

Annual Report and Accounts 2018



Cobham is a leading global technology and services innovator, respected for providing solutions for the most challenging problems, in space, in the air, on land and at sea.

Focusing on our core mission does not just mean on our defence, aerospace and space markets, but also means changing the way we do things. Our turnaround strategy, which enables growth, is driven by our desire to improve delivery to our customers.

The ability to consistently deliver to our customers is fundamental to what we do, which has an emphasis on keeping people alive and protecting assets in harsh or remote environments.

Because what we do is critical to our customers we understand that Every Mission Matters. This is supported by our behaviours which are to be bold, be inventive, be determined and be a team.

Highlights of the year

- Encouraging order intake, up 13% at constant currency and excluding divestments
- Underlying operating profit of £196.1m after £5.5m adverse currency translation and £22.5m lost contribution from divestments
- Strong performance from Mission Systems; Advanced Electronic Solutions underperformed, now planning a cost reduction with anticipated savings in 2019 of US\$20m
- Boeing KC-46 agreement announced on 19 February 2019. Includes non-underlying £86m dispute settlement and £74m costs to complete, with rebased schedule and Boeing payment withhold ended
- Operating cash conversion adversely impacted by £103m utilisation of 2016 exceptional charges
- £10.3m net cash at year end; new capital allocation policy prioritises organic investment with net debt/EBITDA gearing ratio maintained below 1.5x
- Intention to reinstate progressive dividend at 2019 interims; anticipated 1.0p in first full year

Revenue

£1,863.3m

(2017: £2,091.6m**)

Free cash flow*

£62.6m

(2017: £140.6m)

Earnings per ordinary share – underlying*

5.0p

(2017: 6.2p**)

Earnings per ordinary share – basic*

3.1p

(2017: 3.7p**)

* For details, refer to the Chief Financial Officer's Statement on pages 28 to 33

** Restated for the impact of IFRS 15

Visit us online at www.cobham.com

You can also view this Annual Report and Accounts online at www.cobhaminvestors.com

The company is registered in England and Wales under company number 00030470. The Company's registered office is Brook Road, Wimborne, Dorset, BH21 2BJ, England.

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

Front cover image:

Cobham provides innovative, leading edge products for commercial aircraft, including for connectivity. These are set out on pages 14-15 of this Report.

Defence



Aerospace



Space



02-42

Strategic Report

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Four sectors to drive our business forward



Communications and Connectivity

Provides critical and innovative technology to enable resilient connection for complex, harsh, hazardous and regulated environments, in air and space, on land and at sea, and under the ground.

Everywhere, at any time and in the most demanding environments, to be relied on to keep you safely connected around the world.

Revenue

£552.0m

(2017: £700.7m)

Underlying operating profit

£55.9m

(2017: £69.0m)

Main operating locations

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



Mission Systems

Provides proven and trusted solutions in air-to-air refuelling, life support and weapons carriage, delivery assured performance and class leading through life costs.

Helps customers increase the safety and mission capabilities of personnel and equipment in extreme environments.

Revenue

£402.7m

(2017: £431.8m*)

Underlying operating profit

£75.3m

(2017: £55.2m*)

Main operating locations

United States and United Kingdom



Advanced Electronic Solutions

Provides critical solutions for communications on land, at sea, and in the air and space, by moving data through off the shelf and customised products including radio frequency, microwave, and high reliability microelectronics, antenna subsystems and motion control solutions.

Revenue

£595.0m

(2017: £594.7m*)

Underlying operating profit

£52.9m

(2017: £66.1m*)

Main operating locations

United States, Mexico and United Kingdom



Aviation Services

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

Revenue

£315.1m

(2017: £366.6m)

Underlying operating profit

£12.0m

(2017: £22.8m)

Main operating locations

Australia and United Kingdom

The Group in 2018

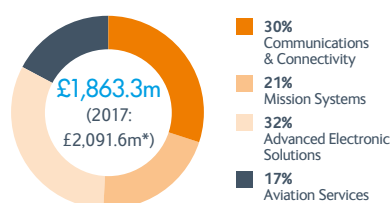
Cobham offers an innovative range of products and services to solve challenging problems in defence, aerospace and space markets with an emphasis on keeping people alive and assets safe in harsh or remote environments.

We employ around 10,000 people and have customers and partners in over 100 countries. We have specialist capabilities and know-how in: wireless; audio; video and data communications, including satellite communications; defence electronics; air-to-air refuelling; aviation services; life support; and mission equipment markets.

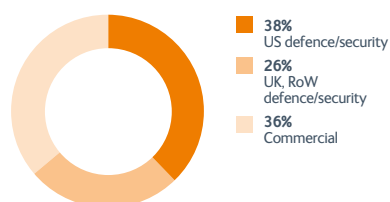
Cobham operates across four Sectors, each with differentiated capabilities and many leading market positions. Three of our Sectors design, manufacture and test intelligent hardware, primarily subsystems, with expertise in components. The fourth provides outsourced aviation services for an international customer base.

Our revenue split by:

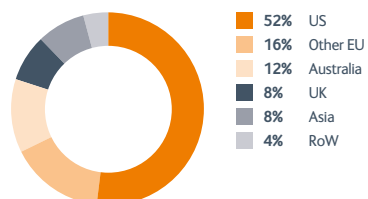
Sector %



Market %

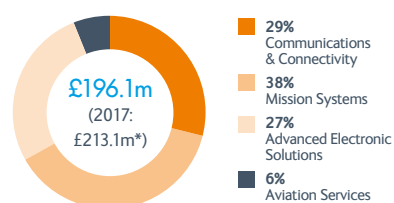


Geography %



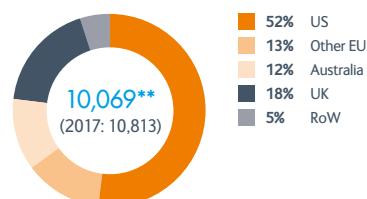
Our underlying operating profit split by:

Sector %



Our employees worldwide:

Geography %



* Restated for the impact of IFRS 15

** Total permanent headcount at 31 December 2018

Focusing on our core mission



“We have strengthened the governance framework over the last two years”

The position today

We can see the benefits of our improvement actions starting to come through across most of the business, particularly so in Mission Systems. However, there has been a disappointing performance from Advanced Electronic Solutions. We have therefore strengthened management, increased focus on execution and formulated an overhead cost reduction plan. While Cobham's overall performance is benefiting from a firm sense of direction and management discipline, the turnaround was always going to require a number of years to complete, and our improvement journey will continue in 2019.

We have completed a number of divestments in the year, most notably exiting the wireless test and measurement market, bringing more coherence, and less volatility, to our portfolio. As a result, we now have a more focused defence, aerospace and space business.

By 31 December 2018, we had eliminated the Group's gearing, reporting a modest net cash position. This achievement was in part a result of the divestment proceeds, in part thanks to the 2017 contribution from shareholders, but also due to an ongoing focus on cash, with work continuing to shape a truly cash-focused culture. Again, there is work left to do, in particular to resolve our remaining contingent liabilities. However, today Cobham has demonstrably a much stronger balance sheet.

We are also making progress resolving our previously reported contingent liabilities. As part of this we settled all the disputed matters relating to the Boeing KC-46 tanker programme damages assertions in February 2019. At the same time, we agreed a revised hose and drogue qualification and production schedule, although this is dependent on receiving key third party approvals, and reassessed the remaining risks on the programme. The 2018 financial impacts from this settlement

Five reasons to invest in Cobham

1. Deep technical expertise, differentiation and significant intellectual property – enabling Cobham to do things others can't to deliver capabilities that are critical to our customers
2. Leading market positions, offering the potential for superior returns on technology investment
3. Broad international demand for the Group's capabilities and know-how from a range of markets including government and commercial customers
4. Positions in markets with significant barriers to entry including lengthy and expensive qualification, complex regulation and a need for a proven reputation
5. A focus on operational improvement with quality, on-time delivery and efficiency expected to drive an increase in the operating margin with enhanced delivery also stimulating revenue growth

have been set out in more detail in the Chief Executive Officer's Statement, which follows.

Separately, we have set out in note 30 on page 147 an ongoing tax dispute, relating to interest deductions on one of the Group's financing arrangements. The Group is actively involved in attempting to resolve this matter ahead of a Tribunal hearing scheduled for autumn 2019.

We also announced in August 2018 that the Financial Conduct Authority had discontinued its investigation into the Company's compliance with the Listing Rules, Disclosure and Transparency Rules and the Market Abuse Regulations between April 2016 and February 2017.

Given the strengthening financial position and improving performance, the Board has approved a new capital allocation policy. This is built on a prudent gearing level and prioritises organic investment in the business. The Board intends to reinstate a dividend payment with the 2019 interims at a prudent level. The Board anticipates a first full-year payment of 1.0p per ordinary share, based on our 2019 expectations. The Board intends to grow the dividend progressively, while ensuring an appropriate level of projected earnings and free cash flow cover.

The journey

When I became Chairman, just over two years ago, it was against a very different and challenging backdrop. This included elevated gearing and a need to strengthen operational and financial discipline.

From the outset, it was clear significant actions were needed. These included supporting the transition of the new Executive management team, to create the conditions to support their future success, as well as a need to strengthen the Balance Sheet.

In addition, a programme of material change was needed to re-invigorate the Board through the appointment of experienced Non-executives. We undertook to perform a review of the Board's governance framework. An enhanced succession planning process was also required to help develop future managers from within.

As I have said, Cobham's financial and operational performance is now showing an improving trend under the new leadership, with relentless focus on customers, on operational improvement priorities and on cash generation, which must always lie at the heart of how the Group is run. We have also launched a new purpose and behaviours, which complements this progress.

When considering the need for Board refresh, I have always tried to balance, as an overriding principle, the need for continuity and stability with the need for change. In 2017, John McAdam was recruited as the Senior Independent Director. John has a wealth of experience on a number of FTSE 100 boards. I am particularly grateful to him for deputising as Chairman during my 2018 surgery and recuperation.

Furthermore, René Médori, Norton Schwarz and Marion Blakey joined the Board in 2018. They have brought in-depth experience of financial matters, our end-user community and aviation regulation and administration respectively. All have operated at the highest levels in their fields. In addition, Alison Wood remains on the Board, offering long experience, in particular of matters relating to strategy and risk. Today, the Board has the relevant experience from which to support and constructively challenge the Executives. Further details on the skills and experience of the Non-executives are contained in the Corporate Governance section on pages 52 and 53.

In addition, the anticipated Board governance framework evaluation was completed, resulting in the implementation of enhancements. Changes include more time spent on strategic matters and on strengthening the Board's knowledge of the Group. The Nomination Committee has been restructured and re-energised, and we now have a Board Risk Committee, comprising a mix of Executive and Non-executive Directors.

We also have a much stronger succession planning process, with a clearer view of strengths and weaknesses and a path to remedy identified gaps. I have always said that done properly, succession planning takes time to embed, and longer to bear fruit. However, I feel confident we now have the foundations from which we can nurture and promote future leaders.

The Cobham Advanced Electronic Solutions (CAES) board was further strengthened by the addition of General Chilton, former head of US Strategic Command. CAES governance reflects proper adherence to our Special Security Agreement (SSA) which enables CAES to participate in US government classified programmes. There were also changes made to the executive team.

In summary, I am proud of what we have done to strengthen the Group's governance framework, consistent with the priorities I previously laid out. Of course, we could not achieve anything meaningful without our employees, and their expertise and hard work have been instrumental in our progress. Their deep domain knowledge and technical expertise, together with their dedication and a willingness to make 'hard yards', have always impressed the Board and we offer our appreciation.

Chairman succession

When I was originally appointed Chairman, I said it would be for a term lasting a little over two years. Having led the Board through a period of significant change and having been a Director of Cobham since December 2010, I have informed the Board of my intention to step down as Chairman. A search for my successor is now underway and it is intended that I will leave the Board by the end of 2019.

Looking forward

There is work left to do but much to be optimistic about. I am confident, based on the sound foundations laid, that 2019 will be another year of progress with the turnaround gaining traction to build on the Group's traditional strengths. When taken together, these provide the Board with confidence in Cobham's medium and longer term prospects.



Michael Wareing

Chairman

7 March 2019

The benefits of our improvement actions are starting to come through



Overview

2018 has been a year of progress with Group financial metrics in-line overall and an agreement reached with Boeing regarding the KC-46 programme.

We expected there would be some significant cash flow challenges during 2018. These related principally to the utilisation of the 2016 exceptional provisions and accelerated interest payments on the debt pay-down. Despite these challenges, we reported £62.6m of free cash flow and ended the year with £10.3m of net cash on the balance sheet.

The headline numbers mask a divergence in performance between the Group's businesses. Mission Systems had a much better year achieving strong underlying operating profit growth. Before the one-off adverse revenue impact from the KC-46 settlement, it also achieved organic revenue growth across its markets – aerial refuelling, pneumatics and actuation. Communications and Connectivity and Aviation Services performed largely as we had anticipated.

“There are considerable opportunities for medium term performance improvement”

Advanced Electronic Solutions underperformed. Although it achieved organic revenue growth, underlying operating profit decreased. This result was driven by its operational performance, due to poor execution, including £9.5m of programme charges, and it also reflected increased overhead costs. Addressing this will be the priority for 2019, and over the last few months we have strengthened the management team. An overhead cost reduction plan has been formulated, which is anticipated to achieve savings in 2019 of US\$20m. Investment is continuing to improve its operating facilities.

We can see the benefits of our actions starting to coming through but, as anticipated, progress has

The merger of Aviation Services UK and EMEA fixed and rotary wing head offices was largely completed during the year.



been uneven and there remains work to do. We have set out a new capital allocation policy which establishes a prudent approach to gearing and prioritises organic investment. We intend to reinstate dividend payments with our 2019 interim results.

We continue to believe that there is considerable potential to improve the performance of the Group over the medium term and our continuing focus on customers, culture, operational improvement, business simplification and cash generation will allow us to realise this.

Market Environment

We have seen increased defence budgets in the US, with ongoing security tensions around the globe. Our strategic positioning in defence/security markets means that our capabilities and know-how are well aligned with end-user priorities. For example, current US Department of Defense (DoD) priorities include capability modernisation for space and communication and situational awareness. While security tensions are likely to persist, there are high levels of government debt and budget deficits in many of our largest accessible defence markets, including the US. This will constrain growth in defence spending and continue the emphasis on value-for-money.

This is the back-drop to our improvement strategy: an environment where demand for our capabilities is accompanied by a requirement for value as well as consistent delivery to customer expectations. We continue to believe that the Group's underlying operating margin enhancement will come from our ability to reduce costs through improved execution, enhanced quality, reduced complexity and effective capital allocation.

Our Improvement Progress

The key components of Cobham's turnaround are:

- Returning the business to financial strength;
- Focusing the portfolio;
- Resolving onerous contracts and other legacy issues;
- Operational execution and culture change;
- New capital allocation policy and dividend.

Returning the Business to Financial Strength

Two years ago there was £1,028m of net debt on the balance sheet and a net debt/EBITDA gearing ratio of 3.0x, putting Cobham in a weak financial and commercial position. In contrast, at the end of 2018 there was £10m of net cash on the Balance Sheet. This transformation has been achieved with the help of our shareholders through the 2017 rights issue, which raised £497m net proceeds. However, the remainder has been achieved through self-help. In 2018 we completed a number of divestments, principally the AvComm and Wireless test and measurement businesses, realising £325m net proceeds. Over the last two years we have also generated free cash flow of £203m, in part from reducing working capital by £67m. This free cash flow result was achieved after £170m of cash was utilised on onerous contracts and other legacy items.

Focusing the Portfolio

We are increasingly focused on our defence, aerospace and space markets having divested the AvComm and Wireless test and measurement businesses and the 'Opera' software businesses in the first half of 2018. In November 2018, we also divested the Group's small lightning test and consultancy business for £1.9m. These were previously all part of Communications and Connectivity.

Resolving Onerous Contracts and Other Legacy Issues

We continue to progress the contract, legal and regulatory issues originally provided for at the 2016 year end. On 19 February 2019 we updated the market on the largest of these, the KC-46 tanker programme. We announced a settlement regarding Boeing's damages assertions, taking a non-underlying charge of £160m in these 2018 results, comprising £86m for dispute settlement and £74m for additional costs to complete. This is in addition to a £40m non-underlying charge taken in the interims.

The £86m settlement will be paid during the first half of 2019, after offset against £37m of withheld hose and drogue invoices. This will result in a £49m balancing payment to Boeing, with the payment withheld against Cobham invoices ended.

David Lockwood responds to questions investors are asking



How will you achieve your medium-term guidance of a Group underlying operating margin 2-3% higher?

I have always believed that improvement in Cobham's underlying operating margin is within our own control and will be driven by our own performance: cost control, effective improvement and investment in operational delivery. To this end, we have been focusing on our cost base, on operational efficiencies, on the supply chain and on enhancing quality. It is from this relentless focus, we will deliver an increasing margin. I have consistently said, delivering the required improvements will not be quick or easy. However, I am pleased to say we are seeing the first fruits of this, although there is more to do.

Is Cobham's turnaround plan, including operational improvement and culture change, on-track?

Against the assessment I made at the start of 2017, I believe we are on-track with our turnaround plan, although the 2018 headline numbers mask a divergence in performance. Mission Systems delivered a much better year but Advanced Electronic Solutions underperformed; however, this uneven progress is not surprising in a turnaround situation. We remain confident we have established a solid foundation from which Cobham can progress by leveraging on our improvement initiatives. These include training in continuous improvement techniques, simplification of structures, reporting and processes as well as investment in technology and infrastructure. We are now starting to embed culture change; all these will continue to be a focus.

When you first joined Cobham, you said it had high value add technology and leading positions in some attractive markets. Do you still believe this to be the case?

Cobham is a business with a history of innovation and technology leadership, and has some truly impressive achievements to its name. My conviction in the quality of its technology and capabilities has not diminished. Our businesses operate in attractive markets, providing opportunities to leverage our technology and know-how. When allied with increased customer engagement, technology investment and an operational improvement focus, I am convinced we will unlock the Group's full potential.

The Balance Sheet is now much stronger than it was – what are your capital allocation plans?

Our capital allocation priority is organic investment for growth and to resolve our legacy issues. We also intend to reinstate an ordinary dividend payment, which will be progressive, taking into consideration underlying earnings and free cash flow cover. After this, we will consider 'bolt-on' acquisitions, where there is strong strategic fit, and the management bandwidth to properly integrate acquisitions, to give an appropriate return on capital. If there is surplus cash we will return it to shareholders. All this will be within the framework of a strong balance sheet, with the net debt/EBITDA gearing ratio to remain below 1.5x.

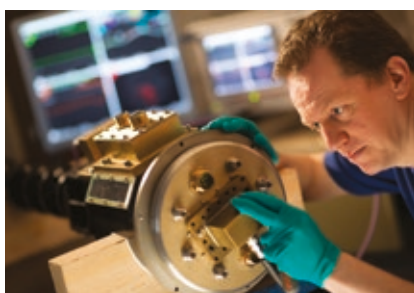
Is the portfolio now as you would like it to be, or should we expect more divestments?

Cobham is best placed to generate value when it focuses on its defence, aerospace and space markets. Following a portfolio review, in 2018 we divested the AvComm and Wireless test and measurement businesses, as well as two smaller businesses. Today, every business in the portfolio lies within our stated boundaries, although inevitably some lie closer to the core of where we truly excel. However, I believe a company's strategy should always evolve, so the Board will keep the portfolio under regular review.

The agreement has settled all disputed matters to the date of the agreement, settled the damages assertions and rebased the schedule for qualification and production of Wing Aerial Refuelling Pod (WARP) and production of the Centerline Drogue System. The stringent terms of the original contract remain in place.

The complex WARP qualification remains in its early stages and is now anticipated to complete around the middle of 2020, with associated flight test commencing in the first half of 2019. The rebased schedule, in which WARP qualification is a critical milestone, has led to a reassessment of the aggregate remaining risks, including supply chain, resource and concurrency ahead of final WARP certification and production. The £74m non-underlying charge for additional costs to complete reflects the best estimate of the retained contract risks, as well as the costs of the revised schedule. The agreed schedule is dependent on certain key third party approvals.

Total remaining balances relating to the exceptional onerous contracts and other legacy issues at 31 December 2018 were £206m (2017: £112m). Net cash outflows relating to these were £103m (2017: £67m) with the balances expected to be utilised primarily over the next two calendar years.



One of Cobham's core capabilities is satellite communication technology, with the Group operating in aerospace, maritime and land markets.

Cobham's Davenport, US facility is, part of Mission Systems, a market leader in pneumatics and actuation technologies as well as aerial refuelling.

Operational execution and culture change

We have consistently stated the route to a 2-3% higher medium term underlying operating margin is within our control and will be achieved through our own improvement efforts. It is therefore pleasing to see the Group's operational performance metrics responding positively to our actions. There has been an increase of 3% points in Cobham's customer on-time to promise metric (on-time delivery to customers) to 87% in the last two years and our quality-related key performance indicators are also improving. Supply chain management is a priority area as, without timely supplier deliveries, we cannot improve our own delivery. The timeliness of supplier deliveries is improving as we consolidate the Group's supply chain to provide best value – reliability and quality at optimal cost.

We have continued to simplify the Sectors, providing additional customer focus. We reorganised Aviation Services into two regionally focused businesses. Following the business unit reorganisation in Communications and Connectivity in the first half, we have announced the merger of some operating sites and these will be completed in 2019. Advanced Electronic Solutions has been reorganised into business units focused around its technology capabilities. We continue to believe that ongoing simplification will yield significant results.

In early 2019 we launched our new Cobham purpose, understanding that an effective culture will enable us to better serve our customers, for whom 'Every Mission Matters'. This is supported by desired behaviours which are to be bold, be inventive, be determined and be a team.

New capital allocation policy and dividend

We have set out a new capital structure and capital allocation policy building on our improving performance and strengthened balance sheet. The Board will continue to chart a prudent financial course with the Group maintaining a net debt/EBITDA gearing ratio below 1.5x. This approach recognises the cash needs of the onerous contracts and other legacy items, the remaining contingent liabilities, as well as the flexibility and customer confidence a strong balance sheet brings.

The Board has also agreed a capital allocation policy which will lie at the core of a disciplined approach to investment and value creation. Priorities for capital allocation are as follows:

1) **Organic investment.** Investing in businesses we know and understand is the best way to deliver

shareholder value. We will invest for capability enhancement and growth, including in technology and people and on capital expenditure for equipment and infrastructure, as well as for the resolution of legacy items;

2) **Dividends.** The Board intends to reinstate an ordinary dividend payment with the 2019 interim results. It intends to follow a progressive policy which will take into consideration the profitability and underlying growth of Cobham's businesses and its capital requirements, while ensuring an appropriate level of earnings and free cash flow cover. It anticipates announcing a first full year dividend of 1.0p. Approximately 40% of the full year dividend will be paid at the interim stage;

3) **Bolt-on M&A.** We will carefully consider bolt-on size business acquisitions and other investments where there is strong strategic fit and management bandwidth to properly integrate;

4) **Shareholder returns.** If, after such investments and distributions and having taken into account forecast cash flows, there is surplus capital, then the Board will look to return cash to shareholders.

Technology investment

Effective investment in technology is a capital allocation priority. We have continued to work hard to enhance project controls that underpin the effectiveness of our investments and we have also addressed tools, processes and training and development. This will help bring to market an exciting pipeline of new products and capabilities.

