addition, the Committee also received reports providing details of any fraud losses.

## Financial reporting and significant financial judgements

The Committee reviews whether suitable accounting policies have been adopted, whether management has made appropriate estimates and judgements and also seeks support from the external auditors to assess them.

The Committee reviewed the following main issues for the year ended 31 December 2013:

Issue	Committee action	Conclusion (with reasoning)
Carrying value of investments and potential impairments.	Reviewed internal papers covering the basis and quantum of valuation.	Satisfied that these were reasonable and appropriate, and that the disclosures made were appropriate.
The accounting for revenue recognition.	Considered accounting policies and external audit reviews.	Satisfied that accounting was reasonable and appropriate.
The accounting for contract profitability, including the recognition of contract loss provisions.	Considered accounting policies, management reports, detailed contract appraisals, legal advice, and internal/external audit reviews.	Considered that accounting and provisions were appropriate.
The control environment of the Group to mitigate the risk of management override of internal controls.	Reviewed the summary of management letters of representation and results of internal and external audit reviews.	Satisfied that the system of internal controls was reasonable and appropriate.

At the request of the Board, the Committee considered whether the 2013 Annual Report and Accounts was fair, balanced and understandable and whether it provided the necessary information for shareholders to assess the Group's performance, business model and strategy. It was satisfied that, taken as a whole, the 2013 Annual Report and Accounts is fair, balanced and understandable. This assessment was underpinned by the following:

- Comprehensive guidance issued to contributors at operational level;
- A verification process dealing with the factual content of the reports;
- Comprehensive reviews undertaken at different levels in the Group that aim to ensure consistency and overall balance; and
- Comprehensive review by the senior management team.

## External auditors

### External audit processes

During the year, PricewaterhouseCoopers LLP (PwC) undertook external audit and certain non-audit work. The Audit Partner, Stuart Watson, together with the Audit Director, attended as representatives of the external auditors at each Audit Committee meeting. Stuart

also attended the 2013 AGM. PwC provided the Committee with information and advice as well as relevant reports on the financial statements and controls.

In July 2013, the Committee reviewed and approved the terms, areas of responsibility and scope of the December 2013 year-end audit as set out in the external auditors' engagement letter. During the year, PwC provided audit related services such as regulatory and statutory reporting. PwC is expected to report to the Committee any material departures from Group accounting policies and procedures that it identifies during the course of its audit work. None were found or reported in the financial year.

The Independent Auditors' report to the members of the Company can be found on pages 70 to 73, and pages 125 and 126.

#### **Independence and objectivity**

The Committee and the external auditors have safeguards to avoid the possible compromise of the auditors' objectivity and independence. These include a policy regarding the supply of audit and non-audit services and a policy on the employment of external audit staff. Non-audit services, as defined from time to time in the policy, can be provided subject to pre-approval by the Committee where the cost of any individual engagement exceeds a pre-defined limit and the cost does not exceed the overall limit set out in the policy.

The total fees paid to PwC in the year ended 31 December 2013 (together with a comparison to fees paid in the year ended 31 December 2012) are set out in the following table. Further disclosure of the non-audit fees paid during the year can be found in note 5 to the Group Financial Statements.

Year £m	Audit fees	Non-audit fees	Total fees paid	Non-audit fees as a % of audit fees
2013	2.1	1.7	3.8	81%
2012	2.0	1.1	3.1	55%

The nature of services received from and fees paid to the external auditors during the year include tax compliance and HR advisory services.

PwC also provides specific assurance to the Committee on the arrangements and safeguards it has in place to maintain its independence and objectivity, including an internal process to pre-approve provision of non-audit services and the use of separate teams where non-audit services are being provided to the Group.

The external auditors follow regulatory requirements to maintain the objectivity of the audit process, which stipulate in relation to the senior engagement auditor, a five year rotation policy. Stuart Watson was appointed as lead audit partner in 2009 and has now come to the end of his tenure with Cobham. Stuart will be succeeded by Pauline Campbell. The Committee is satisfied that the external auditors remain independent.

#### **Auditor appointment and effectiveness**

The Committee conducts an annual review of the performance of the external auditors, including feedback from the finance teams at each of the operating companies. This review was conducted

in February 2014 and overall the feedback was positive. The Committee is, therefore, satisfied that PwC continues to provide an effective audit service.

The Committee has recommended that a resolution be proposed at the AGM to re-appoint the external auditors and to allow the Board to set their remuneration.

#### **External audit tendering**

PwC have been the auditors of Cobham plc for many years.

During the last two years, the Committee has been monitoring and, through its Chairman, contributing to the debate on external audit tendering. The Committee has given preliminary consideration to the potential impact of the requirements by the FRC and the UK Competition Commission regarding audit firm tendering, which are welcomed. However, the Committee notes that the European Commission has proposed potentially conflicting guidelines in this area and that the Competition Commission has revised its administrative timetable to enable it to consider the implications of the European Commission proposals. We will continue to monitor developments in this area and await the outcome of the consultations.

The Committee considered tendering for the provision of the external audit service during 2013. The Committee concluded that, in light of the above continuing regulatory uncertainty and the need to properly plan for a full audit tender process, a tender of the external audit should be delayed, subject to the continued satisfactory performance of PwC, until the finalisation of the European Commission and Competition Commission guidelines. It is, however, our intention to consider carrying out a formal tender process once the regulatory position is clear.

There are no contractual obligations restricting the Company's choice of external auditors.

#### **Internal audit**

During the year, prior to each of the five scheduled Committee meetings, the Chairman of the Committee met with the Head of Internal Audit and his reports were reviewed and discussed in detail. The Committee considered the results of the internal audits and the adequacy of management's response to matters raised in them, including the time taken to resolve any such matters.

In February 2014, the Committee conducted an annual review of the effectiveness of the Group's internal audit function, including its terms of reference, its audit plans, its general performance and its relationship with the external auditors. The Committee is satisfied that the internal audit function continues to provide an effective internal audit service.

**M Wareing**  
**Audit Committee Chairman**

5 March 2014

# Directors' Remuneration Report



Dear Shareholder

2013 was a year of change for the Group. It was the first full year for our new CEO which saw the completion of his relocation to the UK from the US, although he was employed on and will remain on US terms and conditions. In addition, we managed the change of CFO with Warren Tucker handing over to Simon Nicholls during the course of the year.

Cobham has a diverse portfolio of businesses and, while some of the businesses performed very well, those exposed to defence in general and the US defence market in particular, had a difficult year. The short term effect was to depress EPS, one of our longer term reward parameters. However, the Group has won a number of significant long term contracts and the management team is making good progress in reshaping the Group. These changes have been recognised by the market, leading to a 33% TSR achieved in the year and the good free cash flow (which is a key annual reward parameter) has allowed us to cover a 10% increase in the dividend.

The salary of the CEO was increased in line with the whole employee group, while the outgoing CFO received no base salary increase. The Annual Incentive Plan paid out 41% of the maximum to Bob Murphy and 39% (pro rata) to Simon. Warren was awarded 8/12 of his maximum annual bonus against a set of time and individual performance criteria at his agreed departure date.

Long term incentive awards were made to the Executive Directors in line with our normal practice, neither of whom have been with Cobham long enough for any of their LTIPs to mature. Warren was not awarded any LTIPs in the year, while his maturing 2011 Performance Share Plan was significantly reduced at 9% of the award.

All elements of the Executive Director remuneration packages are detailed in the body of the report. Of note this year are the non-recurring payments driven by the departure of Warren and the recruitment of Simon, which are shown in the single figure table on page 55. Warren did not receive any payments for loss of office, but did receive a pro-rated annual bonus payment based on personal performance and was treated as a good leaver under the Performance Share Plan. Simon received a buy-out award upon appointment in respect of remuneration foregone at his previous employer. The value of this award was equivalent to the expected value of the remuneration foregone and will vest over the same time horizons.

We have undertaken a review of our remuneration report to respond to regulatory requirements and in preparation for the first binding vote on our remuneration policy. We have set out where we may need to exercise our discretion and it is important to recognise that no change to our existing, shareholder agreed, policy has been implemented.

Finally, as I will be retiring from the Board and therefore my role of the Chairman to the Remuneration Committee, we appointed one of my fellow committee members to the role. Alison Wood will be taking up her new role as Chair of the Committee immediately following the AGM.

I hope that we can rely on your vote in favour of the Annual Report and Accounts on remuneration and our Directors' remuneration policy for future years.



**Dr J Patterson**  
Remuneration Committee Chairman

## Overview

### Membership and attendance

	Number of meetings attended/held
J Patterson (Chairman)	4/4
J Devaney <sup>1</sup>	1/2
M Ronald	4/4
A Wood	4/4

<sup>1</sup> During the year, the Committee membership was reduced to three Non-executive Directors. The Company Chairman ceased to be a member of the Committee with effect from 25 September 2013, although he continues to attend meetings by invitation of the Remuneration Committee Chairman as appropriate.

No individual is present in meetings relating to decisions around their own remuneration. The Committee's terms of reference are available on the Company's website or on application to the Company Secretary.

### Other attendees

Executive Vice President HR, Vice President Compensation and Benefits, Deloitte LLP, CEO (attends by invitation).

### Role and focus

The Remuneration Committee's main duties are to:

- Make recommendations to the Board on the Group's policies on Executive Directors' remuneration and ensure alignment to the Group's Strategic Plan; and
- Determine, on the Board's behalf, the specific remuneration packages of the Chairman, Executive Directors, Group Executive and Company Secretary.

### Priorities for 2014

- Secure positive support for the remuneration policy and oversight to ensure it continues to support the achievement of the Group's Strategic Plan, the demonstration of the required behaviours and the retention of high potential, high performance, key skilled resource; and
- Review how advice is provided by the Committee.

## The Directors' Remuneration Policy

While we have not made any changes to our remuneration policy, this is the first time we have publicly articulated our policy in preparation for a binding vote. The table below sets out the remuneration policy that the Company intends to apply following the AGM on 24 April 2014, which will become binding from that date, subject to shareholder approval.

### Remuneration and policy (the policy table)

Element	Purpose and link to strategy	Operation	Maximum potential value	Current performance measures
Base pay	To provide fixed remuneration which is market competitive to attract and retain executives of the quality required to deliver the Group's strategy, while taking into account an individual's experience and personal contribution to the Group's Strategic Plan.	<p>Reviewed annually and paid monthly with changes typically effective from 1 March.</p> <p>Consideration is given to a wide range of factors including:</p> <ul style="list-style-type: none"> <li>• Individual and Company performance;</li> <li>• General pay increases across the wider workforce;</li> <li>• The size and scope of the role; and</li> <li>• Pay levels of comparable roles in companies of a similar size and complexity to the Company.</li> </ul>	<p>To avoid setting the expectations of Executive Directors and other employees, no maximum salary is set under the Remuneration Policy.</p> <p>However, base salary increases for the Executive Directors are applied in line with the outcome of the annual review and will typically be in line with the average increase for the wider workforce.</p> <p>Increases may be made either above or below that received by the wider workforce to take account of individual circumstances, which may include but are not limited to:</p> <ul style="list-style-type: none"> <li>• A change in the scope of the role or increase in responsibility;</li> <li>• A significant change in the size and complexity of the Group; and</li> <li>• An individual's development or performance in role (e.g. a newly appointed executive director being moved to be aligned with the market over time).</li> </ul>	Not applicable
Other benefits	To provide fixed remuneration which is market competitive to attract and retain executives of the quality required to deliver the Group's strategy, while taking into account an individual's experience and personal contribution to the Group's Strategic Plan.	<p>The Company provides various market competitive benefits to Executive Directors, which may include: a company car (or cash equivalent), travel allowance, private medical and dental insurance, travel accident policy, life assurance and long term disability benefit.</p> <p>Where appropriate, other benefits may be provided to take account of individual circumstances, such as but not limited to: expatriate allowances, relocation expense, housing allowance and education support.</p>	<p>No maximum level of benefit is set under the remuneration policy and the Remuneration Committee sets the level it considers appropriate taking into account relevant market levels based on the nature and location of the role.</p> <p>Level of benefits set are in line with those paid to other senior executives and with regard to the market.</p>	None
Retirement benefits	To provide fixed remuneration which is market competitive to attract and retain executives of the quality required to deliver the Group's strategy, while taking into account an individual's experience and personal contribution to the Group's Strategic Plan.	<p>The Company may make a payment into a pension scheme (e.g. a defined contribution plan) and/or make a cash allowance payment set as a percentage of salary.</p>	<p>Set at a level which the Remuneration Committee considers appropriate taking into account relevant market levels based on the nature and location of the role.</p> <p>Contributions of up to 30% of base salary may be made to take account of a change in the scope of the role or increase in responsibility.</p> <p>The contribution levels for 2014 are below this level (20% of salary) as disclosed in the annual report on remuneration.</p>	None

# Directors' Remuneration Report continued

Element	Purpose and link to strategy	Operation	Maximum potential value	Current performance measures
Annual Incentive Plan (AIP)	<p>Drives and rewards annual performance against selected financial and operational KPIs and individual objectives that are directly linked to the Group's Strategic Plan.</p> <p>The Committee may adjust the bonus pay-out, either up or down, should the formulaic outcome be considered not to reflect underlying business performance.</p> <p>75% of any bonus is paid in cash and up to 25% of any bonus is mandatorily deferred into Company shares for a period of three years.</p> <p>Up to a further 25% of any bonus may be voluntarily deferred into shares in the Company for a period of three years under the BCP (see below).</p> <p>Clawback provisions are in place which give the Committee discretion to reduce awards or require repayment of cash paid to a participant in relation to annual incentives within the preceding 12 months for material misstatement of financial results, reputational damage to the Group, contravention of internal ethics standards or gross misconduct of the individual.</p> <p>Deferred share awards may be released early on a change of control in line with the plan rules.</p> <p>The Committee may make a dividend equivalent payment (Dividend Equivalents) to reflect dividends that would have been paid over the deferral period on shares that vest. This payment may be in the form of additional shares or a cash payment equal to the value of those additional shares.</p>	<p>Measured over a one-year performance period with pay-out levels determined by the Committee following the year-end.</p> <p>The maximum opportunities for 2014, as disclosed in the annual report on remuneration, are 120% of salary for the CEO and 100% of salary for the CFO.</p> <p>The maximum bonus opportunity for any Executive Director will not exceed 150% of salary. Any opportunity above the 2014 levels noted above will only be made where the Committee considers there to be a commercial rationale that may include but is not limited to:</p> <ul style="list-style-type: none"> <li>• A change in the scope of the role or increase in responsibility;</li> <li>• A reduction to other elements of the remuneration package; and</li> <li>• A significant change in the size and complexity of the Group.</li> </ul> <p>Any increases above the current opportunities will also normally be subject to shareholder consultation.</p>	<p>Performance is assessed over a single financial year based on a combination of financial and individual metrics which are aligned to the strategic objectives of the Company.</p> <p>The majority of the bonus is assessed against key financial performance metrics of the business and the balance based on individual performance.</p> <p>For target performance, up to 50% of the maximum bonus opportunity will be received.</p>	
Bonus Co-investment Plan (BCP)  This plan forms part of the LTI programme.	<p>Incentivise sustainable profitable growth and sector outperformance aligned with the Group's Strategic Plan.</p> <p>Reward share price and dividend growth, providing alignment with shareholders' interests.</p> <p>Supports retention and promotes share ownership.</p>	<p>Individuals may receive a matching award under the BCP in respect of any bonus deferred subject to the achievement of performance conditions.</p> <p>The Committee may adjust the level of the matching award vesting, either up or down, should the formulaic outcome be considered not to reflect underlying business performance.</p> <p>Dividend Equivalents may be made as detailed above under the AIP but in respect of the performance period.</p> <p>Clawback provisions are in place as detailed above under the AIP.</p> <p>Upon a change of control, awards will vest to the extent specified by the Remuneration Committee after taking into account those factors it thinks are relevant. These may include but are not limited to the extent to which the performance conditions have been satisfied and the period elapsed since the date of grant.</p>	<p>The maximum matching award is 1:1 on any net bonus deferred up to 50% of the bonus earned.</p> <p>The matching award of shares is provided against the gross bonus invested.</p>	<p>Performance is assessed over more than one financial year, usually at least three years against key financial metrics aligned to the Group's Strategic Plan.</p> <p>A matching award of 0.5:1 Ordinary Share is received for achieving threshold performance.</p>

Element	Purpose and link to strategy	Operation	Maximum potential value	Current performance measures
Performance Share Plan (PSP)	Incentivise sustainable profitable growth and sector outperformance aligned with the Group's Strategic Plan.	Awards are made under the rules of the PSP, which were approved by shareholders at the 2007 AGM.	Conditional share awards or nil-cost options of up to 150% of base salary may be granted annually.	Performance is assessed over more than one financial year, usually at least three years against key financial metrics aligned to the Group's Strategic Plan.
This plan forms part of the LTI programme.	Reward share price and dividend growth, providing alignment with shareholders' interests over the longer term.	Awards are made on an annual basis and will vest subject to performance after a period of at least three years.	In accordance with the plan rules, which were approved by shareholders at the 2007 AGM, the individual limit of 150% of salary can be exceeded in exceptional circumstances involving the recruitment or retention of a senior employee by approval of the Committee.	The threshold level of vesting may be up to 16.7% of the maximum award.
	Supports retention and promotes share ownership.	The Committee may adjust the level of vesting, either up or down, should the formulaic outcome be considered not to reflect underlying business performance.	Dividend Equivalents may be made as detailed above under the AIP but in respect of the performance period.	
		Change of control provisions apply as detailed in the BCP section above.		
		Clawback provisions are in place as detailed above under the AIP.		
Executive Share Option Scheme (ESOS)	Incentivise sustainable profitable growth and sector outperformance aligned with the Group's Strategic Plan.	Awards are made under the rules of the ESOS, which are currently proposed for updated approval at the 2014 AGM.	Annual awards may be made with an aggregate market value of 200% of salary.	Performance would be assessed over more than one financial year, usually at least three years against key financial metrics aligned to the Group's Strategic Plan.
This scheme forms part of the LTI programme.	Reward share price and dividend growth, providing alignment with shareholders' interests.	Awards under the ESOS are not currently made to Executive Directors. No awards will be made in any year in which an Executive Director receives an award under the PSP.		
	Supports retention and promotes share ownership.	The Committee may adjust the level of vesting, either up or down, should the formulaic outcome be considered not to reflect underlying business performance.		
		Options can become exercisable on a change of control of the Company, or with the consent of the acquiring company, a grant of equivalent rights may be made.		
All employee share schemes	Provides all employees, including Executive Directors the opportunity to voluntarily invest in Company shares.	The Company operates a SAYE scheme and SIP scheme, which are both HMRC approved plans.	Maximum limits are set in line with the HMRC savings limit for approved plans.	None

# Directors' Remuneration Report continued

## Notes to the policy table

### Policy for the remuneration of employees generally

The Company values its wider workforce and aims to provide a remuneration package that is based on a mixture of Group and personal performance. As the Group is worldwide and operates in different countries, employees are appropriately remunerated taking account of the market in the employees' jurisdiction of employment. The following key principles of the remuneration policy outlined above are applied consistently across the employee population:

- To offer a level of remuneration that is appropriate to attract, retain, motivate and reward employees to deliver the Group's Strategic Plan without paying more than is necessary; and
- To seek to remunerate fairly, competitively and consistently for each role with due regard to the marketplace, internal consistency and the Group's ability to pay.

When determining remuneration arrangements for Executive Directors, the Committee takes into consideration, as a matter of course, the pay and conditions of employees throughout the Group. In particular, the Committee paid specific attention to the level of salary increases and the size of the annual bonus pool in the wider population, with particular reference to the year on year change to these figures. No consultation with employees takes place in relation to determining the Directors' Remuneration Policy.

### Performance measures and targets setting

The annual bonus is assessed against both financial and individual targets determined by the Committee. This incentivises Executives to focus on delivering the key financial goals of the Company as well as specific strategic objectives for each Director, which are aligned to delivering the Group's Strategic Plan and ensuring Executives exhibit the right behaviours. Targets are set on an annual basis taking into account the budget forecast and at a level which the Committee considers to be stretching.

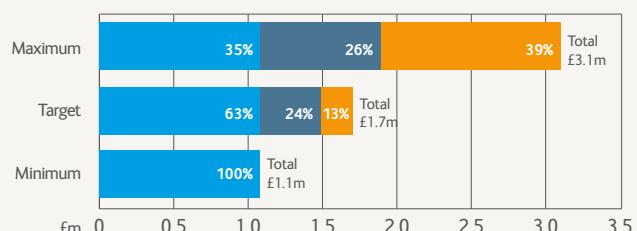
Long term performance measures under the BCP and PSP are chosen by the Committee to be aligned with the long term strategy of the business. They are selected to be aligned with the interests of shareholders and incentivise the delivery of strong, sustainable, financial performance. Targets are set at the time of grant taking into account internal and external forecasts and the market environment. Where TSR is selected as a performance measure, no awards will vest for below median performance.

## Application of remuneration policy

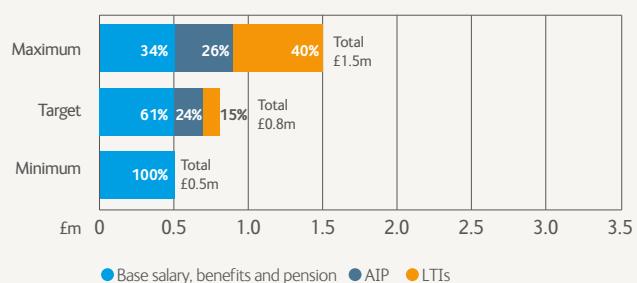
The best way to demonstrate how our policy works is to provide examples of pay-outs under different scenarios.

The charts below illustrate the application of the remuneration policy set out in the policy table for each Executive Director for 2013 under different scenarios:

### CEO – R Murphy



### CFO – S Nicholls



● Base salary, benefits and pension   ● AIP   ● LTIs

### Assumptions

Maximum performance (Maximum)	Total fixed pay as minimum below, plus: Assumes 100% pay-out under the AIP (120% of base salary for R Murphy, 100% for S Nicholls). Assumes 100% pay-out under the BCP Equivalent to 1 to 1 share match based on 50% investment of maximum AIP, noted above, mandatory and voluntary, (R Murphy only). Assumes 100% pay-out under the PSP (150% of base salary for both).
On-target performance (Target)	Total fixed pay as minimum below, plus: Assumes 50% pay-out under the AIP (60% of base salary for R Murphy, 50% for S Nicholls). Assumes 50% pay-out under the BCP (aligned with threshold performance). Equivalent to 0.5 to 1 share match based on 50% investment of target AIP, noted above, mandatory and voluntary, (R Murphy only). Assumes 16.7% pay-out under the PSP (aligned with threshold performance).
Below threshold performance (Minimum)	Fixed elements of remuneration only – base salary, benefits and pension only (salary payable through the year under report and benefits and pension equivalent to that included in the single figure calculation on page 55): refer to the notes below that table for the detail.

### Note:

As required by the regulations, the scenarios do not include any share price growth assumptions or take into account any dividends that may be paid.

### Policy table for the Chairman and Non-executive Directors

Component	Approach of the Company
Chairman fees	<p>The Remuneration Committee and the Senior Independent Director determine the fees of the Chairman and set the fees at a level that reflects the skills, knowledge and experience of the individual, while taking into account appropriate market data.</p> <p>The fee is set as a fixed annual fee and may be paid wholly or partly in cash or Company shares.</p>
Non-executive Director fees	<p>The Executive Directors Committee determines the fees of the Non-executives. Fees are set taking into account the size and complexity of the business and the expected time commitment and contribution for the role.</p> <p>Fees are structured as a basic fee with additional fees payable for membership and/or chairmanship of a committee or other additional responsibilities.</p> <p>The fee is set as a fixed annual fee and may be paid wholly or partly in cash or Company shares.</p>
Benefits	An additional allowance may be provided in respect of additional travelling time required to attend Board meetings for those Directors who are based outside of the UK.

### Approach to recruitment remuneration

When determining the remuneration package for a new Executive Director, the Committee will apply the following principles:

- The package will be market competitive to attract and retain individuals of the calibre required to lead the business and deliver our strategic goals;
- Typically, the remuneration package will be aligned in accordance with the Company's remuneration policy set out above. However, should business needs require, the Remuneration Committee has the discretion to include other remuneration elements which are not included in the remuneration policy, subject to the overall limit on variable remuneration set out below. The Committee does not intend to use this discretion to make non-performance related incentive payments (for example, a golden hello). Any movement from the policy outlined in the table above would only be considered where there is a commercial rationale for doing so, which will be disclosed in the following annual remuneration report; and
- To secure an appointment the Remuneration Committee may need to make awards to buy out an external candidate's remuneration arrangements that are forfeit as a result of leaving their previous employer. In doing so, the Committee will take into account all relevant factors which may include the form and time horizon of awards, any performance conditions attaching to the awards and the likelihood of awards vesting. The Committee will typically seek to buy out awards on a comparable basis to those forfeit, with the intention that the value awarded would be no higher than the expected value of the forfeit arrangements.

The maximum level of variable remuneration that may be granted to a new Executive Director on appointment (excluding any buy out of forfeit awards discussed above) will be 375% of salary, being aligned with the sum total of the stated policy for all variable remuneration for current Executive Directors:

- For any internal candidates, remuneration commitments made prior to the appointment as Director may continue to be honoured, notwithstanding compliance with the remuneration policy set out above; and
- The remuneration package for a newly appointed Non-executive Director would be in line with the structure set out in the policy table for Non-executive Directors.

Any share awards referred to in this section will be granted as far as possible under the Company's existing share plans, if necessary, and subject to the limits referred to above, recruitment awards may be granted outside these plans as currently permitted under the listing rules which allow for the grant of awards to facilitate, in exceptional circumstances, the recruitment of a Director.

### Service contracts and payment for loss of office

The Board's policy for current and new Executive Directors is that service contracts have a notice period that should not exceed one year. However, it recognises that it may be necessary in the case of new executive appointments to offer a longer initial notice period, which would subsequently reduce to one year.

Non-executive Directors have letters of appointment to the Company whereby their appointment may be terminated by a maximum of one month's written notice.

The current Executive Directors' service contracts are terminable on 12 months' notice by either party and can be terminated for cause, which is defined in the contract. The Company may elect to terminate Executive Directors' service contracts by making payments in lieu of notice which will not exceed 12 months' salary and benefits, which can also include, but are not limited to, pension, outplacement and legal fees.

Payments in respect of AIP may also be payable on the date of leaving in cases such as ill health or retirement. These will be pro-rated to reflect the proportion of the financial year worked and subject to performance achieved. In the case of voluntary termination, the AIP may be paid for the period worked until resignation and for any part of the notice period that the departing Executive continues to work, subject to the achievement of objectives, set at the Committee's discretion. The Company recognises and endorses the obligation of departing Directors to mitigate their own losses.

The treatment of unvested shares under the BCP, PSP and ESOS will be as set out in the relevant plan rules. The table below provides details of the treatment that would apply under the plan rules depending on the reason for cessation of employment. To the extent that an award does not vest in accordance with these terms, the award will lapse.

# Directors' Remuneration Report continued

Plan	Reasons for leaving	Treatment
PSP and BCP	Good leaver provisions – death, ill health, injury or disability, redundancy or retirement.	Award will vest at the time and to the extent determined by the Committee after taking into account the extent to which the performance target to which it is subject has been met and the extent that the relevant period has elapsed at the date of cessation of employment.
	Voluntary resignation/any other reason.	Award will lapse unless the Committee determines to preserve and vest all or part of the award on any terms it thinks fit.
ESOS	Good leaver provisions – death, ill health, injury or disability, redundancy or retirement.	Award will become exercisable at the time and to the extent determined by the Committee after taking into account the extent to which the performance target to which it is subject has been met and the extent that the relevant period has elapsed at the date of cessation of employment. Awards are exercisable within six months of date of cessation of employment, with the exception of death where this period is 12 months.
	Voluntary resignation/any other reason.	Award will lapse unless the Committee determines to preserve and vest all or part of the award on any terms it thinks fit.

Where a buy-out award is made under the listing rules, the leaver provisions would be determined at the time of the award.

The Committee reserves the right to make additional exit payments where such payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of settlement or compromise of any claim arising in connection with the termination of a Director's office or employment.

In doing so, the Committee will recognise and balance the interests of shareholders and the departing Executive Director, as well as the interests of the remaining Directors. Where awards which are permitted to vest are subject to performance conditions, these would only be assessed at the end of the relevant period(s).

For Non-executive Directors, discretion is retained to terminate with or without due notice or paying any payment in lieu of notice dependent on what is considered to be in the best interests of the Company in the particular circumstances.

## Statement of consideration of shareholder views

The Committee is committed to regular and transparent communication with shareholders. We believe this ensures we understand shareholders' views on our arrangements and are able to take their comments into consideration when reviewing our remuneration policy.

At the end of 2012, a review of the current remuneration package was undertaken to simplify arrangements, rebalance the performance metrics in line with current strategy and to provide clearer line of sight against targets for those participants in the incentive plans. Major shareholders and representative bodies were consulted following this review and we received a supportive response.

## Payments in relation to existing remuneration arrangements

The Committee reserves the right to make any remuneration payments and payments for loss of office (including exercising any discretions available to it in connection with such payments), notwithstanding that they are not in line with the policy set out above where the terms of the payment were agreed:

- Before the policy came into effect; or
- At a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, the payment was not in consideration for the individual becoming a Director of the Company.

For these purposes, 'payments' includes the Committee satisfying awards of variable remuneration; and, in relation to an award over shares, the terms of the payment are agreed at the time the award is granted.

## The Annual Report on Remuneration

### Single total figure of remuneration for each Director (audited information)

#### Executive Directors

The single figure table below is completed for each person who served as an Executive Director of the Company at any time during the financial year, together with comparatives.

Single total figure table

£k	Salary and fees	Taxable benefits	Annual Incentive Plan	Long term incentives	Pensions	Total
R Murphy						
2013	680	294	280	687	117	2,058
2012	313	195	182	–	63	753
S Nicholls						
2013	267	11	104	–	53	435
W Tucker						
2013	296	17	296	65	120	794
2012	441	18	191	335	150	1,135

### Additional disclosures in respect of the single total figure of remuneration (audited information)

#### Salary and fees

Bob Murphy's employment terms and conditions are based on US law and his salary payments are made in US dollars and have been converted to UK pounds using the average annual conversion rate of \$1.5657:£1, the same conversion rate as is used elsewhere in the accounts. Bob's 2012 salary was \$1,040,000 (pro rata) as reported in the Annual Report and Accounts 2012. On 1 March 2013, his salary was increased by 3%, in line with the pay increases made across the business, to \$1,071,200.

Simon Nicholls was appointed on a salary of £400,000 per annum; the amount shown in the above table is pro-rated from his 1 May 2013 start date.

Warren Tucker's base salary was not increased in the 2013 annual pay review.

#### Taxable benefits

The benefit figures are as follows:

Benefit	R Murphy £k (\$k)	S Nicholls £k	W Tucker £k
Car allowance	7 (11)	10	11
Private petrol allowance	–	–	4
Relocation expenses	100 (157)	–	–
Private medical insurance, disability cover and life insurance	40 (62)	1	1
Expatriation allowance	128 (200)	–	–
Allowance to cover financial/tax advice	19 (30)	–	1

As disclosed last year, Bob Murphy was entitled to be reimbursed up to \$624,000 (60% of his base salary) for the reasonable costs associated with his relocation from the US to the UK. The actual cost of his relocation was \$812,522, split over 2012 and 2013. Bob's actual relocation expenses were reasonable and customary, and in line with relocation expenses paid to other senior executives in the Group. On this basis, the Committee exercised its discretion to approve the payment of the full cost of Bob's relocation from the US to the UK.

Andy Stevens, who retired from his position as a member of the Board in August 2012, was reimbursed business expenses totalling £3,632 during 2013.

# Directors' Remuneration Report continued

## 2013 AIP

AIP payments made for the 2013 performance year are calculated as follows:

Metric	Weighting	Performance	Full year target £m	Actual £m
Trading profit	70%	Threshold	308.5	
		Target	321.9	314.8
		Maximum	335.3	
Free cash flow (before restructuring)	30%	Threshold	203.4	
		Target	224.8	205.3
		Maximum	234.8	

Note:

Trading profit and cash flow metrics are adjusted for the impact of acquisitions and disposals during the year. Performance conditions are set at standard translation exchange rates. The actual results are normalised to these rates for assessment purposes. Trading profit and free cash flow are discussed in more detail in note 3 to the Group Financial Statements and in the KPI definitions on page 140. The above results achieve a business performance factor (BPF) of 0.65.

