22 February 2024

# ROLLS-ROYCE HOLDINGS PLC - 2023 Full Year Results

**Step-change in performance driven by transformation; strong momentum into 2024**

- Underlying operating profit of £1.6bn and underlying margin of 10.3%, reflecting the impact of our strategic initiatives, with commercial optimisation and cost efficiency benefits across the Group
- Record free cash flow of £1.3bn driven by operating profit and continued LTSA balance growth
- Return on capital more than doubled to 11.3% reflecting improved operating profit, disciplined capital allocation and working capital management
- Statutory net cash flow from operating activities of £2.5bn, £1.0bn higher year on year
- Net debt of £2.0bn, down from £3.3bn at the end of 2022, as we strengthen the balance sheet and build resilience
- 2024 guidance: continued progress with underlying operating profit between £1.7bn and £2.0bn and free cash flow between £1.7bn and £1.9bn

*Tufan Erginbilgic, CEO said: "Our transformation has delivered a record performance in 2023, driven by commercial optimisation, cost efficiencies and progress on our strategic initiatives. This step-change has been achieved across all our divisions, despite a volatile environment with geopolitical uncertainty, supply chain challenges and inflationary pressures.*

*We are managing the business differently and our significant performance improvement in the year reflects the hard work and focused actions of all our teams. We are also continuing to invest to drive future sustainable growth. Our strong delivery in 2023 gives us confidence in our 2024 guidance and is a significant step towards our mid-term targets. We are unlocking our full potential as a high-performing, competitive, resilient, and growing Rolls-Royce."*

## Full Year 2023 Group continuing operations

| £ million | Underlying 2023 | Underlying 2022 | Statutory 2023 | Statutory 2022 |
|---|---|---|---|---|
| **Revenue** | **15,409** | 12,691 | **16,486** | 13,520 |
| **Operating profit** | **1,590** | 652 | **1,944** | 837 |
| *Operating margin (%)* | ***10.3%*** | *5.1%* | ***11.8%*** | *6.2%* |
| **Profit/(loss) before taxation** | **1,262** | 206 | **2,427** | (1,502) |
| **Earnings/(loss) per share (pence)** | **13.75** | 1.95 | **28.85** | (14.24) |
| | | | | |
| **Free cash flow** | **1,285** | 505 | | |
| **Return on capital (%)** [1] | **11.3%** | 4.9% | | |
| **Net cash flow from operating activities** [2] | | | **2,485** | 1,524 |
| **Net debt** | | | **(1,952)** | (3,251) |

[1] *Adjusted return on capital is defined on page 52 and is abbreviated to return on capital*

[2] *Represented. See page 18 for further details*

A reconciliation of alternative performance measures to their statutory equivalent is provided on pages 49 to 52

## 2023 performance summary

- **Driving growth in attractive markets:** Large engine flying hours (EFH) in Civil Aerospace recovered to 88% of 2019 levels, up from 65% in 2022. Large engine orders were the highest in more than 15 years, with major orders from Air India and Turkish Airlines. In Defence, the AUKUS submarine agreement was announced, which will be supported by the expansion of our submarines site in Raynesway, and work on our future programmes in the UK and US progressed well. In Power Systems, we are capturing strong demand for power generation solutions and services in the rapidly expanding data centre market.

- **Significantly improved profit and margins:** Underlying operating profit rose by £0.9bn to £1.6bn supported by our transformation programme and strategic initiatives, with commercial optimisation and cost efficiency benefits across the Group. Underlying operating margin more than doubled to 10.3%. Civil Aerospace, Defence and Power Systems all delivered materially higher margins compared to last year. The largest improvement was in Civil Aerospace, which delivered an operating margin of 11.6% compared to 2.5% in the previous year. This was driven by increased aftermarket profit, in both the large engines and business aviation segments, reflecting commercial optimisation and cost efficiencies, as well as volume growth. Defence delivered an improved operating margin of 13.8% (2022: 11.8%), which primarily reflected improved pricing and cost efficiencies. In Power Systems, which reported an operating margin of 10.4% (2022: 8.4%), pricing and cost efficiency actions in the first half of the year resulted in a significantly improved operating profit and margin in the second half and in the full year.

- **Record cash generation:** Free cash flow from continuing operations grew by approximately 150% to £1.3bn, principally due to higher operating profit. Civil net LTSA creditor growth net of risk and revenue sharing agreements (RRSAs) was £1.1bn (2022: £0.8bn). Continued LTSA balance growth reflects higher EFHs and the benefit of commercial optimisation, with LTSA invoiced flying hour receipts of £4.6bn (2022: £3.6bn). Our focus on working capital resulted in a release in the second half despite ongoing supply chain challenges. For the full year there was a net working capital outflow of £0.4bn (2022: £0.5bn). Inventory and debtor days both improved year on year building further confidence in the actions we are taking to improve the quality of cash delivery.

- **Building financial resilience:** Total underlying cash costs as a proportion of underlying gross margin (TCC/GM) ratio improved to 0.59x in 2023 from 0.80x in 2022. Net debt improved to £2.0bn (2022: £3.3bn). We have £4.1bn of drawn debt, of which £0.5bn matures in 2024, £0.8bn in 2025 and £2.8bn in 2026-2028, and £1.7bn of lease liabilities. We have £3.7bn in cash and cash equivalents and £3.5bn undrawn facilities, totalling £7.2bn of liquidity, and expect to repay the 2024 and 2025 bonds from cash. We cancelled a £1.0bn undrawn UK Export Finance (UKEF) backed facility in the year, and a £1.0bn undrawn bank loan facility reflecting our higher cash balance and more resilient financial position.

- **Shareholder payments:** We are not making shareholder payments for 2023. As we shared at our capital markets day in November 2023, once we are comfortably within an investment grade profile and the strength of our balance sheet is assured, we are committed to reinstating and growing shareholder distributions.

## Transformation programme and strategic review

The early results of our transformation programme and strategic initiatives are already evident in the step-change in performance reported for 2023, but there is more still to do. Our strategy framework is founded on four pillars:

- **Portfolio choices & partnerships:** We have clear plans for the markets we will operate and invest in. In Civil Aerospace, we successfully tested our UltraFan demonstrator engine to full power and achieved certification for our Pearl 700 business jet engine. In Defence, investment continued in the growing combat, transport and submarines markets and we progressed well with testing and development on the GCAP and B-52 programmes. In Power Systems, we successfully tested a new engine prototype that will join our portfolio alongside our current Series 4000 and acquired a yacht automation and bridge specialist business to extend our Marine offering. We also identified areas for divestment, which we expect to generate £1.0bn-£1.5bn gross proceeds by 2028. We are in advanced discussions to sell the off-highway lower power range engines division in Power Systems and we decided to exit Electrical in the short term or alternatively, for the right value, reduce our position to a minority with an intention to exit fully in the mid-term.

- **Advantaged businesses & strategic initiatives:** In Civil Aerospace, we have now retrofitted 20% of the Trent 7000 fleet with the improved HPT blade, which has doubled its time on wing, and we expect the same improvement to be certified on the Trent 1000 TEN in 2024. All key Civil Aerospace OEM and major airline contract renegotiations were either concluded or progressed. Our cost initiatives reduced total shop visit costs across large engines dispatched in 2023, which helped to deliver an improved LTSA margin. In Defence, cost efficiencies and value-based pricing helped to deliver improved performance and we delivered strong growth in combat and submarines. In Power Systems, in addition to our pricing and cost actions, we commissioned one of the largest battery and energy storage systems in Europe, helping to integrate renewable energy into the Dutch public grid and grow our power generation business.

- **Efficiency & simplification**: Our actions to deliver sustainable cost efficiencies and improve competitiveness are well underway. In 2023, we delivered around £150m towards an annualised total Efficiency & Simplification savings target of £400m-£500m in the mid-term. We announced a reduction of 2,000-2,500 roles by the end of 2025 with expected annual benefits of approximately £200m and associated severance costs of £200m-£250m, which will be taken as an exceptional charge in 2024. We also have a renewed focus on third party costs, where we delivered gross savings of £130m in the year, making a strong start towards our target to save £1bn gross procurement spend by the mid-term, helping to partly offset inflationary pressures. In 2024, we have launched zero based budgeting, focusing initially on Civil Aerospace.

- **Lower carbon & digitally enabled businesses:** We remain committed to becoming a net zero company by 2050 and supporting our customers to do the same. In 2023 we powered the first 100% sustainable aviation fuelled commercial flight across the Atlantic and met our target for 100% SAF compatibility testing for our in production commercial aero engines. Our S2000 and S4000 engines in Power Systems were approved for use with sustainable fuels and we also progressed our hydrogen test programmes. We invested in digital tools as we look to unlock the potential to remove 20% of repetitive tasks with digital and AI capability.

Delivery of our strategic framework and clear plans for the mid-term will realise our Rolls-Royce proposition to become a high-performing, competitive, resilient and growing business. Our people are energised and aligned to the new One Rolls-Royce ways of working and our progress to date further strengthens our confidence in the delivery of our mid-term targets.

## Outlook and 2024 Guidance

As we continue to deliver our strategy, we expect further improvements towards all our mid-term targets. This is despite the impact of continued supply chain challenges, which we expect to persist for 18-24 months, geopolitical uncertainty and inflationary pressures.

| **2024 financial guidance** | |
|---|---|
| Underlying operating profit | £1.7bn-£2.0bn |
| Free cash flow | £1.7bn-£1.9bn |

In Civil Aerospace, we expect 2024 large EFHs will grow to 100-110% of 2019's level, 500-550 total original equipment (OE) deliveries and 1,300-1,400 total shop visits. Our 2024 free cash flow guidance is based on civil net LTSA creditor growth at the low end of the mid-term range (£0.8bn - £1.2bn), compared to £1.1bn in 2023. Additional detail is included in the results presentation and supplementary data slides.

Strong progress in the early years of our plan demonstrates a front-end loaded delivery of performance improvement. Our 2023 performance and 2024 guidance on operating profit and free cash flow means that by 2024 we will have delivered more than 50% of the improvement set out in our mid-term targets. As a reminder, we are targeting underlying operating profit of £2.5bn-£2.8bn, operating margin of 13-15%, free cash flow of £2.8bn-£3.1bn and return on capital of 16-18% in the mid-term. These targets are based upon our expectations for a 2027 timeframe.

## Underlying financial performance by division

| **£ million** | **Underlying revenue** | **Organic Change [1]** | **Underlying operating profit/(loss)** | **Organic change [1]** | **Underlying operating margin** | **Organic margin change (pts)** |
|---|---|---|---|---|---|---|
| Civil Aerospace | **7,348** | 29% | **850** | 497% | 11.6% | 9.1pt |
| Defence | **4,077** | 12% | **562** | 30% | 13.8% | 1.9pt |
| Power Systems | **3,968** | 16% | **413** | 44% | 10.4% | 2.0pt |
| New Markets | **4** | nm | **(160)** | (20)% | nm | nm |
| Other businesses | **12** | nm | **(15)** | 52% | nm | nm |
| Corporate/eliminations | **–** | nm | **(60)** | (49)% | nm | nm |
| **Total (continuing operations)** | **15,409** | 21% | **1,590** | 143% | 10.3% | 5.2pt |

[1] *Organic change is the measure of change at constant translational currency applying full year 2022 average rates to 2023. All underlying income statement commentary is provided on an organic basis unless otherwise stated*

*All results are shown for Group continuing operations, on an underlying basis, excluding discontinued operations (ITP Aero). For more details, see note 2 of the Condensed Consolidated Financial Statements (page 22).*

*nm is defined as not meaningful*

## Trading cash flow

| **£ million** | **2023** | 2022 |
|---|---|---|
| Civil Aerospace | **626** | 226 |
| Defence | **511** | 426 |
| Power Systems | **461** | 158 |
| New Markets | **(63)** | (57) |
| Other businesses | **5** | 5 |
| Corporate/eliminations | **(57)** | (49) |
| **Total trading cash flow (continuing operations)** | **1,483** | 709 |
| Underlying operating profit charge exceeded by contributions to defined benefit schemes | **(26)** | (32) |
| Taxation | **(172)** | (172) |
| **Total free cash flow (continuing operations)** | **1,285** | 505 |

## Civil Aerospace

| 2023 key operational metrics: | Large engine | Business aviation/ regional | Total | Change |
|---|---|---|---|---|
| Original Equipment (OE) deliveries | 262 | 196 | 458 | 29% |
| LTSA engine flying hours (millions) | 13.5 | 3.0 | 16.5 | 25% |
| Total LTSA shop visits | 839 | 388 | 1,227 | 18% |
| …of which major shop visits | 368 | 363 | 731 | 27% |

Significantly improved Civil Aerospace operating profit and margins reflect higher aftermarket profit, due to increased volumes, commercial optimisation, and cost efficiencies.

Civil Aerospace large EFHs rose by 36% year on year to 88% of 2019 levels, reflecting the continued strong demand for travel coupled with a recovery in traffic in China as COVID-19 restrictions eased. Business aviation demand remained robust. In 2023, around 700 large engines were ordered, the highest level since 2007 including major orders from Air India, Emirates and EVA Air. Turkish Airlines also placed an order for new engine deliveries in 2023, which is set to make them the largest operator of Trent XWB engines in the world. In January 2024 we also received a substantial order from Delta Airlines for 40 Trent XWB-97 engines. Our large engine order book increased by almost 30% to 1,632 engines at year end with a 2023 book to bill of 2.6x.

Total OE engine deliveries rose by 29% year on year, with 196 business aviation deliveries (2022: 165) and 262 total large engine deliveries (2022: 190). In 2023 we delivered 53 large spare engines (2022: 44), which represented 20% of total large engine deliveries (2022: 23%). Total shop visits increased 18% year on year to 1,227 (2022: 1,044), of these 368 were large engine major shop visits (2022: 248). The ramp up in shop visits was achieved despite ongoing supply chain constraints.

Underlying revenue of £7.3bn increased 29% year on year, driven by higher shop visits and OE engine deliveries and commercial optimisation. Underlying OE revenues grew by 36% in the year to £2.7bn and services revenues grew by 25% to £4.6bn. LTSA revenue catch-ups were £(104)m (2022: £360m).

Underlying operating profit was £850m (11.6% margin) versus £143m in 2022 (2.5% margin). The year on year improvement was driven by higher large engine LTSA shop visit volumes and profitability, increased time and materials profits from life limited parts sales for large engines, and higher business aviation profits, again driven by aftermarket profit growth. In each case, our commercial optimisation actions helped drive margin improvements. This was complemented by cost efficiencies, with lower indirect costs net of inflation.

Contract catch-ups were £(29)m (2022: £319m). The prior year benefitted from material positive contract catch-ups mostly associated with inflation assumption changes in 2022. Net onerous provisions/releases were £(25)m (2022: £51m). We made good progress on onerous contracts in the year, releasing £385m of provisions taken in prior periods. However, this was more than offset by £410m new provisions taken in 2023 mostly related to industry wide supply chain constraints.

Trading cash flow was £626m versus £226m in 2022. Improved cash flows were driven by higher operating profit, continued strong growth in the LTSA balance, partly offset by net working capital movements and increased investments in the year including improving time on wing for our Trent engines, investment in the Pearl business aviation engines and the UltraFan demonstrator engine test. LTSA invoiced flying hour receipts increased to £4.6bn (2022: £3.6bn).

## Defence

Higher operating profit in Defence was driven by our commercial optimisation action, cost efficiencies and volume growth in submarines.

Demand remained strong in all key markets – transport, combat and submarines – with order intake of £5.2bn in the year; a book-to-bill ratio of 1.3x. This resulted in a record order backlog of £9.2bn at the year end, with 90% order cover in 2024 and a high degree of cover in 2025 and beyond. Key awards in the year included the AUKUS agreement, which underpins the long-term growth outlook for our submarines business.

Revenues increased by 12% in 2023 to £4.1bn, with year-on-year growth in all major end markets, notably double-digit revenue growth in combat and submarines. Combat growth was driven by the GCAP programme in the UK and the ramp-up of the F130 programme for the B-52 in the US. Total OE revenues grew by 8% in the year to £1.8bn and services revenues grew by 14% to £2.3bn.

Operating profit was £562m (13.8% margin) versus £432m (11.8% margin) in the prior year, reflecting commercial optimisation, cost efficiencies, and growth in submarines. A lower R&D charge reflected increased customer funding and our strategic focus on the most attractive future programmes.

Trading cash flow of £511m improved versus £426m last year, driven by higher underlying operating profit and our working capital initiatives which resulted in inventory reductions, and increased customer deposits.

## Power Systems

In Power Systems, as we stated in our upgraded 2023 guidance at the half year, our cost and pricing actions in the first half of the year supported a significantly higher margin and profit in the second half, and a higher margin for the full year, with a material improvement in power generation profit, taking the division to a level which represents an all-time record in the 114 year history of the business.

Order intake in Power Systems was £4.3bn, flat year on year, but with a book-to-bill ratio of 1.1x and OE order coverage for 2024 of 80%. Demand remained strong with high order intake in power generation and governmental in particular.

Underlying revenue was £4.0bn, an increase of 16% year on year with 34% growth in the power generation end market driven by data centre growth, where we have a leading position. Underlying OE revenues grew by 19% to £2.7bn. Underlying Services revenues grew by 10% to £1.3bn.

Operating profit was £413m, a 44% year on year increase. This was driven by commercial optimisation and cost efficiencies. In power generation, profitability tripled in 2023 as we took steps to ensure we are appropriately remunerated for our products and services through value-based pricing. The year on year improvement in operating margin to 10.4% in 2023 versus 8.4% in 2022 was achieved despite a slight product mix headwind in the year.

Trading cash flow was £461m with a conversion ratio of 112% versus £158m and 56% last year. The increase in trading cash flow was due to increased operating profit and working capital initiatives including a benefit from increased customer advance payments and reduced inventories in the year.

## New Markets

Rolls-Royce SMR (small modular reactors) continued to progress well through stage two of the Generic Design Assessment (GDA) regulatory process in the UK. First power is still planned in the early 2030s, which will be dependent on securing orders and the outcome of the final investment decision by the UK Government. In 2023 we were successfully shortlisted in the first stage of the Great British Nuclear Small Modular Reactor technology selection process and look forward to the next steps.

Planned cost increases in both Electrical and SMR to meet development milestones resulted in an increased operating loss of £(160)m a 20% increase from £(132)m in the prior year.

Trading cash flow was an outflow of £(63)m compared to £(57)m in the prior year, with SMR costs covered by third party funding.

## Statistical and underlying Group financial performance from continuing operations

| £ million | 2023 Statutory | 2023 Impact of hedge book [1] | 2023 Impact of acquisition accounting | 2023 Impact of other non-underlying items | 2023 Underlying | 2022 Underlying |
|---|---|---|---|---|---|---|
| **Revenue** | **16,486** | **(1,077)** | **–** | **–** | **15,409** | 12,691 |
| **Gross profit** | **3,620** | **(461)** | **46** | **26** | **3,231** | 2,477 |
| **Operating profit** | **1,944** | **(475)** | **50** | **71** | **1,590** | 652 |
| Gain arising on disposal of businesses | **1** | **–** | **–** | **(1)** | **–** | – |
| **Profit before financing and taxation** | **1,945** | **(475)** | **50** | **70** | **1,590** | 652 |
| Net financing income/(costs) | **482** | **(915)** | **–** | **105** | **(328)** | (446) |
| **Profit before taxation** | **2,427** | **(1,390)** | **50** | **175** | **1,262** | 206 |
| Taxation [2] | **(23)** | **285** | **(12)** | **(370)** | **(120)** | (48) |
| **Profit for the year from continuing operations** | **2,404** | **(1,105)** | **38** | **(195)** | **1,142** | 158 |
| **Basic earnings per share (pence)** | **28.85** | | | | **13.75** | 1.95 |

1 *Reflecting the impact of measuring revenue and costs at the average exchange rate during the year and the valuation of assets and liabilities using the year end exchange rate rather than the rate achieved on settled foreign exchange contracts in the year or the rate expected to be achieved by the use of the hedge book*

2 *Taxation includes the recognition of a deferred tax asset on UK tax losses of £328m in other non-underlying items*

**Revenue**: Underlying revenue of £15.4bn was up 21%, with double-digit growth in all three core divisions and particularly strong growth in Civil Aerospace. Statutory revenue of £16.5bn was 22% higher compared with 2022. The difference between statutory and underlying revenue is driven by statutory revenue being measured at average prevailing exchange rates (2023: GBP:USD 1.24; 2022: GBP:USD 1.24) and underlying revenue being measured at the hedge book achieved rate during the year (2023 GBP:USD 1.50; 2022: 1.50).

**Operating profit**: Underlying operating profit of £1,590m (10.3% margin) versus £652m (5.1% margin) in the prior year. This was due primarily to strong aftermarket growth in Civil Aerospace and commercial optimisation and cost efficiencies across the Group. The largest year on year improvement in margin was in Civil Aerospace, but Defence and Power Systems margins also rose materially. Statutory operating profit was £1,944m, higher than the £1,590m underlying operating profit largely due to the £475m negative impact from currency hedges in the underlying results. Net charges of £71m were excluded from the underlying results as these related to non-underlying items comprising net transformation and restructuring charges of £102m; partly offset by net impairment reversals of £8m, the write back of exceptional Trent 1000 programme charges of £21m; and a £2m pension past service credit.

**Profit before taxation**: Underlying profit before taxation of £1,262m included £(328)m net financing costs comprising £164m interest receivable, £(275)m interest payable and £(217)m of other financing charges and costs of undrawn facilities. Statutory profit before tax of £2,427m included £515m net fair value gains on derivative contracts, £(205)m net interest payable and net foreign exchange gains of £394m.

**Taxation**: Underlying tax charge of £(120)m (2022: £(48)m) reflects a tax charge on profits of £(198)m net of a tax credit arising on the recognition of a £78m deferred tax asset on previously unrecognised UK tax losses. The 2022 underlying tax charge relates to tax on overseas profits of £(175)m net of a tax credit on the increase in certain UK deferred tax assets of £127m. The statutory tax charge of £(23)m is lower than the underlying charge due to an additional £328m recognition of a deferred tax asset on UK tax losses. This is partially offset by a net tax charge of £(231)m on non-underlying items.