Outlook

We can see the benefits of our improvement actions starting to come through across most of the business, particularly so in Mission Systems. However, Advanced Electronic Solutions underperformed. We have strengthened its management, increased the focus on execution and formulated an overhead cost reduction plan.

Overall the Board's expectations for progress in 2019 remain unchanged with a range of potential outcomes. We continue to believe that there are considerable opportunities to improve the performance of the Group over the medium term and our continuing focus on customers, culture, operational improvement, business simplification and cash will allow us to realise this potential.

David Lockwood
Chief Executive Officer
7 March 2019

Attractive growth opportunities

US defence/security

Represents 38% of Group revenue in 2018

The US defence/security market is growing, primarily driven by elevated security tensions.

Cobham has significant exposure to the US defence budget, in particular to the Procurement and Research, Development, Test and Evaluation accounts, together known as the investment accounts. It has some exposure to other budget line items, including the Operations and Maintenance and Overseas Contingency Operations accounts, as well as to other US Federal budgets including NASA and security agencies.

US defence budgets have been historically impacted by two primary factors. These are macroeconomic conditions, including the level of national debt and Federal budget deficits, as well as global security tensions. Today, Federal debt levels are high, with a sizeable budget deficit, but security tensions are elevated with a number of ongoing regional conflicts, and other potential trouble spots around the globe.

As a result of these ongoing tensions, there was a significant increase in the approved investment accounts' budget for 2018, which has been followed by a smaller increase for 2019. Beyond this time frame, it seems likely that the overall defence budget will flatten out due to growing concerns about Federal deficits. However, neither the budget trajectory nor the investment accounts' share of the overall budget can be ascertained today with certainty.

There is typically a time lag between approval and spending of the defence budget – the latter referred to as 'outlays'. This lag is hard to estimate accurately, as it depends on a number of factors with, for example, certain budget line items being spent over multiple

financial years. However, it is likely that, in the event of a broadly flat budgetary outcome in 2020, some growth in outlays will continue through that year.

The timing of annual budget approvals is also important, with the potential for delays in approvals to cause short term disruption to the allocation of funds and programme level contracting. Without a signed bill, the Department of Defense (DoD) operates under a stop-gap funding measure called a Continuing Resolution, which places additional constraints on spending.

Cobham's relevance to the market

The US DoD's 2018 National Defense Strategy of the United States of America has as a priority the modernisation of key capabilities, including space, missile defence and command, control, communications and computers, intelligence, surveillance and reconnaissance (referred to as C4ISR). The objective to modernise these, and various other capabilities, aligns with Cobham's specialist technologies and capabilities, positioning it well to benefit from US market developments.

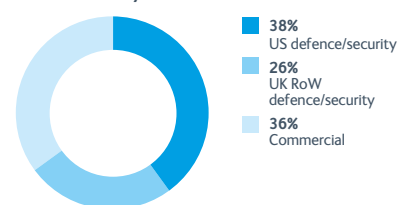
UK, RoW defence/security

Represents 26% of Group revenue in 2018

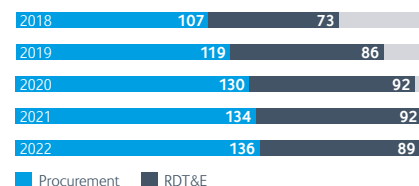
A range of international opportunities across the world.

Cobham supplies its products and services to an addressable global defence/security customer base. Addressable UK, RoW defence/security spending is likely to deliver modest growth overall, driven by security tensions, albeit with regional and inter-regional variations. While international budgets are impacted by a variety of specific regional and local factors, not always mirroring the US, the basic factors that affect US budgets, also impact other national budgets: namely

Revenue by market %



US Department of Defense National Defense Outlays \$bn



Source: National Defense Budget Estimates for FY 2019 (Green Book)

macroeconomic conditions and security. Today, there are elevated security tensions in many parts of the world, including in the Middle East, in Asia, in Eastern Europe and in Africa. In Europe, national debt levels remain high, with budget deficits in many countries. However, the security situation has caused a willingness to spend money on defence after a number of years of cuts. For example, NATO, which includes some significant defence budgets, made a public pledge in 2014 that each of its 29 members should spend a minimum of 2% of Gross Domestic Product (GDP) on defence per year. Only 4 members (including the US) out of 27 spent 2% or more of GDP on defence in that year and it is expected that there will be 8 in 2018, with a further 7 members anticipated to achieve this pledge by 2024.

Outside of NATO, some other large defence budgets have continued to be strong, with growth expected in national budgets including India, the

Middle East and East Asia.

Within international markets Cobham also provides specialist Aviation Services to government customers, including maritime surveillance, search and rescue and operational readiness training for fixed and rotary wing aircraft applications. While these markets are competitive, future market dynamics are expected to be favourable as Cobham is able to supply military related services at the fraction of a cost of a military asset, thereby delivering customers needed services in a very cost effective way.

Indicative Growth Outlook in UK, RoW Defence Expenditure £bn



Source: Strategic Defence Intelligence based on investment budgets in Cobham's addressable markets. Excludes inaccessible defence/security geographies.

Cobham's relevance to the market

The US is the world's largest exporter of defence/security equipment and Cobham benefits from its positions on US platforms and programmes. In addition, Cobham also has good positions on non-US platforms and programmes. These also offer additional export opportunities for Cobham's critical technologies.

Commercial

Represents 36% of Group revenue in 2018

Positions in a number of attractive commercial markets, with aerospace and space at its core.

Cobham's commercial positions are focused around aerospace and space markets. Its products are often used for communication purposes, typically in harsh or remote environments. Demand is driven by an increasing global propensity to travel – leading to a requirement for communication – voice, video and data – in difficult environments.

Demand for communication is driven both by operational efficiency and passenger

requirements. In addition, in many of these markets there are increasing numbers of safety mandates leading to demand for products that save lives and safeguard assets.

Our commercial markets (% of Group revenue)

Aerospace

10%



Space*

10%



Outsourced Aviation Services

8%



Other**

8%



* Includes maritime and land SATCOM

** Includes industrial, mining, medical and energy markets

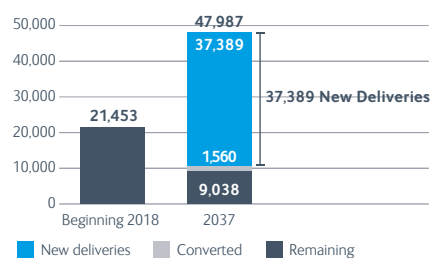
Cobham's largest markets include aerospace, where it supplies products on large commercial transport aircraft, with Cobham products that are fitted in the factory, or used in the aftermarket. The aerospace market is expected to benefit from increases in production over the long term, leading to increased flying.

We have included more detail on some of our capabilities in commercial aerospace markets on pages 14 to 15.

In addition, Cobham also has positions in commercial aviation services in Australia where it provides crew and maintenance services on the Qantas fleet of Boeing 717 aircraft, used for regular passenger airline services. It also provides closed charter flying services for natural resources companies. The latter market has been through a down turn. It is now showing signs of recovery, as commodity prices increase, although market conditions still present challenges.

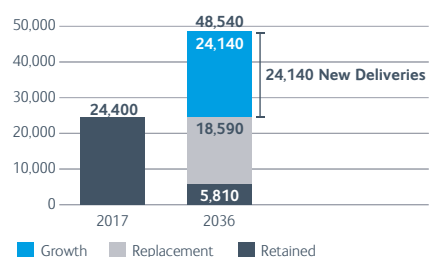
Cobham also has positions in different parts of the space market. In addition to aerospace related products, it also provides satellite communication

Airbus No. of Aircraft



Source: Airbus' Global Market Forecast (GMF) for 2018-2037. Includes passenger aircraft above 100 seats and freighter aircraft above 10 tonnes.

Boeing No. of Aircraft



Source: Boeing commercial market outlook 2018-2037. Includes regional jet, single aisle, wide body and freighter aircraft.

equipment used for ground and sea applications, providing communications links to satellites. It also provides products on satellites, including radiation hardened, high reliability microelectronics and waveguides. Space offers some attractive opportunities, as it undergoes a period of innovation and change. The satellite market should deliver near term growth due to the launch of a number of low and mid-earth orbit mega constellations, which will supplement traditional geostationary satellites.

Cobham's relevance to the market

Cobham has a number of specialist positions on high volume large transport passenger aircraft. It is adding to its capabilities with new products under development, including the AVIATOR S light SATCOM antenna and the digital Radio and Audio Integrated Management System. These products will be fitted on the Airbus A320neo, and other aircraft. Cobham's small, light and easy to maintain Air Separation Module is used in the aftermarket for Boeing 737NG and Airbus A320 aircraft. It mitigates the risk of fuel tank explosions. In maritime markets, Cobham's SATCOM products enable 'smart shipping' by which operators can generate increased data derived information to help lower their costs in a competitive market.

"We have long experience in our three end markets, with broad exposure to each"

How we create value

1.

What we do

Cobham offers an innovative range of technologies and services to solve challenging problems in our defence, commercial aerospace and space markets. To meet often complex customer requirements, we need to deliver consistently. This is particularly important as our products and services often help keep people alive and protect assets in harsh or remote environments.

2.

Where we do it

Cobham's innovative technologies are predominantly used to produce critical products and subsystems (i.e. at tier 2 and tier 3) in our markets. We also provide components (tier 4), particularly when these are key building blocks for our larger and more complex offerings. Within the Aviation Services business, we also provide fully integrated long term contracts at the tier 1 level; not only does this provide recurring revenue streams but it can also help us demonstrate our products to potential customers in a live environment – a 'product in a service' wrapper.

5.

Examples of the industry value chain

Tier 1. Platforms/ Fully Integrated Systems and Services	<ul style="list-style-type: none"> – Aircraft – Missiles – Medical and Industrial Equipment – Satellites (Commercial and Military) – In flight operational readiness training
--	--

Tier 2. Major Subsystems	<ul style="list-style-type: none"> – Complete Apertures – Missile Subsystems – Electronic Warfare Subsystems
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Tier 3. Integrated Assemblies	<ul style="list-style-type: none"> – Radar Modules – Microelectronic Assemblies – Power Distribution Modules – Actuation/Gimbal Assemblies
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Tier 4. Components	<ul style="list-style-type: none"> – Diodes – Radiation Hardened Components – Capacitors – Filters
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4.

How we generate value

We have differentiation in many of our specialist capabilities and know-how. These are often high value add, and support customers with requirements for demanding environments – in space, air, land and sea, which often means a requirement for mobile capability. These requirements for mobility prioritise small, light products that use the least amount of power possible. Given the environments in which our products and services must operate, these are critical to customer success. This is why Every Mission Matters.

How we share value

Shareholders

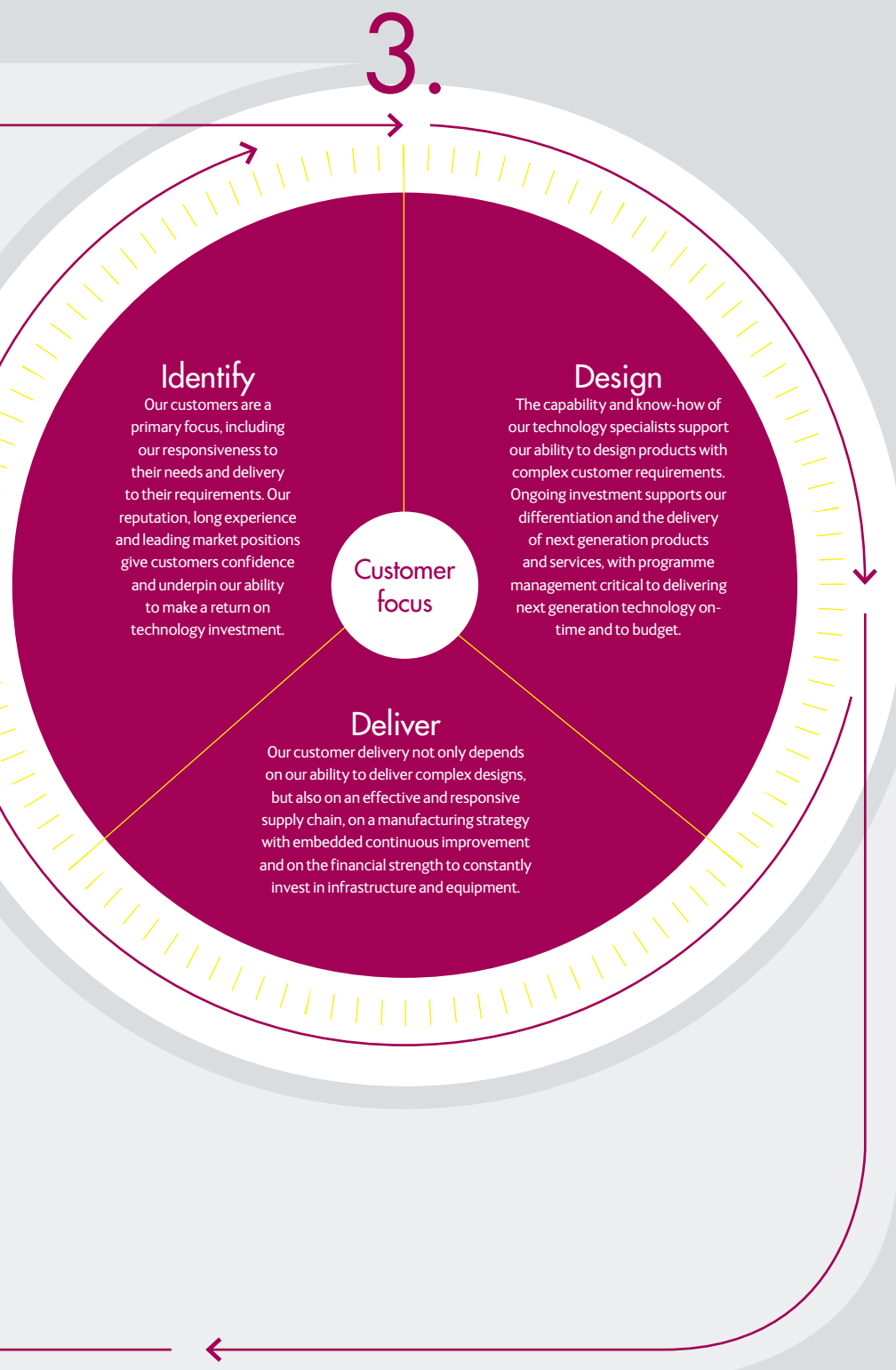
Our technology differentiation and high value add products and services provide a stream of profit and cash from which we provide returns to our shareholders.

Employees

We have around 10,000 employees. The nature of our activities supports high quality, sustainable employment, with an emphasis on highly trained engineers and other skilled professionals.

Customers

We provide highly capable products, which are critical to our customers. We operate in environments where size, weight and power consumption of our technology really matters – in addition to reliability and a compelling value proposition.



Key factors that underpin our business model

Culture

A highly effective culture is key to our success. We understand that 'Every Mission Matters' and we encourage our employees to be bold, be inventive, be determined and be a team. This is what we believe it means to 'Be Cobham'.

Ethics

We operate in highly regulated markets, often dealing with sensitive technologies on behalf of governments, and undertaking critical capabilities for a range of customers. Our ethics training programme is mandated with all employees completing it annually, so that they are aware of their responsibilities and act accordingly, while carrying out their duties on behalf of Cobham.

Health and Safety

We have a proactive Health and Safety programme and look to continuously improve our performance. Our ability to attract and retain talented employees in a competitive environment is in part linked to keeping our employees safe and free from harm. In addition, our operational improvement strategy is also linked to an effective Health and Safety performance.

Environment

Our impact on the environment is manifested through what we do and also what we sell. Our biggest direct impact is in Aviation Services, where we look for efficiencies to improve the fuel consumption of our aircraft. We also recognise the importance of developing smaller, lighter products, helping our customers to reduce energy consumption and lower emissions.

Capabilities in action



Radio and Audio Integrated Management System (RAIMS)

Cobham's digital RAIMS introduces a flexible architecture and digital audio distribution technology. This enables aircrew to control aircraft communications, navigation and data-link systems through a single integrated interface, reducing pilot workload and saving weight and space in the cockpit.



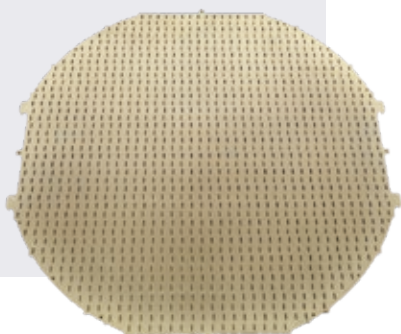
AVIATOR S

Cobham's next generation digital antenna enables aircraft performance data to be relayed to ground crews long before landing, reducing aircraft on ground time and assisting predictive maintenance. Additionally, enhanced positional tracking can be used to allow more aircraft to use the same airspace, significantly improving efficiency and reducing fuel usage.



Weather antenna

Cobham designs and manufactures flat plate slotted array antennas with a variety of applications, including for weather radar on commercial aircraft.

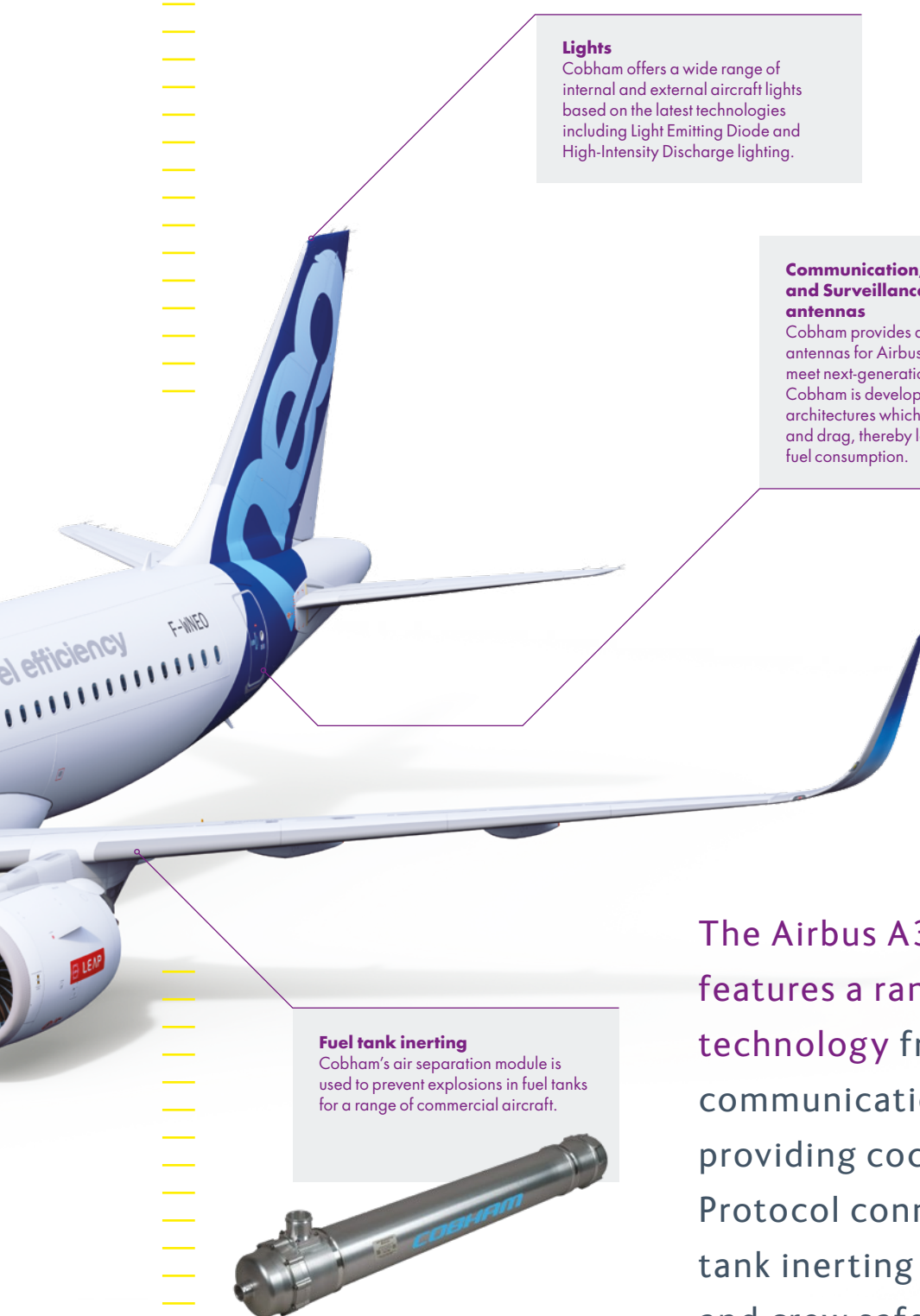


Intercoms

Cobham provides intercoms or aircraft audio address systems, which allow the distribution of music, safety alerts or passenger announcements from either the cockpit or the cabin.

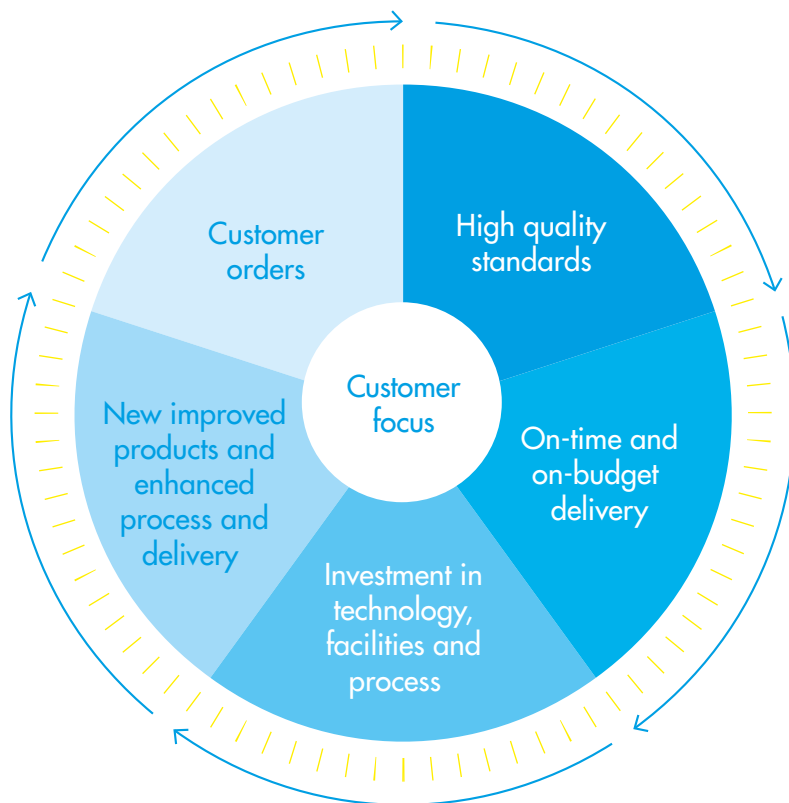
Clocks

Cobham provides Global Positioning System synchronised atomic aircraft clocks. These distribute highly accurate information to on-board avionics systems, enabling them to provide a critical fall back safety system.



The Airbus A320 aircraft features a range of Cobham technology from satellite communication equipment, providing cockpit Internet Protocol connectivity, to fuel tank inerting keeping passengers and crew safe. The aircraft operating environment is an illustration of our ability to provide capable products and know-how that operate in harsh or remote environments.

We are seeing an improving operational performance ...



The Group turnaround strategy's primary focus is on improving operational performance. This is key to delivering improvements in financial performance, including generating revenue growth and underlying operating profit margin enhancement. Late delivery to customers and the rework of products that have failed post-production quality tests are significant costs. They also often result in the need to have in place additional overheads resulting in cost inefficiencies.