	Target bonus (% of salary)	BPF as per table above	Individual performance factor	% of salary achieved	Amount of AIP to be paid £k (\$k)	% subject to mandatory deferral	% of which can be voluntarily deferred
R Murphy	120	0.65	1.05	41	280 (438)	25	25
S Nicholls	100	0.65	1.2	39	104	25	N/A

The individual performance factor is made up of personal objectives including achievements against financial and profitable growth metrics, customer satisfaction, operational excellence, safety, talent development, and inventory control.

During 2013, Warren Tucker stood down from his role as Executive Director and CFO of the Company and was replaced by Simon Nicholls, with effect from 1 May 2013. Warren remained with the Company until 31 August 2013 to ensure an efficient and effective handover was given to his successor, to provide advice on various transactions the Company was considering and assist with the delivery of the half year results. He was paid 8/12 of the maximum annual incentive he would have been entitled to had he stayed with the Company until the normal incentive payment date, based on performance against his personal objectives only.

## Long term incentives

Warren Tucker's LTI amount relates to the awards granted under the PSP in 2011. Vesting was dependent on performance over the three financial years ended 31 December 2013. The performance achieved against the performance targets is shown below:

Performance condition	Level	Performance	% of award vesting at that level	Performance achieved	Total % vest
1/2 TSR	Threshold (target)	TSR equal to peer group TSR index	16.7%	Index (9.4%) per annum/0% vest	
	Maximum (maximum)	TSR equal to or greater than peer group TSR index plus 10%	100%		
1/2 EPS	Threshold (target)	EPS growth of 3% per annum over the period of the vest	16.7%	3.2% per annum/18.2% vest	
	Maximum (maximum)	EPS growth equal to or greater than 11% during the year	100%		
					9.1% vest

The award held by Warren Tucker was as follows:

	No of shares awarded	No of shares vested	Value of shares vesting £k
PSP 2011	262,285	23,868	65.4
<b>Total</b>		<b>23,868</b>	<b>65.4</b>

The PSP will vest at 9.1% on 10 March 2014 based on the performance conditions measured over the three financial years ended 31 December 2013 and outlined on page 56. As the awards had not vested at the date of this report, the average share price for the last three months of the financial year of 273.8 pence has been used to determine the value for the purposes of the single total figure.

The Committee used its discretion and treated Warren Tucker as a good leaver under the relevant plan rules in recognition of his agreement to remain on the Board for a period of 18 months beyond his desired departure date to allow CEO succession and until a successor was found for the CFO role. Warren was not granted any awards under LTI arrangements during 2013.

Warren Tucker's 2012 vested long term incentives and SAYE and SIP holdings were disclosed in the Annual Report and Accounts 2012 and are included in the 2012 long term incentive plan figure above, as appropriate.

Bob Murphy's long term incentives figure above covers the vesting of three awards made to him as buy-out awards to compensate for forfeited equity from his previous employers as a result of leaving to join Cobham. The three awards, which were disclosed in full in the Annual Report and Accounts 2012, are set out below:

Awards vesting	Date of vest	Valuation (pence per share)
126,779	29 April 2013	248.3
72,305	29 April 2013	248.3
72,305	16 December 2013	266.7

All shares have been valued at the mid-market quotation (MMQ) price on the date of vesting.

#### Pensions

The Company contributes to Bob Murphy's retirement plan at the rate of 20% of his base salary. This is comprised of participation in two plans:

- A qualified 401k plan, which has limits on the level of contribution that can be made to it; and
- An executive retirement plan, non-qualifying.

During 2012, he had reached the contribution level in the 401k plan by contributions made by his previous employer. Therefore, his pro-rated contributions of £62,686 were paid in full to the executive retirement plan.

£k	2013	2012
Contributions to 401k plan	10	—
Contributions to executive retirement plan	107	63
<b>Total</b>	<b>117</b>	<b>63</b>

Simon Nicholls' pension figure is a combined amount of £33,333 to an executive defined contribution plan and £20,000 paid as a cash allowance in lieu of additional defined contribution arrangements. Together these payments represent a rate of 20% of his base salary.

Warren Tucker's pension figure is a combined amount of £49,400 paid into a defined benefit pension scheme. The defined benefit pension scheme retirement age for funding purposes is 60; however, the Director may retire from age 55. A further £70,944 was paid as cash allowance in lieu of a defined contribution top-up arrangement.

The Company has obtained written confirmation from each Director that they have disclosed all other items in the nature of remuneration.

# Directors' Remuneration Report continued

## Non-executive Directors (audited information)

The 2013 remuneration, current fees and the details of the terms of appointment of the current and past Non-executive Directors, including the Chairman, are stated below:

£k	Commencement date	Expiry date	Full year fees*			Actuals payable	
			Base fee	Committee fee	Senior Independent Director	2013	2012
J Devaney (Chairman)	1 February 2010	24 April 2016	<b>270</b>	—	—	270	470
M Beresford	1 March 2004	25 April 2013	<b>55</b>	<b>5</b>	<b>10</b>	23	70
J Patterson	1 November 2005	31 October 2014	<b>55</b>	<b>12.5</b>	—	68	68
M Ronald	8 January 2007	24 April 2016	<b>55</b>	<b>2.5</b>	—	63	63
M Hagee	3 December 2008	2 December 2014	<b>55</b>	<b>5</b>	—	65	65
M Wareing	1 December 2010	1 December 2016	<b>55</b>	<b>10</b>	<b>10</b>	72	65
A Wood	1 July 2011	1 July 2014	<b>55</b>	<b>2.5</b>	—	58	55
D Flint	1 May 2013	1 May 2016	<b>55</b>	<b>2.5</b>	—	38	—
<b>Total Non-executive Director remuneration</b>						<b>657</b>	<b>856</b>

\*Members of the Nomination Committee do not receive any additional fees.

Notes:

1. Non-executive Directors only receive fees under their service agreement and do not have any other taxable benefits, annual or long term incentives or pension arrangements provided by the Company.
2. Difference between full year fee and actual is explained by an individual commencing or retiring during the year or prior year or by the payment of a fee of £5,000 per annum in respect of travelling time for the two Directors based in the US.
3. The Company has obtained written confirmation from each Director that they have disclosed all other items in the nature of remuneration.
4. The fee for the Senior Independent Director shown above has been pro-rated for length of service in that role.

Total aggregate Directors' fees for the year, including the Executive Director fees as per the single figure table above, amount to £3,944,000.

### Scheme interests awarded during the financial year (audited information)

The following table sets out the awards made under the long term incentive plans to Executive Directors during the year.

	Type of award	Basis of which award is made	Date of award	Face value of award	Performance period	Performance conditions
<b>R Murphy</b>	Performance Share Plan (performance share award)	150% of base salary	14 March 2013	£1,078,523	1 January 2013 to 31 December 2015	Equal split between TSR, EPS and cash conversion; see note 5 below giving details of the performance conditions.
	Bonus Co-investment Plan (performance share award)	Mandatory 25% of retained, earned AIP	28 March 2013	£18,449	1 January 2013 to 31 December 2015	Economic profit measure is considered to be price sensitive and is not disclosed until the year of vesting.
<b>S Nicholls</b>	Performance Share Plan, nil-cost options (performance share award)	150% of base salary	15 August 2013	£600,000	1 January 2013 to 31 December 2015	Equal split between TSR, EPS and cash conversion; see note 5 below giving details of the performance conditions.
	Buy-out award (performance share award)	Loss of value of vested equity forfeit from former employer; see note 4 below	15 August 2013	£254,053	15 August 2013 to 1 May 2016	Continued employment with a member of the Cobham Group at the date of the vest.

Notes to the table for scheme interests awarded during the year:

1. All awards have been made in accordance with the relevant scheme rules.
2. Warren Tucker was not awarded any scheme interests during 2013.
3. The face value has been calculated by multiplying the number of shares awarded by the MMQ price of those shares for the three trading days immediately preceding the date of the award.
4. This award is in recognition of the loss of value in vested equity forfeit from his former employer and vests in three tranches matched to when Simon Nicholls would have received the equity releases, with the final vest on 1 May 2016.
5. Performance conditions for the PSP are set out in the table below:

Performance condition	Level	Performance	% of award vesting at that level
1/3 TSR	Below threshold (minimum)	TSR less than peer group TSR index	–
	Threshold (target)	TSR equal to peer group TSR index	16.7%
	Maximum (maximum)	TSR equal to or greater than peer group TSR index plus 10%	100%
1/3 EPS	Below threshold (minimum)	EPS growth less than 3%	–
	Threshold (target)	EPS growth of 3% during the year	16.7%
	Maximum (maximum)	EPS growth equal to or greater than 10% during the year	100%
1/3 Cash Conversion	Below threshold (minimum)	Cash conversion less than 90% during the year	–
	Threshold (target)	Cash conversion of 90% during the year	16.7%
	Maximum (maximum)	Cash conversion equal to or greater than 90% during the year	100%

EPS and cash conversion are defined in the KPI definitions on page 140.

# Directors' Remuneration Report continued

## TSR peer group

The companies in the TSR comparator group for awards granted in 2013 are:

BAE Systems	Harris	Northrop Grumman	Smiths Group
Esterline	ITT Industries	QinetiQ	Teledyne Technologies
Finnmeccanica	L-3 Communications	Raytheon	Thales
Flir Systems	Meggitt	Rockwell Collins	Ultra Electronics

## Statement of Directors' shareholding and share interests (audited information)

### Executive Directors' share interests

The interests of the Executive Directors in share awards or share options are shown below (note: there are no options which have vested but not yet been exercised):

Director/award	Share awards subject to performance conditions	Share awards subject to continued employment	Unvested options subject to performance awards
R Murphy			
Buy-out award 2012		72,305	
PSP 2012	451,917		
PSP 2013	453,924		
BCP 2013	7,564		
<b>Total</b>	<b>913,405</b>	<b>72,305</b>	<b>–</b>
S Nicholls			
Buy-out award 2013		86,442	
PSP 2013			204,151
<b>Total</b>	<b>–</b>	<b>86,442</b>	<b>204,151</b>

Warren Tucker's only remaining share interests are shown in the table at the top of page 57.

During the year, the following gains on the exercise of ESOS or PSP nil-cost options were made by the Executive Directors:

Director/award	No of options exercised	Date of exercise	Option exercise price (pence per share)	Market value at exercise date (pence per share)	Gain on exercise of share option (£k)
W Tucker					
ESOS 2004 Approved	2006	22,260	31 May 2013	134.7	285.8
ESOS 2004	2006	133,600	31 May 2013	134.7	285.8
ESOS 2005	2007	180,070	31 May 2013	133.7	285.8
ESOS 2006	2008	186,154	31 May 2013	185.3	285.8
ESOS 2007	2009	178,826	31 May 2013	204.5	285.8
ESOS 2008	2010	84,356	31 May 2013	201.5	285.8
ESOS 2008	2010	106,094	9 August 2013	201.5	294.8
ESOS 2009 Approved	2011	3	9 August 2013	184.0	294.8
ESOS 2009	2011	176,211	9 August 2013	184.0	294.8
<b>Total</b>	<b>1,067,574</b>				<b>1,207.3</b>

All the options noted above have already been recognised as vesting in the years noted above. The decision as to when to exercise an option is considered an investment decision by the Executive Director and accordingly any increase or decrease in the amount realised on the exercise date, as compared to the vesting date, is not included within any further measurement of remuneration.

Non-executive Directors are required, within six months of election to the Board, to acquire and hold a shareholding of 5,000 Ordinary Shares.

The interests of the Non-executive Directors and their families in Ordinary Shares were:

	1.1.13	31.12.13
M Beresford	15,000	15,000
J Patterson	5,000	5,000
M Ronald	5,000	5,000
M Hagee	5,000	5,000
J Devaney	30,000	30,000
M Wareing	20,000	20,000
A Wood	5,000	5,000
D Flint	—	5,000

Ownership guidelines require the Executive Directors to maintain Ordinary Shares. These guidelines state for the CEO to the value of at least two years' salary and for the CFO to the value of at least one year's salary and to retain a minimum of 50% of net vested PSP and BCP matching shares until the relevant shareholding level is met. There is no timeframe over which the guidelines are required to be met and there is no requirement for Directors to hold these shares after leaving the Company. Both Directors have complied with the guidelines but have yet to meet their targets due to the length of their tenure.

Director	Share ownership requirement (% of annual salary)	No of shares owned outright (including connected persons)		No of shares beneficially owned – (BCP Invested Shares)	No of shares beneficially owned – (SIP Partnership Shares)		Ownership requirements met	Tenure in role
		2013	2012		2013	2012		
R Murphy	200%	<b>80,027</b>	—	<b>7,564</b>	—	<b>N/A</b>	N/A	<b>35%</b>
S Nicholls	100%	—	N/A	—	N/A	—	N/A	<b>0%</b>

Interests at 5 March 2014, being a date no more than one month prior to the date of the Notice convening the AGM, were the same as at 31 December 2013.

The market price of the Ordinary Shares as at 31 December 2013 was 274.5 pence per share and the closing price range during the year was 211.2 pence to 307.7 pence.

### Dilution

The Company's share schemes are currently funded through shares purchased in the market and have been since November 2010, prior to which they were funded through new issue shares. Funding of awards through new issue shares is subject to an overall dilution limit of 10% of issued share capital in any ten year period. Of this, 5% may be used in connection with the Company's discretionary share schemes. As of 31 December 2013, 13.1m (1.21%) and 8.6m (0.79%) shares have been issued pursuant to awards made in the previous ten years in connection with all share schemes and discretionary schemes respectively. Awards that are made, but then lapse or are forfeit, are excluded from the calculations.

### Payments to past Directors (audited information)

Payments to past Directors, after their termination date, in respect of unvested long term incentives during the year have been made to Andy Stevens as follows:

	No of shares awarded	No of shares vested	Value of shares vesting £k
PSP 2011	227,245	20,679	56.6
<b>Total</b>	<b>20,679</b>	<b>56.6</b>	

The PSP will vest at 9.1% on 10 March 2014 based on the performance conditions measured over the three financial years ended 31 December 2013 and outlined on page 56. As the awards had not vested at the date of this report, the average share price for the last three months of the financial year of 273.8 pence has been used to determine the value.

These payments have been made because Andy Stevens has been treated as a good leaver under the relevant plan rules. The good leaver provisions allow the Remuneration Committee some element of discretion, which they exercised in this case as Andy Stevens retired from office on the grounds of ill health.

Andy Stevens' BCP award did not vest due to performance conditions not being achieved.

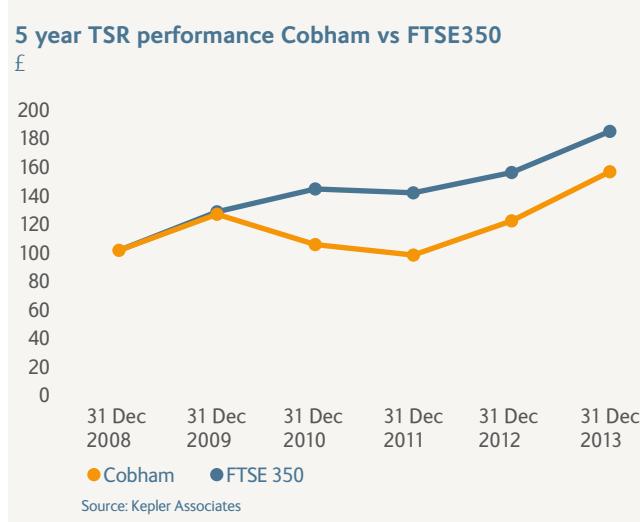
# Directors' Remuneration Report continued

## Payments for loss of office (audited information)

There were no loss of office payments made during the year.

## Performance graph and table

The graph below illustrates the TSR performance (share price growth plus dividends) of the Company against the FTSE350 Index over the past five years. The graph shows the value of £100 invested over the five year period ending 31 December 2013. The FTSE350 Index was chosen as it is a recognised broad equity market index of which the Company was a member during 2013 and is currently, as at 5 March 2014, ranked at 111th.



The table below shows historic CEO total remuneration, calculated on the same basis as that used in the single figure of remuneration table above.

Year	CEO	CEO single figure of total remuneration £k	Annual bonus payout against maximum opportunity %	Long term incentive vesting rates against maximum opportunity %
2013	R Murphy	2,058	34.3% (280)	N/A
2012	R Murphy	753	48.5% (182)	N/A
	A Stevens	1,283	45.0% (267)	58.0% (202)
2011	A Stevens	1,916	92.5% (555)	85.0% (546)
2010	A Stevens	1,478	33.5% (201)	87.0% (471)
2009	A Cook	1,496	93.0% (567)	100.0% (238)

## Percentage change in remuneration of CEO

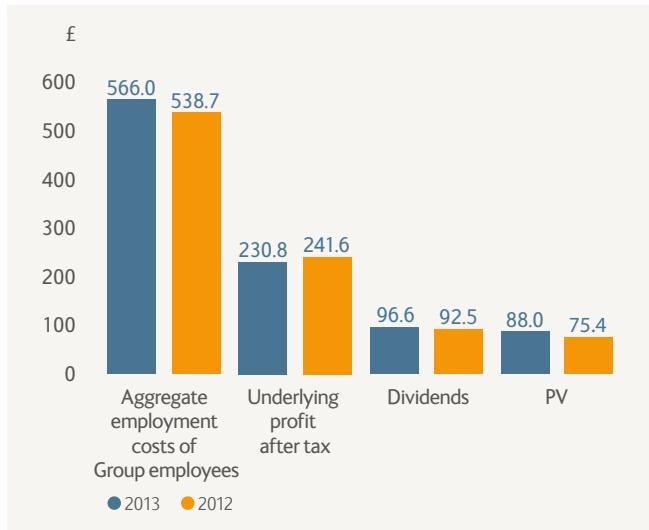
For 2014, UK salary increases were around 2.7%. Salary increases for the Executive Directors were 3% for both Bob Murphy and Simon Nicholls. The UK payroll has been chosen for comparison as the UK is the location of the head office.

The following table shows the year on year change in respect of the three remuneration elements shown in the table for the CEO as compared with that of UK employees generally:

Remuneration element	CEO	Average employee per capita figure
Salary	3.0%	2.7%
Benefits	(25%)	23%
AIP	(23%)	(41%)

## Relative importance of spend on pay

The chart below displays the relative expenditure of the Company on various matters, as required (in the case of Group employees' pay and shareholder distributions) by the relevant remuneration regulations:



The aggregate employment cost of Group employees is detailed in note 5 to the Group Financial Statements and includes employer social security payments. Group underlying profit after tax is shown above as this is profit attributable to the owners of the Group; refer to note 3. Dividends are shown in note 8. PV relates to the amount of profit the Group spends on research and development; refer to note 5.

## Statement of implementation of remuneration policy in the following financial year

Set out below is an explanation on the way the approved policy will be implemented in the current year compared with the reported year.

Element of Directors' remuneration policy	Change
Base pay	Current salaries for the CEO and the CFO effective from 1 March 2014 are £704,477 (\$1,103,000) and £412,000 respectively.
Other benefits/retirement benefits	No change.
AIP	No change. 2014 AIP opportunity is 120% of salary for CEO and 100% for CFO.
BCP	No change. Applicable to the CEO only, 2014 performance will be assessed against stretching economic profit targets, which are considered price sensitive as they are indicative of performance expectations and are not disclosed until the year of vesting.
PSP	No change. Awards to the value of 150% of salary will be made in March 2014. Performance will be equally weighted between EPS growth, relative TSR against a comparator group (see page 60) and cash conversion.

## Advisers to the Remuneration Committee

The Committee received advice during the year from Deloitte LLP. Additional advice was received from the Executive Vice President Human Resources, Vice President Compensation and Benefits and the Company Secretary. The Committee is satisfied that the advice it has received has been objective and independent due to Deloitte's compliance with the Code of Conduct of the Remuneration Consultants Group and the external experience of Committee members. Deloitte's performance is considered by the Committee as part of its performance evaluation. Total fees for advice provided to the Committee during the year amounted to £64,800, and were provided on a time/cost basis.

Adviser	Appointed by	Services provided to the Committee		Other services provided to the Company
		Remuneration Committee in November 2009	Remuneration strategy Incentive design Market data Legal advice	
Deloitte LLP	Remuneration Committee in November 2009	Remuneration strategy Incentive design Market data Legal advice	Take-on controls Tax IT audits	
Jones Day	Remuneration Committee	Legal advice (total fees £8,000)	Not applicable	

While proposals from the Committee take account of the advice received, the ultimate decision is made by the Committee and ratified by the Board in the absence of any advisers.

## 2013 voting at the Annual General Meeting

At the AGM held on 25 April 2013, shareholders approved the Directors' Remuneration Report for the year ended 31 December 2012. Below is the result in respect of the resolution, which required a simple majority (i.e. 50%) of the votes cast to be in favour in order for the resolution to be passed.

Votes for	%	Votes against	%
17,664,913	90.2	1,918,552	9.8
Votes withheld 1,158,730			

By order of the Board



**Dr J Patterson**

Chairman, Remuneration Committee

5 March 2014

# Directors' Report

**The Directors present their report and the audited Group and Parent Company Financial Statements of Cobham plc for the year ended 31 December 2013. The Company is registered in England and Wales under company number 30470. The Company's registered office is Brook Road, Wimborne, Dorset, BH21 2BJ, UK.**

## Dividends

An interim dividend of 2.64 pence per Ordinary Share of 2.50 pence each in the capital of the Company (Ordinary Shares) (2012: 2.40 pence) was paid in November 2013. The Directors are recommending a final dividend of 7.04 pence per Ordinary Share (2012: 6.40 pence) payable on 30 May 2014 to ordinary shareholders on the register as at 2 May 2014, making a total ordinary dividend for the year of 9.68 pence (2012: 8.80 pence).

Details of the total dividend paid out is covered in note 8.

## Directors' indemnity arrangements

The Directors have the benefit of a directors' and officers' liability insurance policy and the Company has entered into qualifying third party indemnity arrangements with them, as permitted by the Companies Act 2006. The policy was in force at the year-end and continues in force at the date of this report. The Directors are permitted to take independent legal advice at the Company's expense within set limits in furtherance of their duties.

## Directors' interests

None of the Directors is or was materially interested in any significant contract during or at the end of the financial year, particulars of which are required to be disclosed by the Listing Rules of the UK Listing Authority.

Details of Directors' share interests and of their rights to subscribe for shares are shown in the Directors' Remuneration Report on pages 48 to 63.

## Share capital

The Company has one class of Ordinary Shares which carry no right to fixed income, representing 99.9% of the total issued share capital.

In addition, 19,700 non-redeemable 6% second cumulative Preference Shares have been issued which represent 0.1% of total issued share capital.

The Directors have been authorised to allot and issue Ordinary Shares. These powers are exercised under authority of resolutions passed at the Company's AGM. No Ordinary Shares were issued during the current or prior year.

At the AGM held on 25 April 2013, the Company was authorised to purchase up to 107,857,590 Ordinary Shares. This authority will expire at the conclusion of the 2014 AGM. A special resolution will be put to shareholders at the AGM to renew the authority to make market purchases of the Company's shares up to a maximum of 10% of the share capital of the Company.

Subject to applicable statutes, and to the rights conferred on the holders of any other shares, shares may be issued with such rights and restrictions as the Company may by ordinary resolution decide or (if there is no such resolution or so far as the resolution does not make specific provision) as the Board may decide. Holders of Ordinary Shares are entitled to attend and speak at general meetings of the Company, to appoint one or more proxies and, if they are corporations, corporate representatives and to exercise voting rights. Holders of Ordinary Shares may receive a dividend and, on a liquidation, may share in the assets of the Company. Holders of Ordinary Shares are entitled to receive the Company's Annual Report and Accounts. Subject to meeting certain thresholds, holders of Ordinary Shares may requisition a general meeting of the Company or the proposal of a resolution at an AGM.

The shareholders of the 6% second cumulative Preference Shares are entitled to receive a fixed cumulative preference dividend at the rate of 6% per annum in priority to the payment of dividends on the Ordinary Shares. In addition, on a return of assets on the liquidation or otherwise of the Company, the assets available for distribution are to be applied first in repaying to the holders of the 6% second cumulative Preference Shares the amounts paid up on their shares.

## Voting rights and restrictions on transfer of shares

The rights and obligations attaching to the Ordinary Shares and 6% second cumulative Preference Shares of £1 each in the capital of the Company are set out in the Articles.

On a show of hands at a general meeting of the Company, every holder of shares present in person or by proxy and entitled to vote has one vote and on a poll every member present in person or by proxy and entitled to vote has one vote for every £1 in nominal value of the shares of which he or she is the holder. None of the Ordinary Shares carry any special rights with regard to control of the Company.

There are no restrictions on transfers of shares other than:

- Certain restrictions which may from time to time be imposed by laws or regulations;
- Pursuant to the Company's Code for Securities Transactions including the requirement on the Directors and designated employees to obtain approval to deal in the Company's shares; and
- Where a person with an interest in the Company's shares has been served with a disclosure notice and has failed to provide the Company with information concerning interests in those shares.

The Company is not aware of any arrangements between shareholders that may result in restrictions on the transfer of securities or voting rights.

## Significant arrangements – change of control

Individual operating companies in the Group have contractual arrangements with third parties in support of the Group's business activities which may take effect, alter or terminate upon a change of control of the Group following a takeover bid. Such contractual arrangements include supply of equipment, goods and services to third parties, such as research, design and production. Such contracts and arrangements may be deemed to be essential to one or more of the operating companies but there are no contracts or arrangements considered to be essential to the operation of the business of the Group as a whole, apart from the following:

- The Company has entered into a number of credit agreements with banks, and has issued senior notes under private placements. The total amount owing under such agreements at the year-end date is shown in note 19 to the Group Financial Statements. All agreements contain clauses such that, in the event of a change of control, the Company can offer to or must repay all such borrowings together with accrued interest, fees and other sums owing as required by the individual agreements.
- Under the Sentinel contract, entered into in March 2006, the Company must seek approval for any material change in the shareholding of the Company. There is an ancillary aircraft lease agreement under which a change of control may result in the termination of the lease if such event is likely to have a material adverse effect on the Company's ability to perform its obligations under the lease.
- Under the FSTA shareholders agreement entered into in June 2008, a change of control of the Company may result in a required sale of the Company's shares in FSTA to the other shareholders.

Further information relating to change of control appears within the remuneration policy table in the Directors' Remuneration Report on pages 50 and 51.

## Employee share schemes – rights of control

If required to do so by the Company, the trustee of the Cobham Share Incentive Plan (the Plan) will, on receipt of notice from the Company of any offer, compromise arrangement or scheme which affects shares held in the Plan, invite participants to direct the trustee on the exercise of any voting rights attaching to the shares held by the trustee on their behalf and/or direct how the trustee shall act in relation to those shares.

The trustee will not vote in respect of any shares held in the Plan in respect of which it has received no directions nor will the trustee vote in respect of any shares which are unallocated under the Plan.

The trustees of the Employee Benefit Trust (which, as at 31 December 2013, hold 9,728,809 Ordinary Shares to be used for settlement of option and share awards under the Company's long term incentive schemes and all employee share option schemes) waive all rights to vote in respect of any shares they hold within the Trust.

## Major interests in shares

As at 31 December 2013, the Company had been notified of the following interests in the Ordinary Shares:

	Number of shares at the date of notification	% at date of notification
Prudential plc group of companies	54,277,614	5.03
Sprucegrove Investment Management	54,070,021	Below 5
Invesco Limited	53,893,724	4.99
BlackRock, Inc.	52,888,997	Below 5
Schroders plc	56,388,880	5.228

Since the year-end and up to 5 March 2014, being a date not more than a month prior to the date of the AGM Notice, the Company had received no notices of interests in the Ordinary Shares in accordance with DTR 5.

## Financial instruments

Notes 16, 23 and 25 to the Group Financial Statements and note 12 to the Parent Company Financial Statements contain disclosures relating to the use of financial instruments. The Group uses derivative financial instruments in its management of financial risks and does not trade in financial instruments or use complex financial instruments.

## People

Information concerning diversity in the workforce and the employment of disabled persons is shown in the CR&S Report on pages 32 to 35.

## Research and development

The Group continues to invest in the important area of research and development; further details can be found on page 23. During the year, the Group expended £88.0m (2012: £75.4m) on non-customer funded research and development.

## Events after the balance sheet date

Note 33 to the Group Financial Statements contains information in respect of post balance sheet events.

## Political donations and expenditure

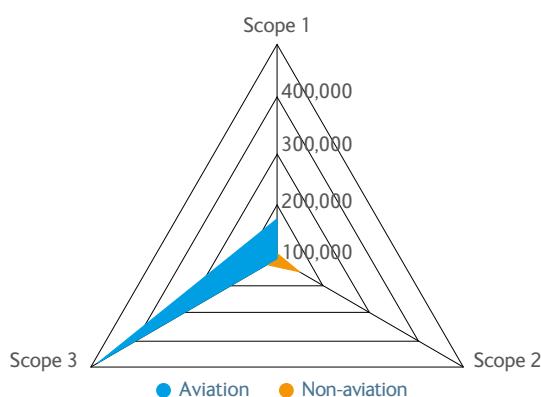
No contributions were made to political organisations during the current or prior year.

# Directors' Report continued

## Greenhouse gas emissions

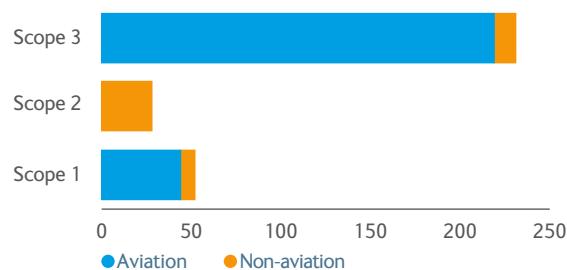
The majority of Cobham's total greenhouse gas emissions (85%) come from its aviation activity (figure 1), mostly being from the Aviation Services business. Growth in this business yields an increase in Cobham's absolute emissions (figure 1) and emissions intensity (figure 2).

**Figure 1 – Aviation and non-aviation emissions (tCO<sub>2</sub>e) for Scopes 1, 2 & 3**



	Aviation		Non-aviation		Total
	tCO <sub>2</sub> e	%	tCO <sub>2</sub> e	%	
*Scope 1	77,066	84	14,277	16	91,343
*Scope 2	N/A	–	48,276	100	48,276
Scope 3	384,860	95	21,640	5	406,500
<b>Total</b>	<b>461,926</b>	<b>85</b>	<b>84,193</b>	<b>15</b>	<b>546,119</b>

**Figure 2 – Aviation and non-aviation emissions (tCO<sub>2</sub>e/£m) for Scopes 1, 2 & 3**



tCO <sub>2</sub> e/£m	Year	Aviation	Non-aviation	% Total change
Scope 1	2012	49	5	
	2013	43	8	(5)
Scope 2	2012	N/A	30	
	2013	N/A	27	(10)
Scope 3	2012	206	8	
	2013	216	12	7

### Definitions:

Scope 1 comprises direct emissions from owned plant and equipment including aviation fuel, natural gas, heating oil, non-automotive diesel, fugitive emissions, solvent emissions and automotive fuel.

Scope 2 comprises indirect emissions from purchased renewable and non-renewable electricity.

Scope 3 comprises indirect emissions from non-owned plant and equipment including aviation fuel and business travel (train, air and car).

## Methodology and data verification

Cobham collects data annually on greenhouse gas emissions from its wholly-owned operational subsidiaries. Cobham uses the World Business Council for Sustainable Development (WBCSD) & World Resources Institute (WRI) Greenhouse Gas (GHG) Protocol method to report its greenhouse gas emissions and defines its emissions boundary as those under its direct operational control.

Reported data excludes joint ventures not under Cobham's operational control, sites with less than five people, sites leased to tenants, vacant properties being disposed of, and any business units that have been closed or divested during the course of the year for which there is less than six months of reported data. A further seven locations were omitted by our business units from reporting in error, although our assessment is that these are not material.

100% of Cobham's wholly-owned operations have been reviewed internally to identify omissions and significant variations from the prior year.