## Free cash flow

| £ million | 2023 Cash flow | 2023 Impact of hedge book | 2023 Impact of acquisition accounting | 2023 Impact of other non-underlying items | 2023 Funds flow | 2022 Funds flow |
|---|---|---|---|---|---|---|
| **Operating profit** | **1,944** | **(475)** | **50** | **71** | **1,590** | 652 |
| Operating profit from discontinued operations | **–** | **–** | **–** | **–** | **–** | 86 |
| Depreciation, amortisation and impairment | **1,019** | **–** | **(50)** | **9** | **978** | 953 |
| Movement in provisions | **(325)** | **46** | **–** | **21** | **(258)** | (23) |
| Movement in Civil LTSA balance | **1,708** | **(377)** | **–** | **–** | **1,331** | 792 |
| Movement in prepayments to RRSAs for LTSA parts | **(315)** | **63** | **–** | **–** | **(252)** | (8) |
| Settlement of excess derivatives [1] | **(389)** | **–** | **–** | **–** | **(389)** | (326) |
| Interest received | **159** | **–** | **–** | **–** | **159** | 36 |
| Other operating cash flows [2] | **(63)** | **(8)** | **–** | **3** | **(68)** | 5 |
| **Operating cash flow before working capital and income tax** | **3,738** | **(751)** | **–** | **104** | **3,091** | 2,167 |
| Working capital (excluding Civil LTSA balance and prepayment to RRSAs) [3] | **(236)** | **(123)** | **–** | **(37)** | **(396)** | (524) |
| Cash flows on other financial assets and liabilities held for operating purposes | **(845)** | **853** | **–** | **–** | **8** | 77 |
| Income tax | **(172)** | **–** | **–** | **–** | **(172)** | (174) |
| **Cash from operating activities** | **2,485** | **(21)** | **–** | **67** | **2,531** | 1,546 |
| Capital element of lease payments | **(291)** | **21** | **–** | **–** | **(270)** | (198) |
| Capital expenditure | **(699)** | **–** | **–** | **4** | **(695)** | (504) |
| Investment | **69** | **–** | **–** | **–** | **69** | 28 |
| Interest paid | **(333)** | **–** | **–** | **–** | **(333)** | (352) |
| Other | **54** | **–** | **–** | **(71)** | **(17)** | (29) |
| **Free cash flow** | **1,285** | **–** | **–** | **–** | **1,285** | 491 |
| **- of which is continuing operations** | **1,285** | | | | **1,285** | 505 |

*[1] The funds flow to 31 December 2022 has been represented to disclose cash flows on settlement of excess derivative contracts as cash flows from operating activities. As a result, operating cash flows before working capital and income tax during the year to 31 December 2022 have reduced by £(326)m to £2,167m. Cash flows on settlement of excess derivative contracts were previously shown after cash from operating activities in arriving at free cash flow. There is no impact to free cash flow*

*[2] Other operating cash flows includes profit/(loss) on disposal, share of results and dividends received from joint ventures and associates, flows relating to our defined benefit post-retirement schemes, and share based payments*

*[3] Working capital includes inventory, trade and other receivables and payables, and contract assets and liabilities (excluding Civil LTSA balances and prepayment to RRSAs). Working capital was previously defined as inventory, trade and other receivables and payables, and contract assets and liabilities, excluding Civil LTSA*

**Free cash flow** in the year was £1.3bn, an improvement of £0.8bn compared with the prior year driven by:

**Operating cash flow before working capital and income tax of £3.1bn**, £0.9bn higher than the prior year. The improvement at the Group level was principally due to our actions on commercial optimisation and cost discipline. The movement in Civil LTSA balance was £1,331m (2022: £792m) driven by higher EFH receipts. RRSA prepayments were £252m (2022: £8m). The movement in provisions of £(258)m largely related to utilisation of the Trent 1000 provision, contract loss provisions and the settlement of a legal claim. The settlement of excess derivative contracts of £(389)m was in line with expectations, with a further cash outflow of £146m expected to be incurred in 2024, £148m in 2025 and £27m in 2026. Interest received was £159m, up from £36m in 2022 due to higher cash balances and higher interest rates in the year.

**Working capital £(396)m**, compared to £(524)m in the prior year. Inventory increased by £(0.2)bn in the year primarily driven by Civil Aerospace as a result of continued supply chain disruption. There was a net £(0.2)bn outflow from receivables, payables and contract liabilities reflecting the net of volume growth in receivables and an increase in advance payments from customers.

**Income tax of £(172)m**, net cash tax payments in 2023 were marginally lower than the prior year of £(174)m, mainly due to the receipt of refunds in respect of prior periods in the US and timing of payments in Germany.

**The capital element of lease payments was £(270)m**, £(72)m higher than the prior year as a result of timing of lease payments.

**Capital expenditure of £(695)m**, mainly £(429)m property, plant and equipment additions and £(284)m intangibles additions. The combined additions were higher than last year as a result of investment in site improvements across the Group.

**Interest paid of £(333)m**, including lease interest payments, has reduced by £19m as a result of the settlement of the UKEF £2bn loan facility in September 2022 slightly offset by higher interest on gross overdrafts.

## Balance Sheet

| £ million | 2023 | 2022 | Change |
|---|---|---|---|
| Intangible assets | **4,009** | 4,098 | (89) |
| Property, plant and equipment | **3,728** | 3,936 | (208) |
| Right of use assets | **905** | 1,061 | (156) |
| Joint ventures and associates | **479** | 422 | 57 |
| Civil LTSA [1] | **(9,080)** | (7,372) | (1,708) |
| RRSA prepayments for LTSA parts [1] | **1,320** | 1,005 | 315 |
| Working capital [1] | **(1,386)** | (2,017) | 631 |
| Provisions | **(2,029)** | (2,333) | 304 |
| Net debt [2] | **(1,952)** | (3,251) | 1,299 |
| Net financial assets and liabilities [2] | **(2,060)** | (3,649) | 1,589 |
| Net post-retirement scheme deficits | **(253)** | (420) | 167 |
| Taxation | **2,605** | 2,468 | 137 |
| Held for sale [3] | **54** | - | 54 |
| Other net assets and liabilities | **31** | 36 | (5) |
| **Net liabilities** | **(3,629)** | (6,016) | 2,387 |
| Other items | | | |
| US$ hedge book (US$bn) | **15** | 19 | |

[1] *The total of these lines represents inventory, trade receivables and payables, contract assets and liabilities and other assets and liabilities in the statutory balance sheet*

[2] *Net debt includes £23m (2022: £86m) of the fair value of derivatives included in fair value hedges and the element of fair value relating to exchange differences on the underlying principal of derivatives in cash flow hedges*

[3] *Held for sale assets relate to the sale of the off-highway engines business in the lower power range based in Power Systems*

Key drivers of balance sheet movements were:

**Civil LTSA:** The £(1.7)bn movement in the net liability balance was mainly driven by an increase in invoiced LTSA receipts exceeding revenue recognised in the year, this is especially prevalent on new contracts where shop visits are not immediately scheduled.

**RRSA prepayments for LTSA parts:** The £0.3bn increase corresponds to the increase seen in the civil LTSA balance above. RRSA prepayments typically move in line with the civil LTSA as the RRSA prepayment represents amounts that we have paid to Risk and Revenue Share Partners for the parts that they will ultimately provide in support of our contracts.

**Working capital**: The £(1.4)bn net working capital position decreased by £0.6bn compared to the prior year. The movement comprised £0.1bn increase in inventory, mainly in Civil Aerospace due to supply chain disruption, £0.9bn increase in receivables due to higher trading volumes and prepayments from customers, £0.5bn reduction in payables due to changes in operational volumes and timing of supplier payments, partly offset by an increase in contract liabilities of £(0.9)bn driven by advanced payments received across the divisions.

**Provisions**: The £0.3bn net reduction was primarily driven by the settlement of a legal claim, utilisation of the Trent 1000 provision, and a net £0.1bn reduction in contract loss provisions due to provision utilisation, renegotiations and extensions of some major contracts resulting in improved margins, partly offset by increased cost estimates from supply chain issues.

**Net debt**: Decreased from £(3.3)bn to £(2.0)bn driven by free cash inflow of £1.3bn. Our liquidity position is strong with £7.2bn of liquidity including cash and cash equivalents of £3.7bn and undrawn facilities of £3.5bn. Two undrawn facilities, totalling £2.0bn, were cancelled in 2023 reflecting our higher cash balance and more resilient financial position. Net debt included £(1.7)bn of lease liabilities (2022: £(1.8)bn).

**Net financial assets and liabilities**: A £1.6bn reduction in the net financial liabilities driven by contracts maturing in the year and a change in fair value of derivative contracts largely due to the impact of the movement in GBP:USD exchange rates.

**Taxation**: The net tax asset has increased by £137m. This includes an overall increase in the deferred tax asset of £267m, due to increases in the deferred tax asset recognised on UK tax losses of £422m and other deferred tax assets of £101m, partly offset by a reduction of £256m on the deferred tax on foreign exchange derivative contracts. Other tax balance movements include increases in the deferred tax liability of £44m and net current tax liabilities of £86m.

**Results meeting and conference call**

Our results presentation will be held at UBS, 5 Broadgate, London EC2M 2QS and webcast live at 09:00 (GMT) today. Downloadable materials will also be available on the Investor Relations section of the Rolls-Royce website: https://www.rolls-royce.com/investors/results-and-events.aspx
To register for the webcast, including Q&A participation, please visit the following link: https://app.webinar.net/3K4kP3kPLYx

Please use this same link to access the webcast replay which will be made available shortly after the event concludes. Photographs and broadcast-standard video are available at www.rolls-royce.com

**Enquiries:**

| | | | |
|---|---|---|---|
| **Investors**: | | **Media**: | |
| Isabel Green | +44 7880 160976 | Richard Wray | +44 7810 850055 |
| Jeremy Bragg | +44 7795 840875 | | |

*This results announcement contains forward-looking statements. Any statements that express forecasts, expectations and projections are not guarantees of future performance and will not be updated. By their nature, these statements involve risk and uncertainty, and a number of factors could cause material differences to the actual results or developments. This report is intended to provide information to shareholders, is not designed to be relied upon by any other party, or for any other purpose and Rolls-Royce Holdings plc and its directors accept no liability to any other person other than under English law.*
LSE: RR.; ADR: RYCEY; LEI: 213800EC7997ZBLZJH69

# Condensed Consolidated Financial Statements

## Condensed consolidated income statement

For the year ended 31 December 2023

| | Notes | **2023 £m** | 2022 £m |
|---|---|---|---|
| **Continuing operations** | | | |
| **Revenue** | 2 | **16,486** | 13,520 |
| Cost of sales [1] | | **(12,866)** | (10,763) |
| **Gross profit** | 2 | **3,620** | 2,757 |
| Commercial and administrative costs | 2 | **(1,110)** | (1,077) |
| Research and development costs | 2, 3 | **(739)** | (891) |
| Share of results of joint ventures and associates | | **173** | 48 |
| **Operating profit** | | **1,944** | 837 |
| Gain arising on disposal of businesses | 23 | **1** | 81 |
| **Profit before financing and taxation** | | **1,945** | 918 |
| | | | |
| Financing income | 4 | **1,163** | 355 |
| Financing costs | 4 | **(681)** | (2,775) |
| **Net financing income/(costs)** [2] | | **482** | (2,420) |
| | | | |
| **Profit/(loss) before taxation** | | **2,427** | (1,502) |
| Taxation | 5 | **(23)** | 308 |
| **Profit/(loss) for the year from continuing operations** | | **2,404** | (1,194) |
| | | | |
| **Discontinued operations** | | | |
| Profit for the year from ordinary activities | | **–** | 68 |
| Loss on disposal of discontinued operations | | **–** | (148) |
| **Loss for the year from discontinued operations** | 23 | **–** | (80) |
| | | | |
| **Profit/(loss) for the year** | | **2,404** | (1,274) |
| | | | |
| **Attributable to:** | | | |
| Ordinary shareholders | | **2,412** | (1,269) |
| Non-controlling interests (NCI) | | **(8)** | (5) |
| **Profit/(loss) for the year** | | **2,404** | (1,274) |
| Other comprehensive (expense)/income (OCI) | | **(171)** | 522 |
| **Total comprehensive income/(expense) for the year** | | **2,233** | (752) |
| | | | |
| **Earnings/(loss) per ordinary share attributable to ordinary shareholders:** | 6 | | |
| **From continuing operations:** | | | |
| Basic | | **28.85p** | (14.24)p |
| Diluted | | **28.70p** | (14.24)p |
| | | | |
| **From continuing and discontinued operations:** | | | |
| Basic | | **28.85p** | (15.20)p |
| Diluted | | **28.70p** | (15.20)p |

[1] Cost of sales includes a net release for expected credit losses (ECLs) of £48m (2022: charge of £73m). Further details can be found in note 12

[2] Included within net financing are fair value changes on derivative contracts. Further details can be found in notes 2, 4 and 18

## Condensed consolidated statement of comprehensive income

For the year ended 31 December 2023

| | Notes | **2023 £m** | 2022 £m |
|---|---|---|---|
| **Profit/(loss) for the year** | | **2,404** | (1,274) |
| **Other comprehensive income/(expense) (OCI)** | | | |
| Actuarial movements in post-retirement schemes | 20 | **116** | (156) |
| Revaluation to fair value of other investments | 10 | **(4)** | (4) |
| Share of OCI of joint ventures and associates | | **1** | 2 |
| Related tax movements | | **(43)** | 89 |
| **Items that will not be reclassified to profit or loss** | | **70** | (69) |
| | | | |
| Foreign exchange translation differences on foreign operations | | **(226)** | 452 |
| Foreign exchange translation differences reclassified to income statement on disposal of businesses | 23 | **1** | 65 |
| Hedging reserves reclassified to income statement on disposal of businesses | | **–** | 111 |
| NCI disposed of on disposal of businesses | | **–** | 1 |
| Movement on fair values charged to cash flow hedge reserve (CFHR) | | **(82)** | (7) |
| Reclassified to income statement from cash flow hedge reserve (CFHR) | | **61** | (55) |
| Costs of hedging | | **–** | 10 |
| Share of OCI of joint ventures and associates | | **1** | – |
| Related tax movements | | **4** | 14 |
| **Items that will be reclassified to profit or loss** | | **(241)** | 591 |
| | | | |
| **Total other comprehensive (expense)/income** | | **(171)** | 522 |
| | | | |
| **Total comprehensive income/(expense) for the year** | | **2,233** | (752) |
| | | | |
| **Attributable to:** | | | |
| Ordinary shareholders | | **2,241** | (748) |
| NCI | | **(8)** | (4) |
| **Total comprehensive income/(expense) for the year** | | **2,233** | (752) |
| | | | |
| **Total comprehensive income/(expense) for the year attributable to ordinary shareholders arises from:** | | | |
| Continuing operations | | **2,241** | (673) |
| Discontinued operations | | **–** | (75) |
| **Total comprehensive income/(expense) for the year attributable to ordinary shareholders** | | **2,241** | (748) |

## Condensed consolidated balance sheet
At 31 December 2023

| | Notes | 2023 £m | 2022 £m |
|---|---|---|---|
| **ASSETS** | | | |
| Intangible assets | 7 | **4,009** | 4,098 |
| Property, plant and equipment | 8 | **3,728** | 3,936 |
| Right-of-use assets | 9 | **905** | 1,061 |
| Investments – joint ventures and associates | 10 | **479** | 422 |
| Investments – other | 10 | **31** | 36 |
| Other financial assets | 18 | **360** | 542 |
| Deferred tax assets | | **2,998** | 2,731 |
| Post-retirement scheme surpluses | 20 | **782** | 613 |
| **Non-current assets** | | **13,292** | 13,439 |
| Inventories | 11 | **4,848** | 4,708 |
| Trade receivables and other assets | 12 | **8,123** | 6,936 |
| Contract assets | 13 | **1,242** | 1,481 |
| Taxation recoverable | | **80** | 127 |
| Other financial assets | 18 | **34** | 141 |
| Short-term investments | | **–** | 11 |
| Cash and cash equivalents | 14 | **3,784** | 2,607 |
| **Current assets** | | **18,111** | 16,011 |
| **Assets held for sale** | 23 | **109** | – |
| **TOTAL ASSETS** | | **31,512** | 29,450 |
| | | | |
| **LIABILITIES** | | | |
| Borrowings and lease liabilities | 15 | **(809)** | (358) |
| Other financial liabilities | 18 | **(448)** | (1,016) |
| Trade payables and other liabilities | 17 | **(6,896)** | (6,983) |
| Contract liabilities | 13 | **(6,098)** | (4,825) |
| Current tax liabilities | | **(143)** | (104) |
| Provisions for liabilities and charges | 19 | **(532)** | (632) |
| **Current liabilities** | | **(14,926)** | (13,918) |
| Borrowings and lease liabilities | 15 | **(4,950)** | (5,597) |
| Other financial liabilities | 18 | **(1,983)** | (3,230) |
| Trade payables and other liabilities | 17 | **(1,927)** | (2,364) |
| Contract liabilities | 13 | **(8,438)** | (7,337) |
| Deferred tax liabilities | | **(330)** | (286) |
| Provisions for liabilities and charges | 19 | **(1,497)** | (1,701) |
| Post-retirement scheme deficits | 20 | **(1,035)** | (1,033) |
| **Non-current liabilities** | | **(20,160)** | (21,548) |
| **Liabilities associated with assets held for sale** | 23 | **(55)** | – |
| **TOTAL LIABILITIES** | | **(35,141)** | (35,466) |
| | | | |
| **NET LIABILITIES** | | **(3,629)** | (6,016) |
| | | | |
| **EQUITY** | | | |
| Called-up share capital | | **1,684** | 1,674 |
| Share premium | | **1,012** | 1,012 |
| Capital redemption reserve | | **167** | 166 |
| Hedging reserves | | **12** | 26 |
| Translation reserve | | **634** | 861 |
| Accumulated losses | | **(7,190)** | (9,789) |
| **Equity attributable to ordinary shareholders** | | **(3,681)** | (6,050) |
| Non-controlling interest (NCI) | | **52** | 34 |
| **TOTAL EQUITY** | | **(3,629)** | (6,016) |

## Condensed consolidated cash flow statement

For the year ended 31 December 2023

| | Notes | 2023 £m | Restated [1] 2022 £m |
|---|---|---|---|
| **Reconciliation of cash flows from operating activities** | | | |
| Operating profit from continuing operations | | **1,944** | 837 |
| Operating profit from discontinued operations | 23 | **–** | 86 |
| Operating profit | | **1,944** | 923 |
| Loss on disposal of property, plant and equipment | | **18** | 18 |
| Share of results of joint ventures and associates | 10 | **(173)** | (48) |
| Dividends received from joint ventures and associates | 10 | **54** | 73 |
| Amortisation and impairment of intangible assets | 7 | **272** | 287 |
| Depreciation and impairment of property, plant and equipment | 8 | **423** | 430 |
| Depreciation and impairment of right-of-use assets | 9 | **334** | 287 |
| Adjustment of amounts payable under residual value guarantees within lease liabilities | | **(10)** | (3) |
| Impairment of and other movements on investments | 10 | **–** | 75 |
| Decrease in provisions | | **(325)** | (197) |
| Increase in inventories | | **(200)** | (887) |
| Movement in trade receivables/payables and other assets/liabilities | | **(1,346)** | (56) |
| Movement in contract assets/liabilities | | **2,703** | 1,753 |
| Cash flows on other financial assets and liabilities held for operating purposes [2] | | **(845)** | (660) |
| Cash flows on settlement of excess derivative contracts [1, 3] | | **(389)** | (326) |
| Interest received | | **159** | 36 |
| Net defined benefit post-retirement cost recognised in profit before financing | 20 | **41** | 27 |
| Cash funding of defined benefit post-retirement schemes | 20 | **(69)** | (81) |
| Share-based payments | | **66** | 47 |
| **Net cash inflow from operating activities before taxation** | | **2,657** | 1,698 |
| Taxation paid | | **(172)** | (174) |
| **Net cash inflow from operating activities** | | **2,485** | 1,524 |
| **Cash flows from investing activities** | | | |
| Movement in other investments | | **1** | (5) |
| Additions of intangible assets | 7 | **(284)** | (237) |
| Disposals of intangible assets | 7 | **4** | 8 |
| Purchases of property, plant and equipment | | **(429)** | (359) |
| Disposals of property, plant and equipment | | **10** | 48 |
| Acquisition of businesses | 23 | **(14)** | – |
| Disposal of businesses (including cash flows on disposals in prior periods) | 23 | **(4)** | 1,398 |
| Movement in investments in joint ventures and associates | | **(9)** | (24) |
| Movement in short-term investments | | **11** | (3) |
| Cash flows on other financial assets and liabilities held for non-operating purposes | | **(12)** | – |
| **Net cash (outflow)/inflow from investing activities** | | **(726)** | 826 |
| **Cash flows from financing activities** | | | |
| Repayment of loans | | **(1)** | (2,024) |
| Proceeds from increase in loans | | **2** | 1 |
| Capital element of lease payments | | **(291)** | (218) |
| **Net cash flow from decrease in borrowings and lease liabilities** | | **(290)** | (2,241) |
| Interest paid | | **(196)** | (235) |
| Interest element of lease payments | | **(85)** | (68) |
| Fees paid on undrawn facilities | | **(52)** | (49) |
| Transactions with NCI [4] | | **77** | 57 |
| Dividends to NCI | | **(2)** | (3) |
| Redemption of C Shares | | **(1)** | (1) |
| **Net cash outflow from financing activities** | | **(549)** | (2,540) |
| **Change in cash and cash equivalents** | | **1,210** | (190) |
| **Cash and cash equivalents at 1 January** | | **2,605** | 2,639 |
| Exchange (losses)/gains on cash and cash equivalents | | **(84)** | 156 |
| **Cash and cash equivalents at 31 December [5]** | | **3,731** | 2,605 |

[1] The cash flow statement to 31 December 2022 has been represented as a result of a change in accounting policy to disclose cash flows on settlement of excess derivative contracts as cash flows from operating activities. As a result, cash flows from operating activities during the year to 31 December 2022 have reduced by £(326)m to £1,524m with the corresponding decrease in cash outflow from financing activities by £326m from £(2,866)m to £(2,540)m. There is no impact to the total change in cash and cash equivalents or to any alternative performance measures. See note 1 for further detail

[2] Predominantly relates to cash settled on derivative contracts held for operating purposes

[3] In 2020, the Group experienced a significant decline in its medium-term outlook and consequently a significant deterioration to its forecast net USD cash inflows. The Group took action to reduce the size of the USD hedge book by $11.8bn across 2020-2026 to reflect the fact that at that time, future operating cash flows were no longer forecast to materialise. To achieve the necessary reduction in the hedge book, a separate and distinct set of foreign exchange derivative instruments were entered into to buy $11.8bn. The associated cash outflow of these transactions is £1,674m and occurs over the period 2020-2026. This action had the impact of fixing the fair value of the over-hedged position and provided certainty over when the cash flows to settle the position would occur in future periods. During the year, the Group incurred a cash outflow of £389m (2022: £326m) and estimates that future cash outflows of £146m will be incurred in 2024 and £175m spread over 2025 and 2026

[4] Relates to NCI investment received in the year, in respect of Rolls-Royce SMR Limited

[5] The Group considers overdrafts (repayable on demand) and cash held for sale to be an integral part of its cash management activities and these are included in cash and cash equivalents for the purposes of the cash flow statement

# Condensed consolidated cash flow statement continued

For the year ended 31 December 2023

In deriving the condensed consolidated cash flow statement, movements in balance sheet line items have been adjusted for non-cash items. The cash flow in the year includes the sale of goods and services to joint ventures and associates – see note 22.

| | **2023 £m** | 2022 £m |
|---|---|---|
| **Reconciliation of movements in cash and cash equivalents to movements in net debt** | | |
| Change in cash and cash equivalents | **1,210** | (190) |
| Cash flow from decrease in borrowings and lease liabilities | **290** | 2,241 |
| Cash flow from (decrease)/increase in short-term investments | **(11)** | 3 |
| **Change in net debt resulting from cash flows** | **1,489** | 2,054 |
| Lease additions, modifications and other non-cash adjustments on borrowings and lease liabilities | **(191)** | (170) |
| Exchange gains/(losses) on net debt | **57** | (150) |
| Fair value adjustments | **7** | 70 |
| Debt disposed of on disposal of businesses | **–** | 53 |
| **Movement in net debt** | **1,362** | 1,857 |
| **Net debt at 1 January** | **(3,337)** | (5,194) |
| **Net debt at 31 December excluding the fair value of swaps** | **(1,975)** | (3,337) |
| Fair value of swaps hedging fixed rate borrowings | **23** | 86 |
| **Net debt at 31 December** | **(1,952)** | (3,251) |