In short, operational improvement completes a virtuous circle which helps us grow revenue by consistently and reliably delivering to our customers, as well as improving our underlying operating margin.

See the Chief Executive Officer's Statement on pages 6-9 for a description of our progress during the year. Our Key Performance Indicators (KPIs) on pages 18 and 19 set out the 2018 progress towards achieving our medium term financial and non-financial targets.

Enhancing programme management is key to our turnaround

Programme management

Effective programme management enables us to deliver to our customers on-time and on-budget, increases control over and execution of a range of major projects and underpins the effective allocation of capital. Programme management sits at the heart of our improvement efforts, impacting our business in a number of important ways.

Programme management overview:

- Over 200 **customer driven projects** ongoing
- £103m* **Private Venture (PV) investment** in 2018 (2017: £122m*)
- Over 100 **internal change projects** ongoing

*including divestments

Our delivery framework

Among a number of other initiatives aimed at enhancing our programme management, we have implemented a new Delivery Framework. This simplifies processes, clarifies responsibilities and assigns project categories according to size, risk and strategic importance.

The Framework is arranged around five guiding principles as follows:

1. **Policies and procedures** – Sets out a clear Framework to deliver leading practice for effective risk management across the range of projects undertaken within the Group.
2. **Guide and templates** – Specifies a clearly accountable leader, or sponsor, with standard templates giving consistency and transparency over decision making.
3. **Decision making** – Ensures that each project is managed according to the same principles, using clearly defined phases; each phase is subject to a formalised review before a project can advance.
4. **Assurance** – Provides for effective assurance processes throughout the life of a project, giving confidence that each is on-track and progressing as expected.
5. **Training** – Ensures that everyone involved in programme delivery receives a consistent level of training, with internal coaching available so experience can be retained and disseminated throughout the Group.

... which underpins our organic growth strategy

Capital allocation

We have announced our target balance sheet structure and capital allocation and dividend policy, reflecting the tremendous progress we have made in strengthening the Group's balance sheet over the last two years. The capital allocation policy is aligned to our strategy development and includes the maintenance of a strong balance sheet, which gives us flexibility, allowing us

to invest in attractive opportunities whenever they arise. Our top priority is to invest organically in the business, consistent with our growth strategy set out at the bottom of the page.

Our second priority is to pay a dividend. The intention to reinstate a dividend with the 2019 interims is evidence of our confidence in the business.

1.

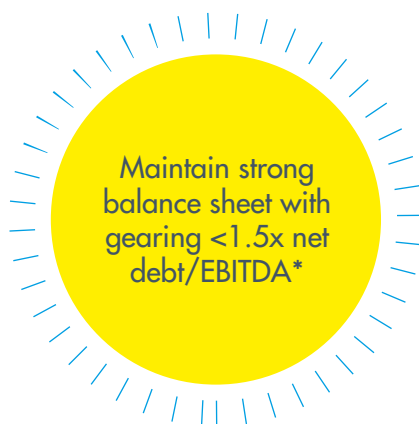
Organic investment

- Invest for growth e.g. capabilities, technology investment, capital expenditure as well as resolution of legacy items

2.

Dividend

- Reinstatement dividend with H1 2019; initial 1.0p full year dividend
- Progressive over time
- Ensure appropriate underlying earnings and FCF** cover



3.

Bolt-on M&A

- Only where there is:
 - A strong strategic fit
 - Management bandwidth to integrate

4.

Capital return

- If there is surplus capital to needs

* After outstanding liabilities for onerous contracts and other legacy items

** Free cash flow

Our Organic Growth Strategy



Our measures of success are aligned with our turnaround priorities

KPI, description	Five year performance	Why this KPI is important	2018 progress and medium term target
1. Organic revenue (%) Organic revenue is revenue stated at constant translation exchange, excluding the incremental effect of acquisitions and divestments. <div>£ A</div>	 <p>2014 2015 2016 2017† 2018</p>	Sustainable organic revenue growth is an important means by which value can be created. It reflects a combination of the conditions in the markets in which we operate and our success in gaining market share.	Group organic revenue decreased by 2%. The result was driven by an adverse revenue adjustment of £79.8m to the KC-46 programme, following a settlement with Boeing. Excluding this, organic revenue increased by 3%. Target: Low-to-mid single digit percentage organic revenue growth.
2. Underlying operating profit margin (%) The underlying operating profit margin is underlying operating profit divided by revenue. <div>A</div>	 <p>2014 2015 2016 2017† 2018</p>	A sustainable increase in the Group underlying operating margin is a key creator of shareholder value.	Group underlying operating margin increased to 10.5%, in particular reflecting the decrease in lower margin KC-46 revenue and increased production volumes in the Mission Systems Sector. This was offset by completion of the UK Defence Helicopter Flying School contract and with the lost contribution from the 2018 divestments. Target: 12-14% underlying operating margin.
3. Underlying EPS (pence) EPS is underlying profit after taxation less amounts attributable to non-controlling interests, divided by the weighted average number of ordinary shares. <div>£ A</div>	 <p>2014 2015 2016 2017† 2018</p>	EPS is an important metric used by shareholders. It is used to summarise the overall financial performance of the Group including revenue growth, operating margin progression, the cost of debt finance and the rate of underlying taxation.	EPS was adversely impacted by currency translation, an increase in the average number of shares, the impact from the divestments and the accelerated interest on debt pay down. Target: Mid-single digit percentage underlying EPS growth.

* On time to promise (OTTP).

** Targets are reassessed annually to drive continuous improvement.

† Restated for the impact of IFRS 15

£ Used as a measure for determining executive remuneration.

A Alternative Performance Measure.

KPI, description

Five year performance

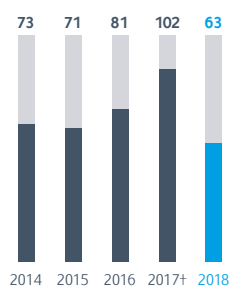
Why this KPI is important

2018 progress and medium term target

4. Operating cash conversion (%)

Operating cash conversion is operating cash flow as a percentage of underlying operating profit, excluding the share of profit from joint ventures and associates.

£ A



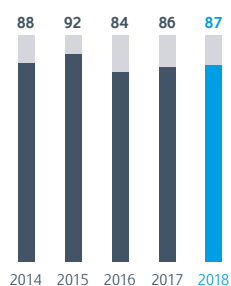
Cash generation is a particular focus for Cobham. It aids investment in the business, enabling the Group to provide returns to shareholders, including a higher share price, increasing dividends and capital returns. Cash generation also supports a strong balance sheet giving customers and suppliers confidence in the future of the Group.

Operating cash conversion was 63%. In particular, cash conversion was adversely impacted by £103m of net cash utilisation of the adjusted 2016 exceptional provisions. This will continue to weigh on cash generation in 2019 and 2020.

Target: Around 90% operating cash conversion.

5. On-time delivery* (%)

On-time delivery is the number of complete orders delivered on time as a percentage of the total number of orders promised for delivery in the same period.



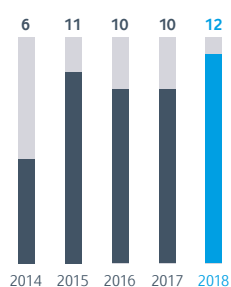
Delivering products and services in line with customer schedules, on budget and to agreed performance and quality standards is essential to winning business and growing market share. It also reduces costs, including eliminating the need for expensive re-work, overtime payments and contractual penalties.

The on-time to promise performance has improved by 3% points to 87%, over the past two years. This reflects ongoing improvement actions, with continuing focus in 2019 on further improvement.

Target: >90% on-time delivery.

6. Voluntary staff turnover (%)

The number of voluntary employee leavers divided by the number of employees at the start of the period. It excludes employees who were made redundant, were dismissed or retired.



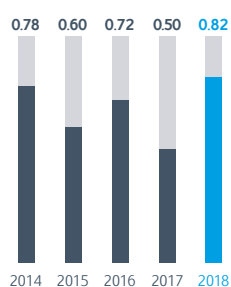
Staff turnover is an important measure which sets out the success in maintaining the balance between retaining existing skills and experience and attracting and promoting employees who bring new ideas and capabilities.

Voluntary staff turnover increased to 12%. This reflects ongoing reorganisation and restructuring. These incorporate changes to established ways of working and an evolving culture as the Group progresses through its improvement strategy.

Target: <10% voluntary staff turnover per annum.

7. Lost work case incident rate

Lost work case incident rate is the number of lost workday injury/occupational illness cases multiplied by 200,000, divided by the number of hours worked.



Ensuring a safe working environment for employees is closely linked to our operational progress. It is also important for attracting and retaining talented employees.

Lost work case incident rate increased to 0.82. During 2019 plans will be implemented to increase business unit management accountability, and increase employee engagement, in particular through encouraging suggestions for improvement.

Target: <0.640** lost work case incident rates

Communications and Connectivity

Provides critical and innovative technology to enable resilient connection for complex, harsh, hazardous and regulated environments, in air and space, on land and at sea, and under the ground. Everywhere, at any time and in the most demanding environments, to be relied on to keep safe connection around the world.

Cobham's FliteLine radio offers high levels of functionality with reduced weight and size. It is in service with the US Coast Guard, the US department of Homeland Security and with Search and Rescue and Emergency Medical Service operators worldwide.



The FliteLine radio was chosen by Boeing to retrofit more than 450 Northrop T-38C trainers operated by the US Air Force, with first deliveries in 2018.



Communications and Connectivity's business units have been reorganised to optimise customer focus and investment. The SATCOM business is now focused on maritime and land markets, with its aerospace activities incorporated within the Aerospace Communications business unit. An Electrical and Electronic Equipment business unit has been established, comprising the microwave, space and slip ring activities previously part of Aerospace Communications. The Antennas business unit has been renamed Aerospace Connectivity.

Total revenue decreased by £146.5m due to the 2018 divestments of AvComm, Wireless test and measurement, Opera software and the lightning test and consultancy businesses. Organic revenue increased by 0.4%. This was driven by the ongoing retrofit of the Sector's FliteLine radios on the USAF fleet of T-38 trainer aircraft, initial shipments of the new RT-7000 aircraft radio, as well as increased sales of 'Minehound' counter-Improvised Explosive Devices detectors to international customers. This was partially offset by lower retrofit SATCOM revenue from airlines complying with the requirement for four minute voice communications in Chinese air space.

Underlying operating profit increased by £3.9m after the impact of divestments and exchange rates. This reflected increased volumes, an improved product mix and operational improvements. However, there was an offsetting increase in PV investment, primarily relating to the next generation Aviator S SATCOM product.

Adding to existing agreements with Airbus for its A320neo, A330neo and A350 aircraft, a Technical Services Agreement was signed with Boeing for the certification of the Aviator 200S SATCOM system on the 737MAX and 777X aircraft. The agreement will make the Cobham product a line fit option, providing next generation SwiftBroadband Safety (SB-S) services to airline users of these aircraft.

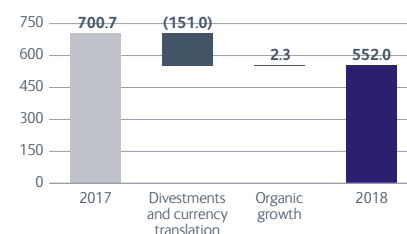
In its maritime markets, the SATCOM business is expected to benefit from its ability to supply Iridium L-Band as part of a VSAT bundle, as well as a standalone terminal. This gives Cobham a competitive advantage as the only manufacturer currently able to offer a combined VSAT and L-Band Iridium solution in the same package.

Inroads are also being made into the important Low Earth Orbit mega-constellation market, with orders received to supply GlobalStar and SpaceX, along with a long term agreement with Airbus Space for microwave products.

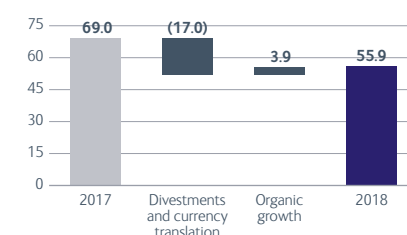
The next generation RT-7000 Integrated Modular Architecture Radio has been released to production with first installations completed on Leonardo helicopter platforms.

Building on the 2018 business unit reorganisation, the Sector has announced the integration of two smaller sites in the US into its existing Prescott, Arizona site. This will be completed during 2019. In addition, the Wireless business unit's production and back-office activities, currently based in Chesham UK, are also expected to be integrated into the Aerospace Connectivity site in Marlow, UK during 2019.

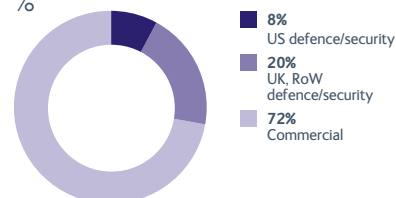
Sector revenue £m



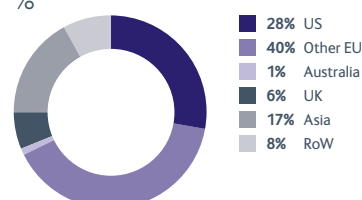
Sector underlying operating profit £m



Revenue by market %



Revenue by geography %



Order
intake

£597.1m
(2017: £715.2m)

Organic
revenue

0.4%
(2017: (3.1)%)

Underlying
operating margin

10.1%
(2017: 9.8%)

Number of
employees

2,394**
(2017: 3,197)

** Total permanent headcount at 31 December 2018

Mission Systems

Provides proven and trusted solutions in air-to-air refuelling, life support and weapons carriage. A leading global supplier of critical control solutions, helping customers increase the safety and mission capabilities of personnel and equipment in extreme environments.

Cobham is a leader in fuel tank inerting technology. There are 4,000 aircraft flying today using Cobham's technology, ranging from commercial and regional aircraft to military helicopters and transports. Cobham developed the technology in 1985 and continues to enhance its offering, having over 18 million flight hours experience.



Cobham signed a fourth major US airline in 2018 to use its leading Boeing 737NG Air Separation Modules. There are now more than 1,600 737NG's flying with this Cobham equipment.



Organic revenue decreased 4%. Excluding the adverse revenue impact from the KC-46 settlement disclosed on page 29 of this report, there was a 15% increase in organic revenue which reflected in part increased air-to-air refuelling production volumes. This included Airbus A330MRTT tanker shipments to Korea, France, Singapore and a multi-nation consortium, as well as increasing production for the Airbus A400M tanker. The first aerial refuelling pods were also shipped to Embraer for its new KC-390 tanker and there was continuing strong aerial refuelling aftermarket demand.

Revenue from fuel tank inerting systems, including for Boeing 737NG Air Separation Modules, also continued to grow with four major US airline aftermarket customers now secured, as well as an international customer. There has also been growth in a number of the Sector's other product lines driven by US defence/security demand, including pneumatic and actuation products. Following a period of growth associated with urgent operational requirements, actuation volumes for a variety of air-to-ground applications are expected to moderate during 2019.

Underlying operating profit increased by £22.1m after the impact of exchange rates. This was driven by the increased production volumes and aftermarket activities. The margin increased to 18.7% (2017: 12.8%), also benefiting from the decrease in lower margin KC-46 revenue related to the Boeing settlement.

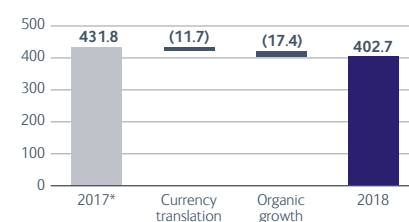
Further details on the KC-46 aerial refuelling settlement and ongoing WARP qualification are contained within the Chief Executive Officer's Statement on pages 6 to 9, including details of the £200.0m charge, which is not in underlying operating profit. There has also been production progress on the programme with the first 26 full production standard aerial refuelling Centerline Drogue Systems and 16 shipsets of Body Fuel Tanks shipped during the year, with further deliveries post year end.

Aftermarket orders were also secured for the Indian Air Force's SU-30 aerial refuelling buddy store. Mission Systems is also providing modelling expertise to support the recently awarded US Navy MQ-25 unmanned tanker programme. This work aids the potential future joint development of an upgraded buddy store.

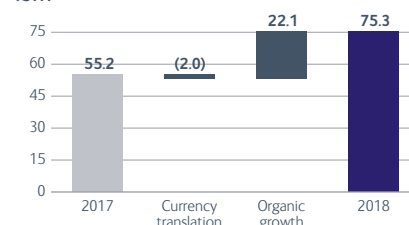
Mission Systems has also secured the first Airbus A320 airline aftermarket customers for its fuel tank inerting air separation modules. The two new US airline customers supplement its success in securing Boeing 737NG customers.

The aerial refuelling aftermarket footprint has continued to be developed. Supplementing the existing US repair and overhaul facility at Fort Walton Beach, FL, a new support centre is being opened close to Tinker Air Force base, OK. The end-user proximity will help serve the customer's aftermarket needs, providing a blueprint for future expansion.

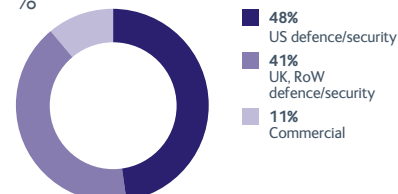
Sector revenue £m



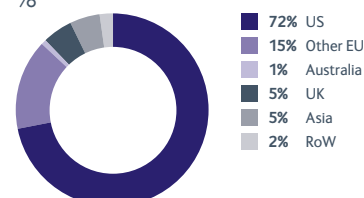
Sector underlying operating profit £m



Revenue by market %



Revenue by geography %



Order
intake

£400.5m
(2017: £517.1m*)

Organic
revenue

(4.1)%
(2017: 6.5%)

Underlying
operating margin

18.7%
(2017: 12.8%*)

Number of
employees

1,981**
(2017: 1,774)

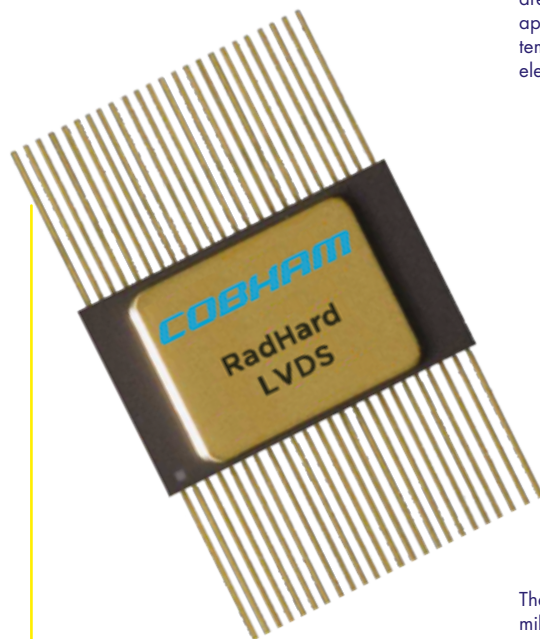
* Restated for the impact of IFRS 15

** Total permanent headcount at 31 December 2018

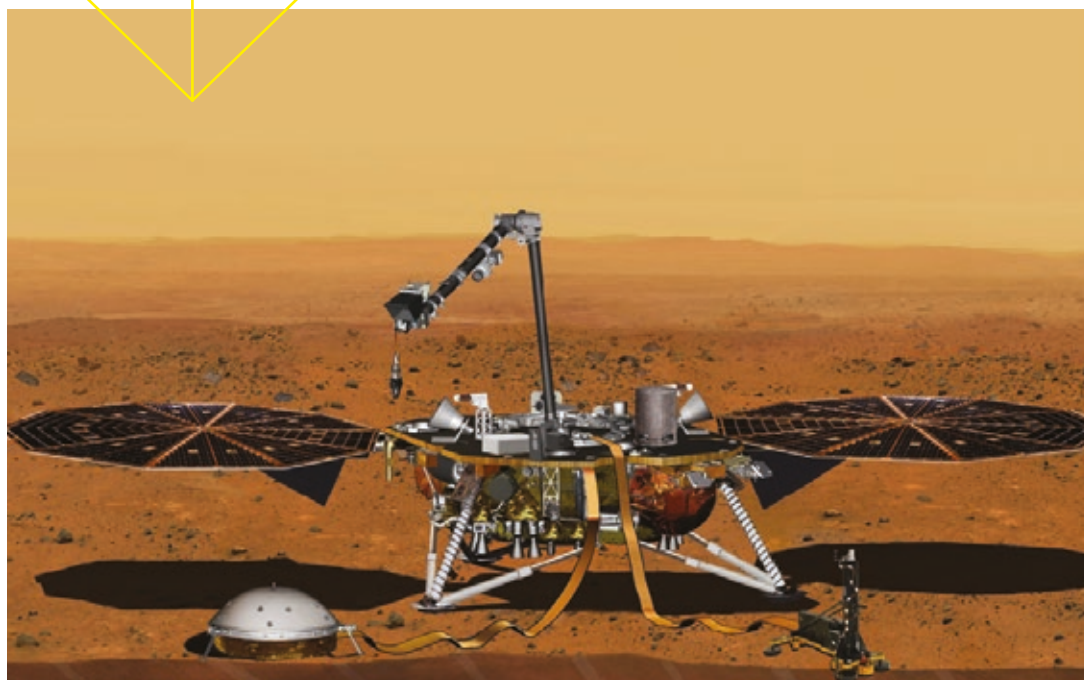
Advanced Electronics Solutions

Provides critical solutions for communication on land, at sea, and in the air and space, by moving data through off the shelf and customised products including radio frequency, microwave, and high reliability microelectronics, antenna subsystems and motion control solutions.

Cobham has engineered radiation hardened and high reliability microelectronics for hundreds of space missions over the last 30 years. Its products are the foundation for many critical space applications, being able to withstand extreme temperature and radiation. It supplied a range of electronics for NASA's 2018 Mars Insight mission.



The Insight mission has travelled over 301 million miles to Mars to begin a two year mission. This includes exploring how a rocky body forms and evolves to become a planet by investigating its interior structure and composition. The mission will also determine the rate of Martian tectonic activity and meteorite impacts.



Credits: NASA/JPL-CalTech

The Sector operates under an SSA, operating under a Sector Board which is critical to its governance and performance. During the year, General Kevin Chilton, a former Commander of US Strategic Command joined the Board, in addition to Mark Santamaria, the new Sector CFO.

Advanced Electronic Solutions has reorganised its operations around its main technology areas, comprising communication, navigation and identification (CNI); electronic warfare; radar; medical, industrial and security; guided munitions and space. The revised structure incorporates a new Chief Operating Officer position to focus on execution and improvement. Together these changes are intended to facilitate collaboration, deliver cost efficiencies and enhance customer focus.

Organic revenue growth increased 4%. This was driven by guided munitions, radar and electronic warfare related revenue. Increasing F-35 Joint Strike Fighter production drove growth in electronic warfare and radar shipments, with new products focused on missile data-link subsystems driving guided munitions revenue.

Underlying operating profit was £11.0m lower after the impact of exchange rates. Profit was adversely impacted by its operational performance, including £9.5m of programme charges, and increased overhead costs. There was also an increase in PV investment, ongoing investment in the Sector's San Diego facility and in IT infrastructure.

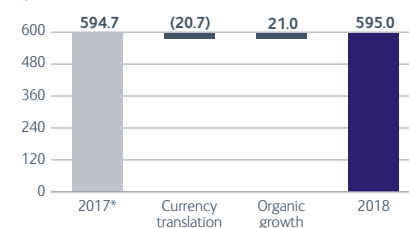
Addressing the underlying operating profit and cash flow performance will be the priority for 2019. The management team has been strengthened and, following the creation of the new COO position, an appointment was made in November 2018, as well as the appointment of the new Chief Financial Officer in the same month. The new management team is working to instil enhanced discipline, including in bidding, contracts and programme management. An overhead cost reduction is planned, with anticipated savings in 2019 of US\$20m.