## Data assurance

We engaged KPMG LLP to undertake a limited assurance engagement, reporting to Cobham plc, using the assurance standards ISAE 3000 and ISAE 3410 over the data that has been highlighted in this report with\*. Their full statement is available at [www.cobhamsustainability.com](http://www.cobhamsustainability.com) and they have provided an unqualified opinion on the data. The level of assurance provided for a limited assurance engagement is substantially lower than a reasonable assurance engagement. In order to reach their opinion they performed a range of procedures which included interviews with management, examination of reporting systems, four site visits to our operations in the UK, Australia and US as well as specific data testing at these sites and Head Office. A summary of the work they performed is included within their assurance opinion.

Limited external assurance was provided on the Group's Scope 1 and Scope 2 GHG data for 2013. Non financial performance information, greenhouse gas quantification in particular, is subject to more inherent limitations than financial information. It is important to read the selected CR&S information contained within the CR&S report in the context of the full limited assurance statement and the reporting guidelines set out in the footnotes to the data tables on 'Energy & Climate' at [www.cobhamsustainability.com](http://www.cobhamsustainability.com).

Further detail on Cobham's CR&S approach, objectives and performance is available on pages 32 to 35.

## Annual General Meeting

The Company's AGM will be held at 12 noon on Thursday, 24 April 2014 at the offices of UBS Investment Bank, 1 Finsbury Avenue, London EC2M 2PP.

The Company arranges for the Notice of AGM and related papers to be sent to shareholders at least 20 working days before the meeting.

By order of the Board

**L Colloff**  
Company Secretary  
5 March 2014

The Directors are responsible for preparing the Annual Report and Accounts, the Directors' Remuneration Report and the Group Financial Statements in accordance with applicable laws and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors have prepared the Group Financial Statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and the Parent Company Financial Statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards) and applicable law. Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the profit or loss of the Group and the Company for that period.

In preparing those financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and accounting estimates that are reasonable and prudent;
- State whether IFRS, as adopted by the EU, and applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Group and the Parent Company Financial Statements respectively; and
- Prepare the Group and Parent Company Financial Statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and the Group and to enable them to ensure that the Group Financial Statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Group's website ([www.cobham.com](http://www.cobham.com)). Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Directors consider that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

## Directors' responsibility statement

Each of the Directors, whose names and functions are listed on pages 36 and 37, confirm that, to the best of their knowledge:

- The Group Financial Statements, which have been prepared in accordance with the IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- The Strategic Report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that it faces.

## Directors' declaration in relation to relevant audit information

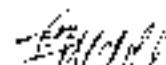
In the case of each Director in office at the date the Directors' Report is approved, that:

- a. So far as the Director is aware, there is no relevant audit information of which the Group's auditors were unaware; and
- b. He or she has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Group's auditors are aware of that information.

The responsibility statement was approved by the Board of Directors on 5 March 2014 and signed on its behalf by:



**R Murphy**  
Chief Executive Officer



**S Nicholls**  
Chief Financial Officer

# Compliance with the UK Corporate Governance Code

For the year ended 31 December 2013, the Board believes that the Company has complied with the principles and provisions of the UK Corporate Governance Code. A full version of the UK Corporate Governance Code can be found on the Financial Reporting Council's website at [www.frc.org.uk](http://www.frc.org.uk). Further details on how compliance is achieved can be found in the Corporate Governance and Directors' Remuneration Reports.

## A

### Leadership

#### A1 The Board's role

The Board meets nine times a year in order to review the Company's performance and strategy against set objectives. The Board's role is to lead the Group with a view to the creation of strong, sustainable financial performance and long term shareholder value, to approve the Group's Strategic Plan and to monitor management performance against plan.

The Board has adopted a clear schedule of matters reserved for its specific approval, including a framework for those decisions which can be delegated to committees or otherwise.

Further details can be found in the Corporate Governance Report.

#### A2 A clear division of responsibilities

The Board's policy is that the roles of the Chairman and CEO should be performed by different people. The division of responsibilities is documented and clearly understood. The Chairman is responsible for the leadership and effectiveness of the Board, and the CEO is responsible for leading the day-to-day management of the Company within the strategy set by the Board.

#### A3 Role of the Chairman

The Chairman sets the agenda for meetings, manages the meeting timetable and facilitates open and constructive dialogue during the meetings.

#### A4 Role of the Non-executive Directors

The Chairman promotes an open and constructive environment in the boardroom and actively invites the Non-executive Directors' views.

The Senior Independent Director, Michael Wareing, held a meeting with the Non-executives in the absence of the Chairman to appraise the Chairman's performance.

The Chairman has held regular meetings with the Non-executives in the absence of Executive Directors, providing an opportunity for any concerns to be discussed.

The Board currently consists of nine individuals, the Chairman, two Executive Directors, and six independent Non-executive Directors.

#### B2 Board appointments

The appointment of new Directors to the Board is led by the Nomination Committee. The Nomination Committee terms of reference, as published on the Company website, document the responsibility regarding Board appointments. The Committee consists of all six Non-executive Directors and the Chairman. Further details of the appointments undertaken during the year and succession planning can be found on page 43.

## B

### Effectiveness

#### B1 The Board's composition

The composition of the Board is reviewed regularly by the Nomination Committee to ensure that there is an appropriate mix of skills on the Board and a range of diverse experience. Board members' biographies are provided on pages 36 and 37, which identify the experience each Director brings to the Board. A table identifying the skills and experience of the Board members may be found on page 43.

The Board determines, through the Nomination Committee, the independence of its members. Conflicts of interest are also monitored and updated at least annually and more frequently as and when required.

#### B3 Time commitments

The time commitments of Non-executive Directors are defined on appointment and regularly evaluated. The Chairman gives consideration to new directorships which may impact existing time commitments.

#### B4 Training and development

On appointment, Directors undertake a structured induction programme, which is supplemented by visits to key locations and meetings with senior executives. Further training for Directors is offered when taking a new role on a Committee, and is otherwise available as required and may be provided through tailored programmes.

Further details can be found in the Directors' professional development section on page 43.

#### B5 Provision of information and support

The Chairman, in conjunction with the Company Secretary, ensures that all Board members receive accurate and timely information.

## B6 Board and committees performance evaluation

The Board and the Board Committees undertook an internal evaluation in 2013. Details of the process undertaken and a table of actions instigated by this evaluation are included on page 40.

## B7 Re-election of the Directors

All Directors were subject to shareholder re-election at the 2013 AGM.

## C Accountability

### C1 Financial and business reporting

The Statement of the Directors' Responsibilities is set out on page 67, and the Independent Auditors' Reports are on pages 70 to 73, and pages 125 and 126.

The Company's business model is explained on pages 4 and 5.

### C2 Risk management and internal control systems

The Board sets the Company's risk appetite and annually reviews the effectiveness of the Company's risk management and internal control systems. The activities of the Audit and Risk Committees, which assist the Board with its responsibilities in relation to risk management, reporting and assurance, are set out on page 46.

### C3 Role and responsibilities of the Audit Committee

Details of the composition of the Audit Committee, and how the Committee has discharged its responsibilities during the year, are provided in the Audit Committee Report on pages 44 to 47.

## D Remuneration

### D1 Levels and elements of remuneration

The Board believes that the Group's Remuneration Policy continues to enable the Group to attract, retain and motivate the executive talent required for the delivery of its business strategy, while linking closely to the long term performance of the Group and the interests of shareholders. For further information, see the Directors' Remuneration Policy on pages 49 to 54.

### D2 Development of remuneration policy and packages

The membership of the Remuneration Committee is made up of Non-executive Directors only. The terms of reference for the Remuneration Committee are reviewed annually and are available on the Company website.

The Remuneration Committee has delegated authority for setting the remuneration of Executive Directors and the Chairman. The fees payable to the Non-executive Directors are determined by the Board, on recommendation from the Executive Directors Committee.

## E Relations with shareholders

### E1 Shareholder engagement and dialogue

Effective communication and engagement with investors are of paramount importance to the continued success of the Company. The Company maintains a relationship with shareholders through a series of roadshows completed

through the year, which are usually attended by the CEO and the CFO. Further details can be found in the Corporate Governance Report on pages 40 and 41.

### E2 Constructive use of the AGM

The Board values the AGM as an important opportunity to engage with investors. Attendees at the AGM have the opportunity to ask questions to the Board and to speak to individual Directors following the formal business of the meeting.

# Independent Auditors' Report to the Members of Cobham plc

## Report on the Group Financial Statements

### Our opinion

In our opinion the Group Financial Statements defined below:

- Give a true and fair view of the state of the Group's affairs as at 31 December 2013 and of the Group's profit and cash flows for the year then ended;
- Have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- Have been prepared in accordance with the requirements of the Companies Act 2006 and Article 4 of the IAS Regulation.

This opinion is to be read in the context of what we say in the remainder of this report.

### What we have audited

The Group Financial Statements, which are prepared by Cobham plc, comprise:

- The Consolidated Income Statement and Statement of Comprehensive Income for the year ended 31 December 2013;
- The Consolidated Balance Sheet as at 31 December 2013;
- The Consolidated Statement of Changes in Equity and Cash Flow Statement for the year then ended; and
- The notes to the Group Financial Statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation comprises applicable law and IFRSs as adopted by the European Union.

Certain disclosures required by the financial reporting framework have been presented elsewhere in the Annual Report and Accounts (Annual Report), rather than in the notes to the Financial Statements. These are cross-referenced from the financial statements and are identified as audited.

### What an audit of Financial Statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & Ireland)). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- Whether the accounting policies are appropriate to the Group's circumstances and have been consistently applied and adequately disclosed;
- The reasonableness of significant accounting estimates made by the Directors; and
- The overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited Group Financial Statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies, we consider the implications for our report.

### Overview of our audit approach

#### Materiality

We set certain thresholds for materiality. These helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the Group Financial Statements as a whole to be £14m which is approximately 5% of underlying profit before taxation. We used underlying profit before taxation to exclude amortisation of intangible assets acquired in business combinations and to remove the effect of volatility such as exceptional costs.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £0.5m as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

#### Overview of the scope of our audit

The Group is structured along four reported segments, being Aerospace and Security, Defence Systems, Mission Systems and Aviation Services. The Group Financial Statements are a consolidation of 59 reporting units within these segments, comprising the Group's operating businesses and centralised functions.

In establishing the overall approach to the Group audit, we determined the type of work that needed to be performed at the reporting units by us, as the Group engagement team, or subsidiary audit teams from other PwC network firms operating under our instruction. Where the work was performed by subsidiary audit teams, we determined the level of involvement we needed to have in the audit work at those reporting units to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the Group Financial Statements as a whole.

Accordingly, of the Group's 59 reporting units, we identified 22 which, in our view, required an audit of their complete financial information, either due to their size, their risk characteristics or because some are covered on a rotational basis over a two or three year cycle. Specific audit procedures on certain balances and transactions were performed at a further 15 reporting units. Audit procedures were performed at principal manufacturing locations, both significant Aviation Services reporting units and new acquisitions in the year.

Where subsidiary audit teams performed work at the reporting unit level on behalf of the Group audit team, this work was performed to lower materiality levels appropriate to the individual units (which are typically subject to local audit requirements). These materiality levels ranged from £0.7m to £4.5m.

The reporting units in scope covered 92% of the Group's underlying profit before taxation and 89% of the Group's revenue. This, together with additional procedures performed at the Group level, gave us the evidence we needed for our opinion on the Group Financial Statements as a whole.

### Areas of particular audit focus

In preparing the financial statements, the Directors made a number of subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We primarily focused our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

In our audit, we tested and examined information, using sampling and other auditing techniques, to the extent we considered necessary to provide a reasonable basis for us to draw conclusions. We obtained audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

We considered the following areas to be those that required particular focus in the current year. This is not a complete list of all risks or areas of focus identified by our audit. We discussed these areas of focus with the Audit Committee. Their report on those matters that they considered to be significant issues in relation to the financial statements is set out on page 46.

	Area of focus	How the scope of our audit addressed the area of focus
► <b>Impairment assessment</b>	<p>The Group has significant goodwill and intangible asset balances arising from acquisitions. The Directors formally assess the carrying value of these assets on an annual basis.</p> <p>We focused on this area because it involves complex and subjective judgements by the Directors about the future results of the business. As a result of the Directors' assessment, an impairment charge of £63m was recorded; see note 11 of the Group Financial Statements.</p>	<p>In evaluating whether any impairment was necessary to the carrying value of goodwill and intangible assets, our audit work involved obtaining evidence regarding its recoverable amount and how it compared to the amount at which it is currently recorded. We evaluated the Directors' future cash flow forecasts, including comparing them with the latest Board approved strategic plans and looked at historic performance. We challenged the Directors' key assumptions within these plans, including the discount rate and growth rates. We also performed sensitivity analysis around those key assumptions. Having ascertained the extent of change in those assumptions that either individually or collectively would be required for the asset to be impaired, we considered the likelihood of such movement in those key assumptions arising. For the asset impaired in the year we checked the calculation of the impairment charge.</p>
► <b>Accounting for contract profitability, including the recognition of contract loss provisions</b>	<p>The Group has a number of significant, complex development and production contracts which span more than one accounting period.</p> <p>We focused on this area as the assessment of contract performance over a long duration is often subjective and dependent upon engineering assessments as well as financial estimates.</p>	<p>We have reviewed the basis of profit recognition on the Group's key contracts. We evaluated the accounting in the context of the Group accounting policies and contract terms.</p> <p>We have assessed the design of controls in place over key contracts, including the adequacy and frequency of programme reviews performed by management.</p> <p>We examined the assumptions behind estimated costs to complete, challenging the reasonableness of these in light of supporting evidence.</p> <p>We evaluated the reasonableness of estimated revenue for customer claims submitted to recover additional costs incurred, including considering legal advice received where appropriate.</p>
► <b>Revenue recognition</b>	<p>ISAs (UK &amp; Ireland) presume there is a risk of fraud in relation to revenue recognition as most businesses, including the Group, face this risk.</p> <p>We focused on cut-off around the year-end because material revenue transactions can occur close to that date and the recognition of significant milestones on development contracts which often involve some judgement surrounding the achievement of those milestones.</p>	<p>We tested manual journals posted to revenue to check whether there was any indication of fraud.</p> <p>We tested the timing of revenue recognition of transactions close to the period end to establish whether they were recorded in the correct period.</p> <p>We tested the basis of revenue recognition on key development contracts, evaluating the revenue recognised against contract terms and evidence of customer acceptance of specific milestones reached.</p>
► <b>Risk of management override of internal controls</b>	<p>ISAs (UK &amp; Ireland) require that we consider this, because management in all businesses are in a position of authority that means they can override internal controls established to prevent fraud or error.</p>	<p>We assessed the overall control environment of the Group.</p> <p>We tested manual journal entries. We examined the significant accounting estimates and judgements relevant to the financial statements for evidence of bias by the Directors that may represent a risk of material misstatement due to fraud. We also incorporated an element of unpredictability into our testing plans.</p>

# Independent Auditors' Report continued

## Going concern

Under the Listing Rules, we are required to review the Directors' statement, set out on page 27, in relation to going concern. We have nothing to report having performed our review. As noted in the Directors' statement, the Directors have concluded that it is appropriate to prepare the Group's financial statements using the going concern basis of accounting. The going concern basis presumes that the Group has adequate resources to remain in operation, and that the Directors intend it to do so, for at least one year from the date the financial statements were signed. As part of our audit, we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Group's ability to continue as a going concern.

## Opinions on matters prescribed by the Companies Act 2006

In our opinion:

- The information given in the Strategic Report and the Directors' Report for the financial year for which the Group Financial Statements are prepared is consistent with the Group Financial Statements; and
- The information given in the Corporate Governance Report set out on pages 38 to 47 in the Annual Report with respect to internal control and risk management systems and about share capital structures is consistent with the financial statements.

## Other matters on which we are required to report by exception

### Adequacy of information and explanations received

Under the Companies Act 2006, we are required to report to you if, in our opinion, we have not received all the information and explanations we require for our audit. We have no exceptions to report arising from this responsibility.

### Directors' remuneration

Under the Companies Act 2006, we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law have not been made, and under the Listing Rules we are required to review certain elements of the report to shareholders by the Board on Directors' remuneration. We have no exceptions to report arising from these responsibilities.

## Corporate governance statement

Under the Companies Act 2006, we are required to report to you, if, in our opinion, a corporate governance statement has not been prepared by the Parent Company. We have no exceptions to report arising from this responsibility.

Under the Listing Rules, we are required to review the part of the corporate governance statement relating to the Company's compliance with nine provisions of the UK Corporate Governance Code (the Code). We have nothing to report having performed our review.

On page 67 of the Annual Report, as required by the Code Provision C.1.1, the Directors state that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Group's performance, business model and strategy. On page 46, as required by C.3.8 of the Code, the Audit Committee has set out the significant issues that it considered in relation to the financial statements, and how they were addressed. Under ISAs (UK & Ireland), we are required to report to you if, in our opinion:

- The statement given by the Directors is materially inconsistent with our knowledge of the Group acquired in the course of performing our audit; or
- The section of the Annual Report describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.

We have no exceptions to report arising from this responsibility.

## Other information in the Annual Report

Under ISAs (UK & Ireland), we are required to report to you if, in our opinion, information in the Annual Report is:

- Materially inconsistent with the information in the audited Group Financial Statements; or
- Apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group acquired in the course of performing our audit; or
- Is otherwise misleading.

We have no exceptions to report arising from this responsibility.

**Responsibilities for the financial statements and the audit****Our responsibilities and those of the Directors**

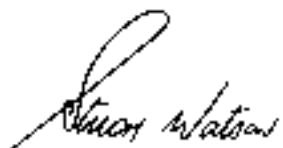
As explained more fully in the Statement of Directors' Responsibilities set out on page 67, the Directors are responsible for the preparation of the Group Financial Statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the Group Financial Statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

**Other matter**

We have reported separately on the Parent Company Financial Statements of Cobham plc for the year ended 31 December 2013 and on the information in the Directors' Remuneration Report that is described as having been audited.


**Stuart Watson**

(Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London  
5 March 2014

# Consolidated Income Statement

For the year ended 31 December 2013

£m	Note	2013	2012 (as restated)
Revenue	4	<b>1,789.7</b>	1,749.4
Cost of sales		<b>(1,220.9)</b>	(1,173.3)
<b>Gross profit</b>		<b>568.8</b>	576.1
Selling and distribution costs		<b>(84.7)</b>	(81.1)
Administrative expenses		<b>(328.4)</b>	(264.9)
Share of post-tax results of joint ventures and associates		<b>3.1</b>	7.4
<b>Operating profit</b>		<b>158.8</b>	237.5
Finance income	6	<b>5.3</b>	6.8
Finance costs	6	<b>(37.5)</b>	(40.3)
<b>Profit before taxation</b>		<b>126.6</b>	204.0
Taxation	7	<b>(12.1)</b>	(32.2)
<b>Profit after taxation for the year</b>		<b>114.5</b>	171.8
Attributable to:			
Owners of the parent		<b>114.3</b>	171.7
Non-controlling interests		<b>0.2</b>	0.1
		<b>114.5</b>	171.8
Earnings per Ordinary Share	9		
Basic		<b>10.70p</b>	15.98p
Diluted		<b>10.65p</b>	15.93p

Trading profit is calculated as follows:

£m	Note	2013	2012 (as restated)
Operating profit		<b>158.8</b>	237.5
Adjusted to exclude:			
Business restructuring – Excellence in Delivery		<b>56.1</b>	37.9
Movements in non-hedge accounted derivative financial instruments		<b>(2.2)</b>	(11.1)
Amortisation of intangible assets arising on business combinations		<b>103.9</b>	68.9
Impairment of goodwill		<b>63.0</b>	–
Revaluation gain arising on equity interests in FBH (2012: Thrane & Thrane)		<b>(62.1)</b>	(1.0)
Other business acquisition and divestment related items		<b>0.1</b>	(0.2)
<b>Trading profit</b>	3	<b>317.6</b>	332.0
<b>Underlying EPS</b>		<b>21.60p</b>	22.48p

The definitions of trading profit and underlying EPS are shown in note 1.

# Consolidated Statement of Comprehensive Income

For the year ended 31 December 2013

Group Financial Statements

£m		Note	2013	2012 (as restated)
<b>Profit after taxation for the year</b>			<b>114.5</b>	171.8
<b>Items that will not be reclassified subsequently to profit or loss</b>				
Remeasurements of defined benefit retirement benefit obligations	24		<b>(25.6)</b>	(13.7)
Actuarial loss on other retirement benefit obligations	24		—	(0.5)
Tax effects	7		<b>4.1</b>	2.0
			<b>(21.5)</b>	(12.2)
<b>Items that may subsequently be reclassified to profit or loss</b>				
Net translation differences on investments in overseas subsidiaries	27		<b>(11.1)</b>	(24.0)
Reclassification of cash flow hedge fair values	23		<b>4.5</b>	7.2
Movements in hedge accounted derivative financial instruments	23		<b>0.6</b>	(3.1)
Tax effects	7		<b>(1.2)</b>	(3.2)
			<b>(7.2)</b>	(23.1)
<b>Total other comprehensive expense for the year</b>			<b>(28.7)</b>	(35.3)
<b>Total comprehensive income for the year</b>			<b>85.8</b>	136.5
Attributable to:				
Owners of the parent			<b>85.6</b>	136.4
Non-controlling interests			<b>0.2</b>	0.1
			<b>85.8</b>	136.5

# Consolidated Balance Sheet

As at 31 December 2013

£m	Note	2013	2012
<b>Assets</b>			
<b>Non-current assets</b>			
Intangible assets	11	<b>1,162.2</b>	1,102.1
Property, plant and equipment	12	<b>350.8</b>	304.8
Investment properties	13	<b>9.9</b>	10.7
Investments in joint ventures and associates	14	<b>3.1</b>	15.8
Trade and other receivables	17	<b>22.2</b>	47.1
Other financial assets	16	<b>6.1</b>	—
Deferred tax	22	<b>9.9</b>	9.8
Derivative financial instruments	23	<b>5.1</b>	3.4
		<b>1,569.3</b>	1,493.7
<b>Current assets</b>			
Inventories	15	<b>315.9</b>	306.4
Trade and other receivables	17	<b>317.7</b>	281.0
Current tax receivables		<b>0.8</b>	7.5
Derivative financial instruments	23	<b>6.6</b>	3.7
Cash and cash equivalents	10	<b>200.7</b>	264.2
Assets classified as held for sale	18	<b>8.2</b>	15.1
		<b>849.9</b>	877.9
<b>Liabilities</b>			
<b>Current liabilities</b>			
Borrowings	19	<b>(344.5)</b>	(307.3)
Trade and other payables	20	<b>(370.3)</b>	(349.9)
Provisions	21	<b>(34.4)</b>	(36.3)
Current tax liabilities		<b>(112.2)</b>	(119.2)
Derivative financial instruments	23	<b>(4.6)</b>	(6.6)
Liabilities classified as held for sale	18	<b>(5.2)</b>	(3.2)
		<b>(871.2)</b>	(822.5)
<b>Non-current liabilities</b>			
Borrowings	19	<b>(309.6)</b>	(316.8)
Trade and other payables	20	<b>(38.0)</b>	(39.1)
Provisions	21	<b>(8.6)</b>	(10.9)
Deferred tax	22	<b>(52.9)</b>	(44.2)
Derivative financial instruments	23	<b>(7.4)</b>	(10.3)
Retirement benefit obligations	24	<b>(87.3)</b>	(73.4)
		<b>(503.8)</b>	(494.7)
<b>Net assets</b>		<b>1,044.2</b>	1,054.4

£m	Note	2013	2012
<b>Equity</b>			
Share capital	26	<b>28.9</b>	28.9
Share premium account		<b>126.6</b>	126.6
Other reserves	27	<b>55.2</b>	64.2
Retained earnings		<b>832.7</b>	834.1
<b>Total equity attributable to the owners of the parent</b>		<b>1,043.4</b>	1,053.8
Non-controlling interests in equity		<b>0.8</b>	0.6
<b>Total equity</b>		<b>1,044.2</b>	1,054.4
Net debt	10	<b>(453.4)</b>	(359.9)

The financial statements on pages 74 to 124 were approved by a duly appointed and authorised committee of the Board on 5 March 2014 and signed on its behalf by:

R Murphy  
Directors

S Nicholls

# Consolidated Statement of Changes in Equity

For the year ended 31 December 2013

£m	Share capital	Share premium account	Other reserves (note 27)	Retained earnings	Attributable to owners of the parent	Total equity	Non- controlling interests in equity	Total equity
Total equity at 1 January 2012	28.9	126.6	83.8	779.3	1,018.6	0.5	1,019.1	
Profit for the year (as restated)	–	–	–	171.7	171.7	0.1	171.8	
Items that will not be reclassified subsequently to profit or loss (as restated)	–	–	–	(12.2)	(12.2)	–	(12.2)	
Items that may subsequently be reclassified to profit or loss	–	–	(23.1)	–	(23.1)	–	(23.1)	
<b>Total comprehensive income for the year</b>	<b>–</b>	<b>–</b>	<b>(23.1)</b>	<b>159.5</b>	<b>136.4</b>	<b>0.1</b>	<b>136.5</b>	
Net purchase of treasury shares	–	–	–	(18.7)	(18.7)	–	(18.7)	
Dividends (note 8)	–	–	–	(92.5)	(92.5)	–	(92.5)	
Share based payments (note 28)	–	–	6.8	–	6.8	–	6.8	
Dividend equivalents paid on vesting of PSP and BCP awards	–	–	(0.1)	–	(0.1)	–	(0.1)	
Release of hedge reserve	–	–	2.8	–	2.8	–	2.8	
Transfers of other reserves to retained earnings	–	–	(6.5)	6.5	–	–	–	
Tax effects (note 7)	–	–	0.5	–	0.5	–	0.5	
<b>Total equity at 31 December 2012</b>	<b>28.9</b>	<b>126.6</b>	<b>64.2</b>	<b>834.1</b>	<b>1,053.8</b>	<b>0.6</b>	<b>1,054.4</b>	
Profit for the year	–	–	–	114.3	114.3	0.2	114.5	
Items that will not be reclassified subsequently to profit or loss	–	–	–	(21.5)	(21.5)	–	(21.5)	
Items that may subsequently be reclassified to profit or loss	–	–	(7.2)	–	(7.2)	–	(7.2)	
<b>Total comprehensive income for the year</b>	<b>–</b>	<b>–</b>	<b>(7.2)</b>	<b>92.8</b>	<b>85.6</b>	<b>0.2</b>	<b>85.8</b>	
Net purchase of treasury shares	–	–	–	(1.8)	(1.8)	–	(1.8)	
Dividends (note 8)	–	–	–	(96.6)	(96.6)	–	(96.6)	
Share based payments (note 28)	–	–	(1.7)	–	(1.7)	–	(1.7)	
Release of hedge reserve	–	–	1.5	–	1.5	–	1.5	
Transfers of other reserves to retained earnings	–	–	(4.2)	4.2	–	–	–	
Tax effects (note 7)	–	–	2.6	–	2.6	–	2.6	
<b>Total equity at 31 December 2013</b>	<b>28.9</b>	<b>126.6</b>	<b>55.2</b>	<b>832.7</b>	<b>1,043.4</b>	<b>0.8</b>	<b>1,044.2</b>	

# Consolidated Cash Flow Statement

For the year ended 31 December 2013

Group Financial Statements

£m	Note	2013	2012
Operating profit (as restated for prior year)		<b>158.8</b>	237.5
Non-cash items:			
Share of post-tax profits of joint ventures and associates		(3.1)	(7.4)
Revaluation gain arising on equity interests	29	(62.1)	(1.0)
Depreciation and amortisation including impairment		<b>235.1</b>	129.2
(Profit)/loss on sale of property, plant and equipment		(1.1)	0.6
Business acquisition and divestment related items		(1.6)	(6.6)
Movements in non-hedge accounted derivative financial instruments	23	(2.2)	(11.1)
Pension contributions in excess of service cost and administration cost (as restated for prior year)	24	(14.5)	(14.3)
Share based payments	28	(1.7)	6.8
Operating cash movements:			
Increase in inventories		(0.3)	(3.6)
(Increase)/decrease in trade and other receivables		(26.2)	34.4
Decrease in trade and other payables		(0.3)	(1.0)
Decrease in provisions		(3.9)	(1.4)
Tax paid		(37.6)	(45.2)
Interest paid		(33.7)	(35.3)
Interest received		5.0	6.6
<b>Net cash from operating activities</b>		<b>210.6</b>	288.2
<b>Cash flows from investing activities</b>			
Dividends received from joint ventures	32	<b>3.7</b>	7.5
Purchase of property, plant and equipment		(58.0)	(48.2)
Purchase of intangible assets		(11.7)	(13.8)
Capitalised expenditure on intangible assets	11	—	(1.4)
Proceeds on disposal of property, plant and equipment		<b>8.0</b>	1.0
Investment in other financial assets		(6.1)	—
Loans repaid by/(issued to) joint ventures		<b>2.1</b>	(36.9)
Investment in loan notes		(18.3)	—
Acquisition of subsidiaries net of cash or debt acquired	29	(126.0)	(282.7)
Contingent consideration paid		(2.5)	(3.0)
Proceeds from vesting of warrants in acquired business		—	8.4
Proceeds of business divestments		<b>0.5</b>	47.4
<b>Net cash used in investing activities</b>		<b>(208.3)</b>	(321.7)
<b>Cash flows from financing activities</b>			
Dividends paid	8	<b>(96.6)</b>	(92.5)
Purchase of treasury shares		(15.3)	(26.3)
Proceeds on allocation of treasury shares		<b>13.5</b>	7.5
New borrowings		<b>67.0</b>	184.5
Repayment of borrowings		(7.7)	(113.1)
<b>Net cash used in financing activities</b>		<b>(39.1)</b>	(39.9)
<b>Net decrease in cash and cash equivalents</b>		<b>(36.8)</b>	(73.4)
Exchange movements		(14.4)	(8.3)
Cash and cash equivalents at start of year		<b>250.2</b>	331.9
<b>Cash and cash equivalents at end of year</b>	10	<b>199.0</b>	250.2

A reconciliation of cash and cash equivalents to the Consolidated Balance Sheet and movement in net debt is detailed in note 10.

# Notes to the Group Financial Statements

## 1. Accounting Policies

### General information

These financial statements are the consolidated financial statements of Cobham plc (the Company), a public company limited by shares, registered and domiciled in the United Kingdom and its subsidiaries (the Group).

### Basis of preparation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, International Financial Reporting Interpretation Council (IFRIC) interpretations and those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

These financial statements have been prepared on a going concern basis under the historical cost convention, as modified by the revaluation of derivative financial instruments and assets held for sale which are held at fair value.

### Principal accounting policies

The principal accounting policies, which have been consistently applied unless otherwise stated, are as set out below.

### Accounting developments

New standards and amendments to standards which have been adopted with effect from 1 January 2013 and which impact these financial statements are as follows:

- The implementation of IFRS 13, Fair Value Measurement has required some amendments to disclosures on financial instruments but has not affected the fair value measurements used.
- The amendment to IAS 19, Employee Benefits has been applied retrospectively. This resulted in a reduction in the prior year reported profit after tax of £1.6m; further details are provided in note 2.
- The amendment to IAS 1, Financial Statement Presentation has impacted the presentation of items within Other Comprehensive Income (OCI), grouping items on the basis of whether they can, or cannot, be subsequently reclassified to profit or loss.

In addition, the following standards, amendments to standards and interpretations have been adopted with effect from 1 January 2013. However no changes to previously published accounting policies or other adjustments were required on their adoption.

- Amendment to IAS 12, Deferred tax: Recovery of Underlying Assets
- Amendment to IFRS 7, Financial Instruments: Disclosures – offsetting Financial Assets and Financial Liabilities
- Amendments to IFRS 1, First time adoption – Government Grants and Hyperinflation
- Annual Improvements 2011
- IFRIC 20, Stripping Costs in the Production Phase of a Surface Mine

### Management judgement and estimation uncertainty

The preparation of financial statements in conformity with IFRS requires the use of estimates and judgements that affect the application of accounting policies and reported amounts of assets, liabilities, revenue and expenses.

These estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The current economic conditions have been considered when evaluating accounting estimates and judgements, including the application of the going concern basis of preparation. Although estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

The Board considers that the key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, which have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities in the next financial year, are as follows:

### Intangible assets recognised on acquisition

On completion of a business combination, the cost is allocated by recognising the identifiable assets, liabilities and contingent liabilities acquired at fair value. Intangible assets are recognised where they are separable or arise from contractual or legal rights, and have a fair value that can be measured reliably. For the Group, these intangible assets usually comprise contractual arrangements, customer relationships and technology based assets, but can also include acquired patents, software rights and licences and development costs.