The movement in net debt (defined by the Group as including the items shown below) is as follows:

| | **At 1 January £m** | **Funds flow £m** | **Net debt on disposal £m** | **Exchange differences £m** | **Fair value adjustments £m** | **Reclassifi-cations £m** | **Other movements £m** | **At 31 December £m** |
|---|---|---|---|---|---|---|---|---|
| **2023** | | | | | | | | |
| Cash at bank and in hand | **847** | **(79)** | **–** | **(29)** | **–** | **–** | **–** | **739** |
| Money market funds | **34** | **1,043** | **–** | **–** | **–** | **–** | **–** | **1,077** |
| Short-term deposits | **1,726** | **297** | **–** | **(55)** | **–** | **–** | **–** | **1,968** |
| **Cash and cash equivalents (per balance sheet)** | **2,607** | **1,261** | **–** | **(84)** | **–** | **–** | **–** | **3,784** |
| Overdrafts | **(2)** | **(51)** | **–** | **–** | **–** | **–** | **–** | **(53)** |
| **Cash and cash equivalents (per cash flow statement)** | **2,605** | **1,210** | **–** | **(84)** | **–** | **–** | **–** | **3,731** |
| **Short-term investments** | **11** | **(11)** | **–** | **–** | **–** | **–** | **–** | **–** |
| Other current borrowings | **(1)** | **(1)** | **–** | **–** | **(13)** | **(462)** | **(1)** | **(478)** |
| Non-current borrowings | **(4,105)** | **–** | **–** | **59** | **20** | **462** | **(4)** | **(3,568)** |
| Lease liabilities | **(1,847)** | **291** | **–** | **82** | **–** | **–** | **(186)** | **(1,660)** |
| **Financial liabilities** | **(5,953)** | **290** | **–** | **141** | **7** | **–** | **(191)** | **(5,706)** |
| **Net debt excluding fair value of swaps** | **(3,337)** | **1,489** | **–** | **57** | **7** | **–** | **(191)** | **(1,975)** |
| Fair value of swaps hedging fixed rate borrowings [1] | **86** | **–** | **–** | **(59)** | **(4)** | **–** | **–** | **23** |
| **Net debt** | **(3,251)** | **1,489** | **–** | **(2)** | **3** | **–** | **(191)** | **(1,952)** |
| 2022 | | | | | | | | |
| Cash at bank and in hand | 795 | 17 | – | 35 | – | – | – | 847 |
| Money market funds | 49 | (15) | – | – | – | – | – | 34 |
| Short-term deposits | 1,777 | (171) | – | 120 | – | – | – | 1,726 |
| Cash and cash equivalents (per balance sheet) | 2,621 | (169) | – | 155 | – | – | – | 2,607 |
| Cash and cash equivalents included within assets held for sale | 25 | (26) | – | 1 | – | – | – | – |
| Overdrafts | (7) | 5 | – | – | – | – | – | (2) |
| Cash and cash equivalents (per cash flow statement) | 2,639 | (190) | – | 156 | – | – | – | 2,605 |
| Short-term investments | 8 | 3 | – | – | – | – | – | 11 |
| Other current borrowings | (2) | 2 | – | (1) | – | – | – | (1) |
| Non-current borrowings | (6,023) | 2,000 | – | (125) | 72 | – | (29) | (4,105) |
| Borrowings included within liabilities held for sale | (59) | 21 | 40 | – | (2) | – | – | – |
| Lease liabilities | (1,744) | 217 | – | (179) | – | – | (141) | (1,847) |
| Lease liabilities included within liabilities held for sale | (13) | 1 | 13 | (1) | – | – | – | – |
| Financial liabilities | (7,841) | 2,241 | 53 | (306) | 70 | – | (170) | (5,953) |
| Net debt excluding fair value of swaps | (5,194) | 2,054 | 53 | (150) | 70 | – | (170) | (3,337) |
| Fair value of swaps hedging fixed rate borrowings [1] | 37 | – | – | 125 | (76) | – | – | 86 |
| Net debt | (5,157) | 2,054 | 53 | (25) | (6) | – | (170) | (3,251) |

[1] Fair value of swaps hedging fixed rate borrowings reflects the impact of derivatives on repayments of the principal amount of debt. Net debt therefore includes the fair value of derivatives included in fair value hedges (2023: £34m, 2022: £38m) and the element of fair value relating to exchange differences on the underlying principal of derivatives in cash flow hedges (2023: £(11)m, 2022: £48m)

# Condensed consolidated statement of changes in equity

For the year ended 31 December 2023

| | | Attributable to ordinary shareholders | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Notes | Share capital £m | Share premium £m | Capital redemption reserve £m | Hedging reserves [1] £m | Merger reserve £m | Translation reserve £m | Accum-ulated losses [2] £m | Total £m | NCI £m | Total equity £m |
| **At 1 January 2023** | | **1,674** | **1,012** | **166** | **26** | **–** | **861** | **(9,789)** | **(6,050)** | **34** | **(6,016)** |
| Profit/(loss) for the year | | **–** | **–** | **–** | **–** | **–** | **–** | **2,412** | **2,412** | **(8)** | **2,404** |
| Foreign exchange translation differences on foreign operations | | **–** | **–** | **–** | **–** | **–** | **(226)** | **–** | **(226)** | **–** | **(226)** |
| Foreign exchange translation differences reclassified to income statement on disposal of businesses | 23 | **–** | **–** | **–** | **–** | **–** | **1** | **–** | **1** | **–** | **1** |
| Actuarial movements on post-retirement schemes | 20 | **–** | **–** | **–** | **–** | **–** | **–** | **116** | **116** | **–** | **116** |
| Fair value movement on CFHR | | **–** | **–** | **–** | **(82)** | **–** | **–** | **–** | **(82)** | **–** | **(82)** |
| Reclassified to income statement from CFHR | | **–** | **–** | **–** | **61** | **–** | **–** | **–** | **61** | **–** | **61** |
| Revaluation to fair value of other investments | | **–** | **–** | **–** | **–** | **–** | **–** | **(4)** | **(4)** | **–** | **(4)** |
| OCI of joint ventures and associates | | **–** | **–** | **–** | **2** | **–** | **(1)** | **1** | **2** | **–** | **2** |
| Related tax movements | | **–** | **–** | **–** | **5** | **–** | **(1)** | **(43)** | **(39)** | **–** | **(39)** |
| **Total comprehensive (expense)/income for the year** | | **–** | **–** | **–** | **(14)** | **–** | **(227)** | **2,482** | **2,241** | **(8)** | **2,233** |
| Issue of ordinary shares | | **10** | **–** | **–** | **–** | **–** | **–** | **–** | **10** | **–** | **10** |
| Redemption of C shares | | **–** | **–** | **1** | **–** | **–** | **–** | **(1)** | **–** | **–** | **–** |
| Shares issued to employee share trust | | **–** | **–** | **–** | **–** | **–** | **–** | **(10)** | **(10)** | **–** | **(10)** |
| Share-based payments - direct to equity [3] | | **–** | **–** | **–** | **–** | **–** | **–** | **49** | **49** | **–** | **49** |
| Dividends to NCI | | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **–** | **(2)** | **(2)** |
| Transactions with NCI [4] | | **–** | **–** | **–** | **–** | **–** | **–** | **57** | **57** | **28** | **85** |
| Related tax movements | | **–** | **–** | **–** | **–** | **–** | **–** | **22** | **22** | **–** | **22** |
| **Other changes in equity in the year** | | **10** | **–** | **1** | **–** | **–** | **–** | **117** | **128** | **26** | **154** |
| **At 31 December 2023** | | **1,684** | **1,012** | **167** | **12** | **–** | **634** | **(7,190)** | **(3,681)** | **52** | **(3,629)** |
| | | | | | | | | | | | |
| **At 1 January 2022** | | 1,674 | 1,012 | 165 | (45) | 650 | 342 | (9,189) | (5,391) | 26 | (5,365) |
| Loss for the year | | – | – | – | – | – | – | (1,269) | (1,269) | (5) | (1,274) |
| Foreign exchange translation differences on foreign operations | | – | – | – | – | – | 452 | – | 452 | – | 452 |
| Hedging reserves reclassified to income statement on disposal of businesses | | – | – | – | 111 | – | – | – | 111 | – | 111 |
| Foreign exchange translation differences reclassified to income statement on disposal of businesses | | – | – | – | – | – | 65 | – | 65 | – | 65 |
| NCI disposed of on disposal of businesses | | – | – | – | – | – | – | – | – | 1 | 1 |
| Actuarial movements on post-retirement schemes | 20 | – | – | – | – | – | – | (156) | (156) | – | (156) |
| Fair value movement on CFHR | | – | – | – | (7) | – | – | – | (7) | – | (7) |
| Reclassified to income statement from CFHR | | – | – | – | (55) | – | – | – | (55) | – | (55) |
| Costs of hedging | | – | – | – | 10 | – | – | – | 10 | – | 10 |
| Revaluation to fair value of other investments | | – | – | – | – | – | – | (4) | (4) | – | (4) |
| OCI of joint ventures and associates | | – | – | – | – | – | – | 2 | 2 | – | 2 |
| Related tax movements | | – | – | – | 12 | – | 2 | 89 | 103 | – | 103 |
| **Total comprehensive expense for the year** | | – | – | – | 71 | – | 519 | (1,338) | (748) | (4) | (752) |
| Redemption of C Shares | | – | – | 1 | – | – | – | (1) | – | – | – |
| Share-based payments - direct to equity [3] | | – | – | – | – | – | – | 46 | 46 | – | 46 |
| Dividends to NCI | | – | – | – | – | – | – | – | – | (3) | (3) |
| Transactions with NCI [4] | | – | – | – | – | – | – | 42 | 42 | 15 | 57 |
| Transfer to realised profit [5] | | – | – | – | – | (650) | – | 650 | – | – | – |
| Related tax movements | | – | – | – | – | – | – | 1 | 1 | – | 1 |
| **Other changes in equity in the year** | | – | – | 1 | – | (650) | – | 738 | 89 | 12 | 101 |
| **At 31 December 2022** | | 1,674 | 1,012 | 166 | 26 | – | 861 | (9,789) | (6,050) | 34 | (6,016) |

## Condensed consolidated statement of changes in equity continued

For the year ended 31 December 2023

[1] Hedging reserves include the cash flow hedge reserve of £12m and the cost of hedging reserve of £nil (2022: £26m and £nil respectively)

[2] At 31 December 2023, 52,912,406 ordinary shares with a net book value of £22m (2022: 11,402,796 ordinary shares with a net book value of £27m) were held for the purpose of share-based payment plans and included in accumulated losses. During the year:

- 7,875,240 ordinary shares with a net book value of £15m (2022: 18,488,558 ordinary shares with a net book value of £39m) vested in share-based payment plans;
- the Company issued 49,100,000 (2022: none) new ordinary shares to the Group's share trust for its employee share-based payment plans with a net book value of £10m (2022: £nil); and
- the Company acquired none (2022: none) of its ordinary shares via reinvestment of dividends received on its own shares and purchased 284,850 (2022: 486,163) of its ordinary shares through purchases on the London Stock Exchange

[3] Share-based payments – direct to equity is the share-based payment charge for the year less the actual cost of vesting excluding those vesting from own shares and cash received on share-based schemes vesting

[4] Relates to NCI investment received in the year in respect of Rolls-Royce SMR Limited

[5] On disposal of ITP Aero on 15 September 2022, the premium recognised on issue of shares for the previous acquisition became realised on receipt of qualifying consideration. As such, the total merger reserve has been transferred to accumulated losses

# Notes to the Condensed Consolidated Financial Statements

## 1 Basis of preparation and accounting policies

### Reporting entity

Rolls-Royce Holdings plc (the 'Company') is a public company limited by shares incorporated under the Companies Act 2006 and domiciled in the UK. These Condensed Consolidated Financial Statements of the Company as at and for the year ended 31 December 2023 consist of the consolidation of the financial statements of the Company and its subsidiaries (together referred to as the 'Group') and include the Group's interest in jointly controlled and associated entities.

The Consolidated Financial Statements of the Group as at and for the year ended 31 December 2023 (2023 Annual Report) are available upon request from the Company Secretary, Rolls-Royce Holdings plc, Kings Place, 90 York Way, London, N1 9FX.

### Statement of compliance

These Condensed Consolidated Financial Statements have been prepared in accordance with UK adopted International Accounting Standards (IAS) and interpretations issued by the IFRS Interpretations Committee applicable to companies reporting under UK adopted IFRS. They do not include all the information required for full annual statements and should be read in conjunction with the 2023 Annual Report.

The Board of Directors approved the Condensed Consolidated Financial Statements on 22 February 2024. They are not statutory accounts within the meaning of section 435 of the Companies Act 2006.

The Group's Financial Statements for the year ended 31 December 2023 were approved by the Board on 22 February 2024. They have been reported on by the Group's auditors and will be delivered to the registrar of companies in due course. The report of the auditors was (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report, and (iii) did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

The comparative figures for the financial year 31 December 2022 have been extracted from the Group's statutory accounts for that financial year. The Board of Directors approved the Group financial statements on 23 February 2023. The report of the auditors was (i) unqualified, (ii) did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report, and (iii) did not contain a statement under section 498(2) or (3) of the Companies Act 2006.

### Revisions to IFRS applicable in 2023

IFRS 17 *Insurance Contracts*

IFRS 17, issued in May 2018, establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the Standard. The Standard is effective for years beginning on or after 1 January 2023 with a requirement to restate comparatives.

The Group has reviewed whether its arrangements meet the accounting definition of an insurance contract. While some contracts, including Civil Aerospace LTSAs, may transfer an element of insurance risk, they relate to warranty and service type agreements that are issued in connection with the Group's sales of its goods or services and therefore will remain accounted for under the existing revenue and provisions standards. The Directors have judged that such arrangements entered into after the original equipment sale remain sufficiently related to the sale of the Group's goods and services to allow the contracts to continue to be measured under IFRS 15 *Revenue from Contracts with Customers* and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

The Group has identified that the Standard will impact the results of its captive insurance company as it issues insurance contracts, however, since the contracts insure other group companies, there is no impact on the Condensed Consolidated Financial Statements.

The Group has assessed that its parent company guarantee arrangements in the form of financial or performance guarantees, that meet the IFRS 17 definition of insurance contracts, have no impact on the Consolidated Financial Statements of the Group for the year to 31 December 2023, however there could be an impact on individual sets of financial statements of companies within the Group.

The Directors are not aware of any other contracts where IFRS 17 would have an impact on the Condensed Consolidated Financial Statements.

Other

IAS 12 *Income Taxes* has been amended to incorporate the following revisions for 'Deferred Tax related to Assets and Liabilities arising from a Single Transaction' and 'International Tax Reform: Pillar Two Model Rules'. There is no material impact on the Group as a result of the amendments relating to Deferred Tax related to Assets and Liabilities arising from a Single Transaction.

The Group is within the scope of the OECD Pillar Two (Global Minimum Tax) model rules. The legislation has been substantively enacted in some of the material jurisdictions in which the Group operates, including the UK and Germany, where the rules will be effective from 1 January 2024. Further information can be found in note 5.

There are no other new standards or interpretations issued by the IASB that had a significant impact on the Condensed Consolidated Financial Statements. Standards and interpretations issued by the IASB are only applicable if endorsed by the UK.

## 1 Basis of preparation and accounting policies continued

### Change in accounting policy

At 31 December 2023, cash flows on settlement of excess derivatives have been reclassified from cash flows from financing activities to cash flows from operating activities in the cash flow statement as a result of a change in accounting policy. In line with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, a change in accounting policy can be made either where it is required by an IFRS or results in the financial statements providing reliable and more relevant information about the effects of transactions, other events or conditions on the entity's financial position, performance or cash flows.

The previous classification as cash flows from financing activities was based on the Directors' judgement of the economic nature of the activities as the cash flows relate to cash payments deferred in connection with the Group's action taken in 2020 to reduce the size of the USD hedge book by $11.8bn across 2020 to 2026. The Directors have reassessed their judgement in line with IAS 7 *Statement of Cash Flows* and have concluded that it would be more appropriate to classify these cash flows as cash flows from operating activities.

As a result of the above, cash flows from operating activities during the year to 31 December 2022 have reduced by £(326)m to £1,524m with a corresponding decrease in cash outflow from financing activities from £(2,866)m to £(2,540)m. There is no impact to the total change in cash and cash equivalents or to any alternative performance measures.

The above change resulted from a review which was prompted by an enquiry arising from a review of the Group's 2022 Annual Report and Accounts by the Corporate Reporting Review team of the Financial Reporting Council (FRC). The FRC review was part of a regular review and assessment of the quality of corporate reporting in the UK undertaken by the FRC. Further information regarding the review of the Group's 2022 Annual Report and Accounts is set out in the Audit Committee report in the 2023 Annual Report. The Group agreed to make the above change within its 2023 Annual Report and Accounts. The FRC review was limited to the published 2022 Annual Report; it did not benefit from a detailed understanding of underlying transactions and provides no assurance that the 2022 Annual Report is correct in all material respects.

### Post balance sheet events

The Group has taken the latest legal position in relation to any ongoing legal proceedings and reflected these in the 31 December 2023 results as appropriate.

## Climate change

In preparing the Condensed Consolidated Financial Statements, the Directors have continued to consider the impact of climate change, particularly in the context of the disclosures made in the Strategic Report within the 2023 Annual Report. The following specific points were considered:

- The Group continues to invest in: onsite renewable energy installations; the procurement of green energy for its facilities; and in energy efficiency improvements to reduce its overall energy demands and operating costs. An estimate of the investment required to meet these scope 1 and 2 emission improvements is included in the forecasts that support the Condensed Consolidated Financial Statements;
- The Group is enabling its customers to operate their products in a way that is compatible with low or net zero carbon emissions and has demonstrated that all the commercial aero engines it produces, and the most popular reciprocating engines (that represent 80% of the Power Systems product portfolio) are compatible for use on sustainable fuels;
- The Group has invested in delivering new products and solutions that can accelerate the global energy transition, including in battery energy storage solutions in Power Systems, and in small modular reactors (SMRs). Future investment required to deliver these technologies is included in the forecasts that support the Consolidated Financial Statements.

The Directors have considered the impact of climate change on a number of key estimates within the financial statements. The climate-related estimates and assumptions that have been considered to be key areas of judgement or sources of estimation uncertainty for the year ended 31 December 2023 are those relating to:

- long-term service agreement revenue recognition and onerous contract provision assumptions, such as the level of EFHs which recognises the future expectations of consumer and airline customer behaviour, and changes in costs due to carbon pricing and commodity price changes;
- the estimates of future cash flows considered for trigger assessments or used in impairment assessments, where applicable, of the carrying value of non-current assets (such as programme intangible assets and goodwill); and
- the estimates of future profitability used in assessing the recoverability of deferred tax assets in the UK (see note 5).

As details of what specific future intervention measures will be taken by governments are not yet available, carbon pricing has been used to quantify the potential impact of future policy changes on the Group. The approach is consistent with that disclosed in note 1 in the 2023 Annual Report.

There have been no significant changes to assumptions, including the potential impact of carbon prices on the Group's cost base, since the year ended 31 December 2022. This is consistent with the assessment that climate change is not expected to have a significant impact on the Group's going concern assessment to August 2025, nor on the viability of the Group over the next five years.

## 1 Basis of preparation and accounting policies continued

## Going concern

***Overview***

In accordance with the requirements of the 2018 UK Corporate Governance Code, the Directors have assessed the prospects of the Group, taking into account its current position, the Group's principal risks and the Group's mid-term forecasts that considered a range of internal and external factors as part of the strategic review to support setting the Group's new mid-term targets which are set out on pages 10 to 12 of the 2023 Annual Report.

The Strategic Report in the 2023 Annual Report on pages 10 to 12 sets out the activities of the Group and the factors likely to impact its future development, performance and position.

The Financial Review on pages 19 to 23 of the 2023 Annual Report sets out the financial position of the Group, its cash flows, liquidity position and the Group's capital framework. The notes to the accounts include the objectives, policies and procedures over financial risk management including financial instruments and hedging activities, exposure to credit risk, liquidity risk, interest rate risk and commodity price risk.

In adopting the going concern basis for preparing the Consolidated and Company Financial Statements, the Directors have undertaken a review of the Group's cash flow forecasts and available liquidity, along with consideration of possible risks and uncertainties over an 18-month period from the date of this report to August 2025. The Directors have determined that an 18-month period is an appropriate timeframe over which to assess going concern as it considers the Group's short to medium-term cash flow forecasts and available liquidity.

***Forecasts***

Recognising the challenges of reliably estimating and forecasting the impact of external factors on the Group, the Directors have considered two forecasts in their assessment of going concern, along with a likelihood assessment of these forecasts. The base case forecast reflects the Directors current expectations of future trading. A stressed downside forecast has also been modelled which envisages a 'stressed' or 'downside' situation that is considered severe but plausible. Both forecasts have been modelled over an 18-month period.

Industry forecasts predict a return to 2019 large engine flying levels in 2024, which is reflected in the Group's base case forecast. Macro-economic assumptions have been modelled using externally available data based on the most likely forecasts with general inflation at around 2%-3%, wage inflation at an average of 3%-5%, interest rates at around 3%-4% and GDP growth at around 2%-3%.

The stressed downside forecast assumes Civil Aerospace large engine flying hours remain at average fourth quarter 2023 levels throughout the 18-month period to August 2025, reflecting slower GDP growth in this forecast when compared with the base case. It also assumes a more pessimistic view of general inflation at around 1%-2% higher than the base case covering a broad range of costs including energy, commodities and jet fuel. Wage inflation in the stressed downside is 1%-5% higher than the base case and interest rates in the stressed downside are 1%-2% higher than the base case. These macro-economic pressures have been modelled across the whole going concern period. The stressed downside also considers lower demand as a result of slower market growth and potential output risks associated with increasing volumes and possible ongoing supply chain challenges.

The future impact of climate change on the Group has been considered through climate scenarios. The climate scenarios modelled do not have a material impact on either the base case or stressed downside forecast over the 18-month period to August 2025.

***Liquidity and borrowings***

During 2023, the Group cancelled a £1bn undrawn UKEF-supported loan facility that was due to mature in March 2026 and a £1bn undrawn bank loan facility due to mature in January 2024. The £2.5bn undrawn revolving credit facility that was due to mature in April 2025 was refinanced in November 2023 with the new facility having a term of three years with the banks having the option to extend with two one-year extension options (3+1+1).

At 31 December 2023, the Group had liquidity of £7.2bn including cash and cash equivalents of £3.7bn and undrawn facilities of £3.5bn. The 18-month going concern period includes the maturity of a €550m bond repayable in May 2024 which the Group does not intend to refinance given the Group's cash and liquidity position, our assessment of the Group's cash flow forecasts and available liquidity over the 18-month period.

Based on borrowing facilities available at the date of this report the Group's committed borrowing facilities at 31 December 2023 and 31 August 2025 are set out below. None of the facilities are subject to any financial covenants or rating triggers which could accelerate repayment.

| £m | 31 December 2023 | 31 August 2025 |
|---|---|---|
| Issued bond notes [1] | 3,995 | 3,511 |
| UKEF £1bn loan (undrawn) [2] | 1,000 | 1,000 |
| Revolving credit facility (undrawn) [3] | 2,500 | 2,500 |
| **Total committed borrowing facilities** | 7,495 | 7,011 |

[1] The value of issued bond notes reflects the impact of derivatives on repayments of the principal amount of debt. The bonds mature by May 2028

[2] The £1bn UKEF sustainability-linked loan matures in September 2027 (currently undrawn)

[3] The refinanced £2.5bn revolving credit facility matures in November 2026 (currently undrawn)

Taking into account the maturity of these borrowing facilities, the Group has committed facilities of at least £7bn available throughout the period to 31 August 2025. The next debt maturity is a $1bn bond that is due to be repaid in October 2025, which is outside the 18-month going concern period.