The order book increased 32% driven by a multi-year guided munition award and continued growth from radar, electronic warfare and space markets. The award of a significant production contract for a Low Earth Orbit satellite constellation has made Advanced Electronic Solutions a leading waveguide provider in this market.

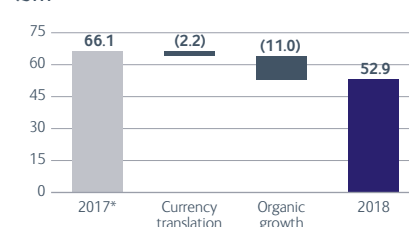
A number of development and Low Rate Initial Production (LRIP) awards have also been received. Within the radar market LRIP deliveries commenced for the US Navy air and missile defence radar programme. Within the electronic warfare market a key position was won on a pod based ship protection system and on the self-protection subsystem for the F-15 aircraft.

The San Diego facility, which is currently increasing its production volumes across a number of programmes, continues to receive significant investment to transform its production performance, on-time delivery and quality management. This project is expected to conclude in the second half of 2019.

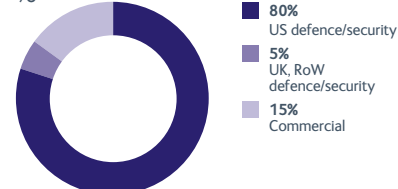
Sector revenue £m



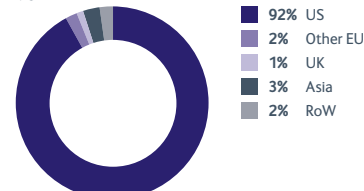
Sector underlying operating profit £m



Revenue by market %



Revenue by geography %



Order
intake

£721.6m
(2017: £563.0m*)

Organic
revenue

3.7%
(2017: 5.8%)

Underlying
operating margin

8.9%
(2017: 11.1%*)

Number of
employees

3,602**
(2017: 3,393)

* Restated for the impact of IFRS 15

** Total permanent headcount at 31 December 2018

Aviation Services

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

Cobham has delivered operational readiness training to the UK, NATO and other customers since the 1980s. This includes delivering electronic warfare and threat simulation using Cobham's own pods.



Operational readiness training is delivered using Cobham owned and operated aircraft, operated by highly experienced aircrew. Cobham is part of a UK company team bidding on the next generation Air Support for Defence Operational Training for the UK Ministry of Defence, which is expected to commence in 2020.



Aviation Services has been restructured into two regionally based businesses during the year, one focused on UK & EMEA and one on Australia. Work on the restructuring has continued, with new management teams in place, enabling improved customer focus and more efficient decision making with simplified reporting lines. In the UK & EMEA region, the relocation of its rotary wing business head office to merge with the fixed wing business was largely completed by the year end.

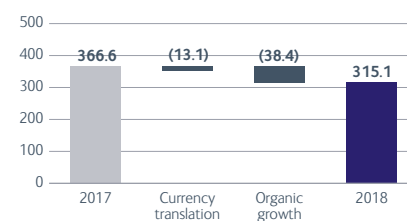
Organic revenue decreased by 11%, driven by the completion of the UK DHFS contract at the end of March 2018, and the prior year completion of a helicopter contract in Qatar. In Australia, additional work was secured in the natural resources sector including new fly-in, fly-out contracts with Oz Minerals, the Independence Group and Dacian Gold, but was offset by lower flying activity for Chevron, following a new contract phase agreed in 2017.

Underlying profit was £10.3m lower after the impact of exchange rates. This largely reflected completion of the DHFS contract and restructuring costs of £3.5m.

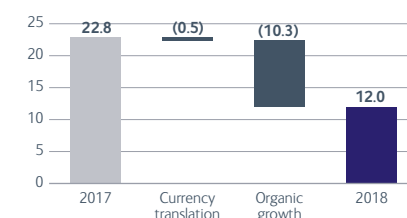
In December 2018, Aviation Services received a multi-year order of over £50m to supply Electronic Warfare training pods as part of the NATO Joint Electronic Warfare Core Staff (JEWCS) capability package. These next generation pods will provide complex and realistic training through radar and communications jamming as well as threat simulation, being designed to meet an evolving threat environment. The JEWCS order, the first of its type for Aviation Services, leverages its long experience in providing Operational Readiness Training services to the UK MoD, as well as international customers.

Aviation Services has continued preparations for the UK MoD Air Support to Defence Operations Training (ASDOT) programme, which will replace its O2O operational readiness training contract from mid-2020. In November 2018, QinetiQ joined the Cobham team, alongside existing members Draken International and 3SDL. Cobham submitted its ASDOT bid in early 2019, with the down-selection of a preferred bidder anticipated around the middle of 2019.

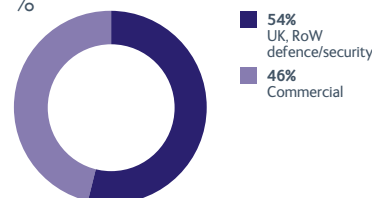
Sector revenue £m



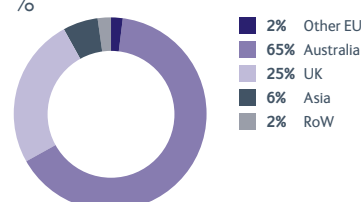
Sector underlying operating profit £m



Revenue by market %



Revenue by geography %



Order intake

£228.7m
(2017: £122.4m)

Organic revenue

(10.9)%
(2017: (2.4)%)

Underlying operating margin

3.8%
(2017: 6.2%)

Number of employees

1,718**
(2017: 2,072)

** Total permanent headcount at 31 December 2018



Returning the Group to financial strength

Summary of underlying results

To assist with the understanding of earnings trends, the Group has included within its published financial statements non-GAAP alternative performance measures including underlying operating profit and underlying profit. The non-GAAP measures used are not defined terms under IFRS and therefore may not be comparable to similar measures used by other companies. They are not intended to be a substitute for, or superior to, GAAP measures.

Management use underlying measures to assess the operating performance of the Group, having adjusted for specific items as detailed in note 3 to the Group Financial Statements. They form the basis of internal management accounts and are used for decision making including capital allocation and a subset also forms the basis of internal incentive arrangements. By using

underlying measures in segmental reporting, this further ensures readers of the financial statements can recognise how incentive performance is targeted. Underlying measures are also presented in this statement because the Directors believe they provide additional useful information to shareholders on comparative trends over time. Finally, this presentation allows for separate disclosure and specific narrative to be included concerning the adjusting items; this helps to ensure performance in any one year can be more clearly understood by the user of the financial statements.

In 2016, certain exceptional items were adjusted for and excluded from underlying measures due to their unusual size and incidence, arising out of the January 2017 Balance Sheet review and included revisions to the carrying value of assets, additional contract loss provisions and legal and other provisions. Where relevant, updates to, and the final outcome of, these items are presented consistently with this treatment as exceptional charges or credits as appropriate.

A reconciliation of statutory to underlying profit numbers is set out on page 29.

A summary of the Group's underlying results is set out below:

£m	2018	2017*
Revenue	1,863.3	2,091.6
Operating profit	196.1	213.1
Operating margin	10.5%	10.2%
Net finance expense	(40.9)	(37.2)
Profit before tax	155.2	175.9
Tax	(35.6)	(37.3)
Tax rate	23.0%	21.2%
Profit after tax	119.6	138.6
Weighted average number of shares (millions)	2,379.8	2,231.8
EPS (pence)	5.0	6.2

*Restated for the impact of IFRS 15

Definitions of the underlying measures can be found on page 107.

Orders

Order intake was £1,946.3m (2017: £1,915.4m). At constant currency and excluding divestments, 2018 order intake increased by 13%, Group book-to-bill was 1.04x (2017: 0.92x); excluding Aviation Services, which is characterised by the receipt of large multi-year orders, book-to-bill was 1.11x (2017: 1.04x).

Reconciliation of underlying measures

£m	2018	2017*
Operating profit	111.9	106.9
Adjusted to exclude:		
Amortisation of intangible assets arising on business combinations	89.8	138.9
Derivative financial instruments	19.7	(28.9)
Net pension adjustments	3.4	–
Impairment of goodwill and other intangible assets	–	33.5
Reversal of impairment of intangible assets	–	(31.8)
Carrying values of other assets provided at 31 December 2016	–	(1.4)
Legal and other provisions provided at 31 December 2016	(1.7)	(8.0)
Dispute settlement and increased cost estimates of fixed price contracts	200.0	–
Amounts related to prior periods restructuring programmes	–	4.7
Profit on divestments and other M&A costs	(227.0)	(0.8)
Total operating reconciling items	84.2	106.2
Underlying operating profit	196.1	213.1
<hr/>		
£m	2018	2017*
Profit before taxation	71.0	69.7
Adjusted to exclude:		
Total operating reconciling items above	84.2	106.2
Underlying profit before taxation	155.2	175.9
Taxation charge on underlying profit	(35.6)	(37.3)
Underlying profit after taxation	119.6	138.6
<hr/>		
Underlying EPS (pence)	5.0	6.2

*Restated for the impact of IFRS 15

Revenue

A summary of the changes to Group revenue in the year is as follows:

£m	2017*	FX translation	Divestments	Organic growth		2018
				KC-46**	Other	
	2,091.6	(50.1)	(146.5)	(79.8)	48.1	1,863.3

*Restated for the impact of IFRS 15

** Impact of 19 February 2019 settlement

Group revenue was £1,863.3m. Revenue was adversely impacted by divestments and currency translation with organic revenue 2% lower. The organic result was driven by an adverse revenue adjustment of £79.8m to the KC-46 programme following the Boeing settlement; excluding this, Group organic revenue increased 3%.

There was organic revenue growth of 4% in Advanced Electronic Solutions, which benefited from higher revenue related to missile data link subsystems and increased F-35 production, driving growth in radar and electronic warfare subsystem shipments. After the adverse revenue impact from the KC-46 settlement, organic revenue in Mission Systems decreased 4%. Excluding this there was a 15% increase with growth from its aerial refuelling, pneumatics and actuation markets. Organic revenue decreased 11% in Aviation Services, primarily driven by the previously reported completion of the UK Defence Helicopter School (DHFS) contract at the end of March 2018.

Analysing the revenue performance by end market, Group organic revenue in the US defence/security market, which was 38% (2017: 37%) of Group revenue, decreased by £35.6m or 4.8%. UK, RoW defence/security organic revenue, which was 26% (2017: 23%) of Group revenue, increased by £1.0m or 0.2%. Organic revenue in the Group's commercial markets, which was 36% (2017: 40%) of Group revenue, increased by £2.9m or 0.4% in the year.

Underlying operating profit

Group underlying profit was £196.1m (2017: £213.1m) after adverse currency translation of £5.5m and the lost contribution from divestments of £22.5m. Excluding these factors, Mission Systems increased its underlying operating profit by £22.1m, driven by higher production volumes and aftermarket activities, with Communications and Connectivity increasing by £3.9m due to improved volume and product mix. However, Advanced Electronic Solutions decreased by £11.0m, due to increased costs on certain

“Order intake increased by 13%. Book-to-bill was 1.04x”

programmes, including £9.5m of charges, and increased overhead costs. In Aviation Services underlying operating profit was £10.3m lower, due to contract completions. The Group's underlying operating profit also benefited from dividends received by Cobham plc from the AirTanker Group of £9.9m (2017: £0.6m), which were slightly higher than anticipated. These dividends formed part of the net allocation of corporate overheads to the Sectors. The benefit of the dividends have been offset by charges within the Sectors for restructuring, property and other items. The increase in Group underlying operating margin to 10.5% (2017: 10.2%) reflected the factors above and the decrease in lower margin KC-46 revenue related to the February 2019 Boeing settlement.

Statutory operating profit

The Group's operating profit was £111.9m (2017: £106.9m). In addition to the underlying operating profit result, statutory profit includes items which have been accounted for as specific adjusting items, consistent with prior years. The favourable year-on-year changes were as follows:

- Profit on divestments and other M&A costs of £227.0m (2017: £0.8m), principally relating to the divestment of AvComm and the Wireless test and measurement businesses.

Further details of the profit on divestments are given below.

- Amortisation of intangibles arising on business combinations of £89.8m (2017: £138.9m).

Goodwill and other intangible assets arising on business combinations are recognised as a result of the purchase price allocation on acquisition of subsidiaries.

In addition, there was £nil (2017: £4.7m charge) for amounts relating to prior periods' restructuring programmes, which had been accounted for as incremental to ongoing operations. There was also £nil (2017: £1.7m charge) relating to the net impairment of goodwill and other assets, relating to an impairment of the Helicopter Services business unit, largely offset by a partial reversal of a previous impairment of other intangible assets within the Wireless business.

Partially offsetting these were some adverse year on year changes as follows:

- The KC-46 dispute settlement and increases in cost estimates of fixed price contracts of £200.0m (2017: £nil).

This charge relates to the settlement of a dispute with Boeing (£86.0m) and increases in the estimates of the costs to complete development of the KC-46 tanker programme (£114.0m) of which £40.0m was included within the interim results. While KC-46 is part of ongoing trading, this charge is shown as exceptional as it represents a change in the exceptional estimate taken at 31 December 2016. Consistent treatment aids traceability of amounts relating to the same programme and separate treatment from other business activities provides transparency on the operational and financial progress made elsewhere. Further details on the KC-46 charge are included within the Chief Executive Officer's Statement on pages 6 to 9.

- Adverse movements in non-hedge accounted derivative financial instruments of £19.7m (2017: £28.9m favourable);

The impact of derivative financial instruments excluded from underlying results includes changes in the marking to market of non-hedge accounted derivative financial instruments. These amounts relate to foreign currency exchange contracts and would not have impacted the results had the Group chosen to comply with IFRS 9 hedge accounting requirements.

- A credit relating to adjustments to legal and other provisions provided at 31 December 2016 of £1.7m (2017: £8.0m).

The credit relates to legal, environmental, warranty and other regulatory matters provided for in 2016 which have been resolved within their original cost estimates.

- A net pension related charge of £3.4m (2017: £nil).

This includes a £5.5m estimated charge reflecting a 2018 UK High Court decision that defined benefit schemes with Guaranteed Minimum Pensions for men and women in the UK must be equalised. Partially offsetting this is a £2.1m gain on curtailment arising from the closure of the US defined benefit scheme to future accrual.

In addition, there was £nil (2017: £1.4m credit) relating to the adjustments to revisions of the carrying values of other assets provided at 31 December 2016. This related to a provision against receivables which were considered doubtful at 31 December 2016, but which were subsequently recovered.

Technology investment

Included within underlying operating profit was £103.2m (2017: £121.9m) of PV investment, excluding bid costs. PV investment in the year represented 6.7% (2017: 7.1%) of revenue. Excluding divestments, and at constant currency, PV investment was £96.0m (2017: £86.8m), representing 6.3% (2017: 5.7%) of revenue.

Net finance expense and profit before tax

The Group's net finance expense was £40.9m (2017: £37.2m). Included was a net finance charge on cash and debt holdings and uncertain tax provisions of £39.4m (2017: £34.9m). Included within this was £20.4m (2017: nil) related to the accelerated interest (make-whole) payments made in the first half. This was incurred as a result of the pay-down of certain medium term debt.

The non-cash finance charge from pension schemes was £1.5m (2017: £2.3m).

Divestments

During the year, Cobham divested its AvComm and Wireless test and measurement businesses for a headline cash consideration of US\$455m. In addition, it also divested the Opera Software business for £7.8m cash and the lightning test and consultancy business for £1.9m cash. The divestment of these businesses, all previously part of Communications and Connectivity, brings additional focus on Cobham's defence, aerospace and space markets.

IFRS 15 (Revenue Recognition), IFRS 9 (Financial Instruments) and IFRS 16 (Leases)

The Group has adopted the new revenue recognition standard, IFRS 15 from 1 January 2018. The standard impacts the timing of revenue recognition on some long term development programmes, notably in Mission Systems and on some US government product based contracts, in Advanced Electronic Solutions, where control transfers to the customer as the product is being manufactured. The Group has restated its 2017 comparative numbers which increases Group revenue by £39.1m and underlying operating profit by £2.8m. There is no impact on the Group's cash generation or net debt. There has also been an increase in net assets of £4.1m at 31 December 2017.

In addition, the Group has adopted the new financial instruments standard IFRS 9, on 1 January 2018. At the date of application, the only material impact has been to increase the Group's minority shareholding investments (and reserves) by £39.0m as these are now required to be held at fair value, rather than cost.

Further details on the application of these standards have been included in note 2 to the Group Financial Statements.

The Group will adopt IFRS 16 from 1 January 2019 on a fully retrospective basis. A detailed review of its lease arrangements has been undertaken and it has estimated right-of-use assets of approximately £100m and associated lease liabilities of approximately £140m at 31 December 2018. Underlying operating profit in 2018 is estimated to increase by approximately £7m, with an increased interest charge of approximately £7m. IFRS 16 is expected to have a neutral impact on underlying EPS. The standard will not impact the Group's revenue or cash generation. Cobham's bank covenants include frozen GAAP terms.

Cash flow

£m	2018	2017*
Underlying operating profit	196.1	213.1
Less: Share of post-tax results of joint ventures	(0.5)	0.2
Underlying operating profit (excluding joint ventures)	195.6	213.3
Depreciation and amortisation	79.0	84.8
Share based payments	5.8	5.5
Decrease in provisions	(103.9)	(38.1)
Pension contributions in excess of pension charges	(13.5)	(17.3)
Decrease in working capital	23.1	44.1
Gross capital expenditure	(69.5)	(79.8)
Proceeds on disposal of property, plant and equipment	6.8	5.1
Operating cash flow	123.4	217.6
Operating cash/underlying operating profit (excluding joint ventures)	63%	102%
Net interest paid	(35.3)	(34.9)
Taxation paid	(25.5)	(32.2)
Amounts related to prior periods' restructuring programmes	–	(9.9)
Free cash flow	62.6	140.6
Dividends paid	–	(0.1)
Proceeds less costs of business divestments	324.7	(0.9)
Net rights issue proceeds and allocation of treasury shares	–	497.2
New finance lease	(14.7)	–
Exchange movements	21.2	7.9
Decrease in net debt	393.8	644.7
Opening net debt	(383.5)	(1,028.2)
Closing cash/(net debt)	10.3	(383.5)

*Restated for the impact of IFRS 15

Taxation

The Group's tax credit was £2.7m (2017: £14.4m credit). As expected, the Group's underlying tax rate was 23.0% (2017: 21.2%) from an underlying tax charge of £35.6m (2017: £37.3m). The lower underlying tax rate in 2017 was due to a one-off credit from the IFRS 15 revaluation of deferred tax and the change in US tax rate.

Interest deductions on one of the Group's financing arrangements has been under challenge for some time. The Group is actively involved in attempting to resolve this matter ahead of a Tribunal hearing which is scheduled for autumn 2019. These issues are set out in more detail in note 7 to the Group Financial Statements.

Earnings per share (EPS)

Basic EPS was 3.1p (2017: 3.7p) being impacted by the specific adjusting items set out in the paragraphs on statutory operating profit above. These included the KC-46 dispute settlement and increased cost estimates of fixed price contract profitability and adverse movements in non-hedge accounted derivative financial instruments. They were partially offset by profit on divestments and the lower amortisation of intangibles arising on business combination.

Underlying EPS decreased to 5.0p (2017: 6.2p). This was due to the adverse impact from currency translation, the increase in the average number of shares following the 2017 rights issue and from

divestments, an adverse impact from the 2018 divestments and the accelerated interest charges on debt pay-down.

Cash flow

Operating cash flow, which is stated after net capital expenditure, but before interest and tax payments was £123.4m (2017: £217.6m) and operating cash conversion was 63% (2017: 102%). Cash generation was adversely impacted by the net cash utilisation of the adjusted 2016 exceptional charges of £103.0m (2017: £66.6m), which is partly included within the overall decrease in provisions of £103.9m (2017: £38.1m) disclosed in the cash flow statement. Cash flow was favourably impacted by a decrease in working capital of £23.1m (2017: £44.1m decrease). There were lower capital expenditure outflows of £69.5m (2017: £79.8m) as a result of deferred spending. Capital expenditure is stated before proceeds from asset disposals of £6.8m (2017: £5.1m).

Free cash flow was £62.6m (2017: £140.6m). This included net interest payments of £35.3m (2017: £34.9m), including accelerated interest payments of £20.4m, arising in the first half. Net tax payments were lower at £25.5m (2017: £32.2m), with the Group benefiting in the first half from a tax refund relating to a prior period. There were no amounts paid in the year relating to prior period restructuring programmes (2017: £9.9m).

Below free cash flow there was a net inflow of £324.7m primarily relating to the divestment of the AvComm and Wireless test and measurement businesses. There was a net debt increase of £14.7m (2017: £nil) relating to an aircraft finance lease signed in the first half. In 2017, the Group received total net rights issue proceeds and sums relating to the allocation of treasury shares of £497.2m.

Dividend and dividend policy

The Board intends to reinstate an ordinary dividend payment with the 2019 interim results. It intends to follow a progressive policy which will take into consideration the profitability and underlying growth of Cobham's business and its capital requirements, while ensuring an appropriate level of earnings and free cash flow cover. It anticipates announcing a first full year dividend of 1.0p. Approximately 40% of the full year dividend will be paid at the interim stage.

While the primary factors driving dividend payments will be underlying EPS and free cash flow cover, the level of gearing and the Group's overall balance sheet strength will also be taken into account in the Board's decision making. In addition, in determining whether to pay a dividend in any one year, in accordance with its policy, the Board will also consider the level of distributable reserves and the requirements of recurring business commitments such as pension obligations and servicing debt providers.

Strategic Report — Chief Financial Officer's Statement continued

The Group's risk profile is also important to its dividend decision and in this context the Board will continue to consider the Group's principal risks, which are set out on pages 36 to 41.

The Group's Parent Company operates as a holding company which primarily derives its net income from dividends paid by its subsidiary companies. At 31 December 2018, Cobham plc had significant distributable reserves, amounting to £1,008.6m, which mainly related to its retained earnings. The Parent Company Balance Sheet is shown on page 151.

Treasury

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

Net debt and gearing

At 31 December 2018, the Group had net cash of £10.3m (2017: £383.5m net debt), including favourable exchange movements of £21.2m (2017: £7.9m). At 31 December 2018, the net cash balance comprised gross debt of £396.6m (2017:

£835.4m) and cash of £406.9m (2017: £451.9m). Included within this are cash deposits, which are primarily denominated in sterling, US dollars, euro, Danish kroner and Australian dollars, and short term bank deposits, net of off-settable overdrafts all within an original maturity of three months or less.

The Group's policy in respect of the impact of foreign currency movements on the net debt/EBITDA ratio, is that in the event that the Group has net debt, the proportion that is denominated in US dollars should be broadly aligned with its US dollar denominated EBITDA to substantially mitigate the risk of currency related gearing volatility.

Under the Group's borrowing agreements, the net debt number used in the net debt/EBITDA ratio calculation is translated using an average foreign exchange rate. On this basis, the Group ended 2018 with £10.4m of net cash and as a result no net debt/EBITDA ratio has been calculated. In 2017, the Group's net debt/EBITDA ratio was 1.3x. For the purposes of the net debt/EBITDA calculation, according to the debt covenants, certain items are excluded from EBITDA, in addition to a requirement for some other less significant adjustments. Interest cover at 31 December 2018 was 12.3x (31 December 2017: 6.8x). The figures for 2017 presented below have

not been restated for the impacts of changes in accounting policies as these covenant ratios will not be restated.