In establishing the fair value for intangible assets recognised on acquisition and their estimated useful lives, the Group takes account of the individual circumstances of the entity acquired. Factors considered include trading data, the value and duration of contracts acquired and the strength, duration and degree of exclusivity of relationships with customers. Valuation estimates are also used, including the estimation of likely external royalty rates that could be associated with technology and branding assets and attributable future cash flows.

### Impairment of goodwill

A review of the carrying value of goodwill is completed at least once a year to ensure that it is not impaired. This requires estimation of the value in use of the cash generating units (CGUs) to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the CGUs and also to choose a suitable discount rate in order to calculate the present value of those cash flows. Further details are given in note 11.

## Taxation

The Group is subject to taxes in numerous jurisdictions. Significant judgement is required in determining the worldwide provision for tax. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred tax provisions and the income statement in the period in which such determination is made.

## Retirement benefits

The Group Financial Statements include costs and liabilities in relation to retirement benefit obligations. A number of assumptions are made in assessing the costs and present value of the pension assets and liabilities, which include the long term rate of increase of salary costs, discount rate, inflation, and mortality rates. The Group uses published indices and independent actuarial advice to select the values of critical assumptions, which are disclosed in note 24.

## Provisions

Where appropriate, the consolidated financial statements include provisions for the estimated outcome of commercial disputes and other claims, including those with long term contract partners. The Directors take account of the advice of experts in quantifying the expected costs of future adverse outcomes. Due to the inherent uncertainty associated with such disputes and any related legal proceedings, the timing and determination of the amount of any payments under such claims could differ from the amounts provided.

## Definitions

### Underlying measures

To assist with the understanding of earnings trends, the Group has included within its published financial statements non-GAAP measures including trading profit and underlying earnings results. These are considered by the Board to be the most meaningful measures under which to assess the true operating performance of the Group.

All underlying measures include the operational results of all operations including those available for sale until the point of sale.

### Trading profit

This has been defined as operating profit from continuing operations excluding the impacts of business acquisition and divestment related activity and business restructuring costs as detailed below. Also excluded are changes in the marking to market of non-hedge accounted derivative financial instruments, impairments of intangible assets, and items deemed by the Directors to be of an exceptional nature.

Business acquisition and divestment related items excluded from trading profit and underlying earnings include the amortisation of intangible assets recognised on acquisition, the revaluation gain arising on the original equity interests in FBH, adjustments to businesses held for sale, the writing off of the pre-acquisition profit element of inventory written up on acquisition, other direct costs associated with business combinations and terminated divestments, and adjustments to contingent consideration related to previously acquired businesses.

Business restructuring costs relate to the restructuring of the Group's portfolio which are incremental to normal operations. These relate exclusively to the ongoing design and implementation of Standard Operating Frameworks within the principal locations, initial development costs of a new ERP computer system, together with site consolidation, consequential asset write downs and workforce reduction costs arising from additional streamlining under the two year extension of the EiD programme to the end of 2015.

### Underlying earnings

Underlying earnings are defined as trading profit less net underlying finance costs, which excludes the unwinding of acquisition related discounting, and after deducting associated taxation and non-controlling interests.

### Net debt

Net debt is defined as the net of borrowings less cash and cash equivalents at the balance sheet date.

### Free cash flow

Free cash flow is defined as net cash from operating activities plus dividends received from joint ventures, less cash flows related to the purchase or disposal of property, plant, equipment and intangible assets but excluding payments relating to M&A related activities.

### Operating segments

The chief operating decision making body for the Group has been identified as the Board. It reviews the Group's internal reporting in order to assess performance and allocate resources. Details of the composition and purpose of the Board can be found on pages 38 and 39.

The Group reports four operating segments whose revenue and results are reported to the Board. These are Aerospace and Security, Defence Systems, Mission Systems and Aviation Services. All operating segments meet the definition of reportable segments as defined in IFRS 8. The principal activities of these segments are described on pages 14 to 21.

The Board assesses the trading performance of operating segments based on revenue and trading profit as defined above. Finance income, finance costs and taxation are not segmented and are reviewed by the Board on a Group basis. Segment net assets are disclosed voluntarily in note 4 and include intangible assets, property, plant and equipment, investment properties, inventory, trade and other receivables, trade and other payables and provisions. They do not include tax, net debt, derivative financial instruments, contingent consideration payable or retirement benefit obligations.

### Basis of consolidation

The Group Financial Statements include the financial statements of the parent company, Cobham plc, and of all its subsidiaries made up to the end of the financial period.

Subsidiaries are all entities over which the Company has control, which is defined as the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Subsidiaries are fully consolidated from the date on which control is transferred to the Company until the date that control ceases. On derecognition, any amounts previously recognised in OCI in respect

# Notes to the Group Financial Statements continued

of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in OCI are reclassified to profit or loss.

Joint ventures are entities where control is shared with one or more third parties. Associates are entities where the Group has significant influence but do not meet the definition of a subsidiary or joint venture. Joint ventures and associates are not consolidated but are accounted for using the equity method. The Group Financial Statements include the Group's share of the post-acquisition change in net assets and the post-tax profit or loss of jointly controlled entities and associates from the date that joint control or significant influence commences until the date this ceases.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

## Foreign currencies

The presentation currency of the Group is sterling. Most Group companies, including the parent company, use their local currency as their functional currency. Transactions in currencies other than the functional currency are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in non-functional currencies are retranslated at the exchange rate ruling at the balance sheet date and any exchange differences arising are taken to the Consolidated Income Statement.

For consolidation purposes, the assets and liabilities of foreign operations are translated at the closing exchange rates. Income statements of such undertakings are consolidated at the average rates of exchange as an approximation for actual rates during the year. Exchange differences arising on these translations are accounted for in OCI and the translation reserve.

## Business combinations

Businesses acquired are accounted for using the acquisition method of accounting with effect from the date control passes. The cost of an acquisition is measured as the fair value of the consideration transferred. This is the fair value of the assets transferred (typically cash), the liabilities assumed and any equity interests issued by the Group, including contingent or deferred amounts.

Where a business combination is completed in stages, any previously held interests are remeasured to fair value at the date at which control is achieved. Any resulting gain or loss is recognised in the Consolidated Income Statement. Acquisition related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the consideration transferred over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill.

Contingent consideration includes amounts which may become payable in connection with completed acquisitions, based upon future operating results of the businesses acquired. It is accounted for as a financial liability measured at fair value on a recurring basis and changes in the fair value are accounted for as gains or losses recognised through profit or loss and excluded from trading profit and underlying earnings.

## Revenue recognition

Revenue is measured at the fair value of the right to consideration, net of returns, rebates and other similar allowances.

Revenue from the sale of goods not under a long term contract is recognised when the significant risks and rewards of ownership and effective control of the goods have been passed to the customer, recovery of the consideration is probable, and the amount of revenue and costs can be measured reliably. In the case of contracts with a long duration, including contracts with a funded development phase, revenue is recognised based upon the fair value of work performed to date assessed with reference to completed contract milestones which have been accepted by the customer.

Long term contract accounting as described in IAS 11, Construction Contracts is not generally applicable to the longer term contracts for sales of goods entered into by Group companies. Where long term contract accounting is applicable, revenue is recognised on a percentage of completion basis whereby a portion of the contract revenue is recognised based on contract costs incurred to date compared with total estimated costs at completion.

Revenue for services is recognised as the services are rendered with reference to the proportion of the service delivered to date. For 'cost-plus' contracts (typically with government departments and agencies), revenue is recognised to the extent of reimbursable costs incurred, plus a proportionate amount of the estimated fee earned. For contracts where revenue is determined on a unit activity basis, revenue is recognised on the basis of activity undertaken in the period.

Revenue excludes intercompany sales, value added tax and other sales taxes.

## Taxation including deferred taxation

The tax expense is the sum of current tax and deferred tax.

Current tax is based on taxable profit for the year, which differs from profit before taxation as reported in the income statement. Taxable profit excludes items of income and expense that are taxable or deductible in other years and also excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying values in the consolidated financial statements.

Deferred tax is calculated using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and that are expected to apply to the period when the asset is realised or the liability is settled. Tax is charged or credited to the income statement except when it relates to items recognised in OCI or directly in equity, in which case the deferred tax is also dealt with in OCI or in equity respectively.

Deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the assets to be recovered.

Deferred tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred taxes relate to the same fiscal authority.

#### **Dividends**

Dividends are recognised as a liability in the period in which they are fully authorised.

#### **Intangible assets**

##### **Goodwill**

Goodwill represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a business at the date of acquisition. Goodwill acquired is allocated at acquisition to the CGUs that are expected to benefit from that business combination. CGUs represent the lowest level within the Group at which the goodwill is monitored for internal management purposes.

Goodwill arising on business combinations is capitalised and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and cannot be subsequently reversed.

On divestment of a business the attributable amount of goodwill is included in the determination of the profit or loss on divestment. This includes any exchange differences reclassified to the income statement from the translation reserve.

##### **Other intangible assets**

Intangible assets other than goodwill which are acquired by the Group are stated at cost less accumulated amortisation and impairment losses. These include customer relationships, technology and software, trademarks, licences and patents. The only internally generated intangible assets are development costs which are capitalised as described below and internally developed software where asset recognition criteria are met. Internally developed software is included within other intangible assets.

All other intangible assets are amortised over the asset's estimated useful life on a straight-line basis as follows:

Customer relationships	5 to 15 years
Technology based assets	5 to 15 years
Development costs	2 to 10 years
Other intangible assets	6 months to 10 years

Useful lives are assessed for each asset on an individual basis, taking into account the specific characteristics of the asset.

#### **Research and development**

Development costs are capitalised when it can be demonstrated that the conditions for capitalisation as described in IAS 38, Intangible Assets are met, paying particular attention to the requirements for the product to be technically feasible and capable of generating a financial return. At that point, further costs are capitalised as an intangible asset until the intangible asset is readily available for use and is then amortised as described above. All development costs not capitalised are written off as incurred together with all research costs.

#### **Property, plant and equipment**

Freehold and leasehold land and buildings, plant and machinery, and fixtures, fittings, tools and equipment are held at historic cost less accumulated depreciation and any recognised impairment losses. Cost comprises the purchase price and any costs directly attributable to the asset.

All property, plant and equipment other than land and assets under construction is depreciated on a straight-line basis to the estimated residual values over the estimated useful lives. These lives are as follows:

Freehold buildings	50 years
Leasehold properties	Period to next break clause
Plant and machinery	3 to 15 years
Fixtures, fittings, tools and equipment	3 to 15 years

Estimated residual values and the estimated useful lives are reviewed annually and adjusted where necessary. Freehold land is not depreciated, but is reviewed for impairment at least annually.

Assets under construction are held at cost and transferred to the appropriate category of property, plant and equipment once construction is complete and they enter into service. They are depreciated from this point in accordance with the policies described above.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

# Notes to the Group Financial Statements continued

## Aircraft overhaul expenditure

Major overhaul expenditure on owned aircraft is capitalised when incurred and the resultant property, plant and equipment is depreciated over its useful economic life. Major overhaul costs that are contractually required on aircraft held under operating leases are provided for over the period between the scheduled maintenance events.

## Investment properties

Investment properties, which are properties held to earn rentals or for capital appreciation, are stated at cost in the balance sheet. They are depreciated on a straight-line basis to their estimated residual value over their estimated useful lives of up to 50 years.

Rental income is recognised as revenue on a straight-line basis.

## Impairment losses

The carrying amounts of the Group's non-financial assets are reviewed at least annually to determine whether there is any indication of impairment. In addition, intangible assets with an indefinite useful life, such as goodwill, are tested for impairment annually and whenever there is an indication that the asset may be impaired.

Where there is an indication of impairment, the asset's recoverable amount is estimated. The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

An impairment loss is recognised where the recoverable amount of an asset is lower than its carrying amount. All impairment losses are recognised in the income statement.

An impairment loss (other than arising on goodwill) is reversed only after a change in the estimates used to assess recoverable amount is identified and only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. Any reversal is recognised in the income statement.

## Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the income statement.

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease. Benefits receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

## Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the first-in, first-out method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution. Provision is made where necessary for obsolete, slow moving and defective items.

## Non-current assets and disposal groups held for sale

Non-current assets and disposal groups classified as held for sale are stated at the lower of carrying amount and fair value less costs to sell. No depreciation is charged in respect of non-current assets classified as held for sale.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and expected to be completed within a year of the balance sheet date. The asset or disposal group should be available for immediate sale in its present condition and actively marketed at a price that is reasonable in relation to its current fair value.

## Fair values

The fair value of an asset or liability is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the balance sheet date. Fair value measurements are used on a recurring basis except where used in the measurement of net assets classified as held for sale, where accounting standards require the use of fair values only in certain circumstances. Non-recurring fair values are also used in the valuation of assets and liabilities in a business combination.

The fair values of derivative financial instruments have been determined by the use of valuation techniques, primarily discounted cash flows, based on assumptions that are supported by observable market prices or rates.

The fair value of contingent consideration is determined based on the estimated payment, discounted to present value and using the entity's own data and unobservable inputs such as the anticipated rate of annual revenue growth, profit margins and discount rates. The estimated payment is calculated using the income approach, considering different scenarios of the relevant profit measure (commonly EBITDA).

For financial assets and liabilities which are not held at fair value in the balance sheet, the carrying values of these items are assumed to approximate to fair value due to their short term nature.

Non-financial assets and liabilities measured at fair value include net assets classified as held for sale and fair values are also used in assessing the assets and liabilities acquired in a business combination. These fair value measurements are based on observable market prices or rates. For non-financial assets, the fair value takes into account the highest and best use of the asset.

There have been no changes to the valuation techniques used during the period. The Group's policy is to recognise transfers in and transfers out of fair value hierarchy levels as at the date of the event or change in circumstances that caused the transfer, although there have been no such transfers during the current or comparative periods.

### **Financial instruments**

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are initially recognised at fair value at trade date.

#### **Financial assets**

The classification of financial assets depends on the purpose for which the assets were acquired. Management determines the classification of an asset at initial recognition and re-evaluates the designation at each reporting date.

Assets held at fair value through profit or loss are those categorised as held for trading under IAS 39 and are classified as current assets or non-current assets dependent upon maturity. Such financial assets are subsequently carried at fair value.

Loans and receivables are non-derivative financial assets with fixed or determinable payments which are not quoted in an active market. These are classified as current or non-current assets dependent upon maturity and included within trade and other receivables. Loans and receivables also includes cash and cash equivalents. The fair value of these financial assets is adjusted for transaction costs that are directly attributable to the acquisition or issue of the asset. Subsequent to initial recognition, loans and receivables are carried at amortised cost using the effective interest method.

Available for sale financial assets are those non-derivative financial assets either designated by management as available for sale or not falling into any other category. Financial assets so categorised include equity instruments which do not have a quoted price in an active market and hence are measured at cost.

None of the Group's material financial assets fall into the held to maturity category, which is defined as non-derivative financial assets with fixed maturity dates that the Group intends to hold to maturity.

#### **Financial liabilities**

Financial liabilities are categorised on initial recognition as held for trading under IAS 39 and are held at fair value through profit or loss, or other liabilities, which are held at amortised cost. All financial liabilities are classified as current or non-current liabilities dependent upon the maturity date of the instruments.

Derivative financial instruments are categorised as held for trading unless they are designated as hedges.

The fair value of financial liabilities held at cost (not at fair value through profit or loss) is adjusted for transaction costs that are directly attributable to the acquisition or issue of the liability. Financial liabilities at fair value through profit or loss are subsequently carried at fair value. Financial liabilities not at fair value through profit or loss are stated at amortised cost using the effective interest method.

#### **Trade and other receivables**

Trade and other receivables are stated at their amortised cost, reduced by appropriate allowances for estimated irrecoverable amounts.

Allowances for irrecoverable amounts are made when there is evidence that the Group may not be able to collect the amount due. All trade receivables which are more than six months overdue are provided for based on estimated irrecoverable amounts determined by reference to past default experience. Amounts which are less than six months overdue are provided where recovery of the balance due is considered to be doubtful.

The impairment recorded is the difference between the carrying value of the receivables and the present value of the estimated future cash flows. Any impairment required is recorded in the income statement in administrative expenses. The balance may be written off in full generally where receivables are in excess of 12 months old. At that time, any amounts previously provided for impairment are released.

#### **Cash and cash equivalents**

Cash and cash equivalents comprise cash balances and bank deposits with an original maturity of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the Consolidated Cash Flow Statement.

#### **Bank borrowings**

Interest bearing bank loans and overdrafts are recorded at the amount of proceeds received, net of direct issue costs. Borrowing costs, net of amounts capitalised, including premiums payable on settlement or redemption and direct issue costs, are charged to the income statement and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise. Borrowing costs that are directly attributable to relevant property, plant and equipment are capitalised as part of the cost of that asset.

#### **Trade payables**

Trade payables do not carry any interest and are stated at their nominal value.

#### **Derivative financial instruments and hedge accounting**

As explained in note 25, the Group's activities expose it to the financial risks of changes in foreign currency exchange rates and interest rates. The Group uses foreign exchange contracts and interest rate swap contracts to reduce these exposures and does not use derivative financial instruments for speculative purposes. Other derivative financial instruments may be used from time to time to hedge other exposures such as inflation risks.

# Notes to the Group Financial Statements continued

The Group has documented its risk management objectives and strategy for undertaking various hedge transactions, and utilises hedge accounting principles in relation to interest rate swaps. These are designated as cash flow hedges which mitigate the Group's exposure to changes in interest rates arising on floating rate debt. From time to time, the Group may also use interest rate swaps to manage its exposure to changes in the fair value of fixed rate borrowings; however there are no such contracts outstanding at the present time.

Foreign exchange contracts entered into to mitigate foreign exchange impacts of trading in non-functional currencies, and inflation swaps entered into to mitigate inflation risks, are not accounted for using hedge accounting. Foreign currency borrowings are used to hedge the effects of changes in the Group's net investment in foreign operations. These borrowings either provide a natural economic hedge through the use of intercompany debt or are designated as fair value hedges of the foreign currency risk attributable to the foreign equity investment and are treated as net investment hedges.

Derivative financial instruments are initially recognised at fair value on the date the contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged.

Where hedge accounting is applied, the relationship between hedging instruments and hedged items is documented at the inception of the transaction. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives used in hedging transactions are highly effective in offsetting changes in cash flows (or fair values if appropriate) of hedged items.

Where interest rate swaps are designated and qualify as cash flow hedges, the effective portion of changes in fair value is recognised in OCI through the hedge reserve. The gain or loss relating to the ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are reclassified to finance income or finance costs in the income statement in the periods when the hedged item affects profit or loss.

When a cash flow hedging derivative expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in the hedge reserve in equity at that time remains in equity and is recognised in the income statement when the forecast transaction is ultimately recognised in the income statement. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in the hedge reserve in equity is immediately transferred to the income statement in that period.

Where net investment hedging applies, the exchange differences arising on the borrowings designated as fair value hedges are recognised in OCI and through profit and loss on disposal of the foreign operation.

The fair value of a hedging derivative is classified as a current asset or liability except when the remaining maturity of the hedged item is more than 12 months.

Where hedge accounting is not applied, the movements in fair value of the derivative instruments are included in the income statement as part of operating profit. The fair value of such derivatives is classified as a current or non-current asset or liability dependent upon the expected realisation of the assets or settlement of the liabilities.

## Provisions

A provision is required when the Group has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required and where the amount can be reliably measured. No provision is recognised where the existence of an obligation is possible but will only be confirmed by uncertain future events.

Provisions for warranty costs are recognised at the date of sale of the relevant products, at management's best estimates of the expenditure required to settle the Group's liabilities, based on past experience and industry averages for defective products.

Contract loss provisions are recognised for onerous contracts when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

Aircraft maintenance provisions are established in respect of significant periodic maintenance costs, where maintenance activity is required on leased operational aircraft or engines on a cycle greater than 12 months. Costs are charged to the income statement on the basis of utilisation of the aircraft and are credited to the provision. The provision is then utilised by absorbing the actual costs incurred in carrying out the maintenance activity. Maintenance carried out on a cycle of 12 months or less is charged to the income statement as incurred.

Provisions also arise in connection with leased aircraft, where contracts contain specific conditions regarding the configuration of the aircraft on its return to the lessor at the end of the lease. The estimated cost associated with fulfilling these requirements is charged to the income statement on an aircraft utilisation basis. The provision is utilised on actual return of the aircraft or on incurring the expenditure required to return the aircraft to the state of maintenance required by the lease before return of the aircraft to the lessor.

Provisions for claims made against the Group and commitments made under performance guarantees are recognised at management's best estimates of the expenditure required to settle the Group's liabilities.

Provisions are discounted at an appropriate risk-free rate when the impact is material.

## Pensions

The Group operates a number of defined benefit and defined contribution schemes.

For defined benefit schemes, current service costs and costs related to the administration of the schemes are charged to operating profit. Gains and losses on settlements and curtailments arising on a business divestment are included in profit on divestment. Past service costs are recognised immediately in the income statement. The interest on net assets or liabilities is shown within finance income and costs. Actuarial remeasurements are recognised immediately in OCI.

Defined benefit schemes are funded, with the assets of the scheme held separately from those of the Group, in separate trustee administered funds. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting net defined benefit asset or liability is presented separately on the face of the balance sheet.

For defined contribution schemes, the amounts charged to the income statement in respect of pension costs and other post-retirement benefits are the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are recorded as either accruals or prepayments in the balance sheet.

## Share capital

Ordinary share capital is classified as equity. Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Preference share capital is classified as a liability if it is redeemable on a specific date or at the option of the preference shareholders or if dividend payments are not discretionary. Dividends on preference share capital classified as liabilities are recognised in the income statement as finance costs.

## Treasury shares

When ordinary share capital recognised as equity is acquired by the Company, the shares are held as treasury shares. The consideration paid, including commissions and taxes, is deducted from retained earnings and total equity. The proceeds of any treasury shares subsequently sold or re-issued, net of commission and taxes, are recognised as an increase in retained earnings and total equity.

## Share based payments

For grants made under the Group's equity settled share based payment schemes, amounts which reflect the fair value of options awarded as at the time of grant are charged to the income statement over the relevant vesting periods, taking into account the Directors' best estimate of the number of awards expected to vest. The Group reviews and updates the vesting estimate, which includes progress against non-market related performance conditions, at each balance sheet date.

The valuation methodology for all schemes is based on the Black-Scholes model, modified where required to allow for the impact of market related performance criteria and taking into account all non-vesting conditions.

## Future accounting developments

A number of new standards, amendments to existing standards and interpretations have been published that are mandatory for future accounting periods. Those endorsed by the EU for use from 1 January 2014 are as follows:

- IFRS 10, Consolidated Financial Statements
- IFRS 11, Joint Arrangements
- IFRS 12, Disclosures of Interests in Other Entities
- IAS 27 (revised 2011), Separate Financial Statements
- IAS 28 (revised 2011), Associates and Joint Ventures
- Amendments to IFRS 10, IFRS 11 and IFRS 12: Transitional Guidance
- Amendments to IFRS 10, IFRS 12 and IAS 27: Investment Entities
- Amendment to IAS 32, Financial Instruments: Presentation on Offsetting Financial Assets and Financial Liabilities
- Amendments to IAS 36, Recoverable Amount Disclosures for Non-financial Assets
- Amendments to IAS 39, Novation of Derivatives and continuation of Hedge Accounting
- IFRIC 21, Levies (not endorsed at 31 December 2013)

None of these have been adopted early by the Group and none are expected to have an impact on the Group's financial reporting.

There are also a number of new standards and amendments to existing standards including Annual Improvements which, once endorsed by the EU, will be effective from 1 January 2015. IFRS 9, Financial Instruments will be adopted once endorsed for use by the EU. Management will assess the impact of these changes on the future reporting of the Group's operations at the appropriate time.

# Notes to the Group Financial Statements continued

## 2. Prior year restatement

Changes to IAS 19, Employee Benefits have resulted in some changes to the accounting for pension schemes. The implications of these changes are explained in this note.

The amendment to IAS 19 replaced an interest charge on pension liabilities and a credit for the expected return on investments held during the year with a single interest charge on net liabilities. The amendment was required to be applied retrospectively, which means that the numbers reported in 2012 have been updated in these financial statements as if these new rules were in place last year. As investments are generally expected to provide returns that are greater than a typical interest rate this change had the effect of increasing the net interest cost for 2012 by £0.9m.

In addition, administrative costs incurred by the Group's pension schemes, which amounted to £1.1m in 2012, are now charged to administrative expenses within the Consolidated Income Statement. These were previously dealt with as part of the finance cost related to pension schemes.

These changes do not impact the valuation of the assets or liabilities of the scheme. Actuarial losses, accounted for within OCI, are restated to maintain the net liabilities as previously reported.

These adjustments are tax effected and the change in profit after taxation impacts on Earnings per Share and underlying measures. The Consolidated Statement of Changes in Equity, the Consolidated Cash Flow Statement and various notes to the financial statements are also affected.

The impacts on the 2012 financial statements can be summarised as follows:

£m	As reported	Adjustment	As restated
<b>Consolidated Income Statement</b>			
Administrative expenses (see note below)	(263.8)	(1.1)	(264.9)
Operating profit (see note below)	238.6	(1.1)	237.5
Finance income – adjustment for expected return on pension scheme assets	33.4	(26.6)	6.8
Finance costs – adjustment for interest on pension scheme liabilities	(66.0)	25.7	(40.3)
Profit before taxation	206.0	(2.0)	204.0
Taxation	(32.6)	0.4	(32.2)
Profit after taxation	173.4	(1.6)	171.8
Profit attributable to owners of the parent	173.3	(1.6)	171.7
Earnings per Ordinary Share			
Basic	16.13p	(0.15p)	15.98p
Diluted	16.08p	(0.15p)	15.93p
<b>Consolidated Statement of Comprehensive Income</b>			
Profit after taxation	173.4	(1.6)	171.8
Remeasurements of defined benefit retirement benefit obligations	(15.7)	2.0	(13.7)
Tax effects	(0.8)	(0.4)	(1.2)
Total comprehensive income	136.5	–	136.5
<b>Underlying measures</b>			
Trading profit (adjustment allocated to Head Office in segment information)	333.1	(1.1)	332.0
Net underlying finance costs	(30.9)	(0.9)	(31.8)
Underlying profit before taxation	302.2	(2.0)	300.2
Taxation charge on underlying profit	(58.9)	0.4	(58.5)
Underlying profit after tax attributable to owners of the parent	243.2	(1.6)	241.6
Underlying EPS	22.63p	(0.15p)	22.48p
<b>Consolidated Cash Flow Statement</b>			
Operating profit	238.6	(1.1)	237.5
Pension contributions in excess of service cost and administration cost	(15.4)	1.1	(14.3)
Net cash from operating activities	288.2	–	288.2

£2.9m reported in the 2012 Annual Report and Accounts on a separate line in the Income Statement 'Business divestments and similar income' has been combined into administrative expenses, with a consequential change to operating profit.

### 3. Underlying measures

Underlying measures, defined in note 1 on page 81, are derived from operating profit as set out below:

£m	Note	2013	2012 (as restated)
Operating profit		<b>158.8</b>	237.5
Business restructuring – Excellence in Delivery		<b>56.1</b>	37.9
Movements in non-hedge accounted derivative financial instruments		<b>(2.2)</b>	(11.1)
Amortisation of intangible assets arising on business combinations		<b>103.9</b>	68.9
Impairment of goodwill	11	<b>63.0</b>	–
Revaluation gain arising on equity interests in FBH (2012: Thrane & Thrane)	29	<b>(62.1)</b>	(1.0)
Other business acquisition and divestment related items			
Net profit on divestment of emergency locator beacons business		–	(7.8)
Additional profit on other divestments in prior years		<b>(2.1)</b>	(7.4)
Adjustments to businesses held for sale		<b>8.3</b>	13.3
Release of contingent consideration	20	<b>(11.9)</b>	(8.7)
Other M&A related costs		<b>5.8</b>	10.4
<b>Trading profit</b>		<b>317.6</b>	332.0
Net underlying finance costs		<b>(29.6)</b>	(31.8)
<b>Underlying profit before taxation</b>		<b>288.0</b>	300.2
Taxation charge on underlying profit		<b>(57.0)</b>	(58.5)
Non-controlling interests		<b>(0.2)</b>	(0.1)
<b>Underlying profit after tax attributable to owners of the parent</b>		<b>230.8</b>	241.6
Underlying basic EPS		<b>21.60p</b>	22.48p
Underlying diluted EPS		<b>21.51p</b>	22.42p

Underlying administrative expenses, which exclude the reconciling items in the table above, amounted to £169.6m (2012: £170.4m as restated), representing 9.5% (2012: 9.7%) of revenue.

Business restructuring costs relate to the restructuring of the Group's portfolio under its EiD programme which are incremental to normal operations. These relate exclusively to the ongoing design and implementation of Standard Operating Frameworks within the principal locations, initial development costs of a new ERP computer system, together with site consolidation, consequential asset write downs and workforce reduction costs arising from additional streamlining under the two year extension of the programme, which continues into 2015.

As disclosed in note 29, on 15 July 2013 an agreement was reached to acquire the 50% shareholding that the Group did not already own in FBH. The proceeds of the deemed disposal of the 50% interest previously held were valued at £74.2m which generated the revaluation gain arising on equity interests in FBH of £62.1m.

Net cash from operating activities is reconciled to free cash flow as follows:

£m	2013	2012
Net cash from operating activities per cash flow statement	<b>210.6</b>	288.2
Dividends received from joint ventures	<b>3.7</b>	7.5
Purchase of property, plant and equipment	<b>(58.0)</b>	(48.2)
Purchase of intangible assets	<b>(11.0)</b>	(13.8)
Capitalised expenditure on intangible assets	–	(1.4)
Proceeds on disposal of property, plant and equipment	<b>8.0</b>	1.0
M&A costs paid	<b>1.7</b>	7.8
<b>Free cash flow</b>	<b>155.0</b>	241.1
<b>Free cash flow before Excellence in Delivery restructuring costs</b>	<b>205.9</b>	272.9

# Notes to the Group Financial Statements continued

## 4. Revenue and segmental information

### Revenue

Revenue comprises income from the sale of goods and services during the year and can be analysed as follows:

£m	2013	2012
Revenue from sale of goods	<b>1,424.8</b>	1,423.1
Revenue from services	<b>364.9</b>	326.3
	<b>1,789.7</b>	1,749.4

### Major customers

Revenue of £130.8m (2012: £162.9m) is directly attributable to US Government departments and agencies, although this is widely spread across different agencies and customers. This accounts for 7.3% of total revenue (2012: 9.3%) and originates in all segments other than Cobham Aviation Services. In addition, a number of customers also sell our products on to various US Government departments and agencies.

### Operating segments

£m	Revenue		Trading profit		Segment net assets	
	2013	2012	2013	2012 (as restated)	2013	2012
Aerospace and Security	<b>743.6</b>	697.3	<b>132.4</b>	149.1	<b>795.5</b>	794.8
Defence Systems	<b>309.0</b>	322.9	<b>46.5</b>	44.9	<b>335.2</b>	377.1
Mission Systems	<b>357.7</b>	372.6	<b>74.0</b>	81.3	<b>294.9</b>	251.9
Aviation Services	<b>365.2</b>	326.6	<b>48.0</b>	38.0	<b>322.9</b>	157.0
Head office, other activities and elimination of inter-segment items	<b>(6.7)</b>	(6.5)	<b>14.2</b>	13.8	<b>20.7</b>	76.5
Core Group	<b>1,768.8</b>	1,712.9	<b>315.1</b>	327.1	<b>1,769.2</b>	1,657.3
Non-core businesses	<b>20.9</b>	36.5	<b>2.5</b>	4.9	<b>(3.1)</b>	(10.5)
<b>Total Group</b>	<b>1,789.7</b>	1,749.4	<b>317.6</b>	332.0	<b>1,766.1</b>	1,646.8
Interests in joint ventures and associates					<b>3.1</b>	15.8
Unallocated assets					<b>(725.0)</b>	(608.2)
<b>Total net assets</b>					<b>1,044.2</b>	1,054.4

Head office results (net of recoveries) are not included within the operating segments as described above. Non-core businesses are those which were identified for divestment in 2011.