***Conclusion***

After reviewing the current liquidity position and the cash flow forecasts modelled under both the base case and stressed downside, the Directors consider that the Group has sufficient liquidity to continue in operational existence for a period of at least 18 months from the date of this report and are therefore satisfied that it is appropriate to adopt the going concern basis of accounting in preparing the Consolidated and Company financial statements.

## 1 Basis of preparation and accounting policies continued

**Key areas of judgement and sources of estimation uncertainty**

The determination of the Group's accounting policies requires judgement. The subsequent application of these policies requires estimates and the actual outcome may differ from that calculated. The key areas of judgement and sources of estimation uncertainty as at 31 December 2023, that were assessed as having a significant risk of causing material adjustments to the carrying amount of assets and liabilities, are set out in note 1 to the Consolidated Financial Statements in the 2023 Annual Report and are summarised below. Sensitivities for key sources of estimation uncertainty are disclosed where this is appropriate and practical.

| Area | Key judgements | Key sources of estimation uncertainty | Sensitivities performed |
|---|---|---|---|
| Revenue recognition and contract assets and liabilities | Whether Civil Aerospace OE and aftermarket contracts should be combined.<br>How performance on long-term aftermarket contracts should be measured.<br>Whether long-term aftermarket contracts contain a significant financing component.<br>Whether any costs should be treated as wastage.<br>Whether the Civil Aerospace LTSA contracts are warranty style contacts entered into in connection with OE sales and therefore can be accounted for under IFRS 15.<br>Whether sales of spare engines to joint ventures are at fair value.<br>When revenue should be recognised in relation to spare engine sales. | Estimates of future revenue, including customer pricing, and costs of long-term contractual arrangements, including the impact of climate change. | Based upon the stage of completion of all large engine LTSA contracts within Civil Aerospace as at 31 December 2023, the following changes in estimate would result in catch-up adjustments being recognised in the period in which the estimates change (at underlying FX rates):<br>- A change in forecast EFHs of 1% over the remaining term of the contracts would impact LTSA income and to a lesser extent costs, resulting in an impact of around £20m.<br>- A 2% increase or decrease in our pricing to customers over the life of the contracts would lead to a revenue catch-up adjustment in the next 12 months of around £280m.<br>- A 2% increase or decrease in shop visit costs over the life of the contracts would lead to a revenue catch-up adjustment in the next 12 months of around £80m. |
| Risk and revenue sharing arrangements (RRSAs) | Determination of the nature of entry fees received. | | |
| Taxation | | Estimates necessary to assess whether it is probable that sufficient suitable taxable profits will arise in the UK to utilise the deferred tax assets recognised. | A 5% change in margin or shop visits (which could be driven by fewer EFHs as a result of climate change) would result in an increase/decrease in the deferred tax asset in respect of UK losses of around £90m.<br>If only 90% of assumed future cost increases from climate change are passed on to customers, this would result in a decrease in the deferred tax asset of around £10m, and if the potential impact of carbon prices on the Group's cost base was to double, the recoverable value of deferred tax assets would decrease by around £50m. |
| Research and development | Determination of the point in time where costs incurred on an internal programme development meet the criteria for capitalisation.<br>Determination of the basis for amortising capitalised development costs. | | |
| Leases | Determination of the lease term. | | |
| Impairment of non-current assets | Determination of cash-generating units for assessing impairment of goodwill.<br>Whether there are indicators of potential reversal of previous impairments of programme-related intangible assets | | |

| Area | Key judgements | Key sources of estimation uncertainty | Sensitivities performed |
|---|---|---|---|
| Provisions | Whether any costs should be treated as wastage.<br><br>Whether the criteria to recognise a transformation and restructuring provisions have been met | Estimates of the time to incorporate a modified and certified high-pressure turbine (HPT) blade into the fleet to resolve technical issues on the Trent 1000, and the implications of this on forecast future costs when assessing onerous contracts.<br><br>Estimates of the future revenues and costs to fulfil onerous contracts.<br><br>Assumptions implicit within the calculation of discount rates. | A 12-month delay in the availability of the modified HPT blade could lead to a £30-50m charge in relation to the Trent 1000 programme.<br><br>An increase in Civil Aerospace large engines estimates of LTSA costs of 1% over the remaining term of the contracts could lead to a £90-120m increase in the provision for contract losses across all programmes.<br><br>A 1% change in the discount rates used could lead to around a £70-80m change in the onerous contract provision. |
| Post-retirement benefits | | Estimates of the assumptions for valuing the net defined benefit obligation. | A reduction in the discount rate of 0.25% from 4.50% could lead to an increase in the defined benefit obligations of the RR UK Pension Fund (RRUKPF) of approximately £185m. This would be expected to be broadly offset by changes in the value of scheme assets, as the scheme's investment policies are designed to mitigate this risk.<br><br>An increase in the assumed rate of inflation of 0.25% (RPI of 3.30% and CPI of 2.85%) could lead to an increase in the defined benefit obligations of the RRUKPF of approximately £75m.<br><br>A one-year increase in life expectancy from 20.8 years (male aged 65) and from 21.5 years (male aged 45) would increase the defined benefit obligations of the RRUKPF by approximately £155m. |

## 2 Segmental analysis

The analysis by segment is presented in accordance with IFRS 8 *Operating Segments*, on the basis of those segments whose operating results are regularly reviewed by the Board (who acts as the Chief Operating Decision Maker as defined by IFRS 8). The Group's four divisions are set out below.

| | | |
|---|---|---|
| Civil Aerospace | - | development, manufacture, marketing and sales of commercial aero engines and aftermarket services |
| Defence | - | development, manufacture, marketing and sales of military aero engines, naval engines, submarine nuclear power plants and aftermarket services |
| Power Systems | - | development, manufacture, marketing and sales of integrated solutions for onsite power and propulsion |
| New Markets | - | development, manufacture and sales of small modular reactor (SMR) and new electrical power solutions |

Other businesses include the trading results of the UK Civil Nuclear business.

**Underlying results**

The Group presents the financial performance of the divisions in accordance with IFRS 8 and consistently with the basis on which performance is communicated to the Board each month.

Underlying results are presented by recording all relevant revenue and cost of sales transactions at the average exchange rate achieved on effective settled derivative contracts in the period that the cash flow occurs. The impact of the revaluation of monetary assets and liabilities (other than lease liabilities) using the exchange rate that is expected to be achieved by the use of the effective hedge book is recorded within underlying cost of sales. Underlying financing excludes the impact of revaluing monetary assets and liabilities to period end exchange rates. Lease liabilities are not revalued to reflect the expected exchange rates due to their multi-year remaining term, the Directors believe that doing so would not be the most appropriate basis to measure the in-year performance. Transactions between segments are presented on the same basis as underlying results and eliminated on consolidation. Unrealised fair value gains/(losses) on foreign exchange contracts, which are recognised as they arise in the statutory results, are excluded from underlying results. To the extent that the previously forecast transactions are no longer expected to occur, an appropriate portion of the unrealised fair value gain/(loss) on foreign exchange contracts is recorded immediately in the underlying results.

Amounts receivable/(payable) on interest rate swaps which are not designated as hedge relationships for accounting purposes are reclassified from fair value movement on a statutory basis to interest receivable/(payable) on an underlying basis, as if they were in an effective hedge relationship.

In the year to 31 December 2023, the Group was a net seller of USD at an achieved exchange rate of GBP:USD 1.50 (2022: 1.50) based on the USD hedge book.

In 2020, the Group experienced a significant decline in its medium-term outlook and consequently a significant deterioration to its forecast net USD cash inflows. The Group took action to reduce the size of the USD hedge book by $11.8bn across 2020-2026 to reflect the fact that, at that time, future operating cash flows were no longer forecast to materialise. An underlying charge of £1.7bn was recognised within the underlying finance costs in 2020 and the associated cash settlement costs occur over the period 2020-2026. The derivatives relating to this underlying charge have been subsequently excluded from the hedge book, and therefore are also excluded from the calculation of the average exchange rate achieved in the current and future periods.

Underlying performance also excludes the following:

- the effect of acquisition accounting and business disposals;
- impairment of goodwill and other non-current and current assets where the reasons for the impairment are outside of normal operating activities;
- exceptional items; and
- certain other items which are market driven and outside of the control of management.

Subsequent changes in items excluded from underlying performance recognised in a prior period will also be excluded from underlying performance. All other changes will be recognised within underlying performance.

*Acquisition accounting, business disposals and impairment*

The Group exclude these from underlying results so that the current period and comparative results are directly comparable.

*Exceptional items*

Items are classified as exceptional where the Directors believe that presentation of the results in this way is useful in providing an understanding of the Group's financial performance. Exceptional items are identified by virtue of their size, nature or incidence.

In determining whether an event or transaction is exceptional, the Directors consider quantitative as well as qualitative factors such as the frequency or predictability of occurrence. Examples of exceptional items include one-time costs and charges in respect of aerospace programmes, costs of exceptional transformation and restructuring programmes and one-time past service charges and credits on post-retirement schemes.

Exceptional items are not allocated to segments and may not be comparable to similarly titled measures used by other companies.

*Other items*

The financing component of the defined benefit pension scheme cost is determined by market conditions and has therefore been included as a reconciling difference between underlying and statutory performance.

The tax effects of adjustments above are excluded from the underlying tax charge. Changes in tax rates are excluded from the underlying tax charge. In addition, changes in the amount of recoverable deferred tax recognised are excluded from the underlying results to the extent that their recognition or derecognition was not originally recorded within the underlying results.

## 2 Segmental analysis continued

The following analysis sets out the results of the Group's businesses on the basis described above and also includes a reconciliation of the underlying results to those reported in the Condensed Consolidated Income Statement.

| | Civil Aerospace £m | Defence £m | Power Systems £m | New Markets £m | Other businesses £m | Corporate and Inter-segment [1] £m | Total underlying £m |
|---|---|---|---|---|---|---|---|
| **Year ended 31 December 2023** | | | | | | | |
| Underlying revenue from sale of original equipment | **2,703** | **1,766** | **2,661** | **2** | **12** | **–** | **7,144** |
| Underlying revenue from aftermarket services | **4,645** | **2,311** | **1,307** | **2** | **–** | **–** | **8,265** |
| **Total underlying revenue** | **7,348** | **4,077** | **3,968** | **4** | **12** | **–** | **15,409** |
| Gross profit/(loss) | **1,394** | **804** | **1,050** | **1** | **(15)** | **(3)** | **3,231** |
| Commercial and administrative costs | **(354)** | **(173)** | **(456)** | **(24)** | **–** | **(57)** | **(1,064)** |
| Research and development costs | **(343)** | **(72)** | **(187)** | **(137)** | **–** | **–** | **(739)** |
| Share of results of joint ventures and associates | **153** | **3** | **6** | **–** | **–** | **–** | **162** |
| **Underlying operating profit/(loss)** | **850** | **562** | **413** | **(160)** | **(15)** | **(60)** | **1,590** |

| | Civil Aerospace £m | Defence £m | Power Systems £m | New Markets £m | Other businesses £m | Corporate and Inter-segment [1] £m | Total underlying £m |
|---|---|---|---|---|---|---|---|
| Year ended 31 December 2022 | | | | | | | |
| Underlying revenue from sale of original equipment | 1,982 | 1,634 | 2,187 | 1 | – | (5) | 5,799 |
| Underlying revenue from aftermarket services | 3,704 | 2,026 | 1,160 | 2 | – | – | 6,892 |
| Total underlying revenue | 5,686 | 3,660 | 3,347 | 3 | – | (5) | 12,691 |
| Gross profit/(loss) | 853 | 726 | 918 | (1) | (29) | 10 | 2,477 |
| Commercial and administrative costs | (371) | (174) | (441) | (23) | (2) | (51) | (1,062) |
| Research and development costs | (452) | (122) | (204) | (108) | – | – | (886) |
| Share of results of joint ventures and associates | 113 | 2 | 8 | – | – | – | 123 |
| Underlying operating profit/(loss) | 143 | 432 | 281 | (132) | (31) | (41) | 652 |

[1] Corporate and Inter-segment consists of costs that are not attributable to a specific segment and consolidation adjustments

## 2 Segmental analysis continued

### Reconciliation to statutory results

| | Total underlying £m | Underlying adjustments and adjustments to foreign exchange £m | Group statutory results £m |
|---|---|---|---|
| **Year ended 31 December 2023** | | | |
| **Continuing operations** | | | |
| Revenue from sale of original equipment | **7,144** | **491** | **7,635** |
| Revenue from aftermarket services | **8,265** | **586** | **8,851** |
| **Total revenue** | **15,409** | **1,077** | **16,486** |
| Gross profit | **3,231** | **389** | **3,620** |
| Commercial and administrative costs | **(1,064)** | **(46)** | **(1,110)** |
| Research and development costs | **(739)** | **–** | **(739)** |
| Share of results of joint ventures and associates | **162** | **11** | **173** |
| **Operating profit** | **1,590** | **354** | **1,944** |
| Gain arising on the disposal of businesses | **–** | **1** | **1** |
| **Profit before financing and taxation** | **1,590** | **355** | **1,945** |
| Net financing | **(328)** | **810** | **482** |
| **Profit before taxation** | **1,262** | **1,165** | **2,427** |
| Taxation | **(120)** | **97** | **(23)** |
| **Profit for the year** | **1,142** | **1,262** | **2,404** |
| | | | |
| **Attributable to:** | | | |
| Ordinary shareholders | **1,150** | **1,262** | **2,412** |
| NCI | **(8)** | **–** | **(8)** |
| | | | |
| Year ended 31 December 2022 | | | |
| Continuing operations | | | |
| Revenue from sale of original equipment | 5,799 | 474 | 6,273 |
| Revenue from aftermarket services | 6,892 | 355 | 7,247 |
| Total revenue | 12,691 | 829 | 13,520 |
| Gross profit | 2,477 | 280 | 2,757 |
| Commercial and administrative costs | (1,062) | (15) | (1,077) |
| Research and development costs | (886) | (5) | (891) |
| Share of results of joint ventures and associates | 123 | (75) | 48 |
| Operating profit | 652 | 185 | 837 |
| Gain arising on the disposal of businesses | – | 81 | 81 |
| Profit before financing and taxation | 652 | 266 | 918 |
| Net financing | (446) | (1,974) | (2,420) |
| Profit/(loss) before taxation | 206 | (1,708) | (1,502) |
| Taxation | (48) | 356 | 308 |
| Profit/(loss) for the year from continuing operations | 158 | (1,352) | (1,194) |
| Discontinued operations [1] | 67 | (147) | (80) |
| Profit/(loss) for the year | 225 | (1,499) | (1,274) |
| | | | |
| Attributable to: | | | |
| Ordinary shareholders | 230 | (1,499) | (1,269) |
| NCI | (5) | – | (5) |

[1] Discontinued operations relate to the results of ITP Aero and are presented net of intercompany trading eliminations and related consolidation adjustments

## 2 Segmental analysis continued

### Disaggregation of revenue from contracts with customers

| Analysis by type and basis of recognition | Civil Aerospace £m | Defence £m | Power Systems £m | New Markets £m | Other businesses £m | Corporate and Inter-segment £m | Total underlying £m |
|---|---|---|---|---|---|---|---|
| **Year ended 31 December 2023** | | | | | | | |
| Original equipment recognised at a point in time | **2,703** | **632** | **2,611** | **2** | **–** | **–** | **5,948** |
| Original equipment recognised over time | **–** | **1,134** | **50** | **–** | **12** | **–** | **1,196** |
| Aftermarket services recognised at a point in time | **1,227** | **854** | **1,206** | **2** | **–** | **–** | **3,289** |
| Aftermarket services recognised over time | **3,335** | **1,457** | **101** | **–** | **–** | **–** | **4,893** |
| **Total underlying customer contract revenue** | **7,265** | **4,077** | **3,968** | **4** | **12** | **–** | **15,326** |
| Other underlying revenue [1] | **83** | **–** | **–** | **–** | **–** | **–** | **83** |
| **Total underlying revenue [2]** | **7,348** | **4,077** | **3,968** | **4** | **12** | **–** | **15,409** |
| Year ended 31 December 2022 | | | | | | | |
| Original equipment recognised at a point in time | 1,982 | 689 | 2,155 | 1 | – | (5) | 4,822 |
| Original equipment recognised over time | – | 945 | 32 | – | – | – | 977 |
| Aftermarket services recognised at a point in time | 865 | 769 | 1,076 | 2 | – | – | 2,712 |
| Aftermarket services recognised over time | 2,772 | 1,257 | 84 | – | – | – | 4,113 |
| Total underlying customer contract revenue | 5,619 | 3,660 | 3,347 | 3 | – | (5) | 12,624 |
| Other underlying revenue [1] | 67 | – | – | – | – | – | 67 |
| Total underlying revenue [2] | 5,686 | 3,660 | 3,347 | 3 | – | (5) | 12,691 |

[1] Includes leasing revenue

[2] Includes £(136)m, of which £(104)m relates to Civil LTSA contracts, (2022: £367m, of which £360m relates to Civil LTSA contracts) of revenue recognised in the year relating to performance obligations satisfied in previous years

| | Total underlying £m | Underlying adjustments and adjustments to foreign exchange £m | Group statutory results [1] £m |
|---|---|---|---|
| **Year ended 31 December 2023** | | | |
| Original equipment recognised at a point in time | **5,948** | **491** | **6,439** |
| Original equipment recognised over time | **1,196** | **–** | **1,196** |
| Aftermarket services recognised at a point in time | **3,289** | **186** | **3,475** |
| Aftermarket services recognised over time | **4,893** | **382** | **5,275** |
| **Total customer contract revenue** | **15,326** | **1,059** | **16,385** |
| Other revenue | **83** | **18** | **101** |
| **Total revenue** | **15,409** | **1,077** | **16,486** |
| Year ended 31 December 2022 | | | |
| Original equipment recognised at a point in time | 4,822 | 474 | 5,296 |
| Original equipment recognised over time | 977 | – | 977 |
| Aftermarket services recognised at a point in time | 2,712 | 164 | 2,876 |
| Aftermarket services recognised over time | 4,113 | 176 | 4,289 |
| Total customer contract revenue | 12,624 | 814 | 13,438 |
| Other revenue | 67 | 15 | 82 |
| Total revenue | 12,691 | 829 | 13,520 |

[1] During the year to 31 December 2023, revenue recognised within Civil Aerospace, Defence and Power Systems of £1,766m (2022: £1,788m) was received from a single customer

## 2 Segmental analysis continued

### Underlying adjustments

| | | 2023 | | | | 2022 | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | **Revenue £m** | **Profit before financing £m** | **Net financing £m** | **Taxation £m** | Revenue £m | Profit before financing £m | Net financing £m | Taxation £m |
| **Underlying performance** | | **15,409** | **1,590** | **(328)** | **(120)** | 12,691 | 652 | (446) | (48) |
| Impact of foreign exchange differences as a result of hedging activities on trading transactions [1] | A | **1,077** | **469** | **394** | **(210)** | 829 | 267 | (358) | (81) |
| Unrealised fair value changes on derivative contracts held for trading [2] | A | **–** | **6** | **514** | **(130)** | – | (3) | (1,768) | 451 |
| Unrealised fair value change to derivative contracts held for financing [3] | A | **–** | **–** | **7** | **(2)** | – | – | 191 | (47) |
| Exceptional programme credits/(charges) [4] | B | **–** | **21** | **–** | **(5)** | – | 69 | (3) | – |
| Exceptional transformation and restructuring charges/(credits) [5] | B | **–** | **(102)** | **–** | **25** | – | (47) | – | 4 |
| Impairment reversals/(charges) [6] | C | **–** | **8** | **–** | **(2)** | – | (65) | – | – |
| Effect of acquisition accounting [7] | C | **–** | **(50)** | **–** | **12** | – | (58) | – | 9 |
| Other [8] | D | **–** | **2** | **(105)** | **24** | – | 22 | (36) | (71) |
| Gains arising on the disposals of businesses | C | **–** | **1** | **–** | **–** | – | 81 | – | (2) |
| Recognition of deferred tax assets [9] | D | **–** | **–** | **–** | **385** | – | – | – | 93 |
| **Total underlying adjustments** | | **1,077** | **355** | **810** | **97** | 829 | 266 | (1,974) | 356 |
| **Statutory performance per condensed consolidated income statement** | | **16,486** | **1,945** | **482** | **(23)** | 13,520 | 918 | (2,420) | 308 |

A – FX and derivatives, B – Exceptional, C – M&A and impairment, D – Other

[1] The impact of measuring revenues and costs at the average exchange rate during the year and the impact of valuation of assets and liabilities using the year end exchange rate rather than the achieved rate or the exchange rate that is expected to be achieved by the use of the hedge book increased statutory revenues by £1,077m (2022: £829m) and increased profit before financing and taxation by £469m (2022: £267m). Underlying financing excludes the impact of revaluing monetary assets and liabilities at the year end exchange rate

[2] The underlying results exclude the fair value changes on derivative contracts held for trading. These fair value changes are subsequently recognised in the underlying results when the contracts are settled

[3] Includes net fair value gain of £1m (2022: gains of £190m) on any interest rate swaps not designated into hedging relationships for accounting purposes

[4] During the year to 31 December 2023, £21m of Trent 1000 wastage costs provision previously recognised in respect of estimated costs to settle obligations have been reversed to reflect the current status of claims in respect of the Trent 1000 technical issues which were identified in 2019

[5] During the year to 31 December 2023, the Group incurred total transformation and restructuring related charges of £102m (2022: £47m). In 2023, the Group announced a major multi-year transformation programme which consists of seven workstreams that are set out in the 2022 Annual Report. During the year, £88m was incurred in relation to this multi-year programme, comprising £45m for advisory fees and transformation office costs, £37m related to impairments and write-offs and £6m related to severance costs. In the year to 31 December 2023, a £14m (2022: £47m) charge related to initiatives to enable restructuring under a previous programme

[6] The Group has assessed the carrying value of its assets. Further details are provided in notes 7,8 and 9

[7] The effect of acquisition accounting includes the amortisation of intangible assets arising on previous acquisitions

[8] Includes interest received of £83m (2022: interest received of £14m) on interest rate swaps which are not designated into hedge relationships for statutory purposes from interest payable on an underlying basis to fair value movement and £2m (2022: credit of £22m) of past-service credit on defined benefit schemes

[9] Relates to the recognition of deferred tax assets on UK tax losses of £328m and foreign exchange derivatives of £57m. The £93m recognised in 2022 relates to foreign exchange derivatives

## 2 Segmental analysis continued

**Balance sheet analysis**

| | Civil Aerospace £m | Defence £m | Power Systems £m | New Markets £m | Total reportable segments £m |
|---|---|---|---|---|---|
| **At 31 December 2023** | | | | | |
| Segment assets | **17,718** | **3,517** | **3,814** | **115** | **25,164** |
| Interests in joint ventures and associates | **444** | **7** | **28** | **–** | **479** |
| Segment liabilities | **(24,447)** | **(3,376)** | **(1,765)** | **(88)** | **(29,676)** |
| **Net (liabilities)/assets** | **(6,285)** | **148** | **2,077** | **27** | **(4,033)** |
| | | | | | |
| At 31 December 2022 | | | | | |
| Segment assets | 17,537 | 3,430 | 4,084 | 135 | 25,186 |
| Interests in joint ventures and associates | 387 | 4 | 31 | – | 422 |
| Segment liabilities | (25,357) | (3,146) | (1,802) | (97) | (30,402) |
| Net (liabilities)/assets | (7,433) | 288 | 2,313 | 38 | (4,794) |