Debt covenants

£m	2018	2017
Net cash / (debt) – balance sheet	10.3	(383.5)
Net cash / (debt) – average rate	10.4	(405.3)
EBITDA	293.4	308.5
Net debt to EBITDA (not to exceed 3.5x)	N/A	1.3
EBITA	228.5	234.3
Net interest	18.6	34.7
Interest cover (not less than 3x)	12.3	6.8

A summary of the Group's borrowings and associated maturities, together with further details of the financial covenants are set out in note 19 to the Group Financial Statements.

As set out in the divestments paragraph, the Group completed the divestment of its AvComm and Wireless test and measurement businesses on 15 March 2018 for an all cash consideration of US\$455m (subject to certain post-completion adjustments and expenses). Following the completion of the divestment and also utilising existing cash, US\$572.8m of private placement debt (senior notes) were repaid in April 2018, resulting in total accelerated interest costs of £20.4m. At the same time the Group also cancelled a US\$75.0m credit agreement.

The chart (left) summarises the Group's main foreign currency transaction exposures (based on forecast revenue) and the hedging in place to mitigate it.

The Group has exposure to a number of financial risks, including liquidity risk and credit risk, which are described in note 24 to the Group Financial Statements. In addition, it has exposure to the effects of changes in foreign currency exchange rates and interest rates, and these are described on the following page.

Hedging transaction exposure

	\$/DKK	\$/£
2019 Total	\$104m	\$122m
Hedging in Place	\$93m 89%	\$113m 93%
Average Hedge Rate	\$1:DKK 6.20	\$1.36:£1
Hedging in Place		
2020	\$35m	\$28m
Average Hedge Rate	\$1:DKK 6.34	\$1.38:£1
2021 to 2023	\$3m	\$25m
Average Hedge Rate	\$1:DKK 5.98	\$1.49:£1

Historic Average Effective Rate
2015 \$1.59: £1
2016 \$1.51: £1
2017 \$1.41: £1
2018 \$1.36: £1

Dollar/Euro exposure predominantly hedged for 2019 with \$45m @ 1.23

Maturity profile of Group's outstanding debt facilities (£m)

2018	801.2
2019	754.6
2020	605.6
2021	540.8
2022	501.9
2023	110.1
2024	–

Foreign currency translation

The following are the average and closing rates for the four foreign currencies that have the most impact on the translation into sterling of the Group's Income Statement and Balance Sheet:

	2018	2017
Income Statement – average rate		
US\$/£	1.33	1.29
AUS\$/£	1.79	1.68
EUR/£	1.13	1.14
DKK/£	8.42	8.49
Balance Sheet – closing rate		
US\$/£	1.27	1.35
AUS\$/£	1.81	1.73
EUR/£	1.11	1.13
DKK/£	8.31	8.39

Foreign exchange translation exposure arises on the earnings of operating companies based largely in the US, Europe and Australia. These are partially offset by foreign currency denominated interest costs due to the Group's policy of funding acquisitions with borrowings denominated in the same currency and also to align the currency mix of EBITDA with the currency mix of net debt. The interest cost of this debt provides a partial offset against currency denominated profits.

The Group's approximate pro-rata Income Statement sensitivity to currency translation is as follows, calculated as the impact of a 10 cent movement in the full year average rate against sterling:

£m	Revenue	Underlying operating profit
US\$	86	10
AUS\$	17	–
EUR/DKK	26	2
Other currencies	3	2
	132	14

Foreign currency transactions

The Group's aim is to reduce, or eliminate, whenever practical, foreign exchange transaction risk. The US dollar/sterling and the US dollar/Danish krone exchange rates are the most significant exposures, together with a number of other, smaller foreign exchange transaction exposures, including the euro/US dollar. All foreign exchange hedging transactions are approved under delegated authority from the Board. A number of financial instruments, such as forward rate contracts, are used to manage transactional foreign exchange exposure. The Group has a policy of hedging at least 80% of estimated transactional exposure for the next 12 months, a proportion of exposures between 12 and 36 months, and firm exposures on long term

contracts. Details of the most significant of these instruments are described in notes 22 and 24 to the Group Financial Statements.

Some 93% of the Group's anticipated transaction exposure to the US dollar/sterling exchange rate is hedged for 2019 at an average rate of US\$1.36/£1, with additional forward sales in place to partially cover anticipated exposure in subsequent years.

Interest rates

Cobham has various borrowings at both fixed and floating rates of interest. The Group monitors its exposure to movements in interest rates to bring greater stability and certainty to its borrowing costs, with the policy being to assess the proportion of borrowings that are fixed and floating in the context of prevailing market conditions.

Retirement obligations

Cobham operates a number of defined benefit schemes, the largest being the Cobham Pension Plan (CPP) in the UK. At 31 December 2018, the estimated deficit for accounting purposes was £46.6m before deferred tax (2017: £63.2m).

The most significant movements in the deficit related to a reduction of £72.4m due to changes in assumptions, including inflation and discount rates and mortality expectations, and a reduction of £14.4m from employer contributions. Partially offsetting these were actuarial losses on investments, primarily due to liability driven investments and insurance policies, which contributed to overall losses of £63.5m. The CPP triennial valuation was completed during the year resulting in reduced deficit contributions from £17.2m to £6.0m per annum, effective September 2018. The Group has also taken a non-underlying net pension charge of £3.4m.

A reconciliation of the movements in the pension deficit during the year is shown in the table below:

£m	2018
Pension deficit at 1 January 2018	(63.2)
Non operating costs	(3.4)
Interest charge	(1.5)
Net employer funding	13.5
Actuarial gains (net)	8.9
Exchange differences	(0.9)
Pension deficit at 31 December 2018	(46.6)

At 31 December 2018, the scheme assets were £746.4m (2017: £816.3m) and the present value of scheme obligations was £793.0m (2017: £879.5m). Further details on the Group's retirement benefit schemes are given in note 23 to the Group Financial Statements.

Going concern

The Group's business activities, together with factors likely to affect its future development, performance and position, are set out in the business overview on pages 1 to 27 and the principal risks on pages 36 to 41. In addition, notes 1, 14, 22 and 24 to the Group Financial Statements include the Group's objectives, policies and processes for managing its capital, financial risk management, details of financial instruments and hedging activities, and its exposure to credit liquidity and other risks.

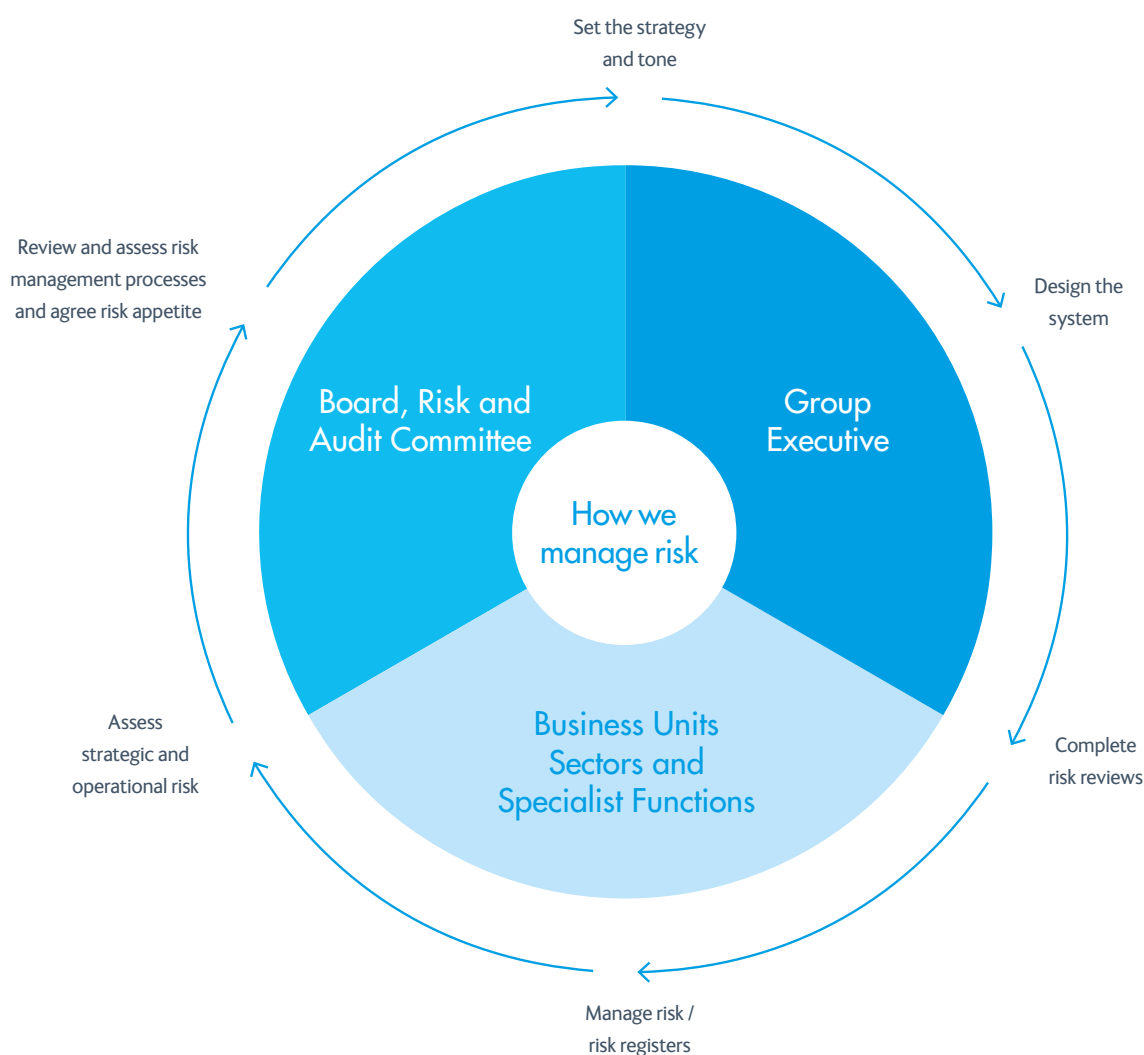
The Group has considerable financial resources with liquidity available on the Balance Sheet from its cash resources and unused credit facilities and it has a spread of maturities on its debt. It has a mix of shorter and longer term contracts and a number of leading market positions with customers across different geographical areas. As a consequence, the Board believes that the Group is well placed to manage its business risks successfully. Accordingly, after making enquiries, the Directors have formed a judgement at the time of approving the financial statements that it is their expectation that the Company and the Group as a whole have adequate financial resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Group and Parent Company Financial Statements.

The UK is set to exit the European Union on 29 March 2019 and the likelihood of a 'no deal' Brexit remains high. On page 36 we have discussed this risk, potential impacts and our mitigating controls in detail. The value of the Group's revenue potentially impacted is approximately £79m from the UK to the EU and £23m from the EU to the UK. Within the supply chain, Cobham's UK businesses spend approximately £33m with EU suppliers, and its EU businesses spend £12m with UK suppliers, of which £11m is from Cobham's UK businesses. A Group Brexit committee has been established to consider risks and propose mitigations. These include buffer inventory put in place where appropriate to mitigate any shortage of key components, assessment of potential options to shift production away from the UK and EU and obtaining appropriate European Aviation Safety Agency 3rd country licences where required. See also the Group's viability statement on page 35.



David Mellors
Chief Financial Officer
7 March 2019

The Group's principal risks have been updated to reflect changes in external factors



How we manage risk

The Board sets the policy for managing risk in the business. It recognises the importance of having effective processes and procedures for identifying, actively monitoring, mitigating and managing the financial and non-financial risks facing the Group.

The Board regularly reviews the Group Principal Risks, which are derived from the detailed risks reported across the Group by businesses and functions, and satisfies itself that these risks are

managed within the Group's appetite for risk. The Board also ensures that the Group's risk exposure remains appropriate and that this links to the effective delivery of its strategic objectives.

The Board has ultimate accountability for the execution of risk management and internal control systems, with the Group Executive responsible for the execution of risk management throughout the Group. The Board Risk Committee provides assurance regarding the management of

principal operational risks. The report from the Chairman of the Board Risk Committee is presented on page 70.

The Board has delegated responsibility for monitoring and reviewing the effectiveness of the Group's risk management and internal control systems to the Audit Committee. Assurance over the effectiveness of these systems is provided through regular management reporting to the Audit Committee. For the Advanced Electronic

Solutions Sector (CAES), which participates in classified US government programmes and so operates under a US DoD SSA, specific assurances and authorised assurance reports are given by CAES management, which has its own Audit Committee. The Group's Chief Executive Officer and Chief Financial Officer both sit on the Board of the SSA, as described on page 59.

The process for monitoring and controlling risk, illustrated in the diagram on page 34, emphasises ongoing evaluation and monitoring by the management teams at each appropriate level: Business Unit, Sector, specialist function and at Group level.

The Group manages risk by operating a three lines of defence risk and control model.

The first line of defence consists of operational management implementing and maintaining effective risk identification, reporting, management and internal control systems. This ensures that risk management remains an integral part of the Group's day-to-day operations and facilitates the escalation of significant risks as and when they are identified.

The second line of defence consists of Group functions who support operational management in their own assessments and also maintain their own risk registers. The second line also includes the Group Executive, who regularly review the Group principal risks and other Group strategic risks and who perform deep-dive reviews on specific risk areas. These lines of assurance also include the Group's ethics reporting system, which enables employees to raise concerns over ethics and compliance matters.

Internal Audit, which forms the third line of defence, is empowered to provide an independent assessment of the effectiveness of risk management and internal control systems, as well as to identify areas for improvement. The Internal Audit and Assurance function reports directly to the Audit Committee Chairman to ensure its independence and objectivity.

Principal risk and uncertainties

The Group maintains a register of principal risks and uncertainties covering the strategic, operational, financial and compliance risks faced by the Group. The Group's risk management framework is structured to ensure that risks are identified promptly by management teams to facilitate timely mitigation and are managed appropriately in support of the delivery of the Group's strategic plan. The risks identified are documented and measured, including the ownership of individual risks. Data from this process have been aggregated and used as the

basis for the Group's principal risk disclosure on pages 36 to 41.

The risks are regularly reviewed and exposure is rated in terms of both inherent risk (before mitigations) and current risk (after mitigations), which allows the Group to identify risks that are heavily dependent on internal mitigating controls and to allocate resources appropriately. Risks are also considered in comparison to an appropriate target exposure (or appetite for risk) which is established by the Board. The appetite for risk is articulated as low, medium or high across the various elements of the risk framework. There is a higher appetite for areas of strategic risk including the promotion of growth, for example in business and product portfolios, and in the strategic planning processes. There is a low appetite for compliance risk – including zero tolerance for ethical issues such as bribery – with a medium appetite for operational and financial/reporting risks. The Group's controls, mitigation activities and associated assurance measures reflect the appetite for risk for each position.

As a result of this process, several changes have been made to the Group's principal risks. The risk relating to the Group operating within a volatile macroeconomic environment has been updated to include further information with respect to the effects on the Group of the United Kingdom's expected exit from the European Union ("Brexit"), and the mitigating actions that are being taken as a result. The rating for the risk related to the Group's Mergers & Acquisitions activities has been reduced to reflect the successful divestment of the AvComm and Wireless test and measurement businesses during 2018. Finally, the rating for the risk related to the Group's defined benefit pension schemes has also been reduced to reflect the completion of the triennial actuarial valuation of the Cobham Pension Plan, and the associated reduction in the deficit and the Group's required deficit funding.

Viability statement

The Board considers the Group's viability as part of its continuing programme of strategic planning, monitoring and managing risk. The Board has concluded that the most relevant time horizon for this review is three years, taking into account the diversity in demand characteristics of the Group's end markets. These range from relatively long cycle businesses such as Aviation Services and some US defense related businesses and air to air refuelling, which contain predominantly multi-year contracts, to the less predictable, largely commercial, shorter cycle businesses, such as SATCOM, which typically operate with an order book of a few months or less.

Assessing viability

The starting point in assessing the prospects of the Group is the annual strategic planning process. The output of this process contains all of the key underlying assumptions that will provide the most appropriate information on which to assess the Group's viability.

In making its assessment of viability, the Board has taken into account a number of different factors to ensure that it fully reflects the Group's current position and future objectives. The main factors considered were:

- The Group's strategic objective, which is to continue the turnaround of the Group's operational performance through focus on customers, delivery, cash and capital allocation. The Group's strategy is set out on pages 2 to 27.
- The Group principal risks and their potential impacts. These are described in detail in the principal risks section of this report on pages 36 to 41. The Board considers the potential financial and operational impact of plausible downside scenarios resulting from these risk events occurring individually or in combination. Consideration was also given to the occurrence of other individual events that in their own right could have a material impact on the Group's viability. Whilst all risks are considered, the risks which have the most significance with regard to the Group's assessment of viability are those relating to the Group's markets (specifically the KC-46 contract) and its potential tax liabilities.
- The capacity of the Group to absorb additional risks which may arise in the future, taking into account both financial and non-financial constraints.

Based on the consolidated financial impact of the sensitivity analyses and associated mitigating internal controls and risk management actions either now in place, or which could be implemented, the Board has concluded that the Group will be able to maintain sufficient bank facilities to meet its funding needs over the three year period.

Confirmation of longer term viability

Based upon the assessment of the principal risks facing the Group and robust downside sensitivity analysis, all of which are described above and on pages 36 to 41, the Board has a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to the end of December 2021.

The Group's going concern statement is detailed on page 33.

Strategic Report — Principal Risks continued

Title	Risks and Impact	Key Mitigating Controls
<p>The Group operates within a volatile macroeconomic environment</p> <p>KPIs</p> <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – On-time delivery – Voluntary staff turnover 	<p>Cobham's revenue and costs are dependent on a complex mix of macroeconomic, fiscal, commercial and strategic defence and security factors, arising from global defence/security and commercial markets within which it participates.</p> <p>38% of the Group's revenue is derived directly or indirectly from the US Government. Despite the agreement of a budget before the commencement of the fiscal year, US defence spending levels are difficult to predict beyond the near term in part due to the recent mid-term election results resulting in a change in control of Congress, as shown by the recent US Federal Government shutdown.</p> <p>26% of the Group's revenue is derived directly or indirectly from non-US governments. While heightened regional security tensions have led to an increase in demand for the Group's capabilities and know-how, the general level of public deficits and indebtedness remains high, which the Group expects will act to limit growth in defence and security investment. The Group also benefited from revenue driven by urgent operational requirements for air to ground systems in 2018.</p> <p>The Group also has some remaining exposure to commercial markets which have experienced downturns in response to weakness in commodity markets such as oil and gas, iron and steel, and precious metals.</p> <p>Government and commercial customers are increasingly focused on pricing as budgetary pressure requires them to do more with less, even where headline budgets are expected to increase, in areas such as US defence. Protectionism by governments is also growing in response to the perceived effects of globalisation on national economies.</p> <p>If the Group does not anticipate changes in the various end markets which it serves (including deterioration in demand or a fundamental shift in how customers procure products and services), changes in input costs, and changes in other macroeconomic factors such as exchange rates and interest rates, its business, results of operations and financial condition could be adversely affected.</p> <p>The UK is set to exit the European Union on 29 March 2019. The terms of withdrawal, any transition period and the future trade relationships, customs arrangements and regulatory framework between the UK, the EU, and other countries are being negotiated, with limited progress being made in the remaining time left to conclude a deal. The likelihood of a 'no deal' Brexit has substantially increased following recent UK Parliamentary votes to approve the negotiated withdrawal terms.</p> <p>The value of the Group's revenue potentially impacted is approximately £79m from the UK to the EU and £23m from the EU to the UK. Within the supply chain, Cobham's UK businesses spend approximately £33m with EU suppliers, and its EU businesses spend £12m with UK suppliers, of which £11m is from Cobham's UK businesses.</p> <p>Depending on the ultimate outcome, Cobham may incur additional costs and other operational issues associated with the transfer of goods between the UK and the EU and third countries as a result of new tariffs, customs delays, the need to meet multiple standards and increased regulatory complexity. These additional costs could include the need for extra inventory, new or additional certifications and changes to its manufacturing strategy. Brexit could also require the Group to modify supplier and customer contracts and we may lose access to research or other funding from EU institutions.</p> <p>The worst case scenario could see a 'no-deal' Brexit, which could lead to severe impacts arising from material shortages throughout the Group's supply chain.</p>	<p>Review of near and long term market trends conducted as part of the Group's annual strategic planning process to ensure that actual and anticipated impacts from macroeconomic risks are minimised and managed effectively.</p> <p>Periodic reviews of externally sourced market demand data are conducted, with subsequent re-forecasting and adjustment of internal planning in line with market demand.</p> <p>A culture of continuous improvement should enable the Group to improve operating performance, while reducing costs. This should enable the Group to grow market share and remain competitive in the face of volume declines or price pressures, whilst retaining flexibility to adjust the cost base appropriately to changing market conditions.</p> <p>Regular meetings are held with key customers to ensure new market developments and technology requirements are understood.</p> <p>The Group uses financial instruments where applicable to assist in the management of foreign exchange and interest rate risks, principally forward exchange contracts and interest rate swaps.</p> <p>A Group Brexit committee has been established to consider risks and propose mitigations. These include the preparation of Brexit impact analyses, including potential effects on both customers and suppliers.</p> <p>Buffer inventory has been put in place where appropriate to mitigate any shortage of key components.</p> <p>Analysis of potential options to shift production away from the UK and EU has been undertaken and contingency plans put in place.</p> <p>Appropriate European Aviation Safety Agency 3rd country licences have been obtained where required. Registration, Evaluation, Authorisation and restriction of Chemicals (REACH) certificates are being applied for where appropriate.</p>
<p>Current Exposure High Target Exposure Medium Risk Trend compared to 2017 Increased Timing of Impact Months (due to potential Brexit impacts)</p>		