The Group's share of the post-tax results of joint ventures and associates arises in Aviation Services (£3.1m, 2012: £7.0m) and Aerospace and Security (£nil, 2012: £0.4m).

Trading profit is reconciled to profit before taxation as follows:

£m	Note	2013	2012 (as restated)
Trading profit		<b>317.6</b>	332.0
Business restructuring – Excellence in Delivery	3	<b>(56.1)</b>	(37.9)
Movements in non-hedge accounted derivative financial instruments	23	<b>2.2</b>	11.1
Amortisation of intangible assets arising on business combinations		<b>(103.9)</b>	(68.9)
Impairment of goodwill	10	<b>(63.0)</b>	–
Revaluation gain arising on equity interests in FBH (2012: Thrane & Thrane)	29	<b>62.1</b>	1.0
Other business acquisition and divestment related items		<b>(0.1)</b>	0.2
Net finance costs	6	<b>(32.2)</b>	(33.5)
<b>Profit before taxation</b>		<b>126.6</b>	204.0

Depreciation of property, plant and equipment, investment properties and amortisation of internally generated intangibles are included in the calculation of trading profit and can be analysed by segment as follows:

£m	2013	2012
Aerospace and Security	<b>17.3</b>	14.7
Defence Systems	<b>13.5</b>	14.8
Mission Systems	<b>6.4</b>	6.5
Aviation Services	<b>30.6</b>	23.6
<b>Core Group</b>	<b>67.8</b>	59.6
Non-core businesses	<b>0.4</b>	0.7
<b>Total Group</b>	<b>68.2</b>	60.3

Details of employees analysed by operating segment can be found in note 5.

### Geographical information

#### Revenue

Revenue from external customers analysed by their geographical location, irrespective of the origin of the goods and services, is shown below. Revenue from customers located in individual countries within the EU (except the UK) and the rest of the world is not considered to be individually material.

£m	UK	USA	Australia	Other EU countries	Asia	Rest of the world	Total
Year to 31 December 2013	<b>235.2</b>	<b>812.5</b>	<b>249.8</b>	<b>277.4</b>	<b>132.8</b>	<b>82.0</b>	<b>1,789.7</b>
Year to 31 December 2012	172.3	885.6	241.4	292.5	99.3	58.3	1,749.4

#### Non-current assets

Non-current assets are analysed by the physical location of the assets and exclude financial instruments and deferred tax assets.

£m	UK	USA	Denmark	Other EU countries	Australia	Rest of the world	Total
At 31 December 2013	<b>402.4</b>	<b>588.9</b>	<b>272.6</b>	<b>101.2</b>	<b>90.5</b>	<b>70.4</b>	<b>1,526.0</b>
At 31 December 2012	212.2	666.2	295.6	106.0	111.2	42.2	1,433.4

### 5. Operating costs

Operating costs include materials costs of £592.7m (2012: £575.4m) within cost of sales in the Consolidated Income Statement.

#### Company funded research and development

£m	2013	2012
Company funded research and development	<b>88.0</b>	75.4

#### Employment costs

The aggregate employment costs of Group employees are as follows:

£m	Note	2013	2012
Wages and salaries		<b>497.0</b>	467.2
Social security costs		<b>41.1</b>	39.0
Pension costs	24	<b>29.6</b>	25.7
Share based payments	28	<b>(1.7)</b>	6.8
		<b>566.0</b>	538.7

# Notes to the Group Financial Statements continued

The average number of employees during the year, analysed by segment, is as follows:

	2013	2012
Aerospace and Security	<b>4,140</b>	4,019
Defence Systems	<b>2,206</b>	2,329
Mission Systems	<b>1,500</b>	1,473
Aviation Services	<b>1,931</b>	1,815
Head office and other activities	<b>184</b>	131
<b>Core Group</b>	<b>9,961</b>	9,767
Non-core businesses	<b>129</b>	225
<b>Total Group</b>	<b>10,090</b>	9,992

## Compensation of key management personnel

The remuneration of Directors and other members of key management during the year was as follows:

£m	2013	2012
Remuneration	<b>6.2</b>	5.8
Post-employment benefits	<b>0.7</b>	0.6
Share based payments	<b>(0.5)</b>	3.8
	<b>6.4</b>	10.2

## Audit fees

During the year the Group obtained the following services from the Company's auditors, PricewaterhouseCoopers LLP and its associates, as follows:

£m	2013	2012
Annual audit of the Parent Company and Group Financial Statements	<b>1.0</b>	1.1
Audit of the Company's subsidiaries	<b>1.1</b>	0.9
<b>Total fees payable for audit services</b>	<b>2.1</b>	2.0
Fees payable for other services		
Tax compliance services	<b>0.3</b>	0.2
Other tax advisory services	<b>1.2</b>	0.8
Other audit related assurance services	<b>0.2</b>	0.1
<b>Total fees payable for other services</b>	<b>1.7</b>	1.1
 <b>Total fees payable to the auditors</b>	<b>3.8</b>	3.1

In addition to the amounts shown above, the auditors received fees of £45,750 in 2012 for the audit of the Group's pension schemes.

A description of the work of the Audit Committee is set out in the Corporate Governance Report on pages 44 to 47 and includes an explanation of how auditor objectivity and independence are safeguarded when non-audit services are provided by the auditors.

## 6. Finance income and costs

£m	Note	2013	2012 (as restated)
Finance income			
Bank interest		<b>3.3</b>	4.0
Other finance income		<b>2.0</b>	2.8
<b>Total finance income</b>		<b>5.3</b>	6.8
Finance costs			
Interest on bank overdrafts and loans		<b>(29.6)</b>	(32.1)
Interest on net pension scheme liabilities	24	<b>(2.8)</b>	(2.9)
Other finance expense		<b>(5.1)</b>	(5.3)
<b>Total finance costs</b>		<b>(37.5)</b>	(40.3)
Net finance costs excluding pension schemes		<b>(29.4)</b>	(30.6)
Net finance costs arising from pension schemes		<b>(2.8)</b>	(2.9)
<b>Net finance costs</b>		<b>(32.2)</b>	(33.5)

Other finance expense above includes £1.5m (2012: £2.8m) in relation to interest rate swaps (previously designated as cash flow hedges) which were terminated during 2009 and have been amortised over the life of the original contracts to August 2013. It also includes £2.6m (2012: £1.7m) relating to the unwinding of acquisition related discounting, excluded from underlying profit in note 3.

## 7. Income tax expense

£m	Note	2013	2012 (as restated)
Current tax			
Charge for the year		<b>44.1</b>	50.0
Adjustments to tax charge in respect of prior years		<b>(14.7)</b>	(2.6)
<b>Current tax</b>		<b>29.4</b>	47.4
Deferred tax			
Credit for the year		<b>(16.5)</b>	(0.5)
Adjustments to tax charge in respect of prior years		<b>0.2</b>	(14.7)
Impact of change in tax rates		<b>(1.0)</b>	–
<b>Deferred tax</b>	22	<b>(17.3)</b>	(15.2)
<b>Total tax charge for the year</b>		<b>12.1</b>	32.2

Income tax is calculated on the estimated assessable profit for the year at the rates prevailing in the relevant tax jurisdiction. The total tax charge for the year includes £7.7m (2012: £6.8m) for the UK.

# Notes to the Group Financial Statements continued

The total charge for the year can be reconciled to the accounting profit as follows:

£m	2013	2012 (as restated)
Profit before tax	<b>126.6</b>	204.0
Tax thereon at the UK income tax rate of 23.25% (2012: 24.5%)	<b>29.4</b>	50.0
Tax effect of share of results of joint ventures and associates	<b>(0.7)</b>	(1.8)
Effect of differences in overseas taxation rates	<b>1.0</b>	6.7
Expenditure qualifying for additional R&D tax relief	<b>(3.7)</b>	(5.7)
Revaluation gain on FBH	<b>(14.4)</b>	–
Goodwill impairment	<b>14.6</b>	–
Adjustments to tax charge in respect of prior years	<b>(14.5)</b>	(17.3)
Impact of other items	<b>0.4</b>	0.3
<b>Total tax charge for the year</b>	<b>12.1</b>	32.2

In addition to the tax expense charged to the income statement, the following charges/(credits) have been included in OCI and equity:

£m	2013	2012 (as restated)
<b>Included in OCI</b>		
<i>Items that will not be reclassified subsequently to profit or loss</i>		
Actuarial loss on retirement benefit obligations	<b>(4.1)</b>	(1.8)
Actuarial loss on other retirement benefit obligations	–	(0.2)
	<b>(4.1)</b>	(2.0)
<i>Items that may subsequently be reclassified to profit or loss</i>		
Movements in hedge accounted derivative financial instruments	<b>1.2</b>	3.2
<b>Included in equity</b>		
Share based payments	<b>2.6</b>	0.5

The rate of UK corporation tax will reduce from 23% to 21% from 1 April 2014 and to 20% from 1 April 2015.

## 8. Dividends

£m	2013	2012
Final dividend of 6.4 pence per share for 2012 (2011: 6.2 pence)	<b>68.5</b>	66.7
Interim dividend of 2.64 pence per share for 2013 (2012: 2.4 pence)	<b>28.1</b>	25.8
<b>Total dividend authorised and paid during the year</b>	<b>96.6</b>	92.5

In addition to the above, the Directors are proposing a final dividend in respect of the financial year ended 31 December 2013 of 7.04 pence per share at an estimated total cost of £75.2m. This dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. If authorised, it will be paid on 30 May 2014 to shareholders who are on the register of members as at 2 May 2014. The total dividend in respect of the financial year ended 31 December 2013 will therefore be 9.68 pence per share (2012: 8.8 pence). The total amount payable in respect of 2013 will be £103.3m.

## 9. Earnings per Ordinary Share

	2013			2012	
	Earnings £m	Weighted average number of shares million	Per share amount pence	Earnings (as restated) £m	Weighted average number of shares million
<b>Basic earnings per share (EPS)</b>					
Earnings attributable to owners of the parent	<b>114.3</b>	<b>1,068.7</b>	<b>10.70</b>	171.7	1,074.7
Effect of dilutive securities		<b>4.3</b>			3.0
<b>Diluted EPS</b>	<b>114.3</b>	<b>1,073.0</b>	<b>10.65</b>	171.7	1,077.7
					15.93

## 10. Cash and cash equivalents and net debt

### Reconciliation of cash and cash equivalents and net debt

£m	2013	2012
Cash and cash equivalents as shown in Cash Flow Statement	<b>199.0</b>	250.2
Bank overdrafts	<b>1.7</b>	14.0
Cash and cash equivalents per Balance Sheet	<b>200.7</b>	264.2
Borrowings – current liabilities	<b>(344.5)</b>	(307.3)
Borrowings – non-current liabilities	<b>(309.6)</b>	(316.8)
<b>Net debt at 31 December</b>	<b>(453.4)</b>	(359.9)

Details of the offsetting of overdrafts with cash and cash equivalents and other financial instruments can be found in note 16.

### Reconciliation of movements in net debt

£m	2013	2012
Net debt at 1 January	<b>(359.9)</b>	(232.5)
Decrease in cash and cash equivalents in the year per Cash Flow Statement	<b>(36.8)</b>	(73.4)
New borrowings	<b>(67.0)</b>	(184.5)
Repayment of borrowings	<b>7.7</b>	113.1
Exchange movements	<b>2.6</b>	17.4
<b>Net debt at 31 December</b>	<b>(453.4)</b>	(359.9)

# Notes to the Group Financial Statements continued

## 11. Intangible assets

£m	Goodwill	Customer relationships	Technology based assets	Development costs	Other	Total
<b>Cost</b>						
At 1 January 2012	678.5	237.8	138.1	3.4	52.9	1,110.7
Additions – purchased	–	–	–	–	13.8	13.8
Additions – internally generated	–	–	–	1.4	–	1.4
Recognised on business combinations	150.5	81.9	55.3	–	3.3	291.0
Business divestments	(22.5)	–	(0.4)	–	(0.2)	(23.1)
Disposals and derecognitions	–	(7.6)	(15.3)	–	(23.3)	(46.2)
Foreign exchange adjustments	(17.4)	(9.8)	(4.5)	(0.1)	(1.7)	(33.5)
Reclassifications	–	–	–	–	0.7	0.7
<b>At 1 January 2013</b>	<b>789.1</b>	<b>302.3</b>	<b>173.2</b>	<b>4.7</b>	<b>45.5</b>	<b>1,314.8</b>
Additions – purchased	–	–	–	–	11.0	11.0
Recognised on business combinations	86.9	59.2	25.4	–	46.1	217.6
Disposals and derecognitions	–	(60.9)	(34.3)	(2.7)	(5.9)	(103.8)
Foreign exchange adjustments	(1.5)	2.3	2.3	0.1	(0.4)	2.8
Reclassifications	–	–	–	–	1.0	1.0
<b>At 31 December 2013</b>	<b>874.5</b>	<b>302.9</b>	<b>166.6</b>	<b>2.1</b>	<b>97.3</b>	<b>1,443.4</b>
<b>Accumulated amortisation and impairment</b>						
At 1 January 2012	–	92.1	61.4	2.1	37.5	193.1
Charge for the year	–	36.0	27.9	0.5	9.3	73.7
Eliminated on business divestments	–	–	(0.2)	–	(0.2)	(0.4)
Disposals and derecognitions	–	(7.6)	(15.3)	–	(23.1)	(46.0)
Foreign exchange adjustments	–	(4.3)	(2.1)	(0.1)	(1.2)	(7.7)
<b>At 1 January 2013</b>	<b>–</b>	<b>116.2</b>	<b>71.7</b>	<b>2.5</b>	<b>22.3</b>	<b>212.7</b>
Amortisation charge for the year	–	53.0	39.9	1.2	14.8	108.9
Impairment provision	63.0	–	–	–	–	63.0
Disposals and derecognitions	–	(60.9)	(34.3)	(2.7)	(5.9)	(103.8)
Foreign exchange adjustments	–	(0.1)	0.4	0.1	(0.5)	(0.1)
Reclassifications	–	–	–	–	0.5	0.5
<b>At 31 December 2013</b>	<b>63.0</b>	<b>108.2</b>	<b>77.7</b>	<b>1.1</b>	<b>31.2</b>	<b>281.2</b>
<b>Carrying amount</b>						
<b>At 31 December 2013</b>	<b>811.5</b>	<b>194.7</b>	<b>88.9</b>	<b>1.0</b>	<b>66.1</b>	<b>1,162.2</b>
<b>At 31 December 2012</b>	<b>789.1</b>	<b>186.1</b>	<b>101.5</b>	<b>2.2</b>	<b>23.2</b>	<b>1,102.1</b>
<b>At 1 January 2012</b>	<b>678.5</b>	<b>145.7</b>	<b>76.7</b>	<b>1.3</b>	<b>15.4</b>	<b>917.6</b>

Amortisation charged during the year relating to intangible assets recognised on business combinations was £103.9m (2012: £68.9m). This has been excluded from underlying profit as shown in note 3. All amortisation charges are included within administrative expenses in the Consolidated Income Statement.

Business combinations during the year represent the acquisition of Axell Wireless and the 50% of the shares of FB Heliservices Limited, FB Leasing Limited and FBS Limited (together FBH) not already owned by Cobham. Axell Wireless forms part of the Antenna Systems strategic business unit (SBU) and FBH operates within the Aviation Services SBU. Further details can be found in note 29.

Customer relationships represents customer lists, customer contracts and the associated benefits of customer relationships recognised on acquisition. Technology based assets represent trade secrets and processes, patented and unpatented technology and know-how recognised on acquisition, together with purchased technology assets. Other intangible assets represent purchased and acquired patents, licences and trademarks, software rights and licences and the order backlog of acquired businesses at the date of acquisition. Order backlog is derecognised when it has been fully amortised.

#### **Goodwill and annual impairment review**

Goodwill represents the premium paid in anticipation of future economic benefits from assets that are not capable of being separately identified and separately recognised, such as the value of the workforce, and is the only indefinite life intangible asset held by the Group.

The Group reviews goodwill for potential impairment of each cash generating unit (CGU) annually, or more frequently if there are indications that goodwill might be impaired. As a result of the site integrations and other EiD activity, CGUs are typically considered to be SBUs.

The recoverable amounts of the CGUs are determined from value in use calculations unless specific conditions at a CGU dictate otherwise. Businesses held for sale are assessed for impairment using expected net proceeds of divestment.

Following an impairment review of the Cobham Tactical Communications and Surveillance SBU (TC&S), part of the Aerospace and Security segment, an impairment loss of £63.0m has been recognised. Elements of the TC&S business have an exposure to short cycle orders from US military and other US government agencies, which were impacted significantly by budget spending constraints, particularly in the second half of 2013. While a recovery in activity is expected in the medium term it is considered appropriate to recognise an impairment of the carrying value in light of the impact of the current situation on the value in use calculation. A discount rate of 9.0% (2012: 9.3%) was used in the value in use calculation. The remaining goodwill related to this SBU is £43.3m.

The key assumptions for the value in use calculations are those regarding the discount rates, growth rates and operating cash projections during the period for which management have detailed plans. Management estimate discount rates using pre-tax rates that reflect current market assessments of the Group's time value of money and the risks specific to the CGU being measured.

As part of its annual strategic planning process, the Group prepares cash flow forecasts for the following five years at CGU level. These are approved by management. These forecasts take into account the current and expected economic environment including factors such as the softening of the US defence market in the near term. The growth rate assumed after this five year period is based on long term GDP projections of the primary market for the CGU. The long term projections used are in the range 2.0% to 2.5%. The growth rates assume that demand for the Group's products in the US and in the UK remains broadly in line with the underlying economic environment in the long term future. Taking into account the expectation of future market conditions, management believe that the evolution of selling prices and direct costs will reflect past practices.

The pre-tax rates used to discount the forecast cash flows are within the range 8.1% to 10.7% (2012: 8.8% to 10.9%), having considered the country and currency risks in the principal territories in which the Group operates.

If the goodwill allocated to a CGU represents more than 10% of the Group's total goodwill carrying value, then the CGU is considered to be individually significant. These CGUs are as follows:

CGU	Operating segment	Goodwill carrying value £m	Headroom £m	Pre-tax discount rate	Projected GDP growth rate
Defence Electronics	Defence Systems	215	153	9.5%	2.5%
SATCOM	Aerospace and Security	205	398	9.0%	2.1%
Antenna Systems	Aerospace and Security	122	699	9.4%	2.2%
Life Support	Mission Systems	85	418	9.5%	2.5%

Sensitivity analysis has been performed on these CGUs and no impairment losses would arise if the discount rate increased by 20%, if the growth rate was zero or if cash flows reduced by 20%. The Directors have not identified any other likely changes in other significant assumptions that would cause the carrying value of recognised goodwill to exceed its recoverable amount.

# Notes to the Group Financial Statements continued

## 12. Property, plant and equipment

£m	Land and buildings			Plant and machinery (including aircraft & vehicles)	Fixtures, fittings, tools and equipment	Payments on account and assets under construction	Total
	Freehold	Long leases	Short leases				
<b>Cost</b>							
At 1 January 2012	84.9	36.4	10.2	565.9	79.6	8.8	785.8
Additions	0.1	1.9	0.5	23.5	5.3	16.3	47.6
Acquired with business combinations	2.9	–	–	2.6	0.9	–	6.4
Business divestments	(1.4)	–	–	(3.1)	(0.5)	–	(5.0)
Disposals	(0.7)	(0.5)	(0.3)	(14.9)	(1.2)	–	(17.6)
Foreign exchange adjustments	(2.3)	(0.6)	(0.4)	(13.5)	(2.3)	(0.3)	(19.4)
Reclassifications	7.7	(0.2)	–	2.2	4.7	(13.8)	0.6
<b>At 1 January 2013</b>	<b>91.2</b>	<b>37.0</b>	<b>10.0</b>	<b>562.7</b>	<b>86.5</b>	<b>11.0</b>	<b>798.4</b>
Additions	2.7	2.0	0.1	33.4	4.4	18.0	60.6
Acquired with business combinations	–	–	–	74.8	2.4	1.6	78.8
Reclassified as held for sale	(2.1)	–	–	–	–	–	(2.1)
Disposals	(2.8)	(7.4)	(3.7)	(31.3)	(6.6)	–	(51.8)
Foreign exchange adjustments	(2.9)	(0.2)	–	(36.3)	(3.2)	(0.3)	(42.9)
Reclassifications	2.3	0.7	0.2	2.5	4.2	(10.9)	(1.0)
<b>At 31 December 2013</b>	<b>88.4</b>	<b>32.1</b>	<b>6.6</b>	<b>605.8</b>	<b>87.7</b>	<b>19.4</b>	<b>840.0</b>
<b>Accumulated depreciation</b>							
At 1 January 2012	25.5	13.8	6.2	364.9	56.8	–	467.2
Depreciation charge for the year	3.7	2.6	1.2	40.2	7.5	–	55.2
Eliminated on business divestments	(0.4)	–	–	(2.6)	(0.4)	–	(3.4)
Eliminated on disposals	(0.6)	–	(0.2)	(13.3)	(0.9)	–	(15.0)
Foreign exchange adjustments	(0.8)	(0.5)	(0.2)	(7.8)	(1.7)	–	(11.0)
Reclassifications	–	(0.2)	–	–	0.8	–	0.6
<b>At 1 January 2013</b>	<b>27.4</b>	<b>15.7</b>	<b>7.0</b>	<b>381.4</b>	<b>62.1</b>	<b>–</b>	<b>493.6</b>
Depreciation charge for the year	4.5	2.5	1.2	45.8	8.8	–	62.8
Eliminated on disposals	(1.3)	(3.6)	(2.9)	(27.0)	(5.8)	–	(40.6)
Reclassified as held for sale	(1.5)	–	–	–	–	–	(1.5)
Foreign exchange adjustments	(1.1)	(0.1)	(0.1)	(20.9)	(2.4)	–	(24.6)
Reclassifications	–	–	0.1	(1.8)	1.2	–	(0.5)
<b>At 31 December 2013</b>	<b>28.0</b>	<b>14.5</b>	<b>5.3</b>	<b>377.5</b>	<b>63.9</b>	<b>–</b>	<b>489.2</b>
<b>Carrying amount</b>							
<b>At 31 December 2013</b>	<b>60.4</b>	<b>17.6</b>	<b>1.3</b>	<b>228.3</b>	<b>23.8</b>	<b>19.4</b>	<b>350.8</b>
At 31 December 2012	63.8	21.3	3.0	181.3	24.4	11.0	304.8
At 1 January 2012	59.4	22.6	4.0	201.0	22.8	8.8	318.6

### 13. Investment properties

£m	2013	2012
<b>Carrying amount at 1 January</b>	<b>10.7</b>	11.2
Disposals	(0.3)	–
Depreciation	(0.4)	(0.3)
Foreign exchange adjustments	(0.1)	(0.2)
<b>Carrying amount at 31 December</b>	<b>9.9</b>	10.7

The total fair value of the Group's investment properties has been assessed to be £14.2m (2012: £18.0m). This includes £7.8m for UK properties based on estimated market prices provided by external valuers, Vail Williams LLP as at 31 December 2013, and £6.4m for the US property, which is based on Directors' estimates using current market data.

Property rental income earned by the Group from its investment properties amounted to £1.9m (2012: £1.8m), which is net of all direct costs associated with the leasing of the property except depreciation. The buildings are leased to commercial users on operating leases with terms of between 5 and 25 years, commencing between 1998 and 2010.

### 14. Investments in joint ventures and associates

The Group has the following interests in joint ventures and associates:

Name	Percentage shareholding	Nature of relationship	Reporting segment	Country of incorporation or registration
Aviation Défense Service SA	45%	Joint venture	Aviation Services	France
Northrop Grumman Cobham Intercoms LLC	50%	Joint venture	Aerospace and Security	USA
Philtech Co., Ltd	30%	Associate	Aerospace and Security	South Korea

The Company's joint ventures and associates all have share capital consisting solely of ordinary shares, which are indirectly held, and the country of incorporation or registration is also their principal place of operation. Details of the acquisition of FB Heliservices Limited, FBS Limited and FB Leasing Limited, which were previously held as joint ventures, are given in note 29. The 45% investment in Aviation Défense Service SA is treated as a joint venture because the governance structure means that the Group has joint control with its partner.

The share of the balance sheets and income statements of the joint ventures, included in the consolidated financial statements, is as follows:

£m	2013	2012
Current assets	2.1	13.1
Non-current assets	4.1	44.4
Current liabilities	(2.8)	(13.5)
Non-current liabilities	(0.3)	(28.2)
<b>Net assets</b>	<b>3.1</b>	15.8
Income	25.2	49.6
Expenses	(20.4)	(39.6)

The assets and results of the associated undertaking are not separately disclosed on the basis of materiality. The address of the principal place of business of Philtech Co., Ltd is Sujeong-gu, Seonngnam-si, Gyeonggi-do, South Korea.

### 15. Inventories

£m	2013	2012
Raw materials and consumables	139.0	128.1
Work in progress	187.0	185.8
Finished goods and goods for resale	36.8	34.2
Allowance for obsolescence	(46.9)	(41.7)
<b>315.9</b>	<b>306.4</b>	

# Notes to the Group Financial Statements continued

During the year £15.2m (2012: £14.0m) was provided, £6.1m (2012: £5.0m) was utilised and £6.4m (2012: £9.4m) of the allowance for obsolescence was reversed.

This allowance is reviewed by management on a regular basis and further amounts are provided or released as considered necessary. The amounts are generally determined based on factors which include ageing and known demand. Subsequent events may give rise to these estimates being revised and, consequently, to the reversal of amounts previously provided.

Inventory will be realised within the normal operating cycle of the businesses. Within the Mission Systems segment, inventory relating to long term contracts expected to be realised after more than 12 months amounts to £39.0m (2012: £34.6m).

## 16. Financial instruments

The Group's financial assets and liabilities can be categorised as follows:

£m	Note	Loans and receivables	Fair value through profit or loss	Amortised cost	Derivatives used for hedging	Total carrying amount	Fair value
<b>Financial assets</b>							
Trade receivables	17	<b>238.3</b>	–	–	–	<b>238.3</b>	<b>238.3</b>
Other receivables	17	<b>76.9</b>	–	–	–	<b>76.9</b>	<b>76.9</b>
Cash and cash equivalents	10	<b>200.7</b>	–	–	–	<b>200.7</b>	<b>200.7</b>
Derivative contracts (not hedge accounted)	23	–	<b>11.7</b>	–	–	<b>11.7</b>	<b>11.7</b>
Other financial assets		–	–	<b>6.1</b>	–	<b>6.1</b>	<b>6.1</b>
<b>Financial liabilities</b>							
Borrowings	19	–	–	<b>(654.1)</b>	–	<b>(654.1)</b>	<b>(687.5)</b>
Trade payables	20	–	–	<b>(117.1)</b>	–	<b>(117.1)</b>	<b>(117.1)</b>
Accruals		–	–	<b>(99.6)</b>	–	<b>(99.6)</b>	<b>(99.6)</b>
Contingent consideration	20	–	<b>(27.4)</b>	–	–	<b>(27.4)</b>	<b>(27.4)</b>
Other financial liabilities	20	–	–	<b>(47.8)</b>	–	<b>(47.8)</b>	<b>(47.8)</b>
Derivative contracts (not hedge accounted)	23	–	<b>(8.8)</b>	–	–	<b>(8.8)</b>	<b>(8.8)</b>
<b>Hedging instruments</b>							
Liabilities	23	–	–	–	<b>(3.2)</b>	<b>(3.2)</b>	<b>(3.2)</b>
<b>Net financial liabilities at 31 December 2013</b>					<b>(424.3)</b>	<b>(457.7)</b>	

<b>Financial assets</b>							
Trade receivables	17	225.2	–	–	–	225.2	225.2
Other receivables	17	82.3	–	–	–	82.3	82.3
Cash and cash equivalents	10	264.2	–	–	–	264.2	264.2
Derivative contracts (not hedge accounted)	23	–	7.1	–	–	7.1	7.1
<b>Financial liabilities</b>							
Borrowings	19	–	–	<b>(624.1)</b>	–	<b>(624.1)</b>	<b>(675.4)</b>
Trade payables	20	–	–	<b>(105.1)</b>	–	<b>(105.1)</b>	<b>(105.1)</b>
Accruals		–	–	<b>(109.9)</b>	–	<b>(109.9)</b>	<b>(109.9)</b>
Contingent consideration	20	–	<b>(16.8)</b>	–	–	<b>(16.8)</b>	<b>(16.8)</b>
Other financial liabilities	20	–	–	<b>(41.8)</b>	–	<b>(41.8)</b>	<b>(41.8)</b>
Derivative contracts (not hedge accounted)	23	–	<b>(8.6)</b>	–	–	<b>(8.6)</b>	<b>(8.6)</b>
<b>Hedging instruments</b>							
Liabilities	23	–	–	–	<b>(8.3)</b>	<b>(8.3)</b>	<b>(8.3)</b>
<b>Net financial liabilities at 31 December 2012</b>					<b>(335.8)</b>	<b>(387.1)</b>	

Borrowings are held at amortised cost which equates to fair value except for the Group's fixed rate senior notes. At 31 December 2013 the fair value of those notes was £250.1m (31 December 2012: £272.2m) compared to their book value of £216.7m (31 December 2012: £220.9m). The fair value of the senior notes and derivative financial instruments have been determined by reference to observable market prices and rates.

Cash and cash equivalents include term deposits in Australia equivalent to £6.4m in total (2012: £7.5m). These term deposits are held primarily to satisfy a requirement to provide security over the residual value of leased assets under an agreement which expires in 2020 but can be realised within three months under the terms of the agreements.

Other financial assets relate to Cobham plc's investments in connection with the FSTA project which are held at cost, totalling £6.1m (2012: £44,000). These trade investments are categorised as available for sale in accordance with IAS 39. The results of these companies are not consolidated within the results of the Group:

- 13% of the voting share capital of AirTanker Holdings Limited.
- 5% of the voting share capital of AirTanker Services Limited.
- 13.3% of the voting share capital of AirTanker Equity Bridge Loan Limited.

The total interest income and expense for financial assets and liabilities not held at fair value through profit or loss is as shown in note 6.

#### Offsetting financial assets and liabilities

The following financial assets and liabilities are subject to offsetting, enforceable master netting arrangements and similar agreements.

Cash and cash equivalents as shown in the balance sheet include overdraft balances on currency cash pooling accounts which have been offset as the accounts will be settled on a net basis as described in note 25. Master netting agreements also cover all bank balances and derivative balances with the same counterparty. These do not meet the criteria for offsetting because the right to offset is only enforceable on the occurrence of future events such as a default and amounts presented in the Balance Sheet are therefore presented on a gross basis.

If full offsetting by counterparty were to be applied, the resulting net amounts would be as follows:

£m	Gross amounts before set off	Amounts set off in the Balance Sheet	Amounts as presented in the Balance Sheet	Amounts not set off in the Balance Sheet	Net amount
<b>Financial assets</b>					
Cash and cash equivalents	<b>343.9</b>	<b>(143.2)</b>	<b>200.7</b>	<b>(1.4)</b>	<b>199.3</b>
Derivative financial assets	<b>11.7</b>	–	<b>11.7</b>	<b>(5.9)</b>	<b>5.8</b>
<b>Financial liabilities</b>					
Bank overdrafts	<b>(144.9)</b>	<b>143.2</b>	<b>(1.7)</b>	<b>1.7</b>	–
Derivative financial liabilities	<b>(12.0)</b>	–	<b>(12.0)</b>	<b>5.6</b>	<b>(6.4)</b>
<b>As at 31 December 2013</b>	<b>198.7</b>	–	<b>198.7</b>	–	<b>198.7</b>
 Financial assets					
Cash and cash equivalents	370.3	(106.1)	264.2	(10.4)	253.8
Derivative financial assets	7.1	–	7.1	(3.0)	4.1
 Financial liabilities					
Bank overdrafts	(120.1)	106.1	(14.0)	11.2	(2.8)
Derivative financial liabilities	(16.9)	–	(16.9)	2.2	(14.7)
<b>As at 31 December 2012</b>	<b>240.4</b>	–	<b>240.4</b>	–	<b>240.4</b>

#### 17. Trade and other receivables

##### 17a. Current

£m	2013	2012
Trade receivables (net of provision for impairment)	<b>238.3</b>	225.2
Accrued income	<b>38.2</b>	15.2
Loans and other receivables	<b>16.5</b>	20.0
Prepayments	<b>24.7</b>	20.6
<b>317.7</b>	281.0	

# Notes to the Group Financial Statements continued

## 17b. Non-current

£m	2013	2012
Loans and other receivables	22.2	47.1

## 17c. Impairment of trade receivables

£m	2013	2012
Trade receivables	239.9	227.9
Provision for impairment of trade receivables	(1.6)	(2.7)
Net trade receivables	238.3	225.2

The Group has not experienced any material change in performance with respect to the recovery of trade receivables. A significant proportion of its business is directly with government agencies or in respect of large government funded military programmes, where risk is considered to remain low. Information concerning credit risk is shown in note 25.