**Reconciliation to the balance sheet**

| | 2023 £m | 2022 £m |
|---|---|---|
| Total reportable segment assets (excluding assets held for sale) | **25,164** | 25,186 |
| Other businesses | **8** | 19 |
| Corporate and Inter-segment | **(2,010)** | (2,460) |
| Interests in joint ventures and associates | **479** | 422 |
| Assets held for sale | **109** | – |
| Cash and cash equivalents and short-term investments | **3,784** | 2,618 |
| Fair value of swaps hedging fixed rate borrowings | **118** | 194 |
| Deferred and income tax assets | **3,078** | 2,858 |
| Post-retirement scheme surpluses | **782** | 613 |
| **Total assets** | **31,512** | 29,450 |
| Total reportable segment liabilities (excluding liabilities held for sale) | **(29,676)** | (30,402) |
| Other businesses | **(58)** | (34) |
| Corporate and Inter-segment | **2,010** | 2,456 |
| Liabilities associated with assets held for sale | **(55)** | – |
| Borrowings and lease liabilities | **(5,759)** | (5,955) |
| Fair value of swaps hedging fixed rate borrowings | **(95)** | (108) |
| Deferred and income tax liabilities | **(473)** | (390) |
| Post-retirement scheme deficits | **(1,035)** | (1,033) |
| **Total liabilities** | **(35,141)** | (35,466) |
| **Net liabilities** | **(3,629)** | (6,016) |

## 3 Research and development

| | 2023 £m | 2022 £m |
|---|---|---|
| Gross research and development costs | **(1,390)** | (1,287) |
| Contributions and fees [1] | **548** | 359 |
| Expenditure in the year | **(842)** | (928) |
| Capitalised as intangible assets | **192** | 131 |
| Amortisation and impairment of capitalised costs | **(89)** | (94) |
| **Net cost recognised in the income statement** | **(739)** | (891) |
| Underlying adjustments relating to the effects of acquisition accounting and foreign exchange | **–** | 5 |
| **Net underlying cost recognised in the income statement** | **(739)** | (886) |

[1] Includes £531m (2022: £350m) of government funding

## 4 Net financing

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | **Statutory £m** | **Underlying [1] £m** | Statutory £m | Underlying [1] £m |
| Interest receivable and similar income [2] | **164** | **164** | 35 | 35 |
| Net fair value gains on foreign currency contracts | **574** | **–** | – | – |
| Net fair value gains on non-hedge accounted interest rate swaps [3] | **1** | **–** | 190 | – |
| Net fair value gains on commodity contracts | **–** | **–** | 106 | – |
| Financing on post-retirement scheme surpluses | **30** | **–** | 24 | – |
| Net foreign exchange gains | **394** | **–** | – | – |
| **Financing income** | **1,163** | **164** | 355 | 35 |
| Interest payable | **(369)** | **(275)** | (343) | (320) |
| Net fair value losses on foreign currency contracts | **–** | **–** | (1,875) | – |
| Foreign exchange differences and changes in forecast payments relating to financial RRSAs | **(1)** | **–** | (7) | – |
| Net fair value losses on commodity contracts | **(60)** | **–** | – | – |
| Financing on post-retirement scheme deficits | **(42)** | **–** | (26) | – |
| Net foreign exchange losses | **–** | **–** | (358) | – |
| Cost of undrawn facilities | **(57)** | **(57)** | (61) | (61) |
| Other financing charges | **(152)** | **(160)** | (105) | (100) |
| **Financing costs** | **(681)** | **(492)** | (2,775) | (481) |
| **Net financing income/(costs)** | **482** | **(328)** | (2,420) | (446) |
| **Analysed as:** | | | | |
| Net interest payable | **(205)** | **(111)** | (308) | (285) |
| Net fair value gains/(losses) on derivative contracts | **515** | **–** | (1,579) | – |
| Net post-retirement scheme financing | **(12)** | **–** | (2) | – |
| Net foreign exchange gains/(losses) | **394** | **–** | (358) | – |
| Net other financing | **(210)** | **(217)** | (173) | (161) |
| **Net financing income/(costs)** | **482** | **(328)** | (2,420) | (446) |

1 See note 2 for definition of underlying results

2 Includes interest income on cash balances and short-term deposits of £117m (2022: £28m) and similar income of £47m (2022: £7m) on money market funds

3 The condensed consolidated income statement shows the net fair value gains/(losses) on any interest rate swaps not designated into hedging relationships for accounting purposes. Underlying financing reclassifies the realised fair value movements on these interest rate swaps to net interest payable

## 5 Taxation

| | UK | | Overseas | | Total | |
|---|---|---|---|---|---|---|
| | **2023** | 2022 | **2023** | 2022 | **2023** | 2022 |
| | **£m** | £m | **£m** | £m | **£m** | £m |
| Current tax charge for the year | **19** | 18 | **256** | 159 | **275** | 177 |
| Adjustments in respect of prior years | **–** | (5) | **2** | (8) | **2** | (13) |
| **Current tax** | **19** | 13 | **258** | 151 | **277** | 164 |
| | | | | | | |
| Deferred tax credit for the year | **224** | (427) | **(69)** | (61) | **155** | (488) |
| Adjustments in respect of prior years | **(5)** | 4 | **2** | 12 | **(3)** | 16 |
| Recognition of deferred tax | **(406)** | – | **–** | – | **(406)** | – |
| **Deferred tax** | **(187)** | (423) | **(67)** | (49) | **(254)** | (472) |
| | | | | | | |
| **(Credited)/charged in the income statement** | **(168)** | (410) | **191** | 102 | **23** | (308) |

**Deferred taxation assets and liabilities**

| | **2023** | 2022 |
|---|---|---|
| | **£m** | £m |
| At 1 January | **2,445** | 1,792 |
| Amount credited to income statement | **254** | 495 |
| Amount credited/(charged) to OCI | **(44)** | 91 |
| Amount credited/(charged) to hedging reserves | **5** | 12 |
| Amount credited to equity | **22** | 1 |
| On disposal of businesses [1] | **(1)** | 28 |
| Exchange differences | **(13)** | 26 |
| At 31 December | **2,668** | 2,445 |
| Deferred tax assets | **2,998** | 2,731 |
| Deferred tax liabilities | **(330)** | (286) |
| | **2,668** | 2,445 |

[1] The 2023 deferred tax relates to the acquisition of Team Italia Marine S.R.L. The 2022 deferred tax relates to the disposal of ITP Aero

Of the total deferred tax asset of £2,998m, £2,399m (2022: £2,183m) relates to the UK and is made up as follows:

- £1,476m (2022: £1,054m) relating to tax losses;
- £412m (2022: £668m) arising on unrealised losses on derivative contracts;
- £162m (2022: £162m) of advance corporation tax; and
- £349m (2022: £299m) relating to other deductible temporary differences, in particular tax depreciation and relief for interest expenses.

The UK deferred tax assets primarily arise in Rolls-Royce plc and have been recognised based on the expectation that the business will generate taxable profits and tax liabilities in the future against which the losses and deductible temporary differences can be utilised.

Most of the UK tax losses relate to the Civil Aerospace large engine business which makes initial losses through the investment period of a programme and then makes a profit through its contracts for services. The programme lifecycles are typically in excess of 30 years.

Deferred tax assets are recognised only to the extent it is probable that future taxable profits will be available against which the assets can be utilised. A recoverability assessment has been undertaken, taking account of deferred tax liabilities against which the reversal can be offset and using latest UK forecasts, which are mainly driven by the Civil Aerospace large engine business, to assess the level of future taxable profits.

The recoverability of deferred tax assets has been assessed on the following basis:

- using the most recent UK profit forecasts, covering the next five years which are consistent with external sources on market conditions;
- the long-term forecast profit profile of existing large engine programmes which are typically in excess of 30 years from initial investment to retirement of the fleet, including the aftermarket revenues earned from airline customers;
- the long-term forecast is adjusted to exclude engine programmes which are in the development stage with no confirmed orders;
- taking into account the risk that regulatory changes could materially impact demand for our products;
- consideration that although all Civil Aerospace large engines are now compatible with sustainable fuels, there is a risk that in the longer term demand will shift towards more sustainable products and solutions;
- the long-term forecast profit and cost profile of the other parts of the UK business;
- taking into consideration past performance and experience as well as a 25% probability of a severe but plausible downside forecast materialising in relation to the civil aviation industry; and
- consideration that, whilst profitable in 2023, the UK business has historically been loss making.

## 5 Taxation continued

The assessment takes into account UK tax laws that, in broad terms, restrict the offset of carried forward tax losses to 50% of current year profits. In addition, the amounts and timing of future taxable profits incorporate:

- the impact of new contracts signed in 2023. These include the trilateral AUKUS agreement involving the UK Defence business;
- the outcomes of strategic initiatives including cost and commercial optimisation;
- the growth in Civil Aerospace engine flying hours; and
- management's assumptions on the impact of macroeconomic factors and climate change on the UK business.

The climate change scenarios previously prepared to assess the viability of our business strategy, decarbonisation plans and approach to managing climate-related risks have continued to develop over the last year. The scale up of sustainable aviation fuel is expected to play a crucial role in reaching net zero carbon emissions by 2050 and the Group has demonstrated that all Civil Aerospace production engines are compatible with sustainable aviation fuels. The impact that this could have on our costs and customer pricing is factored into the deferred tax assessment. However, benefits that may arise in the future from the development of breakthrough new technologies are not taken into account.

Based on the assessment, the Group has recognised a total UK deferred tax asset of £2,399m, which includes the re-recognition of a £57m deferred tax asset on unrealised losses on foreign exchange derivative contracts and recognition of a further £406m (of which £328m is non-underlying and £78m is underlying) deferred tax asset relating to UK tax losses. This reflects the conclusions that:

- Based on current financial results and an improved outlook it is probable that the UK business will generate taxable income and tax liabilities in the future against which these losses can be utilised.
- Using current forecasts and various scenarios these losses and other deductible temporary differences will be used in full within 30-40 years, which is within the expected programme lifecycles. An explanation of the potential impact of climate change on forecast profits and sensitivity analysis can be found in note 1.
- Any future changes in tax law or the structure of the Group could have a significant effect on the use of losses and other deductible temporary differences, including the period over which they can be used. In view of this and the significant judgement involved the Board continuously reassesses this area.

The other significant deferred tax asset arises in Rolls-Royce Deutschland Ltd & Co KG, where the main activity is business aviation. The total net deferred tax asset is £328m (2022: £284m), which has been recognised in full. The deferred tax asset relates to revenue being recognised and taxed earlier under local tax rules resulting in a benefit when revenue is recognised in the accounts.

The Group is within the scope of the OECD Pillar Two (Global Minimum Tax) model rules. The legislation has been substantively enacted in some of the main jurisdictions in which the Group operates including the UK and Germany where the rules will be effective from 1 January 2024. Initial assessments indicate that Pillar Two income taxes will not be material to the Group and a majority of the jurisdictions in which the Group operates will meet one of the transitional safe harbours. For those jurisdictions which are material or where the statutory tax rate is close to 15%, the assessment is based on 2023 data. Elsewhere prior year data has been used.

For the year to 31 December 2023, the Group has applied the mandatory exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.

The temporary differences associated with investments in subsidiaries, joint ventures and associates, for which a deferred tax liability has not been recognised, aggregate to £1,230m (2022: £1,062m). No deferred tax liability has been recognised on the potential withholding tax due on the remittance of undistributed profits as the Group is able to control the timing of such remittances and it is probable that consent will not be given in the foreseeable future.

## 6 Earnings per ordinary share

Basic earnings per share (EPS) is calculated by dividing the profit/(loss) attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the year, excluding ordinary shares held under trust, which have been treated as if they had been cancelled.

Where there is a continuing loss during the year, the effect of potentially dilutive ordinary shares is anti-dilutive.

| | **2023** | | | 2022 | | |
|---|---|---|---|---|---|---|
| | **Basic** | **Potentially dilutive share options** | **Diluted** | Basic | Potentially dilutive share options | Diluted |
| Profit/(loss) attributable to ordinary shareholders (£m): | | | | | | |
| Continuing operations | **2,412** | | **2,412** | (1,189) | | (1,189) |
| Discontinued operations | **–** | | **–** | (80) | | (80) |
| | **2,412** | | **2,412** | (1,269) | | (1,269) |
| Weighted average number of ordinary shares (millions) | **8,361** | **44** | **8,405** | 8,349 | – | 8,349 |
| EPS (pence): | | | | | | |
| Continuing operations | **28.85** | **(0.15)** | **28.70** | (14.24) | – | (14.24) |
| Discontinued operations | **–** | **–** | **–** | (0.96) | – | (0.96) |
| | **28.85** | **(0.15)** | **28.70** | (15.20) | – | (15.20) |

The reconciliation between underlying EPS and basic EPS is as follows:

| | **2023** | | 2022 | |
|---|---|---|---|---|
| | **Pence** | **£m** | Pence | £m |
| **Underlying EPS / Underlying profit from continuing operations attributable to ordinary shareholders** | **13.75** | **1,150** | 1.95 | 163 |
| Total underlying adjustments to profit/(loss) before tax (note 2) | **13.94** | **1,165** | (20.45) | (1,708) |
| Related tax effects | **1.16** | **97** | 4.26 | 356 |
| **EPS / Profit/(loss) from continuing operations attributable to ordinary shareholders** | **28.85** | **2,412** | (14.24) | (1,189) |
| Diluted underlying EPS from continuing operations attributable to ordinary shareholders | **13.68** | | 1.95 | |

## 7 Intangible assets

| | Goodwill £m | Certification costs £m | Development expenditure £m | Customer relationships £m | Software [1] £m | Other [2] £m | Total £m |
|---|---|---|---|---|---|---|---|
| **Cost:** | | | | | | | |
| **At 1 January 2023** | 1,135 | 935 | 3,604 | 512 | 978 | 886 | 8,050 |
| Additions | – | – | 192 | – | 79 | 13 | 284 |
| Acquisition of businesses (see note 23) | 8 | – | – | 2 | – | – | 10 |
| Transferred to assets held for sale [3] | (10) | – | – | – | – | (185) | (195) |
| Transferred to current assets [4] | – | – | – | – | (23) | – | (23) |
| Disposals | – | (4) | – | – | (27) | (2) | (33) |
| Reclassifications [5] | – | – | (1) | – | 3 | (1) | 1 |
| Exchange differences | (32) | (1) | (32) | (16) | (6) | (12) | (99) |
| **At 31 December 2023** | 1,101 | 930 | 3,763 | 498 | 1,004 | 699 | 7,995 |
| | | | | | | | |
| **Accumulated amortisation and impairment:** | | | | | | | |
| **At 1 January 2023** | 36 | 447 | 1,912 | 406 | 675 | 476 | 3,952 |
| Charge for the year [6] | – | 24 | 89 | 41 | 84 | 41 | 279 |
| Impairment | – | – | – | – | – | (7) | (7) |
| Transferred to assets held for sale [3] | – | – | – | – | – | (144) | (144) |
| Transferred to current assets [4] | – | – | – | – | (14) | – | (14) |
| Disposals | – | (4) | – | – | (23) | (2) | (29) |
| Reclassifications [5] | – | – | – | – | 1 | (1) | – |
| Exchange differences | (1) | – | (25) | (14) | (5) | (6) | (51) |
| **At 31 December 2023** | 35 | 467 | 1,976 | 433 | 718 | 357 | 3,986 |
| | | | | | | | |
| **Net book value at:** | | | | | | | |
| **31 December 2023** | 1,066 | 463 | 1,787 | 65 | 286 | 342 | 4,009 |
| **1 January 2023** | 1,099 | 488 | 1,692 | 106 | 303 | 410 | 4,098 |

1 Includes £97m (2022: £93m) of software under course of construction which is not amortised

2 Other intangibles includes trademarks, brands and the costs incurred testing and analysing engines with the longest time in service (fleet leader engines) to gather technical knowledge on engine endurance which will improve reliability and enable us to reduce the costs of meeting our LTSA obligations

3 At 31 December 2023, the Group held for sale the assets and liabilities of the off-highway engines business in the lower power range based in Power Systems. See note 23 for further detail

4 During the year, the Group signed a service concession arrangement with a customer effective from 1 January 2024. Accordingly, assets that will be derecognised have been transferred to trade receivables and other assets to reflect the nature of these assets as current assets

5 Includes reclassifications within intangible assets or from property, plant and equipment when available for use

6 Charged to cost of sales and commercial and administrative costs except development costs, which are charged to research and development costs

The carrying amount of goodwill or intangible assets allocated across multiple CGUs is not significant in comparison with the Group's total carrying amount of goodwill or intangible assets with indefinite useful lives.

Goodwill has been tested for impairment during 2023 on the following basis:

- The carrying values of goodwill have been assessed by reference to the recoverable amount, being the higher of value in use or fair value less costs of disposal (FVLCOD).
- The recoverable amount has been estimated using cash flows from the most recent forecasts prepared by the Directors, which are consistent with past experience and external sources of information on market conditions. These forecasts generally cover the next five years. Growth rates for the period not covered by the forecasts are based on growth rates of 2% which reflects the products, industries and countries in which the relevant CGU or group of CGUs operate. Inflation has been included based on contractual commitments where relevant. Where general inflation assumptions have been required, these have been estimated based on externally sourced data. General inflation assumptions of 2% to 4% have been included in the forecasts, depending on the nature and geography of the flows.
- The key forecast assumptions for the impairment tests are the discount rate and the cash flow projections, in particular the programme assumptions (such as sales volumes and product costs), the impact of foreign exchange rates on the relationship between selling prices and costs, and growth rates. Impairment tests are performed using prevailing exchange rates.
- The Group believes there are significant business growth opportunities to come from Rolls-Royce playing a leading role in the transition to net zero, whilst at the same time climate change poses potentially significant risks. The assumptions used by the Directors are based on past experience and external sources of information. Based on the climate scenarios prepared, the forecasts do not assume a significant deterioration of demand for Civil Aerospace (including Rolls-Royce Deutschland) programmes given that all commercial aero-engines were compatible with sustainable fuels by the end of 2023. Similarly, 80% of the engines in Power Systems are compatible with sustainable fuels. The investment required to ensure our new products will be compatible with net zero operation, and to achieve net zero scope 1 and 2 GHG emissions is reflected in the forecasts used.

## 7 Intangible assets continued

A 1.5°C scenario has been prepared using key data points from external sources, including Oxford Economics, Global Climate Service and Databank and the International Energy Agency. This scenario has been used as the basis of a sensitivity. It is assumed that governments adopt stricter product and behavioural standards and measures that result in higher carbon pricing. Under these conditions, it is assumed that markets are willing to pay for low carbon solutions and that there is an economic return from strategic investments in low carbon alternatives. The sensitivity has considered the likelihood of demand changes for our products based on their relative fuel efficiency in the marketplace and the probability of alternatives being introduced earlier than currently expected. The sensitivity also reflects the impact of a broad range of potential costs imposed by policy or regulatory interventions (through carbon pricing). This sensitivity does not indicate the need for an impairment charge.

The principal assumptions for goodwill balances considered to be individually significant are:

**Rolls-Royce Power Systems AG**

- Recoverable amount represents FVLCOD to reflect the future strategy of the business. The Directors consider that disclosing information prepared on a FVLCOD basis here is a more useful representation of the recoverable amount when considering the future strategy of the business, including the impact of climate-related risks and opportunities. Due to the unavailability of observable market inputs or inputs based on market evidence, the fair value is estimated by discounting future cash flows (Level 3 as defined by IFRS 13 *Fair Value Measurement*) modified for market participants views;
- Trading assumptions (e.g. volume of equipment deliveries, pricing achieved and cost escalation) that are based on current and known future programmes, estimates of market share and long-term economic forecasts;
- Plausible downside scenario in relation to macro-economic factors included with a 25% weighting;
- Cash flows beyond the five-year forecasts are assumed to grow at 2.0% (2022: 1.0%); and
- Nominal post-tax discount rate 9.2% (2022: 10.0%).

The Directors do not consider that any reasonably possible changes in the key assumptions (including taking consideration of the climate-related risks above) would cause the FVLCOD of the business to fall below its carrying value of goodwill.

**Rolls-Royce Deutschland Ltd & Co KG**

- Recoverable amount represents the value in use of the assets in their current condition;
- Trading assumptions (e.g. volume of engine deliveries, flying hours of installed fleet, including assumptions on the recovery of the aerospace industry, and cost escalation) that are based on current and known future programmes, estimates of market share and long-term economic forecasts;
- Plausible downside scenario in relation to macro-economic factors included with a 25% weighting;
- Cash flows beyond the five-year forecasts are assumed to grow at 2.0% (2022: 2.0%); and
- Nominal pre-tax discount rate 14.4% (2022: 13.2%).

The Directors do not consider that any reasonably possible changes in the key assumptions (including taking consideration of the climate-related risks above) would cause the value in use of the goodwill to fall below its carrying value.

**Other cash generating units**

Goodwill balances across the Group that are not considered to be individually significant were also tested for impairment, resulting in no impairment charge (2022: £nil) being recognised at 31 December 2023.

**Material intangible assets (excluding goodwill)**

The carrying amount and the residual life of the material intangible assets (excluding goodwill) for the Group are as follows:

| | Residual life [1] | **2023 £m** | 2022 £m |
|---|---|---|---|
| Trent programme intangible assets [2] | 2-15 years | **1,920** | 1,826 |
| Business aviation programme intangible assets [3] | 11-15 years | **238** | 250 |
| Intangible assets related to Power Systems [4] | | **370** | 466 |
| | | **2,528** | 2,542 |

[1] Residual life reflects the remaining amortisation period of those assets where amortisation has commenced. The amortisation period of 15 years will commence on those assets which are not being amortised as the units are delivered

[2] Included within the Trent programmes are the Trent 1000, Trent 7000 and Trent XWB

[3] Included within business aviation are the Pearl 700 and Pearl 15

[4] Includes £112m (2022: £114m) in respect of a brand intangible asset which is not amortised. Remaining assets are amortised over a range of three to 15 years

Intangible assets (including programme intangible assets) have been reviewed for impairment in accordance with IAS 36 *Impairment of Assets*. Assessments have considered potential triggers of impairment such as external factors including climate change, significant changes with an adverse effect on a programme and by analysing latest management forecasts against those prepared in 2022 to identify any deterioration in performance. Where a trigger event has been identified, an impairment test has been carried out. Where an impairment was required the test was performed on the following basis:

- The carrying values have been assessed by reference to value in use. These have been estimated using cash flows from the most recent forecasts prepared by the Directors, which are consistent with past experience and external sources of information on market conditions over the lives of the respective programmes; and
- The key assumptions underpinning cash flow projections are based on estimates of product performance related estimates, future market share and pricing and cost for uncontracted business. Climate-related risks are considered when making these estimates consistent with the assumptions above.

There have been no (2022: none) individually material impairment charges or reversals recognised during the year.