Title	Risks and Impact	Key Mitigating Controls
<p>The characteristics of the Group's markets and the resulting contractual environment are highly complex</p> <p>KPIs</p> <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion 	<p>Many of the end markets served by Cobham are highly competitive. The Group relies on its ability to win business ahead of its competitors through a combination of differentiated technology, contractual terms and price. There is no assurance that the Group will be able to maintain its current market share with respect to its products or services due to the development of competing technologies, the periodic retender and renewal of existing contracts, the inability to develop existing products due to resource constraints or the emergence of new competitors.</p> <p>The Group has a number of contracts which span more than one accounting period, some of which have a fixed price. If the Group is unable to or fails to accurately estimate the resources and time necessary to meet contractual milestones, the Group may be subject to claims for damages for late delivery. If the costs required for the delivery of such contracts are higher than those expected, as a result of the performance of new or developed products, schedule over-runs or other external factors (such as inflation resulting in an increase in input costs), which cannot be passed on to a customer, the profitability of a contract may be reduced, or result in it becoming loss making.</p> <p>The timing of order receipt from customers could have a material impact on the Group's performance in a given reporting period, as the amounts payable under such contracts can be individually substantial.</p> <p>The Group's existing contractual arrangements are subject to periodic renewal and retender. There can be no assurance that the Group will be able to successfully renew such contracts. For example, the contract with the UK MoD for the provision of airborne operational readiness (the 020 contract) expires at the end of 2019 and is in the process of being retendered, with a number of competing teams bidding for this work.</p> <p>Some of the Group's contracts have terms (which are not unusual in the Group's markets), that provide for unlimited liabilities for the Group or termination rights for the customer and, in some cases, damages and consequential loss exposure. Many of the Group's contracts are also across international borders, leading to increased complexity in interpretation. The contract for aerial refuelling systems for the KC-46 aircraft is the Group's most significant example of this type of contract.</p> <p>The Group is reliant on third party manufacturers and key suppliers, to whom certain manufacturing and engineering functions are outsourced. This can result in a reduction in control over capacity allocation and quality, and may result in disputes regarding the ownership of intellectual property.</p> <p>The occurrence of any or all of these factors may result in the financial performance of the Group being impaired, through reductions in revenue, increased costs or the emergence of unexpected liabilities.</p>	<p>The Group focuses on areas within those markets in which it has deep customer understanding and technical expertise so reducing the likelihood of an emergent technology or competitor affecting the competitive position.</p> <p>Fixed price bids and projects are reviewed for early detection and management of issues which may result in cost over-run or excessive delivery risk.</p> <p>The Group's Lifecycle Management process is applied to significant contracts, to identify and mitigate cost and schedule over-runs or other issues.</p> <p>A Contract Policy is used which is intended to ensure that the Group enters into contracts with an appropriate balance of risk and reward.</p> <p>The Group's bid and approval process is applied to all bids, contracts and development programmes to ensure that a consistent approach is followed.</p> <p>There are appropriately trained personnel within the business to ensure that the contract policy is adhered to, and that delays to negotiating and agreeing contracts are minimised. Training is undertaken for key staff with responsibility for negotiating contracts.</p> <p>The Group's exposure to individual suppliers is reviewed regularly to ensure that the level of reliance is appropriately managed.</p>
<p>Current Exposure High Target Exposure Medium Risk Trend compared to 2017 Increased Timing of Impact Months</p>		
<p>Shortage of appropriate skills and talent</p> <p>KPIs</p> <ul style="list-style-type: none"> – Voluntary staff turnover 	<p>Key to execution of the Group's strategic plan is the recruitment, development and retention of sufficient personnel with the appropriate skills to meet the needs of the business, in engineering, technical and other specialist and managerial roles. These are amongst the most sought after skills within the worldwide labour market.</p> <p>This is exacerbated by nationality restrictions in certain of its markets, which prevent the Group from accessing a worldwide talent pool. Insufficient availability of personnel will generate a resource gap that will impair the Group's ability to deliver against its strategic plan.</p> <p>Employee retention has been and may continue to be challenging, and the Group must continue to engage with its employees and with focus on its strategy and goals.</p> <p>Following Brexit, the ability of the Group to continue to recruit EU nationals to work in the UK may also be reduced.</p> <p>The resulting talent gap could lead to a reduced ability to execute on growth plans and key programmes, resulting in reduced customer confidence and an adverse impact on the Group's financial position and financial outlook.</p>	<p>Workforce planning is undertaken to ensure that skill gaps are identified and plans are established to close them.</p> <p>Compensation planning and review process is undertaken and takes into account any key shortages.</p> <p>Succession planning has been enhanced to ensure that a pipeline of suitable candidates for key roles is maintained.</p> <p>Development programmes are undertaken to ensure that internal candidates develop the skills and experience necessary to undertake more senior roles within the organisation.</p> <p>An upgraded Human Resources information system is being implemented to ensure that talent gaps are identified and resolved quickly</p> <p>See the CR&S section on pages 42 to 49 for further information on talent management actions.</p>
<p>Current Exposure High Target Exposure Medium Risk Trend compared to 2017 No change Timing of Impact Months</p>		

Strategic Report — Principal Risks continued

Title	Risks and Impact	Key Mitigating Controls
Project and Programme Management is not effective KPIs <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – On-time delivery 	<p>The Group designs, develops and delivers products and services that are often customised, utilising complex technologies and outsourced supply chains. It does this through fixed price contracts that can be long term in nature and through internally funded PV projects where it exploits identified market opportunities. Development projects can take place across a wide range of markets and technologies. The decision to outsource, and the selection of the appropriate suppliers can add additional risk to programmes if the supply chain is not properly managed.</p> <p>The Group employs a system of project and programme management known as Lifecycle Management to ensure that all such projects are managed within a common framework. The current deployment of Lifecycle Management across the Group is at varying levels of maturity.</p> <p>Cobham is currently undertaking a number of significant development projects, notably the aerial refuelling development programmes within the Mission Systems Sector and the Aviator 'S' system within the Communications and Connectivity Sector. In addition, all Sectors are increasingly bidding on more complex programmes which require a higher level of integration, such as for the replacement of the 020 contract within the Aviation Services Sector.</p> <p>Failure by the Group to execute or deliver these or other projects or programmes, and to deliver them concurrently in the same locations (for example in Wimborne, UK) gives rise to the risk of increased costs, damages, product liability claims, litigation and other financial liabilities, reduced future profitability and reputational risk. Poor operational performance could also lead to customers withholding new and existing business from the Group.</p> <p>Certain programmes on which the Group has won positions are scheduled to increase production to meet customer requirements, for example the San Diego facility in the US. The growth in production required puts added pressure on quality management and adds additional risk to on-time delivery, contractual performance and reputation.</p>	<p>Where fully deployed, the Group's Lifecycle management framework contributes to ensuring that key contract and programme management risks are appropriately controlled.</p> <p>Investment in strengthening our quality management is being made to improve both in house and supply chain performance. On-time delivery is a Group Key Performance Indicator.</p> <p>A project and programme watch list has been established to ensure increased focus is given to large and technically complex projects.</p> <p>Continuing professional development of project managers is undertaken against agreed standards and identified development needs.</p>
Current Exposure High Target Exposure Low Risk Trend compared to 2017 Increased Timing of Impact Months		
Customer expectations of service, quality and innovation are not met KPIs <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – On-time delivery 	<p>It is crucial to the Group's current and future development that the expectations of its customers are fully understood and fulfilled, in areas such as the development of new products, the delivery of existing products in accordance with customer requirements and the support provided in respect of products that have already been delivered.</p> <p>The Group is increasingly bidding on programmes which involve more complex customer requirements. If the Group fails to understand the future requirements of its customers, or deliver solutions that meet the customers' needs, failure to win new contracts and difficulty in renewing existing contracts may result.</p> <p>In addition, the Group may suffer financial penalties and possibly the loss of existing contracts. Customer pricing pressure may also intensify where customers perceive that the Group is not providing a level of service that is commensurate with expectations.</p>	<p>Customer focus has been a key objective since 2017 and this will continue.</p> <p>Monthly tracking of on-time delivery is undertaken across the Group with target levels for all businesses.</p> <p>Improvements in internal project and programme management capabilities have been made to ensure technical solutions remain closely aligned with customer requirements.</p> <p>An increased level of senior engagement with key customers has been implemented to ensure that customer requirements are fully understood.</p>
Current Exposure Medium Target Exposure Low Risk Trend compared to 2017 No change Timing of Impact Months		
Business change programmes are not successfully executed KPIs <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – On-time delivery 	<p>As part of its turnaround strategy, Cobham is undertaking several business change programmes that are important to the Group's future prospects, in areas such as the implementation of improved Information Technology systems, increased production at certain Business Units and the establishment of a more effective culture throughout the Group.</p> <p>If these programmes are not successfully executed, the Group's ability to deliver its strategic objectives will be impaired, which could lead to reputational damage, deteriorations in financial performance, loss of customer confidence and reduced success in winning new business from existing customers.</p>	<p>Project objectives, schedules and budgets have been defined and are monitored to ensure that successful delivery of projects can be measured.</p> <p>Significant internal projects are being managed under a common governance framework (using the Lifecycle Management process) to ensure that resource requirements are balanced and facilitate delivery against agreed objectives, schedules and budgets.</p>
Current Exposure Medium Target Exposure Low Risk Trend compared to 2017 No change Timing of Impact Months		

Title	Risks and Impact	Key Mitigating Controls
<p>Occurrence of an event leading to a significant business interruption</p> <p>KPIs</p> <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – On-time delivery – Lost work case incident rate 	<p>Cobham's businesses could be impacted by natural disasters or other external events affecting its operational locations, by significant events in the supply chain or by IT systems failures (including from cyber attack), rendering critical systems or manufacturing locations unable to function. In some cases this can be exacerbated by the historic selection of key suppliers which has created significant reliance within the supply chain.</p> <p>Unscheduled interruption to business activities would result in the inability to deliver products to customers in accordance with their expectations. This would result in reduced profits, loss of customer satisfaction, potential cost outlays, and reputational impact.</p>	<p>Programmes have been implemented for the Group's larger manufacturing locations that seek to meet or exceed best practice loss prevention guidance. Employees are trained in relevant loss prevention procedures.</p> <p>The Group maintains major incident/IT failure business continuity plans. IT security and capability is monitored and strengthened when needed.</p> <p>Appropriate insurance cover is maintained, and insurers and other third party experts are consulted to ensure operating infrastructure and processes include robust risk improvement activities.</p> <p>See the Corporate Responsibility and Sustainability section on pages 42 to 49 for further details on mitigating actions against business interruption risk arising from environmental factors.</p>
<p>Current Exposure Medium Target Exposure Low Risk Trend compared to 2017 No change Timing of Impact Days/Weeks</p>		
<p>Failure to comply with laws and regulations</p> <p>KPIs</p> <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – Lost work case incident rate 	<p>Cobham operates in highly regulated environments and is subject to the laws, regulations and restrictions of many jurisdictions, notably including those of the US and the UK as well as many other countries in which it operates.</p> <p>These include but are not limited to anti-bribery provisions, import and export controls, tax, government contracting rules, human rights, environmental, health and safety and data protection regulations. A lack of understanding of legal and regulatory restrictions in force in the jurisdictions in which it operates could lead to the Group being in contravention of applicable laws or regulations.</p> <p>Sanctions for failure by the Group, its sales intermediaries, or others acting on its behalf to comply with laws, regulations and restrictions could include fines, penalties, legal claims, or suspension of the Group from future government contracts for a period of time, as well as having a potentially significant impact on the Group's reputation. Such sanctions could also have an impact on the Group's financial position and future operations.</p> <p>Safety is a key priority throughout the Group, particularly within the Aviation Services Sector which conducts flying operations in support of our customers. Safety is carefully managed through Group-wide processes, but the Group recognises that an accident could have a major impact on its employees, customers and other stakeholders. Such an incident could also result in legal claims, financial damage and reputational loss.</p> <p>Cobham's US defence business is managed through an SSA, which covers the CAES sector, the terms of which are agreed with the US Government. The SSA is intended to ensure that this US defence business is not subject to the effects of Foreign Ownership, Control or Influence (FOCI). Further details of the SSA can be found on page 59. The terms of the SSA may reduce the ability for the Group to effectively manage its US defence operations due to reduced visibility into the business and its performance.</p>	<p>Internal policies and procedures ensure the Group remains in compliance with all legal requirements and regulations, and continues to drive a culture that ensures that ethical, environmental, and health and safety considerations are embedded in all of the Group's activities.</p> <p>Regular review and audit of policies and procedures, including those procedures that relate to the use of sales and marketing representatives, anti-bribery and anti-corruption, gifts and hospitality, whistleblowing, and investigation of ethics and compliance concerns, along with Cobham's Code of Business Conduct.</p> <p>Mandatory training is undertaken by all employees on a variety of compliance related subjects including US Government contracting and anti-bribery and corruption.</p> <p>See the Corporate Responsibility and Sustainability section on pages 42 to 49 for further details on human rights, environmental, and health and safety actions.</p>
<p>Current Exposure Medium Target Exposure Zero Risk Trend compared to 2017 Increased Timing of Impact Days/Weeks</p>		
<p>Governance framework is poorly constructed and implemented</p> <p>KPIs</p> <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion – Voluntary staff turnover 	<p>The Group's organisational structure delegates some operational autonomy and responsibility to its Business Units, including the negotiation and performance of the Group's contracts with its customers. The level of authority that has been delegated may not be fully consistent with the risks within the Group's operations, leading to the over or under control of those risks.</p> <p>This could lead to exposure to unacceptable risks in areas requiring conservatism, potentially damaging the Group's reputation and shareholder value. Conversely, it may also prevent the acceptance of risks required in order to grow the Group's business, hindering the ability to deliver an acceptable return on shareholder investment.</p> <p>The Group has a capital structure that is partially funded through borrowings from banks and other financial institutions. The associated banking agreements incorporate financial covenants and other provisions, breach of which may lead to potential defaults and costs associated with obtaining temporary waivers or the requirement to reduce debt through divestment or additional capital raising.</p>	<p>A streamlined governance framework has been implemented to facilitate appropriate risk taking, and drive improvements in performance through application of effective governance principles.</p> <p>The delegation of authorities is regularly reviewed and issued to ensure that the degree of delegation is commensurate with the management capabilities within each Business Unit, Sector and specialist function.</p> <p>A governance committee has been established to regularly review and update the Group's policies.</p>
<p>Current Exposure Medium Target Exposure Low Risk Trend compared to 2017 No change Timing of Impact Years</p>		

Strategic Report — Principal Risks continued

Title	Risks and Impact	Key Mitigating Controls
Information assurance, risk and security measures are not able to prevent data loss or corruption KPIs <ul style="list-style-type: none"> – Organic revenue – Underlying operating margin – Underlying EPS – Operating cash conversion 	<p>Cobham relies upon its IT systems to store and process its data securely. In part due to the nature of its business, the Group faces various security threats, including cyber security attacks from computer hackers, viruses, malicious code and internal threats intended to gain access to proprietary or sensitive information, as well as threats to the physical security of its IT facilities and infrastructure.</p> <p>Although various bespoke and industry standard procedures and controls are utilised to monitor and mitigate exposure to these threats, the impact of any future attack cannot be predicted with any certainty. We continue to seek the maximum protection possible against any compromise of the security of intellectual property, customer and employee data and the corruption of embedded product data and data for external services.</p> <p>However, due to the evolving nature of these security threats the effectiveness of any such protection cannot be guaranteed.</p> <p>Significant data breaches or losses could also lead to litigation and fines for breaking data privacy law and other regulations. This would result in reputational damage and potentially the loss of new and existing contracts.</p>	<p>Technical monitoring and prevention technologies are introduced as required to ensure compliance with customer and industry standards.</p> <p>Assessment of IT policy compliance is undertaken on a quarterly basis to ensure that the processes and procedures in place are reflective of all legal and regulatory requirements.</p> <p>Constant monitoring of security events is conducted by both internal resources and trusted external third parties.</p> <p>Primary and secondary data centres have been established to provide contingency.</p> <p>Reviews are conducted jointly with customers to assess and validate the effectiveness of our controls.</p>
Current Exposure Medium Target Exposure Low Risk Trend compared to 2017 No change Timing of Impact Days/Weeks		
Taxation liabilities may be larger than anticipated KPIs <ul style="list-style-type: none"> – Underlying EPS 	<p>Cobham is subject to corporate and other tax rules in the jurisdictions in which it conducts its business operations. Changes in tax rates, tax relief and tax laws, changes in practice or interpretation of the law by the relevant tax authorities, increasing challenges by relevant tax authorities, or any failure to manage tax risks adequately could result in increased charges, financial loss, penalties and reputational damage, which may materially adversely affect the Group's financial condition and operations. In addition, tax enforcement has become a higher priority for many tax authorities in jurisdictions in which the Group operates, which has led to an increase in tax audits, enquiries and challenges, or the testing through litigation of the boundaries of the correct interpretation of legislation. Tax authorities may also actively pursue additional taxes based on retrospective changes to tax laws and the Group may have disagreements with tax authorities which could result in a material restatement to the tax position.</p> <p>For example, the availability of interest deductions on one of the Group's internal financing arrangements, principally as a result of various US acquisitions, has been under challenge for some time. Over the life of this financing arrangement, the aggregate tax value of the interest deductions amounted to approximately £130m. If decided adversely to the Group, this could lead to increased tax liabilities in excess of those provided in the Group's Balance Sheet and result in a substantial tax payment becoming due. The Group is actively involved in attempting to resolve this matter ahead of a Tribunal hearing, which is scheduled in autumn 2019. These issues are set out in more detail in note 7 to the Group Financial Statements.</p> <p>In addition, the European Commission (EC) has opened an investigation into the UK's controlled foreign company (CFC) rules. The CFC rules levy a charge on foreign entities controlled by the UK that are subject to a lower rate of tax, however, there is currently an exemption available for 75% of this charge if the activities being undertaken by the CFC relate to financing. The EC is investigating whether this exemption is in breach of EU State Aid rules, but it is too early to assess what the conclusions of this investigation might be. If there was an adverse final determination on the UK's CFC legislation, the Group estimates that its maximum exposure on this matter is approximately £60m.</p> <p>An adverse outcome could also result in potential damage to the Group's reputation.</p>	<p>External advisors are used to assist in the review of all major transactions that may have potential tax implications. External advisors also review significant tax computations prior to submission.</p> <p>Known areas of tax risk, such as transfer pricing, are monitored by the Group and appropriate controls are implemented where applicable.</p> <p>The Group has established and published its tax strategy, in accordance with applicable regulations.</p>
Current Exposure High Target Exposure Low Risk Trend compared to 2017 No change Timing of Impact Months		

Title	Risks and Impact	Key Mitigating Controls
Value creating Mergers and Acquisitions activity is not identified and /or executed KPIs – Organic revenue – Underlying EPS	<p>The Group is not currently seeking acquisition opportunities and as a result is not in a position to execute potentially value enhancing transactions.</p> <p>In addition, following the Aeroflex acquisition undertaken in 2014, the ability of the Group to effectively integrate acquisitions into existing operations is also uncertain.</p> <p>These factors could result in the Group failing to effectively maintain a robust M&A pipeline and as a result the Group may not be in a position to capitalise on time sensitive opportunities. This could cause a failure to unlock Cobham's full potential or create optimal shareholder value.</p>	<p>The focus is currently on operational execution, which may result in the Group not being active in the Mergers & Acquisitions market with the possible exception of smaller "bolt-on acquisitions".</p> <p>The Group is working to develop an M&A capability to ensure that it is able to undertake acquisition activity with effective integration at an appropriate time in the future.</p>
Current Exposure Low Target Exposure Low Risk Trend compared to 2017 Decreased Timing of Impact Years		
The deficit within the Cobham Pension Plan may change KPIs – Underlying EPS – Underlying operating margin – Operating cash conversion	<p>The Group maintains a number of defined benefit pension schemes which are closed to new entrants and future benefit accrual, the largest of which is the Cobham Pension Plan in the UK. This pension scheme is in deficit, and this deficit may change in the future in response to changes in the value of assets and the present value of liabilities.</p> <p>The most recent triennial valuation of the CPP has recently been completed, and showed a significant reduction in the level of the deficit to approximately £35m. According to the resulting schedule of contributions agreed with the Scheme trustees, the Group's contributions to the CPP have been reduced to £6m per annum, effective September 2018.</p> <p>The Trustees view of the strength of the Company covenant is also taken into account in the setting of recovery plans to address the deficit.</p>	<p>The trustees of the Cobham Pension Plan seek to ensure that the Scheme's assets and liabilities remain matched. The most significant element of this is the acquisition of insurance policies that match assets with existing liabilities.</p>
Current Exposure Low Target Exposure Low Risk Trend compared to 2017 Decreased Timing of Impact Years		

Working towards responsible and sustainable growth

Cobham takes a strategic approach to corporate responsibility and sustainability (CR&S), recognising that long term success is not just about generating shareholder value but also about creating value for all the Group's stakeholders. Managing external impacts, capitalising on opportunities and conducting business in a responsible and sustainable way helps mitigate the Group principal risks and strengthen business relationships.

Many of Cobham's products and services provide important environmental and social benefits. This may be through enhancing aviator survival, minimising environmental impact or providing reliable communications in challenging environments.

The decisions and behaviours demonstrated by acting ethically, managing impacts, implementing innovative solutions and engendering positive business relationships also promote and enhance company culture and reputation. In early 2019, Cobham started a journey to transform its culture which includes a new purpose and accompanying values. Identifying meaningful values that resonate with employees across the Group and embedding the new culture is a priority.

Materiality process

Identification and prioritisation of CR&S issues most relevant to key stakeholders is an important part of the Group's business model (for more details see pages 12 and 13). A mapping process that includes stakeholder research and feedback on issues important to the Group's industry sectors, employees, customers and investors is used to identify the Group's material CR&S issues. The Sustainability Accounting Board Standards (SASB), Global Reporting Initiative (GRI), Task Force on Climate Related Financial Disclosures (TCFD) recommendations and United Nations Sustainable Development Goals (SDGs) all inform this process.

Sustainable development goals

Cobham operates in an evolving global landscape of environmental, social and economic risk and opportunity, which is represented by the SDGs. Cobham supports the SDGs and in 2018 mapped them (where possible) against material CR&S issues across the Group. This was to better understand opportunities for value creation and to establish a link between business strategy and the Group's achievements against the SDGs. The non-financial information disclosure table on page 43 summarises Cobham's material CR&S issues, associated policies and actions, key metrics and processes according to three dimensions: economic, social and environmental.

Economic dimension

Business ethics

Cobham operates in specialist markets, a number of which are highly regulated. The Group complies with all applicable laws and regulations. The risk of non-compliance with applicable laws and regulations is a Group principal risk (see page 39).

The Group is committed to sustaining an ethical culture. The Cobham Ethics and Compliance Programme (CECP) has been developed over several years to support this through a range of policies, processes and activities. The implementation and effectiveness of the CECP is overseen by the Business Ethics and Compliance Committee (BECC), and ultimately the Board. The programme is underpinned by the Code of Business Conduct (COBC), which outlines the Group's core values and the behavioural standards it mandates for all its officers, employees and representatives on a range of issues, including anti-bribery and anti-corruption.

Non-financial information disclosure table

Material corporate responsibility & sustainability dimension	Linkage to relevant UN Sustainable Development Goals	Policies, standards and actions which govern our approach (incl. objectives/targets)	Where to find further information	Key metrics	Internal processes to monitor performance
Economic 1. Business Ethics 2. Material sourcing and supply chain management		<ul style="list-style-type: none"> – Code of business conduct – Supplier code of conduct – Cobham Ethics and Compliance Programme – Responsible supply chain management Policy – Anti-Slavery and Human Trafficking Policy 	<ul style="list-style-type: none"> – See page 42 for Economic information – www.cobham.com/the-group/corporate-responsibility-and-sustainability 	<ul style="list-style-type: none"> – % employees trained on Code of Business Conduct 	The implementation and effectiveness of The Cobham Ethics and Compliance Programme (CECP) is overseen by the Business Ethics and Compliance Committee (BECC) and, ultimately, the Board.
Social 3. Talent attraction, development and retention 4. Diversity and inclusion 5. Employee health and safety 6. Product safety 7. Human rights	  	<ul style="list-style-type: none"> – Emerging talent graduate and apprenticeship Programme – Employee development programmes – Safety, Health and Environment (SHE) policy – Product research and development, innovation and design – Lifecycle management policy – Responsible supply chain management policy – Diversity and Inclusion policy – UK Gender Pay Gap Report – Signatory to Women in Aviation and Aerospace charter 	<ul style="list-style-type: none"> – See page 44 for Social information – www.cobham.com/the-group/corporate-responsibility-and-sustainability – See employee workforce engagement case study on page 47 – See gender diversity case study on page 45 	<ul style="list-style-type: none"> – Achievement of 5% club targets (see page 44) – % female representation in total workforce and senior management – Lost work case incident rate – Recordable incident rate – Voluntary staff turnover 	Group Executive monitors SHE performance on a monthly basis, using a balanced scorecard. Annual SHE self-assessment, periodic peer to peer auditing and a biennial external audit. Group Executive monitors voluntary staff turnover, which is a Group KPI, on a monthly basis.
Environmental 8. Energy management 9. Waste and water 10. Greenhouse gas (GHG) emissions	 	<ul style="list-style-type: none"> – Safety, Health and Environmental Policy – Reduction of operational environmental impacts including hazardous and non-hazardous waste and water use – Energy efficiency Programmes 	<ul style="list-style-type: none"> – See page 47 for Environmental information – See page 82 for additional information on GHG emissions – www.cobham.com/the-group/corporate-responsibility-and-sustainability 	<ul style="list-style-type: none"> – Facility GHG emissions – Progress against GHG target – Water intensity – Waste to landfill/recycling intensity 	Energy and GHG management data is audited by Bureau Veritas on a limited assurance basis.