The credit quality of trade receivables can be analysed as follows:

£m	2013	2012
Amounts not yet due and not impaired	186.0	186.4
Amounts past due but not impaired	51.1	37.5
Amounts for which full or partial impairment provision has been made	2.8	4.0
At 31 December	239.9	227.9

Trade receivables which are past due but not considered by management to be impaired are aged as follows:

£m	2013	2012
Due at 31 December	34.3	26.4
1 month overdue	10.1	4.5
2 months overdue	2.8	2.4
3 or more months overdue	3.9	4.2
	51.1	37.5

Other classes of financial assets within trade and other receivables do not include any overdue or impaired assets. Movements in the provision for impairment of trade receivables during the current and prior year were not individually significant.

## 18. Non-current assets and disposal groups held for sale

£m	2013	2012
Intangible assets	—	1.1
Property, plant and equipment	1.9	3.1
Inventories	2.8	6.1
Trade and other receivables	3.5	4.8
<b>Total assets classified as held for sale</b>	<b>8.2</b>	<b>15.1</b>
Trade and other payables	(4.7)	(2.5)
Tax and other liabilities	(0.5)	(0.7)
<b>Total liabilities associated with assets classified as held for sale</b>	<b>(5.2)</b>	<b>(3.2)</b>
 <b>Total net assets of disposal groups and non-current assets held for sale</b>	 <b>3.0</b>	 11.9

Non-current assets and disposal groups held for sale at 31 December 2013 includes businesses and vacant properties which are being actively marketed and are expected to be disposed of within 12 months of the balance sheet date. These assets are measured on a non-recurring basis at fair value (based on an estimated sales price) less costs to sell as this is lower than the original carrying value of those assets.

## 19. Borrowings

£m	2013	2012
Current:		
Bank overdrafts	1.7	14.0
Bank loans	296.4	292.3
Senior notes	46.2	–
Loan notes, finance leases and other borrowings	0.2	1.0
	344.5	307.3
Non-current:		
Bank loans	45.3	–
Senior notes	264.1	316.2
Finance leases	0.2	0.6
	309.6	316.8
<b>Total borrowings</b>	<b>654.1</b>	624.1

The Group's principal borrowings include bank overdrafts, bank loans and senior notes. Bank overdrafts are repayable on demand and accrue interest at floating rates. Interest is payable on all bank loans at LIBOR plus margin and the loans comprise the following:

	Agreement date	Maturity date	Amount drawn		Undrawn facilities	
			2013	2012	2013	2012
			£m	£m	£m	£m
US\$75m credit agreement	December 2008	December 2016	45.3	46.2	–	–
DKK525m multi-currency revolving facility	June 2012	October 2017	52.7	18.9	5.8	38.2
US\$360m multi-currency revolving credit agreement comprising:	October 2011					
US\$90m		October 2016	51.7	53.5	2.6	1.9
US\$270m		October 2018	155.2	160.5	7.9	5.6
EUR70m multi-currency revolving facility	June 2012	June 2017	36.8	13.2	21.4	43.6
			341.7	292.3	37.7	89.3

Under the US\$75m agreement, which expires in 2031, the lender has a series of put options exercisable every three years from December 2016. The US\$360m agreement contains lender's options to extend for up to two years and during 2012 the first extension of one year was confirmed by the lenders of US\$270m. The DKK525m facility contains lender's options that could extend the agreement by up to two years.

A loan agreement for AUS\$90m expiring in October 2018 was signed subsequent to the year-end.

The drawdowns under the revolving multi-currency credit agreements are for periods not exceeding three months and hence these balances are reported as current liabilities.

Senior notes with a total principal value of US\$514.0m are outstanding as set out below:

£m	Issue date	Maturity date	2013	2012
US\$76.5m fixed rate	March 2009	March 2014	46.2	47.1
US\$81m fixed rate	March 2009	March 2016	48.9	49.8
US\$50m floating rate	May 2010	May 2017	30.2	30.8
US\$105m floating rate	January 2010	February/March 2018	63.4	64.5
US\$157.5m fixed rate	March 2009	March 2019	95.0	96.9
US\$44m fixed rate	October 2012	October 2020	26.6	27.1
			310.3	316.2

# Notes to the Group Financial Statements continued

The various loan and note subscription agreements include both financial and non-financial covenants but do not contain any provisions for charges over Group assets. The terms of the financial covenants are based on adjusted IFRS results and are as shown on page 25. There have been no breaches of the terms of agreements or defaults during the current or comparative periods.

## 20. Trade and other payables

### 20a. Current liabilities

£m	2013	2012
Payments received on account	<b>72.3</b>	68.6
Trade payables	<b>116.4</b>	104.8
Other taxes and social security	<b>19.2</b>	20.6
Accruals and deferred income	<b>104.4</b>	116.6
Contingent consideration	<b>15.2</b>	2.5
Other liabilities	<b>42.8</b>	36.8
	<b>370.3</b>	349.9

### 20b. Non-current liabilities

£m	2013	2012
Payments received on account	<b>9.4</b>	11.3
Trade payables	<b>0.7</b>	0.3
Accruals and deferred income	<b>10.7</b>	8.2
Contingent consideration	<b>12.2</b>	14.3
Other liabilities	<b>5.0</b>	5.0
	<b>38.0</b>	39.1

Movements in the fair value of contingent consideration during the year are as follows:

£m	2013
<b>At 1 January 2013</b>	<b>16.8</b>
Acquired on business combinations	<b>22.1</b>
Amounts paid	<b>(2.5)</b>
Gains or losses recognised in profit or loss:	
Released in year	<b>(11.9)</b>
Unrealised change in fair value – discounting included in finance costs	<b>2.6</b>
Foreign exchange adjustments	<b>0.3</b>
<b>At 31 December 2013</b>	<b>27.4</b>

The fair value of contingent consideration is not based on observable market data but is based on management's best estimates of discounted expected payments of contingent consideration reflecting expectations of achievement of earnings targets. The estimated fair value would decrease with lower than anticipated annual revenue growth rates and profit margin or a higher discount rate. Management consider that changing the unobservable inputs to reflect other reasonably possible alternative assumptions would not result in a significant change in the estimated fair value. Of the amount outstanding at 31 December 2013, £12.5m has been paid in January 2014 and the remainder is due to be paid by March 2015.

Contingent consideration has been released in the year following a reassessment of the likely outcome of the agreements relating to acquisitions in a prior year. The amount released is included in administrative expenses in the Consolidated Income Statement and is excluded from underlying profit in note 3.

## 21. Provisions

£m	2013	2012
Current liabilities	<b>34.4</b>	36.3
Non-current liabilities	<b>8.6</b>	10.9
	<b>43.0</b>	47.2

Movements in provisions during the year are as follows:

£m	Provisions related to businesses divested	Warranty claims	Contract loss provisions	Aircraft maintenance provisions	Other	Total
At 1 January 2013	<b>12.8</b>	<b>10.3</b>	<b>5.4</b>	<b>3.4</b>	<b>15.3</b>	<b>47.2</b>
Additional provisions in the year	—	<b>5.0</b>	<b>2.8</b>	<b>2.0</b>	<b>3.7</b>	<b>13.5</b>
Acquired on business combinations	—	<b>0.1</b>	—	—	—	<b>0.1</b>
Utilisation of provisions	(0.7)	(3.1)	(2.3)	(0.4)	(3.2)	(9.7)
Unused amounts reversed in the year	(1.3)	(2.0)	(1.5)	(1.3)	(1.9)	(8.0)
Reclassifications	—	—	—	0.3	—	0.3
Foreign exchange adjustments	—	<b>0.2</b>	—	(0.6)	—	(0.4)
At 31 December 2013	<b>10.8</b>	<b>10.5</b>	<b>4.4</b>	<b>3.4</b>	<b>13.9</b>	<b>43.0</b>

Provisions related to businesses divested relate to longer term warranties given on divestments completed in 2005. Due to uncertainties surrounding the timing of settlement of these items, they have been disclosed as current liabilities.

Provisions for warranty claims and contract losses are generally expected to be crystallised within one year.

Aircraft maintenance provisions relate to significant periodic maintenance costs as well as return conditions for leased aircraft. These conditions may relate to the number of operational hours to be available before a major maintenance check, the physical configuration of the aircraft or direct costs to be incurred by the lessee in the physical return of the aircraft to the lessor. While there is uncertainty over the future level of flying hours, aircraft maintenance provisions are anticipated to crystallise in the next eight years.

Other provisions include amounts provided in respect of announced business restructuring and legal claims and are expected to be settled within one year.

# Notes to the Group Financial Statements continued

## 22. Deferred tax

£m	2013	2012
Deferred tax assets	(9.9)	(9.8)
Deferred tax liabilities	52.9	44.2
	43.0	34.4

The following are the major deferred tax assets and liabilities recognised by the Group, and the movements thereon:

£m	Accelerated tax depreciation	Retirement benefit obligations	Intangible assets	Other	Total
At 1 January 2012	10.8	(17.8)	24.1	(19.9)	(2.8)
(Credit)/charge to income statement (as restated)	7.3	2.6	3.8	(28.9)	(15.2)
Charge/(credit) to other comprehensive income (as restated)	–	(1.8)	–	16.9	15.1
Credit to reserves	–	–	–	(0.5)	(0.5)
Acquired with business combinations	0.6	–	37.4	(2.6)	35.4
Business divestments	–	–	–	1.3	1.3
Foreign exchange adjustments	(0.3)	–	(1.2)	1.3	(0.2)
Reclassifications	–	–	1.3	–	1.3
<b>At 1 January 2013</b>	<b>18.4</b>	<b>(17.0)</b>	<b>65.4</b>	<b>(32.4)</b>	<b>34.4</b>
(Credit)/charge to income statement	2.3	2.7	(20.1)	(2.2)	(17.3)
(Credit)/charge to other comprehensive income	–	(4.1)	–	1.2	(2.9)
Credit to reserves	–	–	–	(2.1)	(2.1)
Acquired with business combinations	(1.6)	–	27.4	2.6	28.4
Foreign exchange adjustments	(0.8)	–	1.2	2.5	2.9
Reclassifications	–	–	(0.4)	–	(0.4)
<b>At 31 December 2013</b>	<b>18.3</b>	<b>(18.4)</b>	<b>73.5</b>	<b>(30.4)</b>	<b>43.0</b>

Other deferred tax assets and liabilities shown above include balances arising from temporary differences in relation to provisions, deferred compensation, share based payments and derivative financial instruments.

Certain deferred tax assets and liabilities have been offset in accordance with the Group's accounting policy. Deferred tax balances (after offset) for balance sheet purposes are analysed as follows:

£m	2013	2012
Deferred tax liabilities fall due as follows:		
Within one year	17.6	7.2
After one year	35.3	37.0
	52.9	44.2
Deferred tax assets are recoverable as follows:		
Within one year	(5.7)	(2.8)
After one year	(4.2)	(7.0)
	(9.9)	(9.8)

Without taking into consideration the offsetting of balances, deferred tax balances are as follows:

£m	Accelerated tax depreciation	Retirement benefit obligations	Intangible assets	Other	Total
Deferred tax assets	—	<b>(18.4)</b>	—	<b>(44.8)</b>	<b>(63.2)</b>
Deferred tax liabilities	<b>18.3</b>	—	<b>73.5</b>	<b>14.4</b>	<b>106.2</b>
<b>At 31 December 2013</b>	<b>18.3</b>	<b>(18.4)</b>	<b>73.5</b>	<b>(30.4)</b>	<b>43.0</b>
Deferred tax assets	(0.8)	(17.0)	—	(42.2)	(60.0)
Deferred tax liabilities	19.2	—	65.4	9.8	94.4
<b>At 31 December 2012</b>	<b>18.4</b>	<b>(17.0)</b>	<b>65.4</b>	<b>(32.4)</b>	<b>34.4</b>

At the balance sheet date, the Group has unused capital losses of £65.7m (2012: £65.7m) potentially available for offset against future capital profits in certain circumstances. No deferred tax asset has been recognised in respect of this amount because of the unpredictability of future qualifying profit streams. These losses can be carried forward indefinitely.

At the balance sheet date, the aggregate amount of temporary differences associated with undistributed earnings of subsidiaries and joint ventures for which deferred tax liabilities have not been recognised is £369.2m (2012: £431.1m).

### 23. Derivative financial instruments

The fair values of derivative financial instruments are as follows:

£m	Interest rate swaps – cash flow hedges	Foreign exchange derivatives	Inflation swap	Total
Non-current assets	—	<b>5.1</b>	—	<b>5.1</b>
Current assets	—	<b>6.6</b>	—	<b>6.6</b>
Current liabilities	<b>(0.5)</b>	<b>(3.6)</b>	<b>(0.5)</b>	<b>(4.6)</b>
Non-current liabilities	<b>(2.7)</b>	<b>(1.8)</b>	<b>(2.9)</b>	<b>(7.4)</b>
<b>Fair value at 31 December 2013</b>	<b>(3.2)</b>	<b>6.3</b>	<b>(3.4)</b>	<b>(0.3)</b>
Non-current assets	—	3.4	—	3.4
Current assets	—	3.7	—	3.7
Current liabilities	(3.5)	(2.6)	(0.5)	(6.6)
Non-current liabilities	(4.8)	(2.7)	(2.8)	(10.3)
<b>Fair value at 31 December 2012</b>	<b>(8.3)</b>	<b>1.8</b>	<b>(3.3)</b>	<b>(9.8)</b>

# Notes to the Group Financial Statements continued

The movements in the fair values of derivative financial instruments during the year are as follows:

£m	Note	Interest rate swaps – cash flow hedges	Foreign exchange derivatives	Inflation swap	Total
At 1 January 2012		(12.4)	(14.4)	(1.7)	(28.5)
Gain/(loss) through income statement – not hedged		–	12.8	(1.7)	11.1
Gain through income statement – other		–	3.4	–	3.4
Gain reclassified to income statement	27	7.2	–	–	7.2
Loss through OCI – hedged items	27	(3.5)	–	–	(3.5)
Foreign exchange adjustments	27	0.4	–	0.1	0.5
<b>At 1 January 2013</b>		<b>(8.3)</b>	<b>1.8</b>	<b>(3.3)</b>	<b>(9.8)</b>
Gain/(loss) through income statement – not hedged		–	2.9	(0.7)	2.2
Gain through income statement – other		–	1.5	–	1.5
Gain reclassified to income statement	27	<b>4.5</b>	–	–	<b>4.5</b>
Foreign exchange adjustments	27	<b>0.6</b>	<b>0.1</b>	<b>0.6</b>	<b>1.3</b>
<b>At 31 December 2013</b>		<b>(3.2)</b>	<b>6.3</b>	<b>(3.4)</b>	<b>(0.3)</b>

Interest rate swaps are designated as cash flow hedging instruments and hedge accounting is applied. There is no material ineffectiveness in cash flow hedges to be reported through the income statement.

Foreign exchange and inflation derivatives are not accounted for using hedge accounting and movements in fair values are recorded in the income statement as part of operating profit. The movement in the fair value of currency swaps which offset movements in currency balances are offset against exchange movements in those balances in the income statement.

Full details of the Group's financial instrument accounting policies and risk management strategies, objectives and policies are set out in the accounting policies in note 1 and in note 25, financial risk management.

## 24. Retirement benefit schemes

Retirement benefit obligations per the Balance Sheet consist of:

£m	2013	2012
Defined benefit scheme assets	<b>577.6</b>	572.4
Defined benefit obligations	<b>(664.9)</b>	(645.8)
	<b>(87.3)</b>	(73.4)

Pension expense included in employment costs in note 5 are as follows:

£m	2013	2012
Defined benefit schemes	<b>5.2</b>	4.6
Defined contribution schemes	<b>24.4</b>	21.1
	<b>29.6</b>	25.7

The Group operates a number of funded defined benefit schemes, the most significant being the Cobham Pension Plan (CPP). The assets of all of these schemes are held separately from those of the Group in funds under the control of trustees. All defined benefit schemes have been closed to new members since 2003. The Group also manages a number of defined contribution pension arrangements.

Actuarial valuations of the present value of the defined benefit obligations for the CPP are carried out on a triennial basis by qualified independent actuaries; the most recent valuation was as at 1 April 2012. Actuarial valuations of other schemes have been carried out at regular intervals as required by the applicable country regulations. The actuarial valuations were updated by qualified independent actuaries for accounting purposes to 31 December 2013.

On 1 July 2013 the liabilities related to past service of pensioners of the CPP on that date were subject to a buy-in arrangement. Under the terms of this arrangement, the CPP transferred assets to an insurance company in return for a qualifying insurance policy which provides an income stream to the Plan equivalent to the Plan's obligations to pensioners covered by the arrangement. This eliminated the Group's exposure to the interest, inflation and longevity risks associated with these liabilities. The liabilities covered by this buy-in amounted to £242m, which had the impact of generating an actuarial loss of £39m. This follows similar buy-in arrangements completed in 2011 related to past service of pensioner and deferred members of some of the smaller defined benefit schemes. The insurance contract assets are measured at a value equal to the related liabilities.

There were no significant contributions outstanding at the end of 2013 or 2012 for the defined benefit schemes. £1.2m (2012: £0.6m) was outstanding in respect of defined contribution schemes but not due for payment at 31 December 2013.

The principal financial assumptions used for the purpose of the actuarial valuations were as follows:

	2013		2012	
	UK schemes	USA scheme	UK schemes	USA scheme
Rate of increase in salary costs	<b>3.80%</b>	<b>3.80%</b>	3.47%	3.47%
Rate of increase in pensions in payment unless overridden by specific scheme rules	<b>3.55%</b>	<b>3.55%</b>	2.97%	2.97%
Rate of increase in deferred pensions	<b>2.55%</b>	<b>3.55%</b>	2.17%	2.97%
Discount rate	<b>4.50%</b>	<b>4.50%</b>	4.40%	4.40%
Inflation assumption	<b>3.55%</b>	<b>3.55%</b>	2.97%	2.97%

# Notes to the Group Financial Statements continued

The mortality assumptions used for the CPP are based upon actuarial tables which reflect actual recent mortality experience and also allow for future mortality improvements. The mortality tables used to estimate life expectancy are known as 'SAPS CMI 09'. In practical terms, this is demonstrated in the table below:

	Year of birth	Year age 65	Further life expectancy
Male	1948	2013	22.7 years
Female	1948	2013	24.8 years
Male	1980	2045	25.8 years
Female	1980	2045	27.9 years

At 31 December 2013 it has been assumed that members will commute on average 20% (2012: 20%) of their pension for cash at retirement. This implies a full take-up of the permitted 25% (2012: 25%) commutation by approximately 80% (2012: 80%) of eligible members on retirement.

The sensitivity of scheme liabilities to changes in certain key assumptions, after adjusting for liabilities covered by insurance contracts, is provided below:

- Increasing the discount rate by 0.1% would decrease scheme liabilities by £6.2m.
- Increasing the inflation rate by 0.1% would increase scheme liabilities by £3.4m.
- If each scheme member was expected to live for an additional year, then scheme liabilities would increase by £9.4m.

The impact of increases and decreases in assumptions are approximately symmetrical.

A summary of the movements in the net liability and the amounts recognised in the income statement and other comprehensive income are as follows:

£m	2013			2012		
	Scheme assets	Defined benefit obligations	Total	Scheme assets	Defined benefit obligations	
Net liability at start of year	<b>572.4</b>	<b>(645.8)</b>	<b>(73.4)</b>	528.7	(599.9)	(71.2)
Amounts recognised in operating profit:						
Current service cost included in administrative expenses	–	<b>(5.2)</b>	<b>(5.2)</b>	–	(4.3)	(4.3)
Past service (cost)/credit included in administrative expenses	–	–	–	–	(0.3)	(0.3)
Scheme administration expenses	<b>(1.4)</b>	–	<b>(1.4)</b>	(1.1)	–	(1.1)
Amounts credited/(charged) to other finance income/costs:						
Net interest	<b>25.2</b>	<b>(28.0)</b>	<b>(2.8)</b>	25.7	(28.6)	(2.9)
Amounts recognised in other comprehensive income:						
Actual return less interest income on pension scheme assets	<b>22.8</b>	–	<b>22.8</b>	14.8	–	14.8
Actuarial loss arising on buy-in transaction	<b>(39.0)</b>	–	<b>(39.0)</b>	–	–	–
Experience gains arising on scheme liabilities	–	–	–	–	12.8	12.8
Actuarial gains and losses arising from changes in financial assumptions	–	<b>(18.1)</b>	<b>(18.1)</b>	–	(40.9)	(40.9)
Actuarial gains and losses arising from changes in demographic assumptions	–	<b>8.7</b>	<b>8.7</b>	–	(0.4)	(0.4)
Amounts included in cash flow statement:						
Employer contributions	<b>21.1</b>	–	<b>21.1</b>	20.0	–	20.0
Member contributions	<b>2.7</b>	<b>(2.7)</b>	–	2.8	(2.8)	–
NI rebates	–	–	–	0.6	(0.6)	–
Benefits paid	<b>(25.9)</b>	<b>25.9</b>	–	(18.4)	18.4	–
Other changes:						
Exchange differences	<b>(0.3)</b>	<b>0.3</b>	–	(0.7)	0.8	0.1
<b>Net liability at end of year</b>	<b>577.6</b>	<b>(664.9)</b>	<b>(87.3)</b>	572.4	(645.8)	(73.4)

Total employer contributions exceeded current service cost, past service cost and scheme administration expenses by £14.5m (2012: £14.3m).

The present value of funded obligations relating to the US scheme is US\$35.5m (2012: US\$34.5m) and the fair value of scheme assets relating to the US scheme is US\$26.2m (2012: US\$21.3m).

The cumulative amount of actuarial gains and losses recognised in the Consolidated Statement of Comprehensive Income since transition to IFRS is £208.1m loss (2012: £182.5m loss). Of the actuarial losses recognised in the year, the changes in financial assumptions are primarily driven by the movements in the discount rate and inflation assumption, and the change in demographic assumptions primarily arose from changes to the assumed proportion of members who are married on the date of their retirement.

The actual return on scheme assets was £48.0m (2012: £40.5m) before accounting for the actuarial loss of £39.0m generated on the buy-in transaction. The Group expects to contribute £22.1m to its defined benefit pension schemes in 2014. This includes £17.6m related to deficit funding. The weighted average duration of the scheme liabilities is estimated to be 19 years.

The fair value of major categories of scheme assets, and as a percentage of total scheme assets, is as follows:

	2013		2012	
	£m	%	£m	%
UK equity instruments	<b>74.7</b>	<b>12.9%</b>	95.7	16.7%
Overseas equities	<b>43.0</b>	<b>7.4%</b>	50.6	8.8%
Emerging markets equities	<b>20.0</b>	<b>3.5%</b>	21.1	3.7%
Gilts	—	—	105.5	18.4%
Corporate bonds	<b>28.8</b>	<b>5.0%</b>	124.0	21.7%
Property	—	—	40.6	7.1%
Diversified growth funds	<b>127.4</b>	<b>22.1%</b>	94.0	16.4%
Insurance contracts	<b>280.7</b>	<b>48.6%</b>	40.1	7.0%
Other assets	<b>3.0</b>	<b>0.5%</b>	0.8	0.2%
	<b>577.6</b>	<b>100.0%</b>	572.4	100.0%

The expected rates of return on individual categories of scheme assets are determined by reference to relevant indices published by, for example, the London Stock Exchange. The overall expected rate of return is calculated by weighting the individual rates in accordance with the anticipated balance in the schemes' investment portfolios.

The scheme assets do not include any of the Group's own financial instruments, nor any property occupied by, or other assets used by, the Group. The history of the scheme for the current and previous four periods is as follows:

£m	2013	2012	2011	2010	2009
Present value of defined benefit obligations	<b>(664.9)</b>	(645.8)	(599.9)	(592.8)	(561.3)
Fair value of scheme assets	<b>577.6</b>	572.4	528.7	510.8	446.1
<b>Net liability</b>	<b>(87.3)</b>	(73.4)	(71.2)	(82.0)	(115.2)
Experience adjustments on scheme liabilities	—	12.8	1.8	1.3	1.8
Experience adjustments on scheme assets	<b>(16.2)</b>	12.8	(40.3)	24.1	13.8

#### Other retirement benefit schemes

A number of the Group's subsidiaries based in France contribute to a retirement indemnity scheme. The liabilities of the scheme were valued by an independent actuary as at 31 December 2012 at EUR4.3m and are recorded in these financial statements at £3.6m (2012: £3.5m). These liabilities are included in other liabilities in note 20. Retirement obligations relating to a subsidiary based in Germany have gross obligations of EUR3.1m (2012: EUR2.2m). These obligations are covered by an insurance policy and therefore there is no net liability.

The actuarial loss for these schemes in the year to 31 December 2013, recognised in OCI, was £nil (2012: £0.5m).

# Notes to the Group Financial Statements continued

## 25. Financial risk management

The Group's multinational operations and debt financing expose it to a variety of financial risks which include the effects of changes in foreign currency exchange rates, interest rates, liquidity risk and credit risk. The Group has in place a risk management programme that seeks to limit the adverse effects on the financial performance of the Group by using foreign currency financial instruments, debt and other instruments, including interest rate swaps. Other derivative financial instruments may be used from time to time to manage other exposures such as inflation risks. The financial risk management policies agreed by the Board have not changed during the year and are summarised below. The Group does not trade in financial instruments.

### Foreign currency risk

The Group is based in the UK, reports in sterling and has significant investment in overseas operations in the USA, Australia and other European countries. As a result, the Group's balance sheet can be affected by movements in these countries' exchange rates. The Group's policy is to reduce, or eliminate where practical, both structural and transactional foreign exchange risk and, consequently, the net foreign exchange losses included in the income statement amounted to £3.2m (2012: £3.6m). All currency exposures are reviewed regularly and all significant foreign exchange transactions are approved by Cobham plc management.

The Group has the following exposure to foreign currency denominated monetary assets and monetary liabilities in its Balance Sheet, translated into sterling at the relevant year-end exchange rates:

£m	2013		2012	
	Monetary assets	Monetary liabilities	Monetary assets	Monetary liabilities
US dollars	188.8	(584.9)	214.2	(620.3)
Euros	86.8	(109.3)	87.8	(49.7)
Australian dollars	56.2	(54.2)	65.9	(72.8)
Danish kroner	18.1	(90.7)	14.0	(92.6)
Other currencies	24.5	(8.3)	17.5	(6.5)
	374.4	(847.4)	399.4	(841.9)
Sterling denominated monetary assets and liabilities	166.2	(117.9)	192.8	(74.8)
	540.6	(965.3)	592.2	(916.7)

Foreign currency borrowings are used to mitigate the impact of foreign currency exchange differences arising from the Group's overseas net assets. The Group typically borrows in the currency of the acquisition and uses intercompany debt to create a natural economic hedge. Monetary liabilities in the table above include US dollar borrowings of £482.4m (2012: £484.2m) and Danish kroner borrowings of £75.9m (2012: £74.0m) which match exposures arising from currency denominated net assets. Foreign currency contracts are also used to manage exposure to currency risks.

On consolidation, the net assets of overseas subsidiaries (which include the monetary assets and liabilities shown in the tables above) are translated at closing exchange rates and exchange differences arising are accounted for in other comprehensive income and in the translation reserve (note 27).

The Group is exposed to foreign currency risk in the income statement where individual subsidiaries hold non-functional currency monetary assets and liabilities and when an operating unit makes sales and purchases in currencies other than its own functional currency. The Group undertakes a formal process to actively manage and mitigate this exposure through a combination of matching non-functional currency revenues and costs, matching non-functional currency monetary assets and liabilities and through the use of forward contracts.

The sterling/US dollar exchange rate is the most important as far as the Group is concerned, particularly given the level of US dollars which non-US based subsidiaries expect to receive from their normal business activities, and the proportion of the Group based in the USA. The Group has the following forward foreign currency contracts outstanding for net sales of US dollars:

	US\$m amount		Average US\$: £ exchange rate	
	2013	2012	2013	2012
Expiring within one year	<b>124.1</b>	138.7	<b>1.59</b>	1.59
Expiring within one to two years	<b>38.0</b>	76.0	<b>1.58</b>	1.61
Expiring after two years	<b>71.6</b>	17.9	<b>1.56</b>	1.58
<b>Contracts outstanding at 31 December</b>	<b>233.7</b>	232.6	<b>1.58</b>	1.60

The latest expiry date of forward foreign currency contracts for sales of US dollars is July 2022 and it is the Group's current belief that the net dollar receipts by its subsidiaries will exceed the level of the outstanding commitment.

The following table details the Group's sensitivity to a weakening in sterling against the respective foreign currencies, with a negative number indicating a reduction in profit after taxation or total equity. The sensitivities below represent management's assessment of the possible changes in foreign exchange rates, based on experience over the previous five years.

£m	2013			2012		
	Sensitivity	Profit or loss	Total equity	Sensitivity	Profit or loss	Total equity
US dollars	<b>11%</b>	<b>(13.8)</b>	<b>(13.8)</b>	16%	(21.0)	(21.0)
Euros	<b>9%</b>	<b>(3.3)</b>	<b>(3.3)</b>	13%	(10.3)	(10.3)

This sensitivity analysis has been based on the assumption that the change is effective throughout the financial year and that all other variables, including interest rates, remain constant. It includes the effect of derivative financial instruments.

In order to provide comparable information, sensitivity has also been assessed based on a 10% weakening in sterling against the respective foreign currency, as follows:

£m	2013			2012		
	Sensitivity	Profit or loss	Total equity	Sensitivity	Profit or loss	Total equity
US dollars	<b>10%</b>	<b>(12.4)</b>	<b>(12.4)</b>	10%	(12.2)	(12.2)
Euros	<b>10%</b>	<b>(3.7)</b>	<b>(3.7)</b>	10%	(7.7)	(7.7)

### Interest rate risk

The Group has long and short-term borrowings at both fixed and floating rates of interest. In managing its borrowing costs, the Group monitors its exposure to movements in interest rates, having regard to prevailing market conditions and, where necessary, uses interest rate swaps to manage the interest rate risk.

# Notes to the Group Financial Statements continued

As noted above, borrowings are held in various currencies and can be analysed between fixed and floating rates as follows:

£m	2013	2012
Fixed rates		
Senior notes	<b>216.7</b>	220.9
Bank loans	<b>45.3</b>	—
	<b>262.0</b>	220.9
Floating rates		
Bank loans and overdrafts	<b>298.1</b>	306.3
Senior notes	<b>93.6</b>	95.3
Loan notes, finance leases and other borrowings	<b>0.4</b>	1.6
	<b>392.1</b>	403.2
<b>Total borrowings</b>	<b>654.1</b>	624.1

All floating rate borrowings have regular repricing dates.

Floating to fixed interest rate swaps, designated as cash flow hedges, have been used to mitigate the interest rate exposure arising on selected floating rate debt. Interest rate swaps outstanding at the year-end are as follows:

Hedged item	Period of swap contract			2013		2012	
	Fixed rate	from	to	Currency value	£m	Currency value	£m
Australian dollar loans	6.30%	May 2006	January 2020	AUS\$58.0m	<b>31.3</b>	AUS\$74.4m	42.3
	6.40%	January 2007	January 2020	AUS\$10.8m	<b>5.8</b>	AUS\$14.3m	8.0
					<b>37.1</b>		50.3

Interest rate swaps which expired during the year to 31 December 2013 were previously used to fix the interest rates on US dollar floating rate loans. At 31 December 2012, these swaps had a total notional currency value of US\$295.0m (£181.5m) and fixed interest rates at between 3.22% and 3.61%.

The Group does not currently hold any fair value hedging instruments such as fixed to floating interest rate swaps.

Surplus funds are placed on short-term fixed rate deposit and as such also give rise to interest rate exposure. There was no material sensitivity to changes in interest rates at the year-end.