## 8 Property, plant and equipment

| | Land and buildings £m | Plant and equipment £m | Aircraft and engines £m | In course of construction £m | Total £m |
|---|---|---|---|---|---|
| **Cost:** | | | | | |
| **At 1 January 2023** | **1,936** | **5,225** | **999** | **400** | **8,560** |
| Additions | **19** | **147** | **34** | **223** | **423** |
| Transferred to current assets [1] | **(90)** | **(93)** | **–** | **(43)** | **(226)** |
| Disposals/write-offs | **(19)** | **(309)** | **(33)** | **(9)** | **(370)** |
| Reclassifications [2] | **69** | **78** | **13** | **(146)** | **14** |
| Exchange differences | **(32)** | **(86)** | **(7)** | **(13)** | **(138)** |
| **At 31 December 2023** | **1,883** | **4,962** | **1,006** | **412** | **8,263** |
| | | | | | |
| **Accumulated depreciation and impairment:** | | | | | |
| **At 1 January 2023** | **695** | **3,507** | **413** | **9** | **4,624** |
| Charge for the year [3] | **70** | **296** | **40** | **–** | **406** |
| Impairment [4] | **4** | **6** | **1** | **6** | **17** |
| Transferred to current assets | **(48)** | **(61)** | **–** | **–** | **(109)** |
| Disposals/write-offs | **(18)** | **(299)** | **(25)** | **–** | **(342)** |
| Reclassifications [2] | **17** | **(9)** | **8** | **(7)** | **9** |
| Exchange differences | **(11)** | **(56)** | **(3)** | **–** | **(70)** |
| **At 31 December 2023** | **709** | **3,384** | **434** | **8** | **4,535** |
| | | | | | |
| **Net book value at:** | | | | | |
| **31 December 2023** | **1,174** | **1,578** | **572** | **404** | **3,728** |
| **1 January 2023** | **1,241** | **1,718** | **586** | **391** | **3,936** |

[1] During the year, the Group signed a service concession arrangement with a customer effective from 1 January 2024. Accordingly, assets that will be derecognised have been transferred to trade receivables and other assets to reflect the nature of these assets as current assets

[2] Includes reclassifications of assets under construction to the relevant classification in property, plant and equipment, right-of-use assets or intangible assets when available for use

[3] Depreciation is charged to cost of sales and commercial and administrative costs or included in the cost of inventory as appropriate

[4] The carrying values of property, plant and equipment have been assessed during the year in line with IAS 36. Material items of plant and equipment and aircraft and engines are assessed for impairment together with other assets used in individual programmes – see potential triggers considered in note 7. Land and buildings are generally used across multiple programmes and are considered based on future expectations of the use of the site, which includes any implications from climate-related risks. As a result of this assessment, there are no (2022: none) individually material impairment charges or reversals in the year

## 9 Right-of-use assets

| | Land and buildings £m | Plant and equipment £m | Aircraft and engines £m | Total £m |
|---|---|---|---|---|
| **Cost:** | | | | |
| **At 1 January 2023** | **506** | **162** | **1,827** | **2,495** |
| Additions/modification of leases | **38** | **56** | **104** | **198** |
| Acquisition of businesses (See note 23) | **2** | **–** | **–** | **2** |
| Disposals | **(6)** | **(22)** | **(54)** | **(82)** |
| Transferred to current assets [1] | **(4)** | **–** | **–** | **(4)** |
| Reclassifications to PPE | **(5)** | **–** | **(10)** | **(15)** |
| Exchange differences | **(18)** | **(2)** | **(3)** | **(23)** |
| **At 31 December 2023** | **513** | **194** | **1,864** | **2,571** |
| | | | | |
| **Accumulated depreciation and impairment:** | | | | |
| **At 1 January 2023** | **230** | **84** | **1,120** | **1,434** |
| Charge for the year [2] | **42** | **42** | **179** | **263** |
| Impairment [3] | **3** | **6** | **62** | **71** |
| Disposals | **(6)** | **(22)** | **(54)** | **(82)** |
| Reclassifications to PPE | **(1)** | **–** | **(8)** | **(9)** |
| Exchange differences | **(9)** | **(1)** | **(1)** | **(11)** |
| **At 31 December 2023** | **259** | **109** | **1,298** | **1,666** |
| | | | | |
| **Net book value at:** | | | | |
| **31 December 2023** | **254** | **85** | **566** | **905** |
| **1 January 2023** | **276** | **78** | **707** | **1,061** |

[1] During the year, the Group signed a service concession arrangement with a customer effective from 1 January 2024. Accordingly, assets that will be derecognised have been transferred to trade receivables and other assets to reflect the nature of these assets as current assets

[2] Depreciation is charged to cost of sales and commercial and administrative costs as appropriate

[3] The carrying values of right-of-use assets have been assessed during the year in line with IAS 36. Material items of plant and equipment and aircraft and engines are assessed for impairment together with other assets used in individual programmes – see potential triggers considered in note 7. Land and buildings are generally used across multiple programmes and are considered based on future expectations of the use of the site (which includes any implications from climate-related risks). As a result of this assessment, the carrying values of assets, where a trigger was identified, have been assessed by reference to value in use considering assumptions such as estimated future cash flows, product performance related estimates and climate-related risks. An impairment charge of £71m has been recognised, which includes £27m in relation to lease engines that have been returned following the termination of the lease by the lessee. In addition, during the year, a number of existing leases were extended as a result of renegotiations. An assessment was performed in reference to value in use to support the increase in asset value over the extended lease term, and as a result, an impairment of £26m has been recognised in Civil Aerospace (2022: no individually material impairment charges or reversals)

## 10 Investments

**Equity accounted and other investments**

| | Equity accounted | | | Other [1] |
|---|---|---|---|---|
| | Joint ventures £m | Associates £m | Total £m | £m |
| **At 1 January 2023** | **422** | **–** | **422** | **36** |
| Additions [2] | **9** | **–** | **9** | **–** |
| Disposals | **(5)** | **–** | **(5)** | **(1)** |
| Share of retained profit [3] | **119** | **–** | **119** | **–** |
| Reclassification of deferred profit to deferred income [4] | **(18)** | **–** | **(18)** | **–** |
| Revaluation of other investments accounted for at FVOCI | **–** | **–** | **–** | **(4)** |
| Exchange differences | **(50)** | **–** | **(50)** | **–** |
| Share of OCI | **2** | **–** | **2** | **–** |
| **At 31 December 2023** | **479** | **–** | **479** | **31** |

1 Other investments includes unlisted investments of £24m (2022: £26m) and listed investments of £7m (2022: £10m)

2 During the year, additions to investments of £9m includes the second instalment of investment related to the joint venture, Beijing Aero Engine Services Company Limited of £6m

3 See table below

4 The Group's share of unrealised profit on sales to joint ventures is eliminated against the carrying value of the investment in the entity. Any excess amount, once the carrying value is reduced to £nil, is recorded as deferred income

Reconciliation of share of retained profit/(loss) to the income statement and cash flow statement:

| | **2023 £m** | 2022 £m |
|---|---|---|
| Share of results of joint ventures and associates | **139** | 9 |
| Adjustments for intercompany trading [1] | **34** | 39 |
| Share of results of joint venture and associates to the Group | **173** | 48 |
| Dividends paid by joint ventures and associates to the Group (cash flow statement) | **(54)** | (73) |
| Share of retained (loss)/profit attributable to continuing operations (above) | **119** | (25) |

1 During the year, the Group sold spare engines to Rolls-Royce & Partners Finance, a joint venture and subsidiary of Alpha Partners Leasing Limited. The Group's share of the profit on these sales is deferred and released to match the depreciation of the engines in the joint venture's financial statements. In 2023 and 2022, profit deferred on the sale of engines was lower than the release of that deferred in prior years

## 11 Inventories

| | **2023 £m** | 2022 £m |
|---|---|---|
| Raw materials | **516** | 479 |
| Work in progress | **1,679** | 1,633 |
| Finished goods | **2,653** | 2,593 |
| Payments on account | **–** | 3 |
| | **4,848** | 4,708 |

## 12 Trade receivables and other assets

| | Current | | Non-current [1] | | Total | |
|---|---|---|---|---|---|---|
| | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m |
| Trade receivables | **2,724** | 2,376 | **40** | 43 | **2,764** | 2,419 |
| Prepayments [2] | **1,032** | 737 | **102** | 37 | **1,134** | 774 |
| RRSA prepayment for LTSA parts [2] | **236** | 149 | **1,084** | 856 | **1,320** | 1,005 |
| Receivables due on RRSAs | **1,159** | 928 | **193** | 255 | **1,352** | 1,183 |
| Amounts owed by joint ventures and associates | **731** | 632 | **10** | 16 | **741** | 648 |
| Other taxation and social security receivable | **160** | 147 | **13** | 9 | **173** | 156 |
| Costs to obtain contracts with customers [3] | **7** | 12 | **109** | 67 | **116** | 79 |
| Other receivables and similar assets [4] | **478** | 617 | **45** | 55 | **523** | 672 |
| | **6,527** | 5,598 | **1,596** | 1,338 | **8,123** | 6,936 |

[1] Trade receivables and other assets have been presented on the face of the balance sheet in line with the operating cycle of the business. Further disclosure is included in the table above and relate to amounts not expected to be received in the next 12 months in line with specific customer payment arrangements, including customers on payment plans

[2] At 31 December 2023, prepayments to RRSA partners for LTSA parts have been shown separately to provide additional detail for the reader. These amounts reflect the contractual share of EFH flows from customers paid to RRSA partners in return for the supply of parts in future periods under long-term supply contracts. In the prior year, these amounts were included within prepayments. There is no change to the total amount of trade receivables and other assets

[3] These are amortised over the term of the related contract in line with engine deliveries, resulting in amortisation of £9m (2022: £11m) in the year. There were no impairment losses

[4] Other receivables includes unbilled recoveries relating to completed overhaul activity where the right to consideration is unconditional

The Group has adopted the simplified approach to provide for expected credit losses (ECLs), measuring the loss allowance at a probability weighted amount incorporated by using credit ratings which are publicly available, or through internal risk assessments derived using the customer's latest available financial information.

The ECLs for trade receivables and other assets has decreased by £104m to £242m (2022: increased by £87m to £346m). This movement is mainly driven by the Civil Aerospace business of £(100)m, of which £(82)m relates to specific customers and £(18)m relates to updates to the recoverability of other receivables.

The movements of the Group's ECLs provision are as follows:

| | **2023 £m** | 2022 £m |
|---|---|---|
| **At 1 January** | **(346)** | (259) |
| Increases in loss allowance recognised in the income statement during the year | **(80)** | (118) |
| Loss allowance utilised | **34** | 22 |
| Releases of loss allowance previously provided | **128** | 45 |
| Exchange differences | **22** | (36) |
| **At 31 December** | **(242)** | (346) |

## 13 Contract assets and liabilities

| | Current | | Non-current [1] | | Total | |
|---|---|---|---|---|---|---|
| | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m |
| **Contract assets** | | | | | | |
| Contract assets with customers | **534** | 621 | **481** | 617 | **1,015** | 1,238 |
| Participation fee contract assets | **26** | 28 | **201** | 215 | **227** | 243 |
| | **560** | 649 | **682** | 832 | **1,242** | 1,481 |

[1] Contract assets and contract liabilities have been presented on the face of the balance sheet in line with the operating cycle of the business. Contract liabilities are further split according to when the related performance obligation is expected to be satisfied and therefore when revenue is estimated to be recognised in the income statement. Further disclosure of contract assets is provided in the table above, which shows within current the element of consideration that will become unconditional in the next year

The balance includes £494m (2022: £885m) of Civil Aerospace LTSA assets and £410m (2022: £263m) Defence LTSA assets.

The decrease in the Civil Aerospace balance is due to higher invoicing than revenue recognised in relation to the completion of performance obligations on those contracts with a contract asset balance. Revenue recognised relating to performance obligations satisfied in previous years was £64m (2022: £26m) in Civil Aerospace.

The increase in the Defence balance is due to revenue recognition in relation to performance obligations completed being higher than the payments received from the customer.

No impairment losses in relation to these contract assets (2022: none) have arisen during the year.

Participation fee contract assets have reduced by £16m (2022: £3m) due to amortisation of £15m and foreign exchange on consolidation of £1m.

The absolute value of ECLs for contract assets has decreased by £15m to £6m (2022: £21m).

## 13 Contract assets and liabilities continued

| | Current | | Non-current | | Total | |
|---|---|---|---|---|---|---|
| | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m |
| **Contract liabilities** | **6,098** | 4,825 | **8,438** | 7,337 | **14,536** | 12,162 |

During the year £3,813m (2022: £3,321m) of the opening contract liability was recognised as revenue.

Contract liabilities have increased by £2,374m. The movement in the Group balance is primarily as a result of increases in Civil Aerospace of £1,865m and Defence of £381m. The Civil Aerospace increase is primarily a result of growth in LTSA liabilities of £1,317m to £9,574m (2022: £8,257m) driven by price escalation, the continued rise in EFHs and the associated customer receipts, as well as commercial discipline driving more timely invoicing and recovery of contractual fees. In 2023 contract liabilities increased by £168m as a result of revenue recognised in relation to performance obligations satisfied in previous years (2022: £334m decrease). The increase in Defence is from the receipt of deposits in advance of performance obligations being completed.

## 14 Cash and cash equivalents

| | **2023 £m** | 2022 £m |
|---|---|---|
| Cash at bank and in hand | **739** | 847 |
| Money-market funds | **1,077** | 34 |
| Short-term deposits | **1,968** | 1,726 |
| Cash and cash equivalents per the balance sheet | **3,784** | 2,607 |
| Overdrafts (note 15) | **(53)** | (2) |
| Cash and cash equivalents per cash flow statement (page 14) | **3,731** | 2,605 |

Cash and cash equivalents at 31 December 2023 includes £279m (2022: £235m) that is not available for general use by the Group. This balance includes £40m (2022: £40m) which is held in an account that is exclusively for the general use of Rolls-Royce Submarines Limited and £195m (2022: £138m) which is held exclusively for the use of Rolls-Royce Saudi Arabia Limited. This cash is not available for use by other entities within the Group. The remaining balance relates to cash held in non-wholly owned subsidiaries and joint arrangements.

Balances are presented on a net basis when the Group has both a legal right of offset and the intention to either settle on a net basis or realise the asset and settle the liability simultaneously.

## 15 Borrowings and lease liabilities

| | Current | | Non-current | | Total | |
|---|---|---|---|---|---|---|
| | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m |
| **Unsecured** | | | | | | |
| Overdrafts | **53** | 2 | **–** | – | **53** | 2 |
| Bank loans | **3** | 1 | **–** | – | **3** | 1 |
| Loan notes | **475** | – | **3,559** | 4,095 | **4,034** | 4,095 |
| Other loans | **–** | – | **9** | 10 | **9** | 10 |
| **Total unsecured** | **531** | 3 | **3,568** | 4,105 | **4,099** | 4,108 |
| **Lease liabilities** | **278** | 355 | **1,382** | 1,492 | **1,660** | 1,847 |
| **Total borrowings and lease liabilities** | **809** | 358 | **4,950** | 5,597 | **5,759** | 5,955 |

All outstanding items described as loan notes above are listed on the London Stock Exchange

## 15 Borrowings and lease liabilities continued

The Group has access to the following undrawn committed borrowing facilities at the end of the year:

| | 2023 £m | 2022 £m |
|---|---|---|
| Expiring within one year | – | – |
| Expiring after one year | 3,500 | 5,500 |
| **Total undrawn facilities** | **3,500** | 5,500 |

Further details can be found in the going concern statement on page 19

During the year to 31 December 2023, the Group cancelled its undrawn £1bn bank loan facility which was due to mature in January 2024 and its undrawn UK Export Finance (UKEF) £1bn facility which was due to mature in March 2026. These facilities had remained undrawn during the year. In addition, the Group replaced the £2,500m committed bank borrowing facility with a new £2,500m facility with a maturity date of November 2026 with the banks having the option to extend with two one-year extension options (3+1+1).

Under the terms of the £1bn UKEF loan facility, the Company is restricted from declaring, making or paying distributions to shareholders unless certain conditions are satisfied. The conditions are linked to free cash flow performance in the prior year, and actual and forecast minimum liquidity levels. At 31 December 2023, these conditions were met but the Group is not making shareholder distributions. Once the Group is comfortably within an investment grade profile and the strength of the balance sheet is assured, the Group is committed to reinstating and growing shareholder distributions. This loan facility expires in 2027. The restrictions on distributions do not prevent the Company from redeeming any unredeemed C Shares issued prior to March 2021.

## 16 Leases

**Leases as lessee**

The net book value of right-of-use assets at 31 December 2023 was £905m (2022: £1,061m), with a lease liability of £1,660m (2022: £1,847m), per notes 9 and 15 respectively. Leases that have not yet commenced to which the Group is committed have a future liability of £5m and consist of mainly plant and equipment and properties. The consolidated income statement shows the following amounts relating to leases:

| | 2023 £m | 2022 £m |
|---|---|---|
| Land and buildings depreciation and impairment [1] | (45) | (41) |
| Plant and equipment depreciation and impairment [2] | (48) | (36) |
| Aircraft and engines depreciation and impairment [3] | (241) | (210) |
| **Total depreciation and impairment charge for right-of-use assets** | **(334)** | (287) |
| Adjustment of amounts payable under residual value guarantees within lease liabilities [3, 4] | 10 | 3 |
| Expense relating to short-term leases of 12 months or less recognised as an expense on a straight-line basis [2] | (49) | (28) |
| Expense relating to variable lease payments not included in lease liabilities [3,5] | (5) | (2) |
| **Total operating costs** | **(378)** | (314) |
| Interest expense [6] | (85) | (68) |
| **Total lease expense** | **(463)** | (382) |
| Income from sub-leasing right-of-use assets | 31 | 32 |
| **Total amount recognised in income statement** | **(432)** | (350) |

1 Included in cost of sales and commercial and administration costs depending on the nature and use of the right-of-use asset
2 Included in cost of sales, commercial and administration costs, or research and development depending on the nature and use of the right-of-use asset
3 Included in cost of sales
4 Where the cost of meeting residual value guarantees is less than that previously estimated, as costs have been mitigated or liabilities waived by the lessor, the lease liability has been remeasured. To the extent that the value of this remeasurement exceeds the value of the right-of use asset, the reduction in the lease liability is credited to cost of sales
5 Variable lease payments primarily arise on a small number of contracts where engine lease payments are solely dependent upon utilisation rather than a periodic charge
6 Included in financing costs

The total cash outflow for leases in 2023 was £429m (2022: £316m). Of this, £375m related to leases reflected in the lease liability, £49m to short-term leases where lease payments are expensed on a straight-line basis and £5m for variable lease payments where obligations are only due when the assets are used. The timing difference between income statement charge and cash flow relates to costs incurred at the end of leases for residual value guarantees and restoration costs that are recognised within depreciation over the term of the lease, the most significant amounts relate to engine leases.

Engine leases in the Civil Aerospace business often include clauses that require the engines to be returned to the lessor with specific levels of usable life remaining or cash payments to the lessor. The costs of meeting these requirements are included in the lease payments. The amounts payable are calculated based upon an estimate of the utilisation of the engines over the lease term, whether the engine is restored to the required condition by performing an overhaul at our own cost or through the payments of amounts specified in the contract and any new contractual arrangements arising when the current lease contracts end. Amounts due can vary depending on the level of utilisation of the engines, overhaul activity prior to the end of the contract, and decisions taken on whether ongoing access to the assets is required at the end of the lease term. During the year, adjustments to return conditions at the end of leases resulted in a credit of £10m to the income statement. The lease liability at 31 December 2023 included £354m relating to the cost of meeting these residual value guarantees in the Civil Aerospace business. Up to £76m is payable in the next 12 months, £185m is due over the following four years and the remaining balance after five years.

## 17 Trade payables and other liabilities

| | Current | | Non-current | | Total | |
|---|---|---|---|---|---|---|
| | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m |
| Trade payables | **1,608** | 1,735 | **–** | – | **1,608** | 1,735 |
| Accruals | **1,134** | 1,477 | **96** | 199 | **1,230** | 1,676 |
| Customer discounts [1] | **1,018** | 828 | **773** | 1,016 | **1,791** | 1,844 |
| Payables due on RRSAs | **1,713** | 1,392 | **–** | – | **1,713** | 1,392 |
| Deferred receipts from RRSA workshare partners | **56** | 32 | **774** | 829 | **830** | 861 |
| Amounts owed to joint ventures and associates | **542** | 567 | **–** | – | **542** | 567 |
| Government grants [2] | **30** | 21 | **54** | 41 | **84** | 62 |
| Other taxation and social security | **92** | 88 | **–** | – | **92** | 88 |
| Other payables [3] | **703** | 843 | **230** | 279 | **933** | 1,122 |
| | **6,896** | 6,983 | **1,927** | 2,364 | **8,823** | 9,347 |

[1] Customer discounts include customer concession credits. Revenue recognised comprises sales to the Group's customers after such items. Customer concession credits are discounts given to a customer upon the sale of goods or services. A liability is recognised to correspond with the recognition of revenue when the performance obligation is met. The largest element of the balance, approximately £1.2bn arises when the Civil business delivers its engines to an airframer. A concession is often payable to the end customer (e.g. an airline) on delivery of the aircraft from the airframer. The concession amounts are known and the payment date is reasonably certain, hence there is no significant judgement or uncertainty associated with the timing of these amounts. Warranty credits of £364m and customer concessions of £1,480m have been represented at 31 December 2023 to be included within customer discounts to better reflect the nature of these balances

[2] During the year, £74m, (2022: £20m) of government grants were released to the income statement

[3] Other payables includes payroll liabilities and HM Government UK levies

The Group's payment terms with suppliers vary on the products and services being sourced, the competitive global markets the Group operates in and other commercial aspects of suppliers' relationships. Industry average payment terms vary between 90 to 120 days. The Group offers reduced payment terms for smaller suppliers, who are typically on 75-day payment terms, so that they are paid in 30 days. In line with civil aviation industry practice, the Group offers a supply chain financing (SCF) programme in partnership with banks to enable suppliers, including joint ventures who are on 90-day standard payment terms, to receive their payments sooner. The SCF programme is available to suppliers at their discretion and does not change rights and obligations with suppliers nor the timing of payment of suppliers. At 31 December 2023, suppliers had drawn £418m under the SCF scheme (2022: £422m) of which £154m (2022: £180m) is drawn by joint ventures. The Group, in some cases, settles the costs incurred by joint venture as a result of them utilising either the Group offered SCF arrangement, or an alternative SCF arrangement. During the year to 31 December 2023, the Group incurred costs of £28m (2022: £12m) to settle the costs incurred by joint ventures as a result of them utilising the Group offered SCF arrangement. These costs are included within other financing charges.