“Cobham has a clearly stated zero tolerance approach to bribery and corruption in any form”

Cobham has a clearly stated zero-tolerance approach to bribery and corruption in any form. All employees, including Board members, receive training on the COBC and Anti-Bribery/Anti-Corruption annually. Cobham maintains an independent Ethics Helpline and website where potential compliance violations can be reported. In 2018, various enhancements were made to the handling of concerns raised via the Ethics Helpline, including providing specialist investigator training to the panel of nominated internal investigators. Cobham has a zero tolerance approach to any kind of retaliation for reporting ethics issues and further details on the Group's approach to ethics and compliance can be found at www.cobham.com/the-group/corporateresponsibility-and-sustainability/ethics/.

In 2018, Cobham completed an Anti-Bribery/Anti-Corruption Risk Assessment. Findings and recommended actions were reviewed and approved by the Audit Committee and various follow-on actions have been incorporated into the CECP plan for 2019.

A related compliance risk issue is the use of third-party intermediaries as a route to market. Failure by an intermediary to comply with laws and regulations, or the failure of the Group to complete appropriate intermediary due diligence, can impact the Group's reputation as well as lead to a range of sanctions, including significant fines or debarments from government contracts and new business. Cobham's Anti-Bribery and Anti-Corruption Policy and Intermediary Policy requires intermediaries to undergo a comprehensive approval process prior to engagement, Cobham also performs ongoing monitoring during the engagement phase itself,

including the use of technology to monitor worldwide databases for red flags on a continuous real time basis and, in 2018, appointing external legal counsel to independently renew intermediaries on a risk-weighted basis to ensure continued compliance.

Cobham measures the effectiveness of the CECP and improvements to it through a range of metrics, one of which is the completion of mandatory COBC/ABAC employee training. In 2018 99.3% (2017: 99.8%) of Cobham employees completed COBC training.

Material sourcing and supply chain management

Cobham continued to consolidate its suppliers in 2018 to reduce risk and cost and improve quality. The Group Supplier Code of Conduct and Responsible Supply Chain Management (RSCM) policy can be found at www.cobham.com/the-group/suppliers/supplier-documents

Group-wide supplier compliance campaigns were conducted with respect to bribery and corruption, modern slavery and human trafficking, and conflict minerals. In addition to reinforcing the Group's responsible business practices, this supported Group regulatory disclosures and customer information requests.

More information on the modern slavery policy and process can be found on the Group website www.cobham.com/the-group/corporate-responsibility-and-sustainability/performance-data-policies/disclosures

During 2019, Cobham will continue to focus on supporting its supplier campaigns and enhancing key supplier engagement. Cobham is legally, and sometimes contractually, required to disclose certain information regarding its global supply chain. Compliance with applicable laws and regulations, the characteristics of its markets and the resulting complex contracting environment have been identified as principal risks (for further details see pages 39 and 37 respectively).

Social dimension

Talent attraction, development and retention

Cobham remains committed to attracting and retaining talented and engaged employees, and 2018 has seen continued focus on the development of its employees to achieve growth plans and deliver ongoing commitments.

Ensuring each employee has the opportunity to reach their full potential is a core aim of Cobham's talent strategy. Throughout 2018, development programmes linked to career frameworks were deployed, and this will continue in 2019. Supporting the continuous growth and development which helps ensure greater engagement and the skills to deliver current and future customer requirements.

Cobham is investing in the development of leaders, recognising the significant role they play. To create a sustainable pipeline of future leaders, the Cobham Certificate in Management Programme, which is a training scheme accredited through the Institute of Leadership and Management, continued during 2018.

The Group recognises the importance of emerging talent, and has increased the number of places within its graduate and apprentice development programmes. Reflecting this, in 2018 the Group employed 7.2% (2017: 4.5%) of its UK workforce as apprentices, graduates or undergraduate placements, meeting its 5% Club commitment one year early. For further information and background see www.5percentclub.org.uk. In total, 11% of the UK workforce are alumni of the graduate or apprentice schemes, illustrating the ongoing commitment to develop emerging talent into leaders of the future. Alumni from these schemes are progressing into senior roles and are increasingly featuring on the Group's succession plans.

Cobham has joined with the Defence Growth Partnership to deliver the Defence Export Executive MBA and the Defence Export Postgraduate Certificate. Cobham is also piloting the Level 4 Associate Project Manager Apprenticeship in 2019.

Voluntary staff turnover, which is one of the Group's KPIs, is used to measure the effectiveness of its talent retention and employee engagement approach. In 2018, the Group's voluntary employee turnover was 12% (2017: 10%). The Group is in a turnaround and in these circumstances it is expected that there might be an increase while the organisation structures, ways of working and culture undergo a period of change. Management expects that this voluntary staff turnover metric will decrease over time.

Diversity and inclusion

Competition for talent is growing in the Group's markets. A combination of ageing populations and declining numbers of suitable university graduates is leading to greater competition for talent across industries and geographies. This is particularly relevant for science, technology, engineering and mathematics disciplines upon which the Group relies. Cobham must attract and retain the right skills to meet its plans and deliver its strategy.

Developing an effective culture supports the creation of a diverse workforce which will enable the Group to attract and retain key talent from all backgrounds. Cobham is committed to developing an inclusive workplace where employee differences are valued, enabling everyone to contribute fully.

Under the UK Equality Act 2010 requirements, applying to legal entities with at least 250 employees, Cobham is required to report gender pay gap data, which is available at www.cobham.com/the-group/corporate-responsibility-and-sustainability/performance-data-policies/disclosures.

In 2018, women were employed in 19% (2017: 16%) of senior management roles. In 2018, Cobham became a signatory to the UK Women in Aviation and Aerospace Charter committing to support the progression of women to senior positions. The diversity, inclusion and family leave policies were updated to reflect the commitment to support its employees.

Ensuring that the Group is able to attract and retain a diverse workforce is linked to the Group's principal risks relating to a shortage of appropriate skills and talent as well as failure to comply with laws and regulations (refer to pages 37 and 39 respectively).

Health and safety

Cobham endeavours to create a safe and healthy culture and a framework that fosters employee engagement at all levels. The SHE Committee has set the objective of transforming the Group's organisational SHE culture. Failure to deliver consistently high standards of health and safety could lead to accidents or incidents which may result in employees being injured or otherwise harmed, which is totally unacceptable. In addition, accidents or incidents may result in prosecutions, fines, loss of assets, business interruption and widespread reputational damage. Health and safety is referenced within the Group's principal risks relating to significant business interruption and failure to comply with laws and regulations (refer to page 39).



Gender Diversity at Cobham

Cobham hosted a number of events in 2018 celebrating and promoting female employees.

In July, at the Farnborough International Air show, Gillian Duggan, Executive Vice-President for HR and Communications recognised the Group's female talent at Cobham's first 'Women in Aerospace and Defence Day'. The day focused on encouraging networking and sharing ideas about promoting a more inclusive and diverse workplace.

The Aviation Services Australian Business Unit also hosted a networking event for 'Women in Aviation/Aerospace Australia' at the VIP terminal at Adelaide Airport.

The theme for the event was 'strategies and policies that are better for women are better for all', and guest speakers included Captain Adelle Blundell, from the Australian Army and Gosia Davis, Engineer Manager, BAE Systems who shared their thoughts and experiences on this theme.

The event was part of a series run by not-for-profit association, Aviation/Aerospace Australia, which is designed to help promote gender diversity, provide a network for women to connect with industry peers, excel in their careers and inspire the next generation of women.

“In 2018 the Group employed 7.2% of its UK workforce as apprentices, graduates or undergraduate placements, meeting its 5% Club commitment one year early”

The Group's long-standing workplace SHE programme, called 'Zero Harm', promotes continuous improvement. Its objective is to minimise injuries and illnesses occurring in the workplace, improve environmental sustainability and ensure employees' wellbeing. Accountability for implementing the Group's SHE strategy is with senior management and progress is monitored by the Group SHE Committee, which is chaired by the CEO. Technical expertise is provided through a Group SHE Council – comprising senior business unit SHE professionals under the leadership of the Vice-President (VP) Group SHE, and the VP Corporate Responsibility and Sustainability.

The Group's three year SHE strategy is to:

- Continually improve safety, health, environmental and sustainability performance;
- Drive a proactive and learning SHE culture through engaged and empowered people at all levels; and
- Derive business efficiencies through the implementation of an integrated, standardised SHE management system across the organisation.

Cobham implemented a new set of global SHE standards in 2017 and the underpinning processes have matured during 2018. The extent of Business Unit compliance with these standards, over and above the legal minimum, is monitored. Cobham's business units are expected to exceed a minimum compliance target which increased by five percentage points in 2018. Monitoring is through an annual self-assessment exercise, periodic peer-to-peer auditing and a biennial external audit. In 2018, 75% of assessed operations achieved or exceeded this more stringent SHE compliance target. This was a reduction on previous years

(although assessed against a higher target) and the underachievement was primarily observed in those operations impacted by ongoing business restructuring.

In addition, the Group Executive monitors SHE performance on a monthly basis, using a balanced scorecard of leading and lagging indicators. Leading indicators (indicators that correlate with future performance) are used to drive correct behaviours. They include safety training, risk assessments, workplace inspections, SHE Committees and reporting of safety observations. Lagging indicators (indicators that are based on historic performance) are used to measure the effectiveness of the approach, and these include the incidence of workplace injuries and illness, environmental issues and regulatory interventions. During 2018, the Group achieved 87% of its leading indicator metrics.

With regard to lagging indicators, there were no fatalities in 2018. The occupational lost time injury and illness incident rate (defined as the number of cases resulting in one or more day's lost time or restricted duties) increased to 0.821 in 2018 from 0.503 incidents per 200,000 hours worked. This is an industry standard metric which Cobham has adopted as one of its key reporting measures. The recordable incident rate (the number of recordable incidents per year per 100 full time equivalent employees) also increased to 1.56 in 2018 from 0.95 in 2017. The increases in both of these metrics were primarily observed again in businesses that were undergoing business restructuring, resulting in a reduction in employee engagement in health and safety matters whilst the business transitions to its future state. Manual handling, minor hand injuries, and slips and trips were the most common

causes of injury or illness that resulted in lost time during 2018, consistent with prior years.

During 2019, plans will be implemented to recover the Group's health and safety performance through increased accountability of leadership teams for health and safety related matters, and improved employee engagement in particular through encouraging more suggestions for improvement.

There was one significant regulatory intervention in the year. In March 2018, a fire code violation on the plating line at the San Diego, US facility resulted in the local fire department issuing a temporary cessation notice on the electroplating operations. Remedial action was taken to reconfigure access and egress routes, and operations were allowed to resume. Further details on Cobham's SHE policy, management standards and performance are at www.cobham.com/the-group/corporateresponsibility-and-sustainability/performance-data-policies/policydownloads/.

Human rights

Human rights remain an important issue for the Group. There are growing requirements to comply with legislation and to respond to customer information requests on human rights issues such as modern slavery and conflict minerals. Compliance with applicable laws and regulations has been identified as a principal risk (refer to page 39).

Cobham supports the principles contained in the Universal Declaration of Human Rights and seeks to reflect these in the context of its business activities. Cobham also respects the rights of its employees in the International Labour Organization Declaration on Fundamental Principles and Rights at Work. Cobham demonstrates its support and respect for human rights through the principles and policies contained in the COBC, the Corporate Framework and the Group's policies and processes.



Workforce engagement

Employees are a key stakeholder group and Cobham recognises that encouraging effective engagement with employees improves participation and productivity.

Across the Group, businesses have been working on improving information flows and engagement opportunities with its 10,000 employees.

Cobham business units and sites have regular 'All Hands' or town hall style meetings. These are opportunities for senior business leaders to share information with employees, such as financial results and business bids, opportunities and wins, as well as updates on policies and procedures when applicable. It is also an opportunity for staff to ask questions of their leadership team.

Information is also shared through Group and local business intranet, sites, internal news bulletins, announcements and executive blogs.

In 2018, the Group issued its second annual Anti-Slavery and Human Trafficking statement in compliance with section 54 of the UK's Modern Slavery Act, 2015. The statement outlines the Group policy and approach to managing risk in Group operations and in its supply chains. The statement can be downloaded at www.cobham.com/the-group/corporateresponsibility-and-sustainability/performance-data-policies/disclosures/.

Charity activity

Cobham believes that community issues are best addressed locally, wherever possible. Each site is encouraged to manage its operations and activities with due consideration for the wellbeing of neighbours and local communities. In 2018, the Group donated £221,057 (2017: £275,726) to a range of good causes, including charities relating to the armed services, rescue and health-based charities, as well as local community interests. It is Cobham's policy not to make political donations.

The CEO chairs the SHE Committee which has responsibility for operational, environmental and sustainability matters. The Committee is also responsible for development and implementation of the Group SHE strategy.

Environmental dimension

Cobham recognises that its operations, activities, products and services have an impact on the environment.

A material environmental issue is the Group's energy use and response to climate change. The following table outlines Cobham's governance, strategy, risk management and performance measurement approach with regard to this issue.

"In 2018, 75% of assessed operations achieved or exceeded a more stringent SHE compliance target"

Task force on climate related disclosures (TCFD)

Governance

The Corporate Responsibility and Sustainability Committee, chaired by the CFO, has overall accountability for CR&S strategy, including climate change and carbon management. The Committee has responsibility for reviewing the effectiveness of controls in place for identifying and managing risks and opportunities, challenging Group performance and maintaining strategic and policy oversight.

Strategy

Climate change affects the Group's approach to meeting its strategic objectives. Climate change regulation, taxes, international agreements (such as the Paris accord) volatile energy costs and changes in weather conditions have all informed the Group's strategic decisions as Cobham adapts to changing operating environments. Investment in new technology that reduces size, weight and power consumption of products and carbon emissions is an important differentiator in the Group's markets.

Material issues identified include:

- GHG emissions from aircraft fuel combustion in Aviation Services (which represents the majority of the Group's GHG emissions);
- GHG emissions from electricity and fuel used in the lighting, heating, ventilation and cooling of its facilities and supply chain Group-wide;
- The impact of the size, weight and power efficiency of Cobham products upon the fuel consumption and GHG emissions of customer aerospace platforms; and
- Business interruption at its facilities, and those of its key suppliers, due to adverse weather events (e.g. flooding, wildfire).

Risk management

Risks and opportunities are monitored, prioritised and managed in a number of ways, including by the Group's insurance partner, in local risk registers and business unit SHE self-assessments. Failure to address environmental sustainability issues aligns with the Group's principal risks of failure to comply with laws and regulations and of significant business interruption (refer to page 39).

The Group addresses environmental sustainability issues by:

- Reducing environmental impacts from its operations wherever practicable;
- Reducing legacy aircraft fuel consumption via operational efficiency programmes and ultimately transitioning to more fuel-efficient aircraft where possible;
- Reducing its GHG emissions across a number of operating sites through practical energy efficiency measures, including lighting, heating, ventilation and air conditioning;
- Investing in design concepts to reduce the size and weight of products as well as energy consumption, with a corresponding reduction in environmental impacts;
- Reinforcing business continuity measures and effective emergency response planning, in preparation for adverse weather events and natural disasters; and
- Aligning the Group's environmental standards to the international environmental management system standard ISO14001 and encouraging business units to certify to the standard.

Performance measurement

In 2018, a new five year reduction target of 15% was set for facility GHG emissions (excluding CAES). Performance remains on track to achieve this target through a number of planned energy-saving initiatives.

Further details on the Group's energy use and GHG emissions can be found in the Other Statutory Information report on page 82.

The Group measures and discloses its GHG emissions strategy, risks, opportunities and performance on www.cobham.com/the-group/corporate-responsibility-and-sustainability and through the annual Carbon Disclosure Project (CDP) investor climate change and customer supply chain surveys.

CDP is a not-for-profit charity that runs a global disclosure system for companies to report their carbon and other environmental impacts primarily for investor understanding of risks and opportunities. In 2018, Cobham achieved a 'B' Leadership rating from CDP, which was a reduction on the 'A' rating achieved in 2017. The reduction was mainly due to a shift in focus in the CDP methodology towards climate change. During 2019 actions will be defined to contribute to improving the rating through increased focus in this area.

Waste and Water

Reduction of operational environmental impacts, including hazardous and non-hazardous waste and water use, are also an important issue for Cobham.

In 2018, the Group's business units were challenged to develop a framework for a new set of intensity metrics to provide data to enable a reduction in waste production as well as water and energy consumption.

Gender diversity in the Cobham workforce

Females/Total %	2018	2017	2016
Board of Directors ¹	2/8 (25%)	2/10 (20%)	2/9 (22%)
Senior Managers ^{1 & 2}	12/86 (14%)	16/112 (14%)	21/113 (19%)
Senior Managers ^{1 & 3}	31/166 (19%)	24/151 (16%)	24/138 (17%)
Total workforce ⁴	2,834/10,359 (27%)	2,877/11,070 (26%)	2,904/10,845 (27%)

1 Full time equivalent employees at year end.

2 Statutory definition – Employees with responsibility for planning, directing or controlling corporate activities.

3 Cobham definition – Vice Presidents and above.

4 Average number of employees for year.

Summary of CR&S key metrics

Key performance indicator	Target ⁴	2018	2017	2016
% Employees trained on Code of Business Conduct	100.0%	99.3%	99.8%	99.5%
Voluntary employee turnover	<10.0%	12%	10%	10%
% Female representation in total workforce	-	27%	26%	27%
Lost Work Case Incident Rate ¹	<0.64	0.82	0.50	0.72
Recordable Incident Rate ²	<1.26	1.56	0.95	0.93
5 Year facility GHG emissions ³	-15% over 5 years	-3.4%	-	-

1 Number of lost workday injury or occupational illness cases multiplied by 200,000 divided by the hours worked.

2 Number of recordable incidents per year per 100 full time equivalent employees.

3 In 2018, a new key metric to track GHG emissions, targeting an absolute reduction of 15% by the end of 2022. This replaced the previous facility energy intensity metric.

4 Targets are reassessed annually to ensure that they drive continuous improvement.

The Strategic Report, covering pages 2 to 49 of the Annual Report and Financial Statements 2018 has been approved by the Board of Directors in accordance with The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013.

On behalf of the Board of Directors



Lyn Colloff
Company Secretary
7 March 2019

A culture of good governance



Cobham plc — Annual Report and Accounts 2018

Michael Wareing
Chairman

What action has the Board taken to help the business deliver on its turnaround strategy?

The Board has provided oversight and supported proposals made by the executive team in relation to: organisational shape and design; culture and talent; supply chain management; operational performance; and cost actions.

Corporate culture is intrinsically linked to the Group's performance: what steps has the Board taken to define the culture of the Group and the values employees are expected to adopt?

Culture has been a key focus during 2018, culminating in the launch of the 'Every Mission Matters' purpose and the revised set of values in January 2019. The embedding of the new purpose and values and their impact on corporate culture will be a key focus for 2019.

How is the Board preparing for the 2018 UK Corporate Governance Code?

The Board welcomes the new Code, issued by the FRC, which applies to the Company from 2019. The Board and its Committees have reviewed the new Code, particularly on how best to formalise areas such as employee engagement, culture, pay ratio, post-employment share ownership, retirement benefits, and remuneration policies and practices in the wider workforce, amongst others.

What is the Board's approach to succession planning?

The Board undertook a skills review in 2018 to feed into the succession plan for Board members. As the Board refreshment exercise draws to a conclusion, we will move into a more normal succession planning process, focusing initially on strengthening the Remuneration Committee, which was highlighted through the evaluation process.

Why has the decision been taken to resume payment of a dividend at this stage of the Group's turnaround?

The Board considered it appropriate to return to the dividend list in 2019, at a prudent level, recognising that it is important to our shareholders to return value as a signal of our confidence in the progress of the turnaround.

The Board is accountable for the Group's management of risk. How does the Board monitor this?

The risk management process is described on pages 34 and 35. The Audit Committee and the Board Risk Committee both have a role in the monitoring of progress, as does the Group Executive. The Board retains the accountability for the setting of the Group's appetite for risk.

How governance has supported our turnaround strategy

Strategy

The Board's actions

What we achieved in 2018

Returning the business to financial strength

- The Board challenged management proposals as part of its strategic review to focus on areas where the Group has strength in capability and customer base.
- The Board has agreed a target for Net Debt: EBITDA of less than 1.5 times.
- The Board has been debating its policy on capital allocation and agreed a target capital structure, including a future dividend policy.
- The Audit Committee has monitored the utilisation of provisions and charges throughout 2018.

- The completion of the AvComm and Wireless test and measurement businesses divestment for US\$455m in March 2018 has helped strengthen the balance sheet.
- The Group is in a net cash position at 31 December 2018, down from a gearing ratio of 1.3x at 31 December 2017. This is significant progress, as Cobham had a gearing ratio of 3.0x 24 months ago.
- The Board has approved a target capital structure and capital allocation policy.
- The remaining unutilised balances relating to the 2016 exceptional charges total £206m at the year end which will continue to unwind as cash outflows.

→ Read more on page 7

Focusing the portfolio on markets we know

- The Board and management have worked together to identify and divest businesses which are not considered to be part of the Group's 'core business'. These divestments were approved by the Board, enabling management to concentrate on the retained businesses in the Group.
- The restructuring of the business units enables better customer focus and a more clearly defined business identity, more closely aligned to end markets. In some parts of the business, a layer of management has been removed, which has simplified the structure and will deliver cost savings.

- The divestment of AvComm and Wireless test and measurement businesses supports the focus of the Group on its defence, aerospace and space markets. As mentioned above, this was completed in March 2018.
- In May 2018, we divested the 'Opera' electromagnetic simulation software business for £78m, and a smaller Lightning Test and Consultancy business was divested in November 2018 for £1.9m. Both of these businesses were part of the Communications and Connectivity Sector.
- We have restructured the Aviation Services Sector into two regional businesses (UK & EMEA and Australia).
- The Communications and Connectivity Sector and the Advanced Electronic Solutions Sector management have also undertaken a re-structuring exercise, to reduce costs and refocus on market-facing businesses.

→ Read more on page 7

Resolving legacy issues

- Resolving legacy issues enables the Board to be more forward looking and to concentrate on the more strategic issues affecting the Group.

- We have continued to progress delivery on the contracts against which we took significant charges in 2016.
- On the largest of these, the KC-46 tanker programme, we announced on 19 February 2019, a settlement regarding Boeing's damage assertions, bringing an immediate end to the Boeing withhold on Cobham invoices.
- The Financial Conduct Authority's investigation in relation to the Company's compliance with the Listing Rules, Disclosure and Transparency Rules and the Market Abuse Regulations between April 2016 and February 2017 has been discontinued.
- The Group is actively involved in attempting to resolve the tax treatment of interest deductions on one of the Group's financing arrangements; refer to note 30 for further details.