## Liquidity risk

The Group's policy on managing liquidity risk throughout the year has been to maintain a mix of short, medium and long term borrowings with lenders. Overdraft and revolving credit facilities provide short term flexibility whilst the revolving credit facilities provide longer term committed funding.

As shown in note 19, undrawn committed borrowing facilities of £37.7m were available to the Group at 31 December 2013 (2012: £89.3m) in various currencies.

At an operating level, the Group has a positive cash flow from operating activities and where practical the funds generated by business units are managed on a regional basis. In the UK and US, most business units utilise local bank facilities within a UK or US group arrangement. This allows a balance to be maintained between continuity of funding, security and flexibility.

The table below summarises the remaining contractual maturity for the Group's borrowings and other financial liabilities, including derivative financial liabilities. The amounts shown are the contractual undiscounted cash flows which include interest, analysed by contractual maturity. The difference between the contractual cash flows and the carrying amount of these liabilities reflects the effects of interest not included in the carrying amount and discounting applied in assessing fair value.

£m	Within one year	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years	Total
<b>At 31 December 2013</b>							
<b>Non-derivative financial liabilities</b>							
Borrowings							
Bank loans and overdrafts	<b>300.2</b>	<b>1.9</b>	<b>47.1</b>	–	–	–	<b>349.2</b>
Senior notes	<b>59.1</b>	<b>12.4</b>	<b>58.7</b>	<b>39.0</b>	<b>71.1</b>	<b>124.5</b>	<b>364.8</b>
Other borrowings	<b>0.2</b>	<b>0.2</b>	–	–	–	–	<b>0.4</b>
	<b>359.5</b>	<b>14.5</b>	<b>105.8</b>	<b>39.0</b>	<b>71.1</b>	<b>124.5</b>	<b>714.4</b>
Trade and other payables							
Trade payables	<b>116.4</b>	<b>0.5</b>	<b>0.2</b>	–	–	–	<b>117.1</b>
Accruals	<b>97.0</b>	<b>0.5</b>	<b>0.3</b>	<b>0.3</b>	<b>0.3</b>	<b>1.2</b>	<b>99.6</b>
Contingent consideration	<b>15.2</b>	<b>12.2</b>	–	–	–	–	<b>27.4</b>
Other liabilities	<b>42.8</b>	<b>1.0</b>	<b>0.7</b>	<b>0.9</b>	<b>0.8</b>	<b>1.6</b>	<b>47.8</b>
	<b>271.4</b>	<b>14.2</b>	<b>1.2</b>	<b>1.2</b>	<b>1.1</b>	<b>2.8</b>	<b>291.9</b>
<b>Derivative liabilities</b>							
Interest rate swaps	<b>1.3</b>	<b>0.8</b>	<b>0.7</b>	<b>0.3</b>	<b>0.2</b>	<b>0.1</b>	<b>3.4</b>
Foreign exchange derivatives							
Gross cash outflows	<b>120.9</b>	<b>16.8</b>	<b>0.2</b>	–	–	<b>7.5</b>	<b>145.4</b>
Gross cash inflows	(118.1)	(15.1)	(0.2)	–	–	(8.0)	(141.4)
Inflation swap	<b>0.5</b>	<b>0.9</b>	<b>1.1</b>	<b>0.7</b>	<b>0.2</b>	–	<b>3.4</b>
	<b>4.6</b>	<b>3.4</b>	<b>1.8</b>	<b>1.0</b>	<b>0.4</b>	(0.4)	<b>10.8</b>
<b>At 31 December 2012</b>							
<b>Non-derivative financial liabilities</b>							
Borrowings							
Bank loans and overdrafts	307.7	–	–	–	–	–	307.7
Senior notes	15.5	60.3	12.7	59.9	39.8	199.4	387.6
Other borrowings	1.0	0.5	0.1	–	–	–	1.6
	324.2	60.8	12.8	59.9	39.8	199.4	696.9
Trade and other payables							
Trade payables	104.8	0.2	0.1	–	–	–	105.1
Accruals	107.8	0.2	0.1	0.2	0.2	1.4	109.9
Contingent consideration	2.5	14.3	–	–	–	–	16.8
Other liabilities	36.8	0.5	1.2	0.7	0.7	1.9	41.8
	251.9	15.2	1.4	0.9	0.9	3.3	273.6
<b>Derivative liabilities</b>							
Interest rate swaps	4.3	1.4	1.0	0.8	0.5	0.5	8.5
Foreign exchange derivatives							
Gross cash outflows	120.2	25.4	15.4	–	–	–	161.0
Gross cash inflows	(117.9)	(24.2)	(14.2)	–	–	–	(156.3)
Inflation swap	0.5	0.6	0.7	0.8	0.5	0.2	3.3
	7.1	3.2	2.9	1.6	1.0	0.7	16.5

# Notes to the Group Financial Statements continued

## Credit risk

The Group's principal financial assets are bank balances, cash and trade and other receivables and there are no significant concentrations of credit risk.

The Group has a conservative policy towards the credit risk related to liquid funds and derivative financial instruments with balances currently spread across a range of reputable financial institutions, such as banks which have satisfactory credit ratings assigned by international credit rating agencies. The levels of credit risk are monitored through the Group's ongoing risk management processes, which include a regular review of the banks' credit ratings. Risk in this area is limited further by setting a maximum level for deposits with any one counterparty.

Concentrations of credit risk with respect to trade receivables are limited due to the Group's customer base being large and unrelated. Customers are typically large global companies or government agencies with long term trading relationships. The Group also has in place procedures that require appropriate credit checks on potential customers before sales are made. Existing customer accounts are monitored on an ongoing basis and appropriate action is taken where necessary to minimise any credit risk. The Directors therefore believe there is no further credit risk provision required in excess of normal provision for impaired receivables shown in note 17.

Group management monitor the ageing of receivables which are more than one month overdue and debtor days on a regular basis. At 31 December 2013, 8.2% (2012: 6.4%) of gross trade receivables were overdue by one month or more.

The maximum exposure to credit risk at 31 December 2013 is the fair value of each class of receivable as disclosed in note 17. Letters of credit are the only collateral held as security against trade receivables. These are obtained in a limited number of cases in accordance with good business practice and secure around £2.3m of receivables.

Bank term balances totalling £6.4m (2012: £7.5m) have been pledged against the residual value of leased assets as described in note 16.

In the UK and the USA, the Group has master netting arrangements in respect of bank balances. In the normal course of business, these bank accounts are settled on a net basis within each currency and as such are presented net in the Balance Sheet as shown in note 16. In the event of an automatic enforcement event, the bank balances are automatically set off against each other to achieve a net position.

Derivatives can also be offset by counterparties in the event of a default; net amounts that result on this basis are shown in note 16.

## Inflation risk

The Group's exposure to inflation is considered to be a general business risk which is mitigated through normal commercial activity.

The Group has one swap contract which was designed to manage the inherent inflation risk in a specific operational contract. The fair value of this swap contract is included in derivative financial instruments shown in note 23.

## Capital risk management

Group policy is to maintain a strong capital base, defined as total equity, excluding non-controlling interests, totalling £1,043.4m at 31 December 2013 (2012: £1,053.8m), so as to maintain stakeholder confidence and to sustain future development of the business. Within this overall policy, the Group seeks to maintain an appropriate finance structure through a mixture of debt and retained earnings. Funding needs are reviewed periodically and also each time a significant acquisition or business divestment is made. A number of factors are considered which include the net debt/EBITDA ratio, future funding needs (usually potential acquisitions) and proposed dividend levels. Group banking arrangements are also considered; these include financial covenants which are based on adjusted IFRS results as outlined on page 25. This policy has been reviewed by the Board on a regular basis during the year and, given the current economic climate, continues to be considered appropriate.

## 26. Share capital

£m	Number of shares	2013	2012
<b>Authorised</b>			
Ordinary Shares of par value 2.5 pence	1,479,200,000	<b>37.0</b>	37.0
6% second cumulative Preference Shares of £1	20,000	—	—
<b>Issued and fully paid</b>			
Ordinary Shares of par value 2.5 pence	1,154,527,625	<b>28.9</b>	28.9

As at 31 December 2013, 85,680,533 (2012: 87,699,405) Ordinary Shares were held in treasury including 9,728,809 (2012: 11,747,681) shares held in the Cobham Employee Benefit Trust. At 31 December 2013, the market value of treasury shares was £235.2m (2012: £193.6m), including shares with a market value of £26.7m (2012: £25.9m) held by the Cobham Employee Benefit Trust.

During the year ended 31 December 2013, treasury shares were used to satisfy awards and options under the Group's PSP, BCP, ESOS and ShareSave schemes. The net cost of treasury shares after receipts from option exercises is deducted from retained earnings and total equity.

Further details of the share capital of Cobham plc can be found in the Directors' Report on page 64.

## 27. Other reserves

£m	Note	Translation reserve	Hedge reserve	Share options reserve	Total other reserves
At 1 January 2012		65.1	(5.7)	24.4	83.8
Foreign exchange differences on translation of overseas operations		(19.2)	—	—	(19.2)
Reclassification of foreign exchange on divestment of overseas operation		(4.8)	—	—	(4.8)
Movements on cash flow hedges	23	0.4	(3.5)	—	(3.1)
Reclassification of fair value of cash flow hedges to income statement		—	7.2	—	7.2
Release of hedge reserve		—	2.8	—	2.8
Transfer of hedge reserve to retained earnings		—	(3.7)	—	(3.7)
Transfer of translation reserve on settlement of cash flow hedge contracts		0.3	(0.3)	—	—
Transfer of share options reserve on exercise		—	—	(2.8)	(2.8)
Share based payments recognised in reserves	28	—	—	6.8	6.8
Dividend equivalents paid on vesting of PSP and BCP awards		—	—	(0.1)	(0.1)
Tax effects		(0.1)	(3.1)	0.5	(2.7)
<b>At 1 January 2013</b>		<b>41.7</b>	<b>(6.3)</b>	<b>28.8</b>	<b>64.2</b>
Foreign exchange differences on translation of overseas operations		(11.1)	—	—	(11.1)
Movements on cash flow hedges	23	0.6	—	—	0.6
Reclassification of fair value of cash flow hedges to income statement		—	4.5	—	4.5
Release of hedge reserve		—	1.5	—	1.5
Transfer of translation reserve on settlement of cash flow hedge contracts		1.5	(1.5)	—	—
Transfer of share options reserve on exercise		—	—	(4.2)	(4.2)
Share based payments recognised in reserves	28	—	—	(1.7)	(1.7)
Tax effects		(0.5)	(0.7)	2.6	1.4
<b>At 31 December 2013</b>		<b>32.2</b>	<b>(2.5)</b>	<b>25.5</b>	<b>55.2</b>

The translation reserve comprises all foreign exchange differences arising on the results and financial position of subsidiaries whose functional currencies differ from the Group's reporting currency. Foreign exchange movements arising on interest rate swaps designated as cash flow hedges are also included here and, following the settlement of the financial instrument, any balances remaining are transferred to retained earnings.

# Notes to the Group Financial Statements continued

The hedge reserve reflects movements in fair values on cash flow hedging derivatives as detailed in notes 23 and 25.

The share options reserve includes the cost of share options as assessed under IFRS 2 together with deferred tax provided under IAS 12 relating to share based payments, where the calculated future tax benefit is in excess of the amount charged to date under IFRS 2. The appropriate proportion of the share options reserve is transferred to retained earnings following exercise.

## 28. Share based payments

The total amount included in the income statement arising from the Group's equity settled share based payment schemes is as follows:

£m	2013	2012
PSP	4.7	4.5
Other schemes	1.2	2.3
Release of amounts charged in previous years	(7.6)	—
	(1.7)	6.8

During the year ended 31 December 2013, £7.6m which has been charged to the Income Statement in previous years has been released, reflecting actual vesting experience of vested awards and a reassessment of the expected future vesting of awards which are unvested at the year-end, based on non-market related performance conditions.

The Group operates the following equity settled share based payment schemes:

The PSP scheme is offered to senior executives across the Group and allows for annual grants of conditional shares with vesting conditions based on the Group's financial performance, taking into account both market based conditions such as TSR growth and non-market based measures such as EPS growth or cash conversion respectively. The scheme includes buy-out awards granted in 2012 and 2013 to the Group's CEO and CFO.

Until 2012, share options were also awarded to senior executives under the ESOS scheme, with exercise conditional upon the Group's underlying EPS growth over a three year period. Awards have been made in 2013 to US employees under the 'time-only' section of the ESOS. This allows for options to be granted with 25% vesting on each annual anniversary, conditional only on continued employment within the Group.

The Bonus Co-investment Plan (BCP) is offered to a small number of senior executives and provides matching shares where bonus awards are invested in shares.

Finally the Group operates a ShareSave scheme which is open to all UK employees. The fair values of ESOS and ShareSave awards are significantly lower than for PSP and BCP awards due to the effect of the exercise price which is set based upon the market value of the Group's Ordinary Shares around the date of grant.

Further details of all the schemes can be found in the Directors' Remuneration Report on pages 50 and 51.

The number of options outstanding at 31 December are as follows:

Number of awards (thousands of shares)	2013	2012
PSP	8,544	7,794
ESOS	10,161	17,698
BCP	190	350
ShareSave	5,447	6,498
At 31 December	24,342	32,340

Details of movements in the awards under the PSP scheme are as follows:

<b>Number of awards (thousands of shares)</b>	<b>2013</b>	<b>2012</b>
At 1 January	<b>7,794</b>	6,838
Awards granted	<b>3,531</b>	3,076
Awards forfeited or cancelled	<b>(2,315)</b>	(1,629)
Exercised	<b>(466)</b>	(490)
Expired	—	(1)
<b>At 31 December</b>	<b>8,544</b>	7,794
Weighted average remaining contractual life of PSP awards outstanding	<b>1.38 years</b>	1.28 years
Number of PSP awards exercisable at 31 December (thousands)	<b>669</b>	212
Effective date of grant for awards made in the year	<b>4 April, 19 August</b>	26 March, 14 September
Average fair value at date of grant	<b>£2.223</b>	£1.735

The average fair values above were calculated using the Black-Scholes option pricing model modified by a Monte Carlo simulation to determine the likely impact of market related performance conditions. The inputs into the models were as follows:

	<b>2013</b>	<b>2012</b>
Weighted average share price	<b>£2.472</b>	£2.250
Weighted average exercise price	<b>nil</b>	nil
Expected volatility	<b>26%</b>	31%
Expected life	<b>2.96 years</b>	2.79 years
Expected employee cancellation rate	<b>1.8%</b>	2.2%
Risk free rate	<b>0.3%</b>	1.3%

Expected volatility was determined through the assessment of the historical volatility over a period consistent with the expected life of the award. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability and behavioural considerations. The expected employee cancellation rate is based on an assessment of historic rates of voluntary cancellations of contracts by employees. Most participants of the PSP scheme receive the benefit of dividend payments and therefore dividend yields are not taken into consideration in the valuation model.

# Notes to the Group Financial Statements continued

## 29. Business combinations

### Businesses acquired during the year

The purchase of the entire share capital of Avenue 64 Limited, the parent company of the Axell Wireless group (Axell), was completed on 9 May 2013. On a debt and cash free basis, total consideration was £85m including conditional cash consideration of up to £25m payable during 2014 and 2015, contingent on future performance.

Axell is a leading global provider of Distributed Antenna Systems and wireless solutions for the public safety and cellular markets, with a specific focus on communication systems for buildings and critical infrastructure applications. Axell brings technology that is complementary to the Group's existing Antenna Systems and Tactical Communications and Surveillance businesses and its acquisition is in line with the Group's strategic objectives. The company has approximately 250 employees worldwide and is headquartered in Chesham, UK. It is reported through the Antenna Systems Strategic Business Unit, within the Aerospace and Security Division.

On 15 July 2013 it was announced that an agreement was reached to acquire the 50% shareholding that the Group did not already own in FB Heliservices Limited, FB Leasing Limited and FBS Limited (together FBH), from its long standing joint venture partner, Bristow Helicopters Limited (Bristow). The transaction comprised cash consideration of £74m payable on completion, together with the assumption of Bristow's share of FBH's net debt. FBH specialises in defence helicopter training in the UK and elsewhere, including a contract with the Ministry of Defence to train helicopter crews for all branches of the armed forces, as well as the provision of search and rescue, logistics and emergency medical services for government customers globally.

In accordance with IFRS 3, the revaluation gains on previously held equity interests in FBH that arise on gaining full control of the company have been recognised in the income statement. This business is now part of Aviation Services.

### Fair value information

Components of the fair value of the business combinations during the year are as follows:

£m	Axell	FBH	Total
Cash consideration	55.5	74.2	129.7
Revaluation gains arising on equity interests on transfer of control	–	62.1	62.1
Investment in joint venture on date of transfer	–	12.2	12.2
Contingent consideration	22.1	–	22.1
Total fair value at date control achieved	77.6	148.5	226.1

Revaluation gains arising on equity interests on transfer of control are excluded from underlying profits as shown in note 3. Contingent consideration has been provided at fair value which is considered to be the discounted maximum payable under the agreement. Further details can be found in note 20.

A summary of the fair values of the net assets acquired are as follows:

£m	Axell	FBH	Total
Non-current assets	48.0	161.5	209.5
Current assets	22.5	23.8	46.3
Current liabilities	(15.9)	(72.2)	(88.1)
Non-current liabilities	(12.0)	(16.5)	(28.5)
Net assets acquired	42.6	96.6	139.2
Goodwill	35.0	51.9	86.9
Total value of business acquired	77.6	148.5	226.1

The fair values of net assets acquired in respect of FBH are provisional and subject to potential adjustment.

All intangible assets were recognised at their respective fair values. The residual excess of the total cost over the fair value of the net assets acquired is recognised as goodwill in the financial statements. Goodwill represents the premium paid in anticipation of future economic benefits from assets that are not capable of being separately identified and separately recognised, such as the value of the workforce. Goodwill is not anticipated to be deductible for tax purposes.

The fair values of acquired receivables included in current assets in the table above are £6.0m for Axell and £12.2m for FBH. These relate to trade and other receivables and are considered to be recoverable in full. Current liabilities of FBH on acquisition included £43.2m payable to Cobham.

### **Results of business combinations**

Third party revenue of Axell and FBH, since acquisition, was £34.9m and £42.3m respectively. The result after tax since the date of acquisition was £6.0m loss and £3.7m loss. These include the impacts of amortisation of the intangible assets which are recognised as a result of the business combination and writing off the pre-acquisition profit element of inventory written up on acquisition. Operating profit was £6.2m for Axell and £8.5m for FBH.

If these business combinations had taken effect on 1 January 2013, it is estimated that Group total revenues would have been £1,842.7m and profit after tax £108.0m. This information is not necessarily indicative of the results had the operations been acquired at the start of the period, nor of future results of the combined operations.

The net cash flows resulting from business combinations are as follows:

£m	Total
Cash consideration paid for the business combinations completed in the year	130.1
Net debt acquired with the business combinations completed in the year	(4.1)
	126.0

Costs of £1.7m were incurred in relation to business combinations. These costs are recognised within administrative expenses in the Consolidated Income Statement and included within other M&A related costs excluded from underlying profit as shown in note 3.

### **30. Operating lease arrangements**

At the balance sheet date the Group had outstanding commitments for minimum lease payments due under non-cancellable operating leases as follows:

£m	2013	2012
Within one year	<b>26.0</b>	26.1
Between one and two years	<b>23.4</b>	23.1
Between two and three years	<b>21.0</b>	21.6
Between three and four years	<b>18.8</b>	18.7
Between four and five years	<b>16.3</b>	17.3
After five years	<b>63.4</b>	88.0
	<b>168.9</b>	194.8

Operating lease payments during the year totalled £30.4m (2012: £31.1m) including rental costs of £7.1m (2012: £8.4m) relating to operational aircraft used in its service businesses; the remainder primarily relates to the rental of office and operating facilities.

# Notes to the Group Financial Statements continued

## 31. Contingent liabilities and commitments

At 31 December 2013, the Company and the Group had contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the ordinary course of business. Where it is expected that a material liability will arise in respect of these matters, appropriate provision is made within the Group Consolidated Financial Statements.

The Company and various of its subsidiaries are, from time to time, parties to various legal proceedings and claims. Management do not anticipate that the outcome of these, either individually or in aggregate, would have a material adverse effect upon the Group's financial position as at 31 December 2013.

As notified in prior years, the Group has previously identified one, more significant, contractual breach dating back some years. The contract was in respect of goods provided into a geographic market which represents only a small amount of revenue for the Group. The circumstances surrounding this remain under review and neither the outcome nor the timing of resolution can be estimated. No further information is disclosed as it could be prejudicial.

The nature of much of the contracting work done by the Group means that there are reasonably frequent contractual issues, variations and renegotiations that arise in the ordinary course of business, whose resolution is uncertain and could materially impact the Group's future reported earnings. In particular, on fixed price development contracts, where there is currently a high level of activity, costs incurred and anticipated can significantly exceed amounts estimated at inception as a result of material enhancements to the specifications originally agreed under the contracts. Judgement is therefore required as regards the outcome of negotiations and the amounts recoverable under these contracts. The Directors take account of the advice of experts in making these judgements and believe that the outcome of negotiations will result in an appropriate recovery of costs.

On 24 February 2014 the Group voluntarily contacted the United States Department of Justice (DoJ) to inform it that Cobham had undertaken an initial internal investigation into potentially irregular sales practices concerning sales to Asia of certain commercial, non-classified products manufactured by TracStar Systems Inc. (TracStar). TracStar is based in Orlando, Florida and is part of the group's SATCOM business. The business manufactures a range of inertial stabilisation and satellite tracking systems used by government and commercial customers globally for land based applications. Its total worldwide revenue in 2013 was under £15m, representing less than 1% of Group revenue. Cobham will continue to co-operate with the DoJ in relation to this matter however, the circumstances are under review and neither the outcome nor the timescale for resolution can be estimated at present.

At 31 December 2013, the Group had commitments for the acquisition of property, plant and equipment of £13.6m (2012: £17.2m).

## 32. Related party transactions

£m	2013	2012
Transactions between Group entities and joint ventures and associates during the year		
Sales of goods	0.4	0.3
Purchases of goods	0.3	0.4
Dividends received from joint ventures	(3.7)	(7.5)
Loan advanced to joint venture	—	40.0
Loan repayments and interest received from joint ventures	(3.0)	(3.1)
Amounts owed by joint ventures at the year-end	—	45.4

Sales of goods to related parties were made at the Group's usual list prices for sales to non-related parties.

The amounts owed are unsecured, will be settled in cash and are included in other receivables in note 17. No guarantees have been given to, or received from, related parties. No expense has been recognised in the period for bad or doubtful debts in respect of the amounts owed by related parties.

### Compensation of key management personnel

Details of the compensation of key management personnel can be found in note 5.

The Directors of Cobham plc had no material transactions with the Company during the year, other than as a result of service agreements. Details of Directors' remuneration are disclosed in the Directors' Remuneration Report on pages 48 to 63.

**33. Events after the balance sheet date**

In February 2014, a loan agreement was signed for AUS\$90m expiring in October 2018.

**34. Subsidiaries**

All subsidiary undertakings have been included in the Group consolidation. The undertakings held at 31 December 2013 which, in the opinion of the Directors, principally affected the results for the year or the net assets of the Group were:

<b>Operating segment</b>	<b>Strategic Business Unit and principal activities</b>	<b>Name of undertaking</b>	<b>Place of incorporation (or registration) and operation</b>
<b>Cobham Aerospace and Security</b>			
<b>Cobham Aerospace Communications</b>			
	Design and manufacture of navigation, communication and airborne networking products and systems for commercial, business, homeland security and military aircraft.	Air Précision SAS Chelton Avionics, Inc Chelton Telecom and Microwave SAS TEAM SA	France USA France France
<b>Cobham Antenna Systems</b>			
	Design and manufacture of communication systems and navigation antennas that enable people and systems to communicate on land, in the air and at sea.	Axell Wireless Limited Chelton Limited Chelton, Inc Cobham Advanced Composites Limited Cobham Composite Products Inc Cobham CTS Limited Continental Microwave & Tool Co, Inc Trivec-Avant Corporation	England England USA England USA England USA USA
<b>Cobham SATCOM</b>			
	Development, manufacture, sales and support of satellite and radio communication equipment and earth stations for maritime based, land based and aeronautical applications.	Omnipless Manufacturing (Pty) Limited Sea Tel, Inc Thrane & Thrane A/S	South Africa USA Denmark
<b>Cobham Tactical Communications and Surveillance</b>			
	Provision of specialist communications, security and surveillance products including integrated systems and solutions.	Cobham Defence Communications Limited Cobham TCS Limited DTC Communications, Inc	England England USA
<b>Cobham Defence Systems</b>			
<b>Cobham Defence Electronics</b>			
	Design and manufacture of antenna systems and radomes, ground data link terminals, active microwave components, assemblies and subsystems for the aerospace and defence industries.	Cobham Electronic Systems Inc REMEC Defense & Space, Inc Sensor & Antenna Systems, Lansdale, Inc	USA USA USA

# Notes to the Group Financial Statements continued

<b>Operating segment</b>	<b>Strategic Business Unit and principal activities</b>	<b>Name of undertaking</b>	<b>Place of incorporation (or registration) and operation</b>
<b>Cobham Mission Systems</b>			
	<b>Cobham Life Support</b> Life support, safety and personal survival equipment systems including oxygen systems for aviators and astronauts, crew restraints and flotation gear along with fuel tank inerting capabilities.	Carleton Life Support Systems, Inc * Carleton Technologies, Inc *	USA USA
	<b>Cobham Mission Equipment</b> Design, development and manufacture of critical technology for air-to-air refuelling, weapons carriage and release systems and unmanned explosive ordnance robot applications for both military and homeland security markets.	Carleton Life Support Systems, Inc * Carleton Technologies, Inc * Flight Refuelling Limited ** Telerob Gesellschaft für Fernhantierungstechnik mbH	USA USA England Germany
<b>Cobham Aviation Services</b>			
	<b>Cobham Aviation Services</b> Delivers specialist aviation services for commercial, government and defence customers worldwide through airborne special mission operations, outsourced commercial aviation, military training, aircraft engineering, flight inspection and air traffic services.	FR Aviation Limited FB Heliservices Limited Jet Systems Pty Limited National Jet Express Pty Limited National Jet Systems Pty Limited Surveillance Australia Pty Limited	England England Australia Australia Australia Australia

\* Carleton Life Support Systems, Inc and Carleton Technologies, Inc both operate across the Cobham Life Support and Cobham Mission Equipment SBUs.

\*\* Issued shares in Flight Refuelling Limited are held by Cobham plc. Otherwise shares are held by, or by a nominee for, a subsidiary of Cobham plc.

The Group owns 100% of the share capital of all subsidiaries with the exception of TEAM SA (98.7% owned).

A full list of subsidiary companies is annexed to the Company's annual return to the Registrar of Companies.

# Independent Auditors' Report to the Members of Cobham plc

Parent Company Financial Statements

## Report on the Parent Company Financial Statements

### Our opinion

In our opinion the Parent Company Financial Statements, defined below:

- give a true and fair view of the state of the Parent Company's affairs as at 31 December 2013;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

This opinion is to be read in the context of what we say in the remainder of this report.

### What we have audited

The Parent Company Financial Statements, which are prepared by Cobham plc, comprise:

- the Parent Company Balance Sheet as at 31 December 2013;
- the Parent Company Reconciliation of Movements in Shareholders' Funds for the year then ended; and
- the Notes to the Parent Company Financial Statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in their preparation comprises applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

In applying the financial reporting framework, the Directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Certain disclosures required by the financial reporting framework have been presented elsewhere in the Annual Report and Accounts, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

### What an audit of financial statements involves

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & Ireland)). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Parent Company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited Parent Company Financial Statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit.

If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### Opinions on matters prescribed by the Companies Act 2006

In our opinion:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the Parent Company Financial Statements are prepared is consistent with the Parent Company Financial Statements.
- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

### Other matters on which we are required to report by exception

#### Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company Financial Statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

### Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law have not been made.

We have no exceptions to report arising from this responsibility.

### Other information in the Annual Report and Accounts

Under ISAs (UK & Ireland), we are required to report to you if, in our opinion, information in the Annual Report and Accounts is:

- materially inconsistent with the information in the audited Parent Company Financial Statements; or
- apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Parent Company acquired in the course of performing our audit; or
- is otherwise misleading.

We have no exceptions to report arising from this responsibility.

# Independent Auditors' Report continued

## **Responsibilities for the financial statements and the audit**

### **Our responsibilities and those of the Directors**

As explained more fully in the Statement of Directors' Responsibilities on page 67, the Directors are responsible for the preparation of the Parent Company Financial Statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the Parent Company Financial Statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### **Other matter**

We have reported separately on the Group Financial Statements of Cobham plc for the year ended 31 December 2013.



**Stuart Watson**

(Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London  
5 March 2014

# Parent Company Balance Sheet (under UK GAAP)

As at 31 December 2013

Parent Company Financial Statements

£m	Note	2013	2012
<b>Fixed assets</b>			
Intangible assets	6	–	0.2
Tangible assets	7	<b>0.1</b>	0.2
Investments in Group and other undertakings	5	<b>776.8</b>	779.1
Other investments	5	<b>6.1</b>	–
Financial assets: derivative financial instruments	12	<b>18.1</b>	14.2
		<b>801.1</b>	793.7
<b>Current assets</b>			
Financial assets: derivative financial instruments	12	<b>8.3</b>	5.8
Debtors	8	<b>1,118.9</b>	1,107.2
Cash at bank and in hand		<b>74.1</b>	71
		<b>1,201.3</b>	1,120.1
Creditors: amounts falling due within one year	9	<b>(651.7)</b>	(567.3)
<b>Net current assets</b>		<b>549.6</b>	552.8
<b>Total assets less current liabilities</b>		<b>1,350.7</b>	1,346.5
Creditors: amounts falling due after more than one year	10	<b>(723.7)</b>	(731.3)
Provisions for liabilities	11	<b>(6.6)</b>	(6.6)
<b>Net assets</b>		<b>620.4</b>	608.6
<b>Capital and reserves</b>			
Called up share capital	13	<b>28.9</b>	28.9
Share premium account	14	<b>126.6</b>	126.6
Special reserve	14	<b>43.6</b>	43.6
Other reserves	14	<b>14.8</b>	16.9
Profit and loss account	14	<b>406.5</b>	392.6
<b>Equity shareholders' funds</b>		<b>620.4</b>	608.6

The financial statements on pages 127 to 135 were approved by a duly appointed and authorised committee of the Board on 5 March 2014 and signed on its behalf by:

R Murphy  
Directors

S Nicholls

# Reconciliation of Movements in Shareholders' Funds

For the year ended 31 December 2013

£m	Note	2013	2012
<b>Profit for the financial year</b>		<b>108.1</b>	164.3
Dividends	2	(96.6)	(92.5)
Retained profit for the financial year		11.5	71.8
Treasury shares	14	(1.8)	(18.7)
Movements in hedge reserve	14	3.8	(0.6)
Reclassification of hedge reserve	14	—	3.8
Share based payments	14	(1.7)	6.8
Dividend equivalents paid on vesting of PSP and BCP awards	14	—	(0.1)
<b>Net addition to shareholders' funds</b>		<b>11.8</b>	63.0
Shareholders' funds at 1 January		<b>608.6</b>	545.6
<b>Shareholders' funds at 31 December</b>		<b>620.4</b>	608.6

## Profit for the financial year

In accordance with the concession granted under Section 408 of the Companies Act 2006, the profit and loss account of Cobham plc has not been separately presented in these financial statements.

# Notes to the Parent Company Financial Statements

Parent Company Financial Statements

## 1. Parent Company accounting policies

### Accounting convention

These financial statements have been prepared on the going concern basis, under the historical cost convention as modified by the revaluation of derivative contracts which are held at fair value, and in accordance with the Companies Act 2006 and applicable accounting standards in the United Kingdom (UK GAAP).

The principal accounting policies, which have been consistently applied, are as set out below.

### Dividends

Dividends payable are recognised as a liability in the period in which they are fully authorised. Dividend income is recognised when the shareholders' right to receive payment has been established.