## 18 Financial assets and liabilities

### Carrying value of other financial assets and liabilities

| | Derivatives | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Foreign exchange contracts £m** | **Commodity contracts £m** | **Interest rate contracts [1] £m** | **Total derivatives £m** | **Financial RRSAs £m** | **Other £m** | **C Shares £m** | **Total £m** |
| **At 31 December 2023** | | | | | | | | |
| Non-current assets | **72** | **–** | **254** | **326** | **–** | **34** | **–** | **360** |
| Current assets | **10** | **6** | **8** | **24** | **–** | **10** | **–** | **34** |
| **Assets** | **82** | **6** | **262** | **350** | **–** | **44** | **–** | **394** |
| Current liabilities | **(351)** | **(10)** | **(13)** | **(374)** | **(10)** | **(41)** | **(23)** | **(448)** |
| Non-current liabilities | **(1,766)** | **(15)** | **(73)** | **(1,854)** | **(7)** | **(122)** | **–** | **(1,983)** |
| **Liabilities** | **(2,117)** | **(25)** | **(86)** | **(2,228)** | **(17)** | **(163)** | **(23)** | **(2,431)** |
| | **(2,035)** | **(19)** | **176** | **(1,878)** | **(17)** | **(119)** | **(23)** | **(2,037)** |
| At 31 December 2022 | | | | | | | | |
| Non-current assets | 58 | 25 | 436 | 519 | – | 23 | – | 542 |
| Current assets | 87 | 40 | 2 | 129 | – | 12 | – | 141 |
| Assets | 145 | 65 | 438 | 648 | – | 35 | – | 683 |
| Current liabilities | (966) | (1) | (2) | (969) | (8) | (15) | (24) | (1,016) |
| Non-current liabilities | (3,030) | (2) | (98) | (3,130) | (14) | (86) | – | (3,230) |
| Liabilities | (3,996) | (3) | (100) | (4,099) | (22) | (101) | (24) | (4,246) |
| | (3,851) | 62 | 338 | (3,451) | (22) | (66) | (24) | (3,563) |

[1] Includes the foreign exchange impact of cross-currency interest rate swaps

## 18 Financial assets and liabilities continued

### Derivative financial instruments

Movements in fair value of derivative financial assets and liabilities were as follows:

| | Year ended 31 December 2023 £m | | | | | Year ended 31 December 2022 £m |
|---|---|---|---|---|---|---|
| | **Foreign exchange instruments £m** | **Commodity instruments £m** | **Interest rate instruments – hedge accounted [1] £m** | **Interest rate instruments – non-hedge accounted £m** | **Total** | Total |
| **At 1 January** | **(3,851)** | **62** | **125** | **213** | **(3,451)** | (2,913) |
| Movements in fair value hedges | **–** | **–** | **(71)** | **–** | **(71)** | (74) |
| Movements in cash flow hedges | **–** | **–** | **(78)** | **–** | **(78)** | 86 |
| Movements in other derivative contracts [2] | **574** | **(60)** | **–** | **1** | **515** | (1,579) |
| Contracts settled | **1,242** | **(21)** | **69** | **(83)** | **1,207** | 1,029 |
| **At 31 December** | **(2,035)** | **(19)** | **45** | **131** | **(1,878)** | (3,451) |

[1] Includes the foreign exchange impact of cross-currency interest rate swaps

[2] Included in net financing

### Financial risk and revenue sharing arrangements (RRSAs) and other financial assets and liabilities

Movements in the carrying values were as follows:

| | Financial RRSAs | | Other - assets | | Other - liabilities | |
|---|---|---|---|---|---|---|
| | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m | **2023 £m** | 2022 £m |
| **At 1 January** | **(22)** | (12) | **25** | 15 | **(101)** | (75) |
| Exchange adjustments included in OCI | **1** | (2) | **–** | 2 | **2** | (4) |
| Additions | **–** | (6) | **–** | 11 | **(80)** | (35) |
| Financing charge [1] | **–** | – | **–** | – | **(8)** | (4) |
| Excluded from underlying profit: | | | | | | |
| Changes in forecast payments [1] | **(1)** | (7) | **–** | – | **–** | – |
| Cash paid | **5** | 5 | **–** | (3) | **11** | 8 |
| Other | **–** | – | **–** | – | **13** | 9 |
| **At 31 December** | **(17)** | (22) | **25** | 25 | **(163)** | (101) |

[1] Included in net financing

## 18 Financial assets and liabilities continued

Fair values of financial instruments equate to book values with the following exceptions:

| | 2023 | | 2022 | |
|---|---|---|---|---|
| | **Book value £m** | **Fair value £m** | Book value £m | Fair value £m |
| Other assets – Level 2 | **12** | **12** | – | – |
| Borrowings – Level 1 | **(4,034)** | **(3,977)** | (4,095) | (3,812) |
| Borrowings – Level 2 | **(65)** | **(67)** | (13) | (15) |
| Financial RRSAs – Level 3 | **(17)** | **(16)** | (22) | (22) |

The fair value of a financial instrument is the price at which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arms-length transaction. There have been no transfers during the year from or to Level 3 valuation. Fair values have been determined with reference to available market information at the balance sheet date, using the methodologies described below.

- Non-current investments primarily comprise unconsolidated companies where fair value approximates to the book value. Listed investments are valued using Level 1 methodology.
- Money market funds, included within cash and cash equivalents, are valued using Level 1 methodology. Fair values are assumed to approximately equal cost either due to the short-term maturity of the instruments or because the interest rate of the investments is reset after periods not exceeding six months.
- The fair values of held to collect trade receivables and similar items, trade payables and other similar items, other non-derivative financial assets and liabilities, short-term investments and cash and cash equivalents are assumed to approximate to cost either due to the short-term maturity of the instruments or because the interest rate of the investments is reset after periods not exceeding six months.
- Fair values of derivative financial assets and liabilities and trade receivable held to collect or sell are estimated by discounting expected future contractual cash flows using prevailing interest rate curves or cost of borrowing, as appropriate. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the balance sheet date. These financial instruments are included on the balance sheet at fair value, derived from observable market prices (Level 2 as defined by IFRS 13 *Fair Value Measurement*).
- Borrowings are carried at amortised cost. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the balance sheet date. The fair value of borrowings is estimated using quoted prices (Level 1 as defined by IFRS 13) or by discounting contractual future cash flows (Level 2 as defined by IFRS 13).
- The fair values of RRSAs and other liabilities, which primarily includes royalties to be paid to airframers, are estimated by discounting expected future cash flows. The contractual cash flows are based on future trading activity, which is estimated based on latest forecasts (Level 3 as defined by IFRS 13).
- Other assets and borrowings are carried at amortised cost. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the balance sheet date. The fair value of borrowings is estimated by discounting contractual future cash flows (Level 2).
- In addition, other assets can be included on the balance sheet at fair value, derived from observable market prices or latest forecast (Level 2/3 as defined by IFRS 13). At 31 December 2023, Level 3 assets totalled £25m (31 December 2022: £25m).
- The fair value of lease liabilities are estimated by discounting future contractual cash flows using either the interest rate implicit in the lease or the Group's incremental cost of borrowing (Level 2 as defined by IFRS 13).

## 19 Provisions for liabilities and charges

| | At 1 January 2023 £m | Charged to income statement [1] £m | Reversed £m | Utilised £m | Transfer to held for sale £m | Exchange differences £m | At 31 December 2023 £m |
|---|---|---|---|---|---|---|---|
| Contract losses | **1,592** | **500** | **(433)** | **(185)** | **–** | **(2)** | **1,472** |
| Warranty and guarantees | **317** | **112** | **(14)** | **(91)** | **(8)** | **(10)** | **306** |
| Trent 1000 wastage costs | **179** | **45** | **(29)** | **(79)** | **–** | **–** | **116** |
| Employer liability claims | **33** | **1** | **(7)** | **(3)** | **–** | **–** | **24** |
| Tax related interest and penalties | **16** | **9** | **–** | **(2)** | **–** | **(1)** | **22** |
| Claims and litigation | **122** | **71** | **(39)** | **(111)** | **–** | **–** | **43** |
| Other | **74** | **26** | **(18)** | **(35)** | **–** | **(1)** | **46** |
| | **2,333** | **764** | **(540)** | **(506)** | **(8)** | **(14)** | **2,029** |
| Current liabilities | **632** | | | | | | **532** |
| Non-current liabilities | **1,701** | | | | | | **1,497** |

[1] The charge to the income statement within net financing includes £59m (2022: £33m) as a result of the unwinding of the discounting of provisions previously recognised

### Contract losses

Provisions for contract losses are recorded when the direct costs to fulfil a contract are assessed as being greater than the expected recoverable amount. Provisions for contract losses are measured on a fully costed basis and during the year, £185m of the provision has been utilised. Additional contract losses for the Group of £500m have been recognised as a result of increases in the estimates of future LTSA costs, due to inflationary increases and costs associated with supply chain challenges. Contract losses of £433m previously recognised have been reversed following the renegotiation of some major contracts resulting in contract extensions and improved margins. The Group continues to monitor the contract loss provision for changes in the market and revises the provision as required. The value of the remaining contract loss provisions reflect, in each case, the single most likely outcome. The provisions are expected to be utilised over the term of the customer contracts, typically within eight to 16 years.

IAS 37 requires a company to recognise any impairment loss that has occurred on assets used in fulfilling the contract before recognising a separate provision for an onerous contract. No impairments were required for any of the assets used solely for the fulfilment of onerous contracts. However, as per note 9, a number of aero engine lease right-of-use assets were impaired during the year and these will be used on a range of contracts some of which are onerous.

The Trent 1000 intangible assets (certification costs and development costs) and Trent 1000 spare engines (right of use and owned) are tested for impairment as part of the Trent 1000 Cash generating unit (CGU) and no impairment was required.

### Warranty and guarantees

Provisions for warranty and guarantees relate to products sold and are calculated based on an assessment of the remediation costs related to future claims based on past experience. During the year, £112m of additional provision has been recognised representing the single best estimate of warranty and guarantee costs to be incurred on relevant sales and £91m of previously recognised costs have been utilised. The provision generally covers a period of up to three years.

### Trent 1000 wastage costs

In November 2019, the Group announced the outcome of testing and a thorough technical and financial review of the Trent 1000 TEN programme, following technical issues which were identified in 2019, resulting in a revised timeline and a more conservative estimate of durability for the improved HP turbine blade for the TEN variant. During the year, the Group has utilised £79m of the Trent 1000 wastage costs provision. This represents customer disruption costs and remediation shop visit costs attributable to the wastage costs provision. During the year, a net charge to the provision of £16m has been recognised reflecting the discount unwind and updates to forecasted costs based on the latest available information. The value of the remaining provision reflects the single most likely outcome and is expected to be utilised in 2024.

### Employer liability claims

The provision relating to employer healthcare liability claims is as a result of an historical insolvency of the previous provider and is expected to be utilised over the next 30 years.

## 19 Provisions for liabilities and charges continued

### Claims and litigation

Provisions for claims and litigation represent ongoing matters where the outcome for the Group may be unfavourable. On 3 July 2023, judgement in respect of a legal claim was rendered by the High Court, resulting in a charge to the income statement of £34m. The judgment was satisfied in August 2023 resulting in a £92m utilisation. The value of any remaining provisions reflects the single most likely outcome in each case.

The balance also includes the best estimate of any retained exposure by the Group's captive insurance company for any claims that have been incurred but not yet reported to the Group as that entity retains a portion of the exposures it insures on behalf of the remainder of the Group. Such exposures include policies for aviation claims, employer liabilities and healthcare claims. Significant delays can occur in the notification and settlement of claims and judgement is involved in assessing outstanding liabilities, the ultimate cost and timing of which cannot be known with certainty at the balance sheet date. The insurance provisions are based on information currently available, however it is inherent in the nature of the business that ultimate liabilities may vary if the frequency or severity of claims differs from estimated.

### Other

Other items are individually immaterial. The value of any remaining provisions reflects the single most likely outcome in each case.

## 20 Post-retirement benefits

The net post-retirement deficit as at 31 December 2023 is calculated on a year to date basis, using the latest valuation as at 31 March 2023 for the UK scheme, updated to 31 December 2023 for the principal schemes.

**Amounts recognised in the balance sheet in respect of defined benefit schemes**

| | UK schemes £m | Overseas schemes £m | Total £m |
|---|---|---|---|
| **At 1 January 2023** | **594** | **(1,014)** | **(420)** |
| Exchange adjustments | **–** | **33** | **33** |
| Current service cost and administrative expenses | **(8)** | **(33)** | **(41)** |
| Past service cost | **–** | **2** | **2** |
| Financing recognised in the income statement | **29** | **(41)** | **(12)** |
| Contributions by employer | **–** | **69** | **69** |
| Actuarial gains/(losses) recognised in OCI [1] | **164** | **(62)** | **102** |
| Returns on plan assets excluding financing recognised in OCI [1] | **(12)** | **26** | **14** |
| Transfers | **–** | **(2)** | **(2)** |
| Transfer to held for sale | **–** | **2** | **2** |
| **At 31 December 2023** | **767** | **(1,020)** | **(253)** |
| Post-retirement scheme surpluses – included in non-current assets [2] | **767** | **15** | **782** |
| Post-retirement scheme deficits – included in non-current liabilities | **–** | **(1,035)** | **(1,035)** |

[1] Actuarial gains and losses arising from financial assumptions arise primarily due to changes in discount rate and inflation

[2] The surplus in the Rolls-Royce UK Pension Fund (RRUKPF) is recognised as, on ultimate wind-up when there are no longer any remaining members, any surplus would be returned to the Group, which has the power to prevent the surplus being used for other purposes in advance of this event

### Changes to defined benefit schemes

During the year, Power Systems continued to replace a number of their existing defined benefit schemes with a new company pension scheme to offer payment options at time of retirement for other employee populations not included in 2022. The new system, which is similar in structure to a defined contribution scheme with a guarantee from the company in accordance with German legislation, significantly reduces interest risks and longevity risks for the employer for future commitments. A past service cost of £3m has been recognised within non-underlying operating profit in relation to this new scheme.

In addition, Rolls-Royce Power Systems concluded a works agreement resulting in a change to jubilee benefits offered to employees based in Friedrichshafen. A past service credit of £5m has been recognised within non-underlying operating profit.

### Other

The Group is aware of a UK High Court legal ruling in June 2023 between Virgin Media Limited and NTL Pension Trustees II Limited, which decided that certain historic rule amendments were invalid if they were not accompanied by the actuarial certifications. The ruling is subject to appeal and the Group is monitoring developments. Whilst this ruling was in respect of another scheme, any final judgment would need to be reviewed for its relevance to the RRUKPF scheme. As yet the RRUKPF pension advisers have not completed any analysis and, as the outcome of the appeal is still unknown, no adjustments have been made to the Condensed Consolidated Financial Statements at 31 December 2023.

### Contributions

The Group expects to contribute approximately £73m to its overseas defined benefit schemes in 2024 (2023: £70m).

In the UK, any cash funding of RRUKPF is based on a statutory triennial funding valuation process. The Group and the Trustee negotiate and agree the actuarial assumptions used to value the liabilities (Technical Provisions); assumptions which may differ from those used for accounting are set out above. The assumptions used to value Technical Provisions must be prudent rather than a best estimate of the liability. Most notably, the Technical Provisions discount rate is currently based upon UK Government bond yields plus a margin (0.5% at the 31 March 2023 valuation) rather than being based on yields of AA corporate bonds. Once each valuation is signed, a Schedule of Contributions (SoC) must be agreed which sets out the cash contributions to be paid. The most recent valuation, as at 31 March 2023, agreed by the Trustee in October 2023, showed that the RRUKPF was estimated to be 115% funded on the Technical Provisions basis (estimated to be 113% at 31 December 2023). All cash due has been paid in full and the current SoC does not currently require any cash contributions to be made by the Group.

## 21 Contingent liabilities and commitments

In January 2017, after full cooperation, the Company concluded deferred prosecution agreements (DPA) with the SFO and the US Department of Justice (DoJ) and a leniency agreement with the MPF, the Brazilian federal prosecutors. The terms of both DPAs have now expired. The Company has submitted a final report to the Controller General, Brazil (CGU) under the terms of a two-year leniency agreement signed in October 2021 relating to the same historical matters. Certain authorities are investigating members of the Group for matters relating to misconduct in relation to historical matters. The Group is responding appropriately. Action may be taken by further authorities against the Group or individuals. In addition, the Group could still be affected by actions from other parties, including customers, customers' financiers and the Company's current and former investors, including certain potential claims in respect of the Group's historical ethics and compliance disclosures which have been notified to the Group. The Directors are not currently aware of any matters that are likely to lead to a material financial loss over and above the penalties imposed to date, but cannot anticipate all the possible actions that may be taken or their potential consequences.

The Group has, in the normal course of business, entered into arrangements in respect of export finance, performance bonds, grant funding, countertrade obligations and minor miscellaneous items, which could result in potential outflows if the requirements related to those arrangements are not met. Various Group undertakings are party to legal actions and claims (including with tax authorities) which arise in the ordinary course of business, some of which are for substantial amounts.

In connection with the sale of its products, the Group will, on some occasions, provide financing support for its customers, generally in respect of civil aircraft. The Group's commitments relating to these financing arrangements are spread over many years, relate to a number of customers and a broad product portfolio and are generally secured on the asset subject to the financing. These include commitments of $0.9bn (2022: $1.2bn) (on a discounted basis) to provide facilities to enable customers to purchase aircraft (of which approximately $0.7bn could be called during 2024). These facilities may only be used if the customer is unable to obtain financing elsewhere and are priced at a premium to the market rate. Significant events impacting the international aircraft financing market, the failure by customers to meet their obligations under such financing agreements, or inadequate provisions for customer financing liabilities may adversely affect the Group's financial position.

Customer financing provisions are made to cover guarantees provided for asset value and/or financing where it is probable that a payment will be made. These are reported on a discounted basis at the Group's borrowing rate to better reflect the time span over which these exposures could arise. The values of aircraft providing security are based on advice from a specialist aircraft appraiser. There were no provisions for customer financing provisions at 31 December 2023 or 31 December 2022.

The Group has responded appropriately to the Russia-Ukraine conflict to comply with international sanctions and export control regime, and to continue to implement the business decision to exit from Russia. The Group could be subject to action by impacted customers, suppliers and other contract parties.

While the outcome of the above matters cannot precisely be foreseen, the Directors do not expect any of these arrangements, legal actions or claims, after allowing for provisions already made, to result in significant loss to the Group.

## 22 Related party transactions

| | **2023 £m** | 2022 £m |
|---|---|---|
| Sale of goods and services | **6,700** | 5,074 |
| Purchases of goods and services [1] | **(7,471)** | (5,577) |
| Lease payments to joint ventures and associates | **(244)** | (163) |
| Guarantees of joint arrangements' and associates' borrowings | **2** | 3 |
| Guarantees of non-wholly owned subsidiaries' borrowings | **3** | 3 |
| Dividends received from joint ventures and associates | **54** | 73 |
| Other income received from joint ventures and associates | **6** | 2 |

[1] The Group has both sales and purchasing arrangements with its maintenance, repair and overhaul joint ventures. As part of this arrangement, the Group issues and receives credit notes usable against amounts receivable and payable to these related parties. Purchases of goods and services from related parties are presented to be shown gross of these concessions. This is consistent with the presentation of sales to related parties. Purchases from related parties incurred during the year to 31 December 2022 have been represented on this basis resulting in an increase to this balance of £662m

Included in sales of goods and services to related parties are sales of spare engines amounting to £48m (2022: £19m). Profit recognised in the year on such sales amounted to £88m (2022: £50m), including profit on current year sales and recognition of profit deferred on similar sales in previous years. Cash receipts relating to the sale of spare engines amounted to £73m (2022: £40m).

Included in other financing charges in the income statement are interest costs of £34m (2022: £17m) incurred during the year which have been settled by the Group on behalf of joint ventures, including the £28m of costs incurred of using the Group offered SCF arrangement set out in note 17.

## 23 Acquisitions, disposals, held for sale and discontinued operations

### Acquisitions

On 30 June 2023, the Group completed its acquisition of Team Italia/Onyx Marine SRL for a cash consideration of £14m. Team Italia specialises in yacht bridges and marine navigation and automation systems. The acquisition will provide key technology for marine automation systems and will strengthen Power Systems' position as a yacht market leader. The acquisition price of £14m has been allocated to £8m of goodwill, £2m of customer relationships, £2m to right-of-use assets and £2m to other current assets and liabilities.

### Disposals

During the year, the Group divested their 49% shareholding in joint venture, Shanxi North MTU Diesel Co. Limited to the current JV partner for proceeds of £5m. The carrying value of the Group's investment that was disposed was £5m. This has been derecognised on the disposal resulting in nil profit on disposal.

| **Reconciliation of profit on disposal of businesses in continuing operations to the income statement:** | **Total** |
|---|---|
| | **£m** |
| Profit before taxation on disposal | **–** |
| Cumulative currency translation loss on liquidation of joint venture | **(1)** |
| Adjustment to consideration on disposals completed in prior periods | **2** |
| **Profit on disposal of businesses per income statement** | **1** |

| **Reconciliation of cash flow on acquisition and disposal of businesses to the cash flow statement:** | **Total** |
|---|---|
| | **£m** |
| Proceeds on disposal (see above) | **5** |
| Cash outflow on acquisitions | **(14)** |
| Cash outflow on disposals completed in prior periods | **(9)** |
| **Cash flow on acquisition and disposal of businesses per cash flow statement** | **(18)** |

### Businesses held for sale

At 31 December 2023, the Group was in positive discussions with Deutz AG for the sale of the off-highway engines business in the lower power range based in Power Systems. The business is available for sale in its current condition and the sale is considered highly probable based on the agreement-in-principle reached as at 31 December 2023. In line with IFRS 5, the assets and liabilities related to the business have been classified as held for sale and measured at the lower of their carrying value or fair value less costs to sell, resulting in a £7m impairment reversal.

The table below summarises the categories of assets and liabilities classified as held for sale at 31 December 2023. There were no assets or liabilities held for sale at 31 December 2022.

| | **2023<br>£m** |
|---|---|
| Intangible assets | **51** |
| Inventory | **11** |
| Trade receivables and other assets | **47** |
| **Assets held for sale** | **109** |
| Trade payables and other liabilities | **(41)** |
| Contract liabilities | **(4)** |
| Provisions for liabilities and charges | **(8)** |
| Post-retirement scheme deficits | **(2)** |
| **Liabilities associated with assets held for sale** | **(55)** |
| **Net assets held for sale** | **54** |

## 23 Acquisitions, disposals, held for sale and discontinued operations continued

### Discontinued operations

ITP Aero represented a separate major line of business and was classified as a disposal group held for sale up to the date of disposal. Therefore the results up to 15 September 2022, in line with IFRS 5, were presented as discontinued operations.

The financial performance and cash flow information presented reflects the operations for the year that have been classified as discontinued operations.

| | **2023 £m** | 2022 £m |
|---|---|---|
| **Revenue** | **–** | 275 |
| **Operating profit** [1] | **–** | 86 |
| **Profit before taxation** [1] | **–** | 78 |
| Income tax charge [1] | **–** | (10) |
| **Profit for the year from discontinued operations on ordinary activities** | **–** | 68 |
| Costs on disposal of discontinued operations [2] | **–** | – |
| Loss on disposal of discontinued operations | **–** | (148) |
| **Profit for the year from discontinued operations** | **–** | (80) |
| | | |
| Net cash inflow from operating activities [2] | **–** | 85 |
| Net cash outflow from investing activities [2] | **–** | (67) |
| Net cash outflow from financing activities | **–** | (25) |
| Exchange gains | **–** | – |
| **Net change in cash and cash equivalents** | **–** | (7) |

[1] Profit/(loss) from discontinued operations on ordinary activities is presented net of intercompany trading eliminations and related consolidation adjustments

[2] Cash flows from investing activities include £nil (2022: £42m) costs of disposal paid during the year that are not a movement in the cash balance of the disposal group as they were borne centrally

## 24 Derivation of summary funds flow statement

| | 2023 | | | | | 2022 |
|---|---|---|---|---|---|---|
| | **Cash flow £m** | **Impact of hedge book £m** | **Impact of acquisition accounting £m** | **Impact of other non-underlying items £m** | **Funds flow £m** | Funds flow £m |
| **Operating profit** | **1,944** | **(475)** | **50** | **71** | **1,590** | 652 |
| Operating profit from discontinued operations | **–** | **–** | **–** | **–** | **–** | 86 |
| Depreciation, amortisation and impairment | **1,019** | **–** | **(50)** | **9** | **978** | 953 |
| Movement in provisions | **(325)** | **46** | **–** | **21** | **(258)** | (23) |
| Movement in Civil LTSA balance | **1,708** | **(377)** | **–** | **–** | **1,331** | 792 |
| Movement in prepayments to RRSAs for LTSA parts | **(315)** | **63** | **–** | **–** | **(252)** | (8) |
| Settlement of excess derivatives | **(389)** | **–** | **–** | **–** | **(389)** | (326) |
| (Profit)/loss on disposal of property, plant and equipment [1] | **18** | **–** | **–** | **–** | **18** | 18 |
| Joint venture trading [1] | **(119)** | **–** | **–** | **–** | **(119)** | 25 |
| Interest received | **159** | **–** | **–** | **–** | **159** | 36 |
| Contributions to defined benefit schemes in excess of underlying operating profit charge [1] | **(28)** | **–** | **–** | **2** | **(26)** | (32) |
| Share-based payments [1] | **66** | **–** | **–** | **–** | **66** | 47 |
| Other [1] | **–** | **(8)** | **–** | **1** | **(7)** | (53) |
| **Operating cash flow before working capital and taxation [2]** | **3,738** | **(751)** | **–** | **104** | **3,091** | 2,167 |
| Increase in inventories | **(200)** | **–** | **–** | **–** | **(200)** | (887) |
| Movement in trade receivables/payables and other assets/liabilities (excluding prepayments to RRSAs for LTSA parts) [3] | **(2,090)** | **(164)** | **–** | **(37)** | **(2,291)** | (745) |
| Movement in contract assets/liabilities (excluding Civil LTSA) [3] | **995** | **51** | **–** | **–** | **1,046** | 892 |
| Revaluation of trading assets (excluding exceptional items) [3] | **206** | **(10)** | **–** | **–** | **196** | (521) |
| Realised derivatives in financing [3] | **853** | **–** | **–** | **–** | **853** | 737 |
| Cash flows on other financial assets and liabilities held for operating purposes | **(845)** | **853** | **–** | **–** | **8** | 77 |
| Income tax | **(172)** | **–** | **–** | **–** | **(172)** | (174) |
| **Cash from operating activities [2]** | **2,485** | **(21)** | **–** | **67** | **2,531** | 1,546 |
| Capital element of lease payments | **(291)** | **21** | **–** | **–** | **(270)** | (198) |
| Capital expenditure | **(699)** | **–** | **–** | **4** | **(695)** | (504) |
| Investment | **69** | **–** | **–** | **–** | **69** | 28 |
| Interest paid | **(333)** | **–** | **–** | **–** | **(333)** | (352) |
| Other (M&A, restructuring and exceptional transformation costs) | **54** | **–** | **–** | **(71)** | **(17)** | (29) |
| **Free cash flow** | **1,285** | **–** | **–** | **–** | **1,285** | 491 |
| *Of which is continuing operations* | ***1,285*** | | | | ***1,285*** | *505* |

[1] Included in other operating cash flows in the summarised free cash flow on page 8

[2] The funds flow to 31 December 2022 has been represented to disclose cash flows on settlement of excess derivative contracts as cash flows from operating activities. As a result, operating cash flows before working capital and income tax during the year to 31 December 2022 have reduced by £(326)m to £2,167m. Cash flows on settlement of excess derivative contracts were previously shown after cash from operating activities in arriving at free cash flow. There is no impact to free cash flow

[3] Included in working capital (excluding Civil LTSA balance) in the summarised free cash flow on page 8

The comparative information to 31 December 2023 has been presented in a different format to align to the current year presentation. In some instances, the groupings of items may have changed.