### Pensions

The Company operates and contributes to multi-employer defined benefit pension schemes. Contributions and pension costs are apportioned across the schemes as a whole and assessed in accordance with the advice of qualified actuaries. The schemes are closed to new members and have a high proportion of deferred and pensioner members from businesses that no longer participate in the schemes. The Company is therefore not able to identify its share of underlying assets and liabilities of the schemes on a reasonable and consistent basis and in accordance with the multi-employer exemption contained in FRS 17, Retirement Benefits, the schemes have been accounted for as if they were defined contribution schemes. The charge to the profit and loss account therefore reflects payments for the year.

Contributions to defined contribution schemes are charged to the profit and loss account in the period the contributions are payable.

The Company also makes contributions for certain employees to individual personal pension and stakeholder schemes. Contributions are charged to the profit and loss account in the year to which they relate.

### Deferred taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date.

A net deferred tax asset is recognised as recoverable when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of underlying timing differences can be deducted.

Deferred tax is measured at the tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax has not been discounted.

### Intangible assets

Intangible assets, comprising software, are stated at cost less accumulated amortisation and impairment losses. They are

amortised on a straight-line basis over their estimated useful lives, which range from three to five years.

### Tangible fixed assets

Fixed assets are initially recognised at cost and depreciated on a straight-line basis to their estimated residual values over their estimated useful lives, which range from three to six years.

### Investments in Group and other undertakings

Investments in subsidiary undertakings are stated at cost less any provision for impairment in value and include the fair value at the date of grant of share options awarded to employees of subsidiary undertakings, net of amounts recovered as management charges.

Other investments are stated at cost less any provision for impairment in value.

### Provisions

A provision is recognised when the Company has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required of an amount that can be reliably estimated.

### Share capital

Ordinary share capital is classified as equity. Financial liabilities and equity instruments are classified according to the substance of the contractual agreements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities.

Preference share capital is classified as a liability if it is redeemable on a specific date or at the option of the preference shareholders or if dividend payments are not discretionary. Dividends on preference share capital classified as liabilities are recognised in the profit and loss account as interest expense.

### Treasury shares

When ordinary share capital recognised as equity is acquired by the Company, the shares are held as treasury shares. The consideration paid, including commissions and taxes, is deducted from retained earnings and total shareholders' equity.

### Foreign currencies

The functional currency of the Company is sterling. Transactions in currencies other than the local currency are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in non-functional currencies are retranslated at the exchange rate ruling at the balance sheet date. Investments in subsidiary undertakings denominated in foreign currencies which are financed by foreign currency borrowings are translated at the year-end exchange rate. Investments denominated in foreign currencies not financed by foreign currency borrowings are translated at the rate of exchange ruling at the date of the original transaction.

All exchange differences arising are taken to the profit and loss account.

In order to manage the Company's exposure to certain foreign exchange risks, the Company enters into forward contracts and options which are accounted for as derivative financial instruments.

# Notes to the Parent Company Financial Statements continued

## Derivative financial instruments and hedge accounting

The Company's activities expose it to the financial risks of changes in foreign currency exchange rates and interest rates. The Company uses foreign exchange contracts and interest rate swap contracts to reduce these exposures and does not use derivative financial instruments for speculative purposes. Other derivative financial instruments may be used from time to time to hedge other exposures such as inflation risks.

The Company has documented its risk management objectives and strategy for undertaking various hedge transactions and utilises hedge accounting principles in relation to interest rate swaps. These are designated as cash flow hedges which mitigate the Company's exposure to changes in interest rates arising on floating rate debt.

Foreign exchange contracts entered into to mitigate foreign exchange impacts of trading in non-functional currencies and inflation swaps entered into to mitigate inflation risks are not accounted for using hedge accounting.

Derivative financial instruments are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged.

Where hedge accounting is applied, the relationship between hedging instruments and hedged items is documented at the inception of the transaction. The Company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives used in hedging transactions are highly effective in offsetting changes in cash flows (or fair values if appropriate) of hedged items.

Where interest rate swaps are designated and qualify as cash flow hedges, the effective portion of changes in fair values of derivatives that are designated and qualify as cash flow hedges are recognised in reserves. The gain or loss relating to the ineffective portion is recognised immediately in the profit and loss account. Amounts accumulated in reserves are recycled to the profit and loss account in the periods when the hedged item affects profit or loss.

When a cash flow hedging derivative expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any

cumulative gain or loss existing in reserves at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the profit and loss account. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in reserves is immediately transferred to the profit and loss account in that period.

The fair value of a hedging derivative is classified as a current asset or liability except when the remaining maturity of the hedged item is more than 12 months.

Where hedge accounting is not applied, the movements in fair value of the derivative instruments are included in the profit and loss account. The fair value of such derivatives is classified as a current or non-current asset or liability dependent upon the maturity of the contracts.

## Other financial instruments

Amounts receivable from and owed to subsidiaries are recognised at amortised cost using the effective interest method and are reduced by appropriate allowances for estimated irrecoverable amounts.

Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs and subsequently held at amortised cost. Interest is accounted for on an accruals basis in the profit and loss account using the effective interest rate method and is added to the carrying amount of the instrument to the extent that the expenses are not settled in the period in which they arise.

## Share based payments

For grants made to employees of Cobham plc under the Group's share based payment schemes, amounts which reflect the fair value of options awarded as at the time of grant are charged to the profit and loss account over the vesting period. The vesting estimates are reviewed and updated at each balance sheet date; this includes progress against non-market related performance conditions.

The fair value of options awarded to employees of subsidiary undertakings, net of amounts recovered as management charges, is recognised as a capital contribution and recorded in investments.

The valuation of the options utilises a methodology based on the Black-Scholes model, modified where required to allow for the impact of market related performance criteria and taking into account all non-vesting conditions.

## 2. Dividends

£m	2013	2012
Final dividend of 6.4 pence per share for 2012 (2011: 6.2 pence)	<b>68.5</b>	66.7
Interim dividend of 2.64 pence per share for 2013 (2012: 2.4 pence)	<b>28.1</b>	25.8
Total dividend authorised and paid during the year	<b>96.6</b>	92.5

In addition to the above, the Directors are proposing a final dividend in respect of the financial year ended 31 December 2013 of 7.04 pence per share which will absorb an estimated £75.2m of shareholders' funds. This dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. If authorised, it will be paid on 30 May 2014 to shareholders who are on the register of members as at 2 May 2014. The total dividend in respect of the financial year ended 31 December 2013 will therefore be 9.68 pence per share (2012: 8.8 pence). The total amount payable in respect of 2013 will be £103.3m.

### 3. Directors' emoluments and pension costs

Disclosures in respect of Directors' emoluments can be found in the Directors' Remuneration Report on pages 48 to 63 of the Annual Report and Accounts.

#### Defined benefit pension schemes

The Company operates and participates in the Cobham Pension Plan (CPP) and the Cobham Executive Pension Plan (CEPP). The pension schemes are of the defined benefit type and assets are held in separate trustee administered funds. The funds are valued every three years by a professionally qualified independent actuary and the rates of contribution payable are determined by the actuary. The latest effective dates of the actuarial assessment of the CPP and CEPP were 1 April 2012 and 1 April 2013 respectively. The assessments were updated to 31 December 2013, at which date the total net liabilities of the schemes were assessed to be £81.7m. The Directors will continue to monitor the pension deficits and take advice from independent actuaries as appropriate.

The schemes have been accounted for as if they were defined contribution schemes and the charge to the profit and loss account therefore reflects payments for the year.

Contributions to the Group schemes for 2013 were £0.3m (2012: £0.3m) of normal funding and £9.4m (2012: £9.3m) of deficit funding. No contributions were outstanding at the end of 2013 or 2012.

#### Defined contribution pension schemes

The Company also operates and participates in the Cobham plc money purchase pension arrangements. The assets of the schemes are held separately from those of the Company in independently administered funds. The pension cost charged represents contributions payable by the Company to the funds and amounted to £1.0m (2012: £0.7m). No contributions were outstanding at the end of 2013 or 2012.

### 4. Share based payments

Employees of Cobham plc participate in the following equity settled share based payment schemes which are operated by the Group for certain senior executives:

- The Cobham Performance Share Plan (PSP).
- The Cobham Executive Share Option Scheme (ESOS).
- The Cobham Bonus Co-investment Plan (BCP).

Employees also participate in the Cobham Savings Related Share Option Scheme (ShareSave) operated by the Group, which is open to all UK employees.

The Company recognised a total credit of £2.2m (2012: £2.9m expense) related to equity settled share based payment transactions during the year (excluding national insurance). This includes charges of £2.3m less a reversal of £4.5m of amounts charged in previous years due to the reassessment of assumptions during the year. As shown in note 5, investments in Group and other undertakings have been adjusted by £2.3m to reflect the value of options granted to employees of the Company's subsidiaries, less amounts recharged during the year.

At 31 December, the following awards were outstanding under each of the schemes:

Number of awards (thousands of shares)	2013	2012
PSP	3,821	4,265
ESOS	817	5,467
BCP	111	258
ShareSave	269	314
	5,018	10,304

Further details of these schemes can be found in the Directors' Remuneration Report on pages 50 and 51 and in note 28 to the Group Financial Statements on pages 118 and 119.

# Notes to the Parent Company Financial Statements continued

## 5. Investments in Group and other undertakings

£m	Shares	Options	Total
Cost and net book amount			
At 1 January 2013	764.7	14.4	779.1
Options granted to employees of Group undertakings net of recoveries	—	(2.3)	(2.3)
<b>At 31 December 2013</b>	<b>764.7</b>	<b>12.1</b>	<b>776.8</b>

In the opinion of the Directors the value of investments in subsidiary undertakings is not less than the aggregate amount at which they are shown above.

A list of significant subsidiaries is provided in note 34 to the Group Financial Statements. The market capitalisation of the Group as a whole is given in the Group Financial Record on page 136.

The Company has minority shareholdings in three companies in connection with the FSTA project and has issued loan notes during the year which are included in debtors in note 8. The total amount invested is £6.1m (2012: £44,000) and this is held as a trade investment.

## 6. Intangible assets

£m	Software
Cost	
At 1 January and 31 December 2013	0.8
Accumulated amortisation	
At 1 January 2013	0.6
Charge for the year	0.2
<b>At 31 December 2013</b>	<b>0.8</b>
Net book amount	
<b>At 31 December 2013</b>	<b>—</b>
At 31 December 2012	0.2

## 7. Tangible fixed assets

£m	Plant, machinery, fixtures and fittings
Cost	
At 1 January 2013	1.0
Disposals	(0.3)
<b>At 31 December 2013</b>	<b>0.7</b>
Accumulated depreciation	
At 1 January 2013	0.8
Charge for the year	0.1
Disposals	(0.3)
<b>At 31 December 2013</b>	<b>0.6</b>
Net book amount	
<b>At 31 December 2013</b>	<b>0.1</b>
At 31 December 2012	0.2

## 8. Debtors

£m	2013	2012
Amounts owed by Group undertakings	1,093.5	1,089.6
Corporation tax receivable	–	4.4
Deferred tax	2.8	5.4
Loan notes	18.3	–
Prepayments and accrued income	4.3	7.8
	1,118.9	1,107.2

Amounts owed by Group undertakings, excluding trading balances, are unsecured, interest bearing and repayable on demand.

Loan notes were issued during the year in connection with the FSTA project. These accrue interest at LIBOR plus margin and are due for repayment in 2035.

The net deferred tax asset can be analysed as follows:

£m	2013	2012
Derivative financial instruments	1.3	2.2
Share based payments	1.0	1.9
Other timing differences	0.5	1.3
	2.8	5.4

Movements in the net deferred tax asset are as follows:

£m	2013
At 1 January 2013	5.4
Charge to reserves	(0.7)
Charge to profit and loss account	(1.9)
<b>At 31 December 2013</b>	<b>2.8</b>

The deferred tax asset is considered recoverable on the basis that sufficient taxable profits will be available to utilise any tax losses that may arise.

## 9. Creditors: amounts falling due within one year

£m	Note	2013	2012
Bank overdrafts		143.2	116.6
Bank loans		296.4	292.3
Senior notes		46.2	–
Total borrowings		485.8	408.9
Trade creditors		1.9	3.2
Amounts owed to Group undertakings		125.8	115.5
Derivative financial instruments	12	8.8	10.0
Corporation tax payable		7.4	–
Other tax and social security		1.9	1.3
Accruals and deferred income		20.1	28.4
		651.7	567.3

Details of the Company's principal borrowing facilities are disclosed in note 19 to the Group Financial Statements.

Interest is charged on amounts owed to Group undertakings at rates varying between 0.4% and 9.0%. These amounts are unsecured and are repayable on demand.

# Notes to the Parent Company Financial Statements continued

## 10. Creditors: amounts falling due after more than one year

£m	Note	2013	2012
Bank loans		<b>45.3</b>	—
Senior notes		<b>264.1</b>	316.2
Amounts owed to Group undertakings		<b>403.5</b>	403.5
Derivative financial instruments	12	<b>10.8</b>	11.6
		<b>723.7</b>	731.3

The bank loan due after more than one year is due for repayment by December 2016 at the latest. Senior notes falling due after more than one year mature as follows:

£m	2013	2012
Between one and two years	—	47.1
Between two and five years	<b>142.5</b>	80.6
After five years, maturing in 2019 and 2020	<b>121.6</b>	188.5
	<b>264.1</b>	316.2

Amounts owed to Group undertakings consist of frozen loans which are unsecured, interest free and not repayable within one year.

## 11. Provisions for liabilities

Other provisions of £6.6m (2012: £6.6m) relate to longer term warranties given on divestments completed in 2005. All amounts have been determined based on the Directors' current estimates of likely outcomes and the timing of any claims is uncertain.

## 12. Derivative financial instruments

The fair values of derivative financial instruments are as follows:

£m	Interest rate swaps – cash flow hedges	Foreign exchange derivatives	Inflation swap	Total
Fixed assets	—	<b>15.2</b>	<b>2.9</b>	<b>18.1</b>
Current assets	—	<b>7.8</b>	<b>0.5</b>	<b>8.3</b>
Creditors: amounts falling due within one year	(0.5)	(7.8)	(0.5)	(8.8)
Creditors: amounts falling due after more than one year	(2.7)	(5.2)	(2.9)	(10.8)
<b>At 31 December 2013</b>	<b>(3.2)</b>	<b>10.0</b>	—	<b>6.8</b>
Fixed assets	—	11.4	2.8	14.2
Current assets	—	5.3	0.5	5.8
Creditors: amounts falling due within one year	(3.5)	(6.0)	(0.5)	(10.0)
Creditors: amounts falling due after more than one year	(4.8)	(4.0)	(2.8)	(11.6)
<b>At 31 December 2012</b>	<b>(8.3)</b>	<b>6.7</b>	—	<b>(1.6)</b>

## 13. Called up share capital

£m	2013	2012
<b>Allotted, issued and fully paid</b>		
Equity		
1,154,527,625 (2012: 1,154,527,625) 2.5 pence Ordinary Shares	<b>28.9</b>	28.9
<b>Non-equity</b>		
19,700 (2012: 19,700) 6% second cumulative Preference Shares of £1	—	—

As at 31 December 2013, 85,680,533 (2012: 87,699,405) Ordinary Shares were held in treasury. This includes 9,728,809 (2012: 11,747,681) shares held in the Cobham Employee Benefit Trust. At 31 December 2013, the market value of treasury shares was £235.2m (2012: £193.6m), including shares with a market value of £26.7m (2012: £25.9m) held by the Cobham Employee Benefit Trust.

The Preference Shares which have been issued are classified as borrowings with a value of £19,700. Further details of the share capital of Cobham plc can be found in the Directors' Report on page 64.

#### 14. Reserves

£m	Share premium account	Special reserve	Other reserves		Profit and loss account
			Hedge reserve	Share options reserve	
At 1 January 2013	<b>126.6</b>	<b>43.6</b>	(6.3)	23.2	<b>392.6</b>
Profit for the financial year	—	—	—	—	<b>108.1</b>
Dividends	—	—	—	—	<b>(96.6)</b>
Purchase of treasury shares	—	—	—	—	<b>(1.8)</b>
Reclassifications to profit and loss account	—	—	4.5	—	—
Tax effect of hedge reserve movements	—	—	(0.7)	—	—
Share based payments recognised in reserves	—	—	—	(1.7)	—
Transfer of share options reserve on exercise	—	—	—	(4.2)	4.2
<b>At 31 December 2013</b>	<b>126.6</b>	<b>43.6</b>	<b>(2.5)</b>	<b>17.3</b>	<b>406.5</b>

The profit and loss account includes the purchase of Ordinary Shares by the Cobham Employee Benefit Trust in connection with the PSP, BCP, ESOS and ShareSave plans described in note 4, and the allocation of shares upon vesting of share awards and the exercise of options. Unallocated shares are held as treasury shares as described in note 13. During the year, 5,847,422 (2012: 12,598,162) shares were purchased and 7,866,294 (2012: 4,878,372) shares were allocated to employees. £15.3m (2012: £26.3m) was paid for these shares during the year and £13.5m (2012: £7.5m) was received following the exercise of share options.

The special reserve was created in 1996, with the sanction of the High Court, against which goodwill arising on subsequent acquisitions may be charged.

The share options reserve relates to provisions made in accordance with FRS 20 for shares allocated to the Company's employees under the Group's share option schemes. Where share options which gave rise to charges under FRS 20 have been exercised, the appropriate proportion of the share options reserve is transferred to the profit and loss account in equity.

The audit fee in respect of the Parent Company Financial Statements was £45,000 (2012: £44,000).

#### 15. Contingent liabilities and commitments

The Company has contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the ordinary course of business entered into for, or on behalf of, certain Group undertakings.

As the conditions of the above guarantees are currently being met, no obligating event is foreseeable and therefore no provision has been made at the year-end.

The Company had no capital commitments at 31 December 2013 (2012: £nil).

#### 16. Related party transactions

The Directors of Cobham plc had no material transactions with the Company during the year, other than as a result of service agreements. Details of the Directors' remuneration are disclosed in the Directors' Remuneration Report on pages 48 to 63.

Exemption has been taken under FRS 8 (revised) from disclosing related party transactions with wholly owned group companies. The only transactions with non-wholly owned subsidiaries relate to the receipt of management and brand charges totalling £1.1m (2012: £0.6m) from TEAM SA which is 98.7% owned. No amounts were outstanding at the current or prior year-end.

#### 17. Events after the balance sheet date

In February 2014, a loan agreement was signed for AUS\$90m expiring in October 2018.

# Group Financial Record

£m	2009	2010	2011	2012	2013
Revenue	1,880.4	1,902.6	1,854.4	1,749.4	<b>1,789.7</b>
Underlying profit before taxation	295.3	306.1	327.9	300.2	<b>288.0</b>
Profit before taxation	244.9	189.3	234.3	204.0	<b>126.6</b>
Taxation	(59.0)	(36.5)	(46.3)	(32.2)	<b>(12.1)</b>
Profit after taxation for the year	185.9	152.8	188.0	171.8	<b>114.5</b>
<b>Net assets employed</b>					
Intangible assets	1,063.0	1,048.4	917.6	1,102.1	<b>1,162.2</b>
Property, plant and equipment (including investment properties)	329.5	350.9	329.8	315.5	<b>360.7</b>
Investments	17.4	17.2	16.1	15.8	<b>3.1</b>
Other non-current assets	69.0	31.2	36.3	60.3	<b>43.3</b>
Current assets	963.2	1,123.2	983.7	877.9	<b>849.9</b>
	2,442.1	2,570.9	2,283.5	2,371.6	<b>2,419.2</b>
Current liabilities	(903.7)	(827.8)	(749.0)	(822.5)	<b>(871.2)</b>
Non-current liabilities excluding retirement benefit obligations	(474.9)	(584.9)	(444.2)	(421.3)	<b>(416.5)</b>
Net assets excluding retirement benefit obligations	1,063.5	1,158.2	1,090.3	1,127.8	<b>1,131.5</b>
Retirement benefit obligations	(115.2)	(82.0)	(71.2)	(73.4)	<b>(87.3)</b>
Net assets including retirement benefit obligations	948.3	1,076.2	1,019.1	1,054.4	<b>1,044.2</b>
<b>Financed by</b>					
Ordinary share capital	28.6	28.9	28.9	28.9	<b>28.9</b>
Reserves	919.4	1,046.9	989.7	1,024.9	<b>1,014.5</b>
Total equity attributable to the owners of the parent	948.0	1,075.8	1,018.6	1,053.8	<b>1,043.4</b>
Non-controlling interests in equity	0.3	0.4	0.5	0.6	<b>0.8</b>
Total equity	948.3	1,076.2	1,019.1	1,054.4	<b>1,044.2</b>
Net debt	(412.6)	(326.1)	(232.5)	(359.9)	<b>(453.4)</b>
Operating cash flow	293.2	271.4	337.1	339.3	<b>268.5</b>
Operating cash conversion	89%	79%	95%	104%	<b>85%</b>
<b>pence</b>					
Dividend paid per Ordinary Share	5.09	5.60	6.17	8.60	<b>9.04</b>
Earnings per Ordinary Share – underlying	18.80	19.68	22.05	22.48	<b>21.60</b>
Earnings per Ordinary Share – basic	16.26	13.27	16.80	15.98	<b>10.70</b>
Earnings per Ordinary Share – diluted	16.17	13.20	16.76	15.93	<b>10.65</b>
Net assets per Ordinary Share	82.7	93.2	88.3	91.3	<b>90.4</b>
<b>£m</b>					
Market capitalisation as at 31 December	2,883	2,349	2,117	2,549	<b>3,169</b>

In the above table figures for 2012 have been restated, where appropriate, for the impact of IAS 19 described in note 2 to the Group Financial Statements. On the basis of materiality prior periods have not been restated.

## Analysis of shareholders

Analysis of ordinary shareholders on the register at 31 December 2013:

Size of holding	Number of registered holders	Percentage of registered holders	Number of Ordinary Shares held	Percentage of Ordinary Shares
Up to 1,000	1,603	30.46	795,057	0.07
1,001–10,000	2,555	48.56	9,171,660	0.85
10,001–50,000	630	11.97	13,152,411	1.22
50,001–250,000	221	4.20	25,416,043	2.36
250,001–1,000,000	123	2.34	64,936,774	6.02
1,000,001 and above	130	2.47	965,103,956	89.48
Total	5,262	100.00	1,078,575,901	100.00

Source: Equiniti Limited

At 31 December 2013, there were 5,262 ordinary shareholders on the register compared with 5,620 at 31 December 2012.

## Registrars

Enquiries concerning shareholdings or dividends should, in the first instance, be addressed to the Company's registrars, Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA (telephone: 0871 384 2163\* or +44 (0)121 415 7047 if calling from outside the UK). Shareholders should promptly notify the registrars of any change of address or other particulars.

The registrars provide a range of shareholders' services online. The portfolio service provides access to information on investments including balance movements, indicative share prices and information on recent dividends and also enables address and mandate details to be amended online. For further information and practical help on transferring shares or updating your details, please visit [www.shareview.co.uk](http://www.shareview.co.uk). The share dealing service enables shares to be sold by UK shareholders by telephone, post or over the internet. For telephone sales, please call 0845 603 7037 between 8am and 4:30pm, Monday to Friday. For postal sales, please send your completed documentation to the address above. For internet sales, please visit [www.shareview.co.uk/dealing](http://www.shareview.co.uk/dealing).

## Individual Savings Accounts (ISAs)

The registrars also offer an ISA for Cobham shareholders. Further information may be obtained by visiting [www.shareview.co.uk](http://www.shareview.co.uk), or telephone 0845 300 0430 (or +44 (0)121 415 0105 if calling from outside the UK).

You should bear in mind that investments, both their value and the income they provide, can go down as well as up and you might not get back what you originally invested.

## Capital gains tax

For the information of shareholders who held Cobham plc Ordinary Shares on 31 March 1982, the market value, adjusted for capitalisation and rights issues, of the Company's Ordinary Shares on that date for capital gains tax purposes, unadjusted for the share sub-division of July 2005, was 86.02 pence.

## ShareGift

Do you have a small shareholding which is uneconomical to sell? You may want to consider donating it to ShareGift (registered charity no. 1052686), a charity that specialises in the donation of small, unwanted shareholdings to good causes. You can find out more by visiting [www.sharegift.org](http://www.sharegift.org) or calling +44 (0)20 930 3737.

## Shareholder security

Shareholders are advised to be wary of any unsolicited advice, offers to buy shares, or offers of free reports about the Company. Details of any share dealing facilities that the Company endorses will be included in Company mailings or on our website. If you receive any unsolicited advice, make sure you get the correct name of the person and organisation and check that they are appropriately authorised by the FCA by visiting [www.fca.org.uk](http://www.fca.org.uk). You can also call the FCA Consumer Helpline on 0800 111 6768 (or +44 (0)20 7066 1000 if calling from outside the UK).

## Financial calendar

AGM	24 April 2014
Final dividend – x-div date	30 April 2014
Final dividend – record date	2 May 2014
Final dividend	30 May 2014
Interim results	7 August 2014
Interim dividend – x-div date	9 October 2014
Interim dividend – record date	10 October 2014
Interim dividend	7 November 2014

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\* Calls to this number cost 8 pence per minute, plus network charges. Lines are open from 8:30am to 5:30pm, Monday to Friday.

# Glossary

Acronym	Full name	Description
A350	Airbus A350 XWB aircraft	A twin-engine wide-body jet aircraft for commercial use. The aircraft is in development and had its first flight in 2013.
A400M	Airbus A400M airlifter	A versatile large military aircraft that performs three differing duties, within challenging operating conditions: short-medium range flights, long range flights and the ability to provide aerial refuelling capabilities.
AESA	Active Electronically Scanned Array radar	Used to detect, target, track and enable self-protection capabilities. The radar is used for defence, surveillance and strike scenarios.
AMDR	Air and Missile Defence Radar	An advanced radar suite for US Navy destroyers. It provides protection against advanced anti-ship and ballistic missile threats.
AMRAAM	Advanced Medium-Range Air-to-Air Missile	A new generation of air-to-air missile with an all-weather, beyond-visual-range capability.
B717	Boeing 717 aircraft	The B717 is a narrow-body aircraft designed for short-haul, high frequency commercial use.
DAS	Distributed Antenna Systems	Fibre optic communication systems for infrastructure such as buildings, tunnels and metros. Covering a wide range of frequencies, it encompasses both public safety and cellular bands, providing coverage for network operators, transportation and public safety authorities.
ERP	Enterprise Resource Planning	A software system which integrates all business processes, including manufacturing, finance and accounting, human resources, sales and marketing, purchasing and distribution, and inventory and warehouse into one central cohesive repository. It allows businesses to run more efficiently, with real time access to data across many business functions.
Eurofighter	Eurofighter Typhoon fighter aircraft	A multi-role combat aircraft covering a full spectrum of air operations, from air policing, to peace support, through to high intensity conflict.
F-#	USAF designated fighter aircraft	Designation given by the US Air Force to aircraft designed for air-to-air combat or for multiple roles, including ground support missions.
FBH	FB Heliservices	The Group's combined interests in FB Heliservices Limited, FB Leasing Limited and FBS Limited.
FSTA	Future Strategic Tanker Aircraft	A UK Private Finance Initiative funded project to replace the UK's air-to-air refuelling fleets, and elements of the air transport work previously undertaken by the RAF VC10 and TriStar fleets.
Global Xpress	Inmarsat Global Xpress	A satellite service, with global coverage expected by the end of 2014, which will be the world's first to offer global mobile broadband coverage. Global Xpress will provide increased data speeds and bandwidth to customers in the government, maritime and aeronautical sectors.
Gripen	Saab Gripen fighter aircraft	A multi-role fighter aircraft capable of air-to-air combat, air-to-surface combat and reconnaissance roles.
IED	Improvised Explosive Device	Homemade bombs thought to be the weapon of choice for terrorists due to their availability and destructiveness.
KC-390	Embraer KC-390 Aerial Refuelling Tanker	A medium-lift military transport and aerial refuelling tanker aircraft currently being developed by Embraer. Production is scheduled to commence in 2015.

# Glossary continued

Other Information

Acronym	Full name	Description
KC-46	Boeing KC-46 Aerial Refuelling Tanker	An aerial refuelling tanker, currently being developed for the US Air Force to replace its ageing fleet of KC-135 Stratotankers. The KC-46, with initial flights scheduled for 2014, offers improved cargo and passenger capability.
Mi-17	Mi-17-1V multi-purpose medium helicopter	A multi-purpose helicopter with the ability to carry passengers, stretchers or cargo.
Minehound		A hand-held device to detect metallic, minimum-metal and non-metallic threats underground. Used in the detection of improvised explosive devices and mines.
NH-90	NHIndustries NH-90 military helicopter	A medium lift, multi-role military helicopter developed from NATO requirements. Used for troop and cargo transport, casualty evacuation, search and rescue and anti-submarine hunting.
SATCOM	Satellite Communication	Enables voice and data communications such as telephone calls, TV pictures or internet connections, using an orbiting satellite to transfer data around the earth.
SIGINT	Signals Intelligence	Intelligence gathering using electronic signals and systems such as radars, communications and weapons systems.
Super Puma	Airbus Super Puma Helicopter	Designed to operate in extreme environments, a medium-large helicopter capable of carrying heavy objects and passengers.
UAV	Unmanned Aerial Vehicle	Unmanned aircraft that generally carry cameras, sensors, communications equipment or other payloads. They are used in reconnaissance and intelligence gathering roles with more challenging roles envisioned, including combat missions.
WGS	Wideband Global Satellite Programme	The US Department of Defense's highest-capacity satellite communications system. It supports requirements such as tactical command and control, battle management, reconnaissance, intelligence, surveillance and combat support.

# Definitions

## KPI definitions

### Group organic revenue growth

Revenue growth stated at constant translation exchange rates, excluding the incremental effect of acquisitions and disposals.

### Underlying EPS growth at constant translation exchange rates

The year on year increase of the underlying profit after taxation, stated at constant translation exchange rates, divided by the weighted average number of Ordinary Shares.

### Operating cash conversion

Operating cash flow as a percentage of trading profit, excluding profit from joint ventures.

### Return on invested capital

Trading profit as a percentage of the average invested capital during the year.

Invested capital comprises net assets adjusted to exclude net debt, retirement benefit obligations, derivative financial instruments, current and deferred tax, provisions and other financial assets. Intangible assets recognised on business combinations are grossed up to their original cost before amortisation and an adjustment is also made to reinstate the historic goodwill previously written off directly to reserves.

### PV investment

PV (Private Venture) or company funded R&D (Research and Development) measures exclude Aviation Services, where there is no R&D activity.

### Staff safety – major accident incident rate

The number of accidents resulting in more than three days absence per 100,000 employees.

### Voluntary staff turnover

The number of voluntary leavers divided by the average number of employees over the period, excluding employees who became redundant, were dismissed or retired.

## Further financial definitions

The following notes apply throughout the Annual Report and Accounts:

To assist with the understanding of earnings trends, the Group has included within its published financial statements trading profit and underlying earnings results. Trading profit has been defined as operating profit from continuing operations excluding the impacts of certain M&A related costs and business restructuring costs as detailed below. Also excluded are changes in the marking to market of non-hedge accounted derivative financial instruments, impairments of intangible assets, and items deemed by the Directors to be of an exceptional nature.

M&A related costs excluded from trading profit and underlying earnings include the amortisation of intangible assets recognised on acquisition and the writing off of the pre-acquisition profit element of inventory written up on acquisition. M&A related costs also include other direct costs associated with business combinations, adjustments to contingent consideration related to previously acquired businesses and direct costs from terminated divestments.

Business restructuring costs or gains associated with the restructuring of the Group's portfolio which are incremental to normal operations.

Underlying earnings are defined as trading profit less net underlying finance costs, which excludes the unwinding of acquisition related discounting, and after deducting associated taxation and non-controlling interests.

A reconciliation of operating profit and profit before taxation to the respective underlying numbers is shown on page 24.

Operating cash flow is defined as net cash from operating activities before payment of tax, interest, restructuring costs and M&A related costs but after cash flows from the purchase or disposal of property, plant, equipment and intangible assets.

Free cash flow is defined as net cash from operating activities plus dividends received from joint ventures, less cash flows related to the purchase or disposal of property, plant, equipment and intangible assets but excluding payments relating to M&A related activities.

Net debt is defined as the net of borrowings less cash and cash equivalents at the balance sheet date.

When providing divisional analysis by geography, US revenue includes revenue to US based customers on programmes that could be designated as export and is therefore non-US defence/security from a market analysis perspective.

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Our website provides further information including shareholder services and governance, details of our products and services, corporate responsibility and sustainability and more.

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