Free cash flow is a measure of the financial performance of the businesses' cash flows which is consistent with the way in which performance is communicated with the Board. Free cash flow is defined as cash flows from operating activities including capital expenditure and movements in investments, capital elements of lease payments, interest paid, amounts paid relating to the settlement of excess derivatives and excluding amounts spent or received on activity related to business acquisitions or disposals and other material exceptional or one-off cash flows. The Board considers that free cash flow reflects cash generated from the Group's underlying trading.

Cash flow from operating activities is determined to be the nearest statutory measure to free cash flow. The reconciliation between free cash flow and cash flow from operating activities can be found on page 51.

## Reconciliation of Alternative Performance Measures (APMs) to their statutory equivalent

### Alternative Performance Measures (APMs)

Business performance is reviewed and managed on an underlying basis. These alternative performance measures reflect the economic substance of trading in the year. In addition, a number of other APMs are utilised to measure and monitor the Group's performance.

Definitions and reconciliations to the relevant statutory measure are included below. All comparative periods relate to 31 December 2022.

### Underlying results from continuing operations

Underlying results are presented by recording all relevant revenue and cost of sales transactions at the average exchange rate achieved on effective settled derivative contracts in the period that the cash flow occurs. Underlying results also exclude: the effect of acquisition accounting and business disposals, impairment of goodwill and other non-current assets where the reasons for the impairment are outside of normal operating activities, exceptional items and certain other items which are market driven and outside of managements control. Statutory results have been adjusted for discontinued operations and underlying results from continuing operations have been presented on the same basis. Further detail can be found in note 2 and note 23.

| | **2023 £m** | 2022 £m |
|---|---|---|
| ***Revenue from continuing operations*** | | |
| Statutory revenue | **16,486** | 13,520 |
| Derivative and FX adjustments | **(1,077)** | (829) |
| **Underlying revenue** | **15,409** | 12,691 |
| | | |
| ***Gross profit from continuing operations*** | | |
| Statutory gross profit | **3,620** | 2,757 |
| Derivative and FX adjustments | **(461)** | (262) |
| Programme exceptional credits | **(21)** | (69) |
| Exceptional transformation and restructuring charges | **55** | 8 |
| Acquisition accounting and M&A | **46** | 53 |
| Impairments | **(8)** | (10) |
| **Underlying gross profit** | **3,231** | 2,477 |
| | | |
| ***Commercial and administrative costs from continuing operations*** | | |
| Statutory commercial and administrative (C&A) costs | **(1,110)** | (1,077) |
| Derivative and FX adjustments | **1** | (2) |
| Exceptional transformation and restructuring charges | **47** | 39 |
| Other underlying adjustments | **(2)** | (22) |
| **Underlying C&A Costs** | **(1,064)** | (1,062) |
| | | |
| ***Research and development costs from continuing operations*** | | |
| Statutory research and development (R&D) costs | **(739)** | (891) |
| Derivative and FX adjustments | **(4)** | – |
| Acquisition accounting | **4** | 5 |
| **Underlying R&D costs** | **(739)** | (886) |
| | | |
| ***Operating profit from continuing operations*** | | |
| Statutory operating profit | **1,944** | 837 |
| Derivative and FX adjustments | **(475)** | (264) |
| Programme exceptional credits | **(21)** | (69) |
| Exceptional transformation and restructuring charges | **102** | 47 |
| Acquisition accounting and M&A | **50** | 58 |
| Impairments | **(8)** | 65 |
| Other underlying adjustments | **(2)** | (22) |
| **Underlying operating profit** | **1,590** | 652 |
| **Underlying operating profit margin** | **10.3%** | 5.1% |

| | **2023 pence** | 2022 pence |
|---|---|---|
| ***Basic EPS from continuing operations*** | | |
| Statutory basic EPS | **28.85** | (14.24) |
| Effect of underlying adjustments to profit/(loss) before tax | **(13.94)** | 20.45 |
| Related tax effects | **(1.16)** | (4.26) |
| Basic underlying EPS | **13.75** | 1.95 |

## Reconciliation of Alternative Performance Measures (APMs) to their statutory equivalent continued

### Underlying results from discontinued operations

| | 2023 £m | 2022 £m |
|---|---|---|
| ***Results from discontinued operations*** | | |
| Profit for the year on ordinary activities | – | 68 |
| Loss on disposal of discontinued operations | – | (148) |
| Statutory operating profit | – | (80) |
| Acquisition accounting and M&A | – | 179 |
| Derivative and FX adjustments | – | (1) |
| Related tax effects | – | (31) |
| Underlying operating profit | – | 67 |

### Organic change

Organic change is the measure of change at constant translational currency applying full year 2022 average rates to 2023. The movement in underlying change to organic change is reconciled below.

All amounts below are shown on an underlying basis and reconciled to the nearest statutory measure above.

| Total Group income statement | 2023 £m | 2022 £m | Change £m | FX £m | Organic Change £m | Organic Change % |
|---|---|---|---|---|---|---|
| **Underlying revenue** | **15,409** | 12,691 | 2,718 | 88 | 2,630 | 21% |
| **Underlying gross profit** | **3,231** | 2,477 | 754 | 22 | 732 | 30% |
| **Underlying operating profit** | **1,590** | 652 | 938 | 5 | 933 | 143% |
| Net financing costs | **(328)** | (446) | 118 | – | 118 | (26)% |
| **Underlying profit before taxation** | **1,262** | 206 | 1,056 | 5 | 1,051 | – |
| Taxation | **(120)** | (48) | (72) | (1) | (71) | – |
| **Underlying profit for the year (continuing operations)** | **1,142** | 158 | 984 | 4 | 980 | – |

| Civil Aerospace | 2023 £m | 2022 £m | Change £m | FX £m | Organic Change £m | Organic Change % |
|---|---|---|---|---|---|---|
| **Underlying revenue** | **7,348** | 5,686 | 1,662 | 17 | 1,645 | 29% |
| Underlying OE revenue | **2,703** | 1,982 | 721 | 15 | 706 | 36% |
| Underlying services revenue | **4,645** | 3,704 | 941 | 2 | 939 | 25% |
| **Underlying gross profit** | **1,394** | 853 | 541 | 1 | 540 | 63% |
| Commercial and administrative costs | **(354)** | (371) | 17 | (1) | 18 | (5)% |
| Research and development costs | **(343)** | (452) | 109 | (3) | 112 | (25)% |
| Joint ventures and associates | **153** | 113 | 40 | – | 40 | 35% |
| **Underlying operating profit** | **850** | 143 | 707 | (3) | 710 | – |

| Defence | 2023 £m | 2022 £m | Change £m | FX £m | Organic Change £m | Organic Change % |
|---|---|---|---|---|---|---|
| **Underlying revenue** | **4,077** | 3,660 | 417 | (11) | 428 | 12% |
| Underlying OE revenue | **1,766** | 1,634 | 132 | (4) | 136 | 8% |
| Underlying services revenue | **2,311** | 2,026 | 285 | (7) | 292 | 14% |
| **Underlying gross profit** | **804** | 726 | 78 | – | 78 | 11% |
| Commercial and administrative costs | **(173)** | (174) | 1 | (1) | 2 | (1)% |
| Research and development costs | **(72)** | (122) | 50 | 1 | 49 | (40)% |
| Joint ventures and associates | **3** | 2 | 1 | – | 1 | 50% |
| **Underlying operating profit** | **562** | 432 | 130 | – | 130 | 30% |

| Power Systems | 2023 £m | 2022 £m | Change £m | FX £m | Organic Change £m | Organic Change % |
|---|---|---|---|---|---|---|
| **Underlying revenue** | **3,968** | 3,347 | 621 | 82 | 539 | 16% |
| Underlying OE revenue | **2,661** | 2,187 | 474 | 55 | 419 | 19% |
| Underlying services revenue | **1,307** | 1,160 | 147 | 27 | 120 | 10% |
| **Underlying gross profit** | **1,050** | 918 | 132 | 21 | 111 | 12% |
| Commercial and administrative costs | **(456)** | (441) | (15) | (8) | (7) | 2% |
| Research and development costs | **(187)** | (204) | 17 | (4) | 21 | (10)% |
| Joint ventures and associates | **6** | 8 | (2) | – | (2) | (25)% |
| **Underlying operating profit** | **413** | 281 | 132 | 9 | 123 | 44% |

| New Markets | 2023 £m | 2022 £m | Change £m | FX £m | Organic Change £m | Organic Change % |
|---|---|---|---|---|---|---|
| **Underlying revenue** | 4 | 3 | 1 | – | 1 | 33% |
| Underlying OE revenue | 2 | 1 | 1 | – | 1 | 100% |
| Underlying services revenue | 2 | 2 | – | – | – | – |
| **Underlying gross profit/(loss)** | 1 | (1) | 2 | – | 2 | – |
| Commercial and administrative costs | (24) | (23) | (1) | – | (1) | 4% |
| Research and development costs | (137) | (108) | (29) | (2) | (27) | 25% |
| **Underlying operating loss** | (160) | (132) | (28) | (2) | (26) | 20% |

### Trading cash flow

Trading cash flow is defined as free cash flow (as defined below) before the deduction of recurring tax and post-employment benefit expenses. Trading cash flow per segment is used as a measure of business performance for the relevant segments.

| | 2023 £m | 2022 £m |
|---|---|---|
| Civil Aerospace | **626** | 226 |
| Defence | **511** | 426 |
| Power Systems | **461** | 158 |
| New Markets | **(63)** | (57) |
| Total reportable segments trading cash flow | **1,535** | 753 |
| Other businesses | **5** | 5 |
| Central and inter-segment | **(57)** | (49) |
| Trading cash flow from continuing operations | **1,483** | 709 |
| Discontinued operations | **–** | (12) |
| Trading cash flow | **1,483** | 697 |
| Underlying operating profit charge exceeded by contributions to defined benefit schemes | **(26)** | (32) |
| Tax [1] | **(172)** | (174) |
| Free cash flow | **1,285** | 491 |

[1] See page 14 for tax paid in the statutory cash flow statement

### Free cash flow

Free cash flow is a measure of the financial performance of the businesses' cash flows which is consistent with the way in which performance is communicated with the Board. Free cash flow is defined as cash flows from operating activities including capital expenditure and movements in investments, capital elements of lease payments, interest paid, amounts paid relating to the settlement of excess derivatives and excluding amounts spent or received on activity related to business acquisitions or disposals and other material exceptional or one-off cash flows. Free cash flow from continuing operations has been presented to remove free cash flow from discontinued operations as defined in note 23. For further detail, see note 24.

| | 2023 £m | 2022 £m |
|---|---|---|
| Statutory cash flows from operating activities [1] | **2,485** | 1,524 |
| Capital expenditure | **(699)** | (540) |
| Investment (including investment from NCI and movement in joint ventures, associates and other investments) | **69** | 28 |
| Capital element of lease payments | **(291)** | (218) |
| Interest paid | **(333)** | (352) |
| Exceptional transformation and restructuring costs | **69** | 76 |
| M&A costs | **2** | 2 |
| Other | **(17)** | (29) |
| Free cash flow | **1,285** | 491 |
| Discontinued operations free cash flow [2] | **–** | 14 |
| Free cash flow from continuing operations | **1,285** | 505 |

[1] Statutory cash flows from operating activities at 31 December 2022 have been represented. See note 1.

[2] Discontinued operations free cash flow excludes: transactions with parent company of £nil (2022: £(65)m), movements in borrowings of £nil (2022: £22m), exceptional restructuring costs of £nil (2022: £nil), M&A costs of £nil (2022: £44m) and other of £nil (2022: £(6)m)

### Gross R&D expenditure

In year gross cash expenditure on R&D excludes contributions and fees, amortisation and impairment of capitalised costs and amounts capitalised during the year. For further detail, see note 3.

### Gross capital expenditure

Gross capital expenditure during the year excluding capital expenditure from discontinued operations. All proposed investments are subject to rigorous review to ensure that they are consistent with forecast activity and provide value for money. The Group measures annual capital expenditure as the cash purchases of PPE acquired during the year.

| | 2023 £m | 2022 £m |
|---|---|---|
| Purchases of PPE (cash flow statement) | **429** | 359 |
| Less: capital expenditure from discontinued operations | **–** | (14) |
| Net capital expenditure | **429** | 345 |

**Key performance indicators**
The following measures are key performance indicators and are calculated using APMs or statutory results. See below for calculation of these key performance indicators. All comparative periods relate to 31 December 2022, unless otherwise stated.

**Order backlog**
Order backlog, also known as unrecognised revenue, is the amount of revenue on current contracts that is expected to be recognised in future periods. Civil Aerospace OE orders where the customer has retained the right to cancel (for deliveries in the next seven to 12 months) are excluded.

**Adjusted return on capital (abbreviated to return on capital)**

Return on capital is defined as net operating profit after tax ('NOPAT') as a percentage of average invested capital. NOPAT is defined as underlying net profit excluding net finance costs and the tax shield on net finance costs. Invested capital is defined as current and non-current assets less current liabilities. It excludes pension assets, cash and cash equivalents, and borrowings and lease liabilities. Return on capital assesses the efficiency in allocating capital to profitable investments.

| | **2023 £m** | 2022 £m |
|---|---|---|
| Underlying operating profit | **1,590** | 652 |
| Less: taxation [1] | **(151)** | (48) |
| Underlying operating profit (post-taxation) | **1,439** | 604 |
| | | |
| Total assets | **31,512** | 29,450 |
| Less: post-retirement scheme surpluses | **(782)** | (613) |
| Less: cash and cash equivalents | **(3,784)** | (2,607) |
| Current liabilities | **(14,926)** | (13,918) |
| Liabilities held for sale | **(55)** | – |
| Less: borrowings and lease liabilities | **809** | 358 |
| Invested capital (closing) | **12,774** | 12,670 |
| Invested capital (average) | **12,722** | 12,334 |
| | **%** | % |
| Return on invested capital | **11.3** | 4.9 |

[1] Excluding underlying taxation on underlying finance income/(costs) of £31m (2022: £nil)

**Total underlying cash costs as a proportion of underlying gross margin (abbreviated to TCC/GM)**

Total underlying cash costs during the year (represented by underlying research and development (R&D) expenditure and underlying commercial and administrative (C&A) costs) as a proportion of underlying gross profit. This measure provides an indicator of total cash costs relative to gross profit. A reduction in total cash costs relative to gross profit indicates how effective the business is at managing and/or reducing its costs.

| | **2023 £m** | 2022 £m |
|---|---|---|
| Underlying R&D expenditure [1] | **836** | 928 |
| Underlying C&A | **1,064** | 1,062 |
| Total cash costs | **1,900** | 1,990 |
| Underlying gross profit | **3,231** | 2,477 |
| | | |
| Total cash costs as a proportion of underlying gross profit | **0.59** | 0.80 |

[1] Excludes £6m (2022: £nil) impact of derivative and FX adjustments

## Principal risks and uncertainties

Our risk management system is described on pages 50 to 57 of our 2023 Annual Report. It sets out requirements for managing risk across the organisation, in a continuous process where risk owners define, quantify, control, assure and respond to risks, including ongoing monitoring and oversight.

In November 2023, we refreshed the risk profile to reflect where risks could impact the organisation in light of the strategy review. As a result, elements of the previous competitive environment risk are now captured in the strategy, execution and technology risks, with strategy risk also replacing some elements of the previous transformation risk. Information and data includes cyber risk and has been expanded to include physical data. In addition, business continuity which was previously a standalone risk has now been captured within business interruption. As part of this, we also looked at risk interdependencies, categorising principal risks as either a 'pillar' or a 'driver', with drivers being those risks that could cause one or more risk pillars to happen and/or make them worse if they do. All principal risks facing the Group are summarised below and reported in detail on pages 52 to 57 of our 2023 Annual Report.

**Principal risk pillars**

**Safety**

Failure to: i) provide safe products; or ii) create a place to work which minimises the risk of harm to our people, those who work with us, and the environment, would adversely affect our reputation and long-term sustainability.

**Compliance**

Non-compliance by the Group with legislation or other regulatory requirements in the heavily regulated environment in which we operate (e.g. export controls; data privacy; use of controlled chemicals and substances; anti-bribery and corruption; human rights; and tax and customs legislation). This could affect our ability to conduct business in certain jurisdictions and would potentially expose us to: reputational damage; financial penalties; debarment from government contracts for a period of time; and suspension of export privileges (including export credit financing), each of which could have a material adverse effect.

**Strategy**

Failure to develop an optimal strategy and continuously evolve it, investing in key areas for performance improvement and growth (taking into account risk reward), making difficult decisions for competitive advantage and the right portfolio and partnership choices, could result in us underperforming against our competitors and significantly reduce our ability to build a high performing, competitive, resilient and growing company.

**Execution**

Failure to deliver as One Rolls-Royce on short- to medium-term financial plans, including efficient and effective delivery of quality products, services and programmes, or falling significantly short of customer expectations, would reduce our resilience and have potentially significant adverse financial and reputational consequences, including the risk of impairment of the carrying value of the Group's intangible assets and the impact of potential litigation.

**Business interruption**

A major disruption of our operations and ability to deliver our products, services and programmes could have an adverse impact on our people, internal facilities or external supply chain which could result in failure to meet agreed customer commitments and damage our prospects of winning future orders.

Disruption could be caused by a range of events, e.g. extreme weather or natural hazards (e.g. earthquakes or floods) which could increase in severity or frequency given the impact of climate change; political events; financial insolvency of a critical supplier; scarcity of materials; loss of data; fire; pandemic or other infectious disease.

**Principal risk drivers**

**Climate change**

Failure to become a net zero company by 2050, leveraging technology to transition from carbon intensive products and services at pace could impact our ability to win future business; achieve operating results; attract and retain talent; secure access to funding; realise future growth opportunities; or force government intervention to limit emissions.

In addition, physical risks from extreme weather events (and/or natural hazards) could potentially materialise, which may result in disruption.

**Information and data**

Failure to protect the integrity and availability of data, both physical and digital, from attempts to cause us harm, such as through a cyber attack. Potential impacts include hindering data driven decision making, disrupting internal business operations and services for customers, or a data breach, all of which could damage our reputation, reduce resilience, and cause financial loss.

Causes include ransomware threats, unauthorised access to property or systems for the extraction, corruption, destruction of data, or availability of access to critical data and intellectual property.

**Market and Financial shock**

The Group is exposed to market and financial risks, some of which are of a macroeconomic nature (e.g. economic growth rates, foreign currency, oil price, interest rates) and some of which are more specific to us (e.g. reduction in air travel or defence spending, disruption to other customer operations, liquidity and credit risks).

Significant extraneous market events could also materially damage our competitiveness and/or creditworthiness and our ability to access funding. This would affect operational results or the outcomes of financial transactions.

Demand for our products and services could be adversely affected by factors such as current and predicted air traffic, fuel prices and age/replacement rates of customer fleets. A large proportion of our business is reliant on the civil aviation industry, which is cyclical in nature.

**Political risk**

Geopolitical factors leading to an unfavourable business climate and significant tensions between major trading parties or blocs could impact our strategy, execution, resilience, safety and compliance. Examples include: changes in key political relationships, explicit trade protectionism, differing tax or regulatory regimes, potential for conflict or broader political issues, and heightened political tensions.

**Talent and capability**

Failure to create a company where our people can build a successful career with better choices for development and personal growth will hinder our ability to identify, attract, retain and apply the critical capabilities and skills needed in appropriate numbers for the successful execution of our business strategy.

## Payments to shareholders

Our capital framework is focused on three clear priorities: a strong balance sheet with an investment grade profile; a commitment to reinstating and growing shareholder returns; and a disciplined approach to investments. Strengthening the balance sheet is a clear priority. We are positioning Rolls-Royce to withstand better volatility and external shocks and to give us financial flexibility for the future. When the Board is confident that the strength of the balance sheet is assured and we are comfortably within an investment grade profile, we are committed to reinstating and growing shareholder distributions.

Shareholders wishing to redeem their existing C Shares, or participate in the CRIP must lodge instructions with the Registrar to arrive no later than 5.00pm on 31 May 2024 (CREST holders must submit their election in CREST by 2.55pm). The payment of C Share redemption monies will be made on 4 July 2024 and the CRIP purchase will begin as soon as practicable after 5 July 2024.

## Statement of Directors' responsibilities

The statements below have been prepared in connection with the Company's full Annual Report for the year ended 31 December 2023. Certain parts are not included in this announcement.

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

Each of the Directors, whose names and functions are listed in the Directors' Report, confirm that to the best of their knowledge:

- the Group Financial Statements, which have been prepared in accordance with UK-adopted international accounting standards, give a true and fair view of the assets, liabilities, financial position and loss of the Group;
- the Company Financial Statements, which have been prepared in accordance with United Kingdom Accounting Standards, comprising FRS 101, give a true and fair view of the assets, liabilities, financial position of the Company;
- the Strategic Report includes a fair review of the development and performance of the business and the position of the Group and Company, together with a description of the principal risks and uncertainties that it faces; and

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

- so far as the Director is aware, there is no relevant audit information of which the Group's and Company's auditors are unaware; and
- they have taken all steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Group's or Company's auditor are aware of that information.

By order of the Board

| | |
|---|---|
| Tufan Erginbilgic | Helen McCabe |
| Chief Executive | Chief Financial Officer |
| 22 February 2024 | 22 February 2024 |