→ Read more on page 7

Improving operational execution and effecting cultural change

- Improvement of performance and delivery to customers leading to more business being awarded and thus enhancing order intake, and ultimately assisting in margin improvement. This can be demonstrated by KPIs 1,2 and 5 on pages 18 and 19.
- Improved employee working conditions and culture support achievement of strategic objectives and help resolve some legacy cultural issues.
- Launched new purpose statement and values to support cultural change.

- We are continuing to invest in the infrastructure at a number of sites – including Wimborne, UK and San Diego in the US – to address some long-standing operational issues.
- We are focusing on improving our operational performance to reduce the significant costs related to late delivery to customers and the re-work of product that has failed post-production quality tests.
- The senior management team was brought together in various forums to ensure that a more customer focused, performance based culture with common values is adopted.
- We are in the process of implementing a global Human Resources information system which will give the transparency to allocate resources more effectively, manage skill groups, assist in succession planning and develop talent across the Group.

→ Read more on page 9

The right skills and experience to deliver our strategy

Full biographies can be found at www.cobhaminvestors.com/our-business/our-board



Michael Wareing

Chairman

CMG, FCA, FCCA, MCSI

Tenure on Board: 8 years, including 2 years as Chairman

Independent on appointment in December 2010

Committee membership: Chair of the Nomination Committee; Chair of the Board Risk Committee.

Nationality: British

Relevant skills: Michael had a global career holding senior executive and non-executive roles in FTSE 100 companies (Intertek plc, Wolseley plc), KPMG and as an envoy and advisor to the British Government. He brings extensive international commercial and financial experience to the Board.

Key external appointments: none



John McAdam

Senior Independent Director

BSc, PhD

Tenure on Board: 1 year 5 months

Independent on appointment in August 2017

Committee membership: Member of the Audit Committee, Remuneration Committee and Nomination Committee.

Nationality: British

Relevant skills: John has a wealth of executive experience in blue chip companies, most notably ICI plc, as well as holding senior non-executive roles in FTSE 100 companies including Rolls-Royce plc amongst others. He brings valuable senior leadership experience gained across a range of sectors to the Board.

Key external appointments: Chairman at Rentokil Initial plc (stepping down in May 2019) and United Utilities Group plc; Non-executive Director at Wilmcote Holdings plc.



David Lockwood

Chief Executive Officer, Executive Director OBE, BA, FCA, FRSA, FAeS

Tenure on Board: 2 years

Independent: No

Committee membership: Chair of the Executive Directors Committee.

Nationality: British

Relevant skills: David has senior management experience in international operations including with BAE Systems plc, Laird plc and Thales Group in the aerospace and electronics sectors. He has held advisory positions in the fields of cyber security and technology and was awarded the OBE for services to industry in Scotland.

Key external appointments: Member of the Dunedin International Advisory Board.

Overall Board and Committee meeting attendance table

The figures represent attendance at formal meetings.

	Board	Audit Committee	Board Risk Committee	Nomination Committee	Remuneration Committee
Michael Wareing	7 of 9*		3 of 3	3 of 4*	
John McAdam	9 of 9	5 of 5***		4 of 4	4 of 4
Alison Wood	9 of 9	5 of 5***	3 of 3	4 of 4	4 of 4
René Médori	8 of 9**	7 of 7	3 of 3	4 of 4	
Norton Schwartz	8 of 9**	5 of 5***	3 of 3		4 of 4
Marion Blakey	3 of 3	3 of 3			
David Lockwood – Executive Director	9 of 9				
David Mellors – Executive Director	9 of 9				
Alan Semple	3 of 3	3 of 3			
Birgit Nørgaard	3 of 3	3 of 3			
Michael Hagee	3 of 3	3 of 3			

* Michael Wareing missed two Board meetings and one Nomination Committee meeting due to surgery/ill health. John McAdam, in his capacity as Senior Independent Director, deputised as Chairman in his absence.

** René Médori and Norton Schwartz missed one Board meeting each, due to travelling.

*** Alison Wood, John McAdam and Norton Schwartz joined the Audit Committee on 25 April 2018.



David Mellors

Chief Financial Officer, Executive Director MA, ACA

Tenure on Board: 2 years

Independent: No

Committee membership: Member of the Executive Directors Committee.

Nationality: British

Relevant skills: A chartered accountant, David has extensive senior management experience in the defence, security and aerospace market in the FTSE 250, in a Chief Financial Officer and interim Chief Executive Officer capacity. Previous roles have afforded global finance experience in the IT, software and mining sectors.

Key external appointments: None



Alison Wood

Independent Non-executive Director MA, MBA

Tenure on Board: 7 years 5 months

Independent on appointment in July 2011

Committee membership: Chair of the Remuneration Committee; member of the Audit Committee, Nomination Committee and Board Risk Committee.

Nationality: British

Relevant skills: Alison brings extensive strategic experience and understanding of the aerospace, defence and regulated capital intensive businesses from her previous executive roles at BAE Systems plc and National Grid plc. She has valuable knowledge and understanding of the executive reward arena gained at other blue chip companies.

Key external appointments: Non-executive Director and Chair of the Remuneration Committee of Costain Group plc, TT Electronics plc and The British Standards Institution (a non-listed Royal Charter Company).



René Médori

Independent Non-executive Director Economics Doctorate Degree, Finance Masters

Tenure on Board: 1 year

Independent on appointment in January 2018

Committee membership: Chair of the Audit Committee; member of the Board Risk Committee and Nomination Committee.

Nationality: French/British

Relevant skills: René brings considerable technical financial expertise to the Board, gained from a global finance background, in the mining, multinational industrials and utilities sectors, most notably at Anglo American plc. He also brings a strong reputation for integrity and excellent investor relations.

Key external appointments: Chair of Petrofac Limited; Non-executive director at Newmont Mining Corporation and at Vinci SA (where he will be appointed Audit Chair in April 2019).



Norton Schwartz

Independent Non-executive Director BSc, MA

Tenure on Board: 1 year

Independent on appointment in January 2018

Committee membership: Member of the Audit Committee, Remuneration Committee, and Board Risk Committee.

Nationality: US Citizen

Relevant skills: Norton's long and distinguished US Air Force career brings invaluable insight into the US military process and programmes, with a particular strength in defence technology. He held a number of senior military positions culminating in the role of 19th Chief of Staff of the US Air Force. He brings SSA experience from his role at CAE USA Inc.

Key external appointments: Member of the Board of Wesco Aircraft Holdings, Inc; Board of Directors of CAE Inc; President and CEO of Business Executives for National Security (BENS) in the US.



Marion Blakey

Independent Non-executive Director BA

Tenure on Board: 5 months

Independent on appointment in August 2018

Committee membership: Member of the Audit Committee.

Nationality: US Citizen

Relevant skills: Marion brings a commercial strength to the Board, alongside extensive experience in the airline industry arena. Her customer focus, evidenced in her role as Chair, President and CEO of Rolls-Royce North America Inc and at the Federal Aviation Administration, a role requiring White House/Senate approval, complements and strengthens the skills on the Board.

Key external appointments: Non-executive Director of Alaska Air Group Inc., Chair of its Compensation Committee and a member of the Safety Committee. Chair of Board of Trustees of Noblis Inc.

Changes to the Board of Directors

René Médori	René was appointed as a Non-executive Director on 1 January 2018
Norton Schwartz	Norton was appointed as a Non-executive Director on 1 January 2018
Michael Hagee	Michael retired from the Board at the 2018 AGM, 26 April 2018
Birgit Nørgaard	Birgit retired from the Board at the 2018 AGM, 26 April 2018
Alan Semple	Alan retired from the Board at the 2018 AGM, 26 April 2018
Marion Blakey	Marion was appointed as a Non-executive Director on 3 August 2018

For more details see
www.cobhaminvestors.com/our-business/our-board

Board statements

Requirement	Board statement	Where to find further information
Compliance with the Code	The ordinary shares are listed on the London Stock Exchange. In accordance with the Listing Rules of the UK Listing Authority, the Company confirms that throughout the year ended 31 December 2018 and at the date of this Annual Report, it was compliant with the provisions of the Code.	See page 55 which describes how the Company has applied, and complied with, the Code. The Code is published by the Financial Reporting Council (FRC) and is available from its website www.frc.org.uk .
Going concern basis	The Board believes that the Group is well placed to manage its business risks successfully. Accordingly, after making enquiries, the Directors have formed a judgement at the time of approving the financial statements that it is their expectation that the Company and the Group as a whole have adequate financial resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Group and Parent Company Financial Statements.	Group's going concern assessment on page 33.
Viability statement	Based on the assessment of the principal risks facing the Group and robust downside sensitivity analysis, all of which are described on pages 36 to 41, the Board has a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to December 2021.	Group's viability statement on page 35.
Robust assessment of the principal risks facing the Group	The Board regularly reviews the Group Principal Risks reported across the Group by businesses and functions, and is satisfied that these risks are managed within the Group's appetite for risk. The Board ensures that the Group's risk exposure remains appropriate and that this links to the effective delivery of its strategic objectives.	Principal risks are set out on pages 36 to 41.
Annual review of systems of risk management and internal control	The Board has reviewed all material controls, including financial, operational and compliance controls and risk management systems. It has gained the appropriate assurance that the day to day risk management and internal control systems which are embedded in the business, have operated effectively in the review period.	Refer to pages 68 and 69 for further details on the risk management and internal control review undertaken.
Fair, balanced and understandable	The Board considers the 2018 Annual Report and Accounts to be fair, balanced and understandable. In forming its opinion, the Board reflected on the information it had received and its discussions throughout the year. The assessment was assisted by an internal verification of the factual content by management, a review at different levels of the Group to ensure consistency and overall balance, and a comprehensive review by the senior management team.	Refer to page 69 for further details on the fair, balanced and understandable review undertaken.

→ Membership of all committees can be found on page 52

Statement of compliance with provisions of the Code

The ordinary shares are listed on the London Stock Exchange. In accordance with the Listing Rules of the UK Listing Authority, the Company confirms that throughout the year ended 31 December 2018 and at the date of this Annual Report, it was compliant with the provisions of the Code.

A. Leadership

A.1. The Board's role

Refer to page 56, and to page 58 for Board and Committee structure and purposes.

A.2. A clear division of responsibilities

The Board's policy is that the roles of Chairman and CEO should be performed by different people.

A.3. Role of the Chairman

The Chairman is responsible for the leadership and effectiveness of the Board. He sets the agendas for meetings and manages the meeting timetable. The Chairman facilitates open and constructive dialogue between Executive and Non-executive Directors and also ensures effective communication with shareholders. The Chairman has held regular meetings with the Non-executives, both collectively and individually, in the absence of Executive Directors, providing an opportunity for any concerns to be discussed.

A.4. Role of the Non-executive Directors

The primary role of the Non-executive Directors is to constructively challenge and help the CEO formulate proposals on strategy. They also scrutinise the performance of management in meeting agreed objectives, monitor the reporting of performance and satisfy themselves on the integrity of the financial information and that financial controls and risk management processes are robust and defensible. The Board has appointed a Senior Independent Director to provide a sounding board for the Chairman and to serve as an intermediary for the other Directors, where necessary.

B. Effectiveness

B.1. The Board's composition

Details of the composition of the Board are set out on page 56. The Board determines, through the Nomination Committee, the independence of its members. Conflicts of interest are also monitored and updated at least annually.

B.2. Board appointments

The appointment of new Directors to the Board is led by the Nomination Committee – see Board and Committee structure on page 58. The Nomination Committee's terms of reference, as published on the Company website, document its responsibility regarding Board appointments. Further details of succession planning and the Board's policy on diversity, including gender, can be found on pages 64 and 56 respectively.

B.3. Time commitments

The time commitments of Non-executive Directors are defined in their appointment letters and are regularly reviewed. The impact of any new role proposed by a Non-executive Director on existing time commitments is considered by the Chairman before approval is granted.

B.4. Training and development

A structured induction programme is available to each new Board member, which is supplemented by visits to key locations and meetings with management. Further training for Directors is offered when taking a new role on a committee and is otherwise available as required. Further details can be found in the Directors' professional development section on page 65.

B.5. Provision of information and support

The Chairman, in conjunction with the Company Secretary, ensures that all Board members receive accurate and timely information. All the Directors have access to independent professional advice at the Company's expense, where they judge it necessary in order to discharge their responsibilities.

B.6. Board and Committee performance evaluation

An external evaluation of Board and Committee performance was held in 2018. See page 59 for details of the evaluation.

B.7. Directors' re-election

All Directors are subject to shareholder vote at the AGM.

C. Accountability

C.1. Financial and business reporting

The Statement of Directors' Responsibility is set out on page 85, and the Independent Auditors' Report commences on page 86. The Company's business model is explained on pages 12 and 13.

C.2. Risk management and internal control systems

The Board, through the Board Risk Committee, conducts a robust assessment of the operational principal risks. An annual review of the effectiveness of the Group's risk management and internal control systems is undertaken by the Audit Committee. Further details on the work of the Audit Committee and the Board Risk Committee can be found on pages 66 and 70 respectively.

C.3. Role and responsibilities of the Audit Committee

Details of how the Committee has discharged its responsibilities during the year are provided in the Audit Committee Report on page 66. The terms of reference for the Audit Committee are reviewed at least annually and are available on the Company website.

D. Remuneration

D.1. Levels and components of remuneration

The Board believes that the Group's Remuneration Policy is appropriately designed to promote the long term success of the Company, while enabling the Group to attract, retain and motivate the executive talent required for the delivery of its business strategy. For further information, see the Directors' Remuneration Report on page 71.

D.2. Development of remuneration policy and packages

The terms of reference for the Remuneration Committee are reviewed at least annually and are available on the Company website. The Remuneration Committee has the delegated authority for setting the remuneration of Executive Directors and the Chairman. The fees payable to the Non-executive Directors are determined by the Chairman, on recommendation from the Executive Directors Committee.

E. Relations with shareholders

E.1. Shareholder engagement and dialogue

Effective communication and engagement with investors is of paramount importance to the continued success of the Company, and roadshows are held during the year between investors and the Chairman and Director of Investor Relations. The CEO and CFO have held meetings with existing shareholders through the investor relations programme during 2018, see page 62. Further details of the Capital Markets Day can be found on page 63.

E.2. Constructive use of general meetings

The Board values all general meetings as an important opportunity to engage with investors. Attendees at general meetings have the opportunity to ask questions to the Board and to speak to individual Directors following the formal business of the meeting. This year the AGM is being held in the afternoon, in response to shareholder requests.

The Board composition

The Board comprises a Non-executive Chairman, a CEO, a CFO, a Senior Independent Director and four other Non-executive Directors. All Non-executive Directors, except the Chairman, are considered to be independent and the Chairman was considered to be independent on appointment. The Board's policy is that the roles of Chairman and CEO should be performed by different people. The division of responsibilities is documented and clearly understood. The Chairman is responsible for the leadership and effectiveness of the Board and the CEO is responsible for leading the day to day management of the Company, formulating the strategy and delivering against the strategy when approved by the Board.

Biographies of the Directors are set out on pages 52 and 53. The attendance of Directors at Board meetings is set out on page 52.

The rules for the appointment and replacement of Directors are set out in the Company's Articles of Association (the Articles), copies of which can be obtained from Companies House in the UK or by contacting the Company Secretary. Changes to the Articles must be approved by shareholders passing a special resolution. The Directors and the Company (in the latter case by ordinary resolution) may appoint a person who is willing to act as a Director, either to fill a vacancy or as an additional Director.

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

All Directors currently in office will retire and those eligible and wishing to be reappointed will seek re-election at the AGM. The Chairman confirms to shareholders when proposing reappointment that the individual's performance continues to be effective and that the individual continues to demonstrate commitment to the role. Non-executive Directors are subject to Companies Act provisions relating to the removal of a Director.

Board proceedings

Board meetings

Board meetings, scheduled in accordance with the annual timetable, were held six times during the year on a face to face basis and three times by telephone. In addition, there were two short notice meetings to support Board decisions required between scheduled meetings. There is also contact between Board meetings to progress the Group's business as required. Meetings are held in London, Wimborne and at other UK and international operational locations.

Performance reviews

The Senior Independent Director, together with the Non-executives, appraised the Chairman's performance. The Chairman held meetings with the Non-executives to assess the Executive Directors' performance, and held one to one appraisals with each Non-executive Director and the CEO.

Board appointments and induction

As the Group continued its Board refresh programme, and recognising the short tenure of most Board members, a complete induction session was held with the full Board present. Materials covered the history of the Group, supply chain management, culture, talent and a 'deep dive' into each Sector.

Board diversity

The Diversity and Inclusion Policy applies to employees, non-permanent staff, and Board members. Specifically it states that all persons covered by the policy must promote and role model the development of a diverse and

inclusive work culture. Further it states that recruitment, development, reward, promotion or any other work-based opportunity must be based solely on performance, ability and the demonstration of Cobham's values, and that such decisions must be recorded to confirm compliance with this policy.

The Board is, by necessity, a diverse group of individuals, some with business backgrounds, and others with defence specific or more general management experience. This level of diversity of thought is needed to make sure the decisions made have the right input and challenge, and assists the Board in understanding and influencing the culture around the business. This was a key focus for the Group's Board through 2018 and into 2019.

The Nomination Committee ensures and oversees a diverse pipeline for succession to both Board and GE positions.

Other Board proceedings

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

Matters reserved for the Board

The Board has adopted a schedule of matters reserved for its specific approval. The schedule provides the framework for those decisions that can be made by the Board and those that can be delegated. Among the key matters on which the Board alone may make decisions are the Group's strategy, its three year financial plan, its consolidated budget, Group policies, dividends, acquisitions and disposals, and all appointments to and removals from the Board. Authority is delegated to management by way of a delegation matrix in accordance with the provisions of the Group's Corporate Framework, ensuring that proper management oversight exists at the appropriate level. Matters delegated in this way include, within defined parameters: the approval of bids and contracts; capital expenditure; and financing arrangements.

Strategy

Key Activities and discussions

- Confirmed strategic focus of the business to remain space, aerospace and defence.
- Oversight of organisational restructure in Sectors.
- Review and approval of divestment of the AvComm and Wireless test and measurement businesses.
- Review and approval of the electromagnetic simulation software business divestment.
- Consideration of the Group's manufacturing footprint.
- Undertook a supply chain review.
- Held an Investor Capital Markets Day.
- Oversight of all transformation activity, to improve traction and pace.

Key Priorities for 2019

- Continued oversight of transformational activities, including: Sector restructure; culture change and talent management; supply chain management; operational performance focusing on cost of quality and execution.
- The markets we serve to be kept under review.

Risk

Key Activities and discussions

- Received a brief on cyber security matters.
- Completed an analysis of the capacity of the Group to deal with additional risk.
- See also the work of the Board Risk Committee at page 70.

Key Priorities for 2019

- Continued emphasis on embedding risk management into business activities.

Governance

Key Activities and discussions

- Oversight of the KC-46 programme and Boeing relationship, and other major customer relationships.
- Appointment of Marion Blakey as a NED.
- Full co-operation with the FCA through their now discontinued investigation.
- Completed an external Board evaluation.
- Held indepth induction session with the full Board.
- Completed an extensive audit tender process.

Key Priorities for 2019

- Monitoring of progress against onerous contracts.
- Chairman succession and induction.
- Strengthen succession planning from Board, through the senior management team.
- Consideration of how to deliver employee feedback into the Boardroom.
- Review processes to achieve an enhanced role for the Board in key stakeholder management.

Board Activity

Financial

Key Activities and discussions

- Monthly review of operational and financial performance metrics.
- Review and approval of the financial statements in support of the divestment of the AvComm and Wireless test and measurement businesses.
- Consideration of capital allocation policy.
- See also the work of the Audit Committee on page 66.

Key Priorities for 2019

- Approval of capital allocation policy.
- Ongoing focus on closure of the remaining legacy items and reduction of remaining provisions as a consequence.
- Oversee the transfer of the external audit to EY, if approved at the AGM.
- Continued strengthening of the financial control environment.

Culture

Key Activities and discussions

- Undertook third culture assessment using Heidrick and Struggles Organisation Assessment Questionnaire.
- Started an exercise to identify and launch new purpose and values.
- Revised talent and senior management development programmes.

Key Priorities for 2019

- Support the cultural realignment, primarily focusing on bedding in the new purpose and values across the businesses.
- Develop KPIs to monitor cultural change

Safety, Health and Environment (SHE)

Key Activities and discussions

- Monthly monitoring of SHE performance metrics, annual review and assessment completed.
- Received a brief on environmental matters.

Key Priorities for 2019

- Oversight of the strengthening of SHE resource and the performance in the second year of a 3 year SHE strategy.

Board and Committee structure

Board of Directors

The Board's role is to lead the Group with a view to the creation of strong, sustainable financial performance and long term shareholder value, to review and approve the Group's strategic plan, and to supervise the conduct of the Group's activities within a framework of prudent and effective internal controls.

The Board has adopted a schedule of matters reserved for its specific approval. For other matters, authority is delegated to management by way of a delegation matrix in accordance with the provisions of the Group's Corporate Framework.

Principal Board Committees

The Audit Committee

monitors the integrity of financial statements and has ultimate responsibility for internal control systems.

For full details of the Committee's work see report on page 66.

The Board Risk Committee

provides assurance to the Board regarding the management of the Group's principal operational risks.

For full details of the principal risks see pages 36 to 41 and for details of the Committee's work see report on page 70.

The Remuneration Committee

determines the Remuneration Policy for the Executive Directors and is responsible for oversight of the remuneration policies and practices of the wider workforce.

For full details of the Committee's work see report on page 71.

The Nomination Committee

reviews the composition of Board, considers succession planning at both Board and senior management level and leads the process of appointments to Board.

For full details of the Committee's work see report on page 64.

The Disclosure Committee

ensures that policies, systems and controls exist so that potential share price sensitive information is escalated, considered, verified and promptly released to the market, where required.

The Executive Directors Committee

assists the CEO in the performance of his duties. Its terms of reference include the discharge of obligations arising under the Company's share plans; the recommendation of the remuneration of the Non-executive Directors; the approval of banking facilities; and the approval of bids and contracts above the limits delegated to the Sectors.

Principal Management Committees

The Group Executive (GE)

reviews the performance of the Company (and of individual Business Units, Sectors, and functions) against the financial budgets and operational targets approved by the Board; retains accountability for the effective management of operational risks, including mitigating actions, controls, ownership and risk register maintenance; monitors SHE performance and customer metrics; promotes a corporate risk culture, through the raising of risk awareness and sharing knowledge and best practice. Oversees, at a strategic level, the process to identify, develop and retain key talent in the business, feeding in to the Nomination Committee as appropriate.

The Safety, Health and Environment Committee

oversees the Group's organisational SHE culture.

Technical expertise is provided through a Group SHE Council – comprising senior business unit SHE professionals under the leadership of a dedicated Group SHE Senior Director and the VP Corporate Responsibility and Sustainability.

The Corporate Responsibility and Sustainability Committee

is accountable for CR&S strategy, including climate change and carbon management.

Reviews the effectiveness of controls in place for identifying and managing risks and opportunities, challenging Group performance, and maintaining strategic and policy oversight.

The Business Ethics and Compliance Committee

oversees the Cobham Ethics and Compliance Programme.

Reports into the Audit Committee and oversees the Group's Ethics Champions programme, the Ethics Helpline and compliance training and communications.

The Governance Committee

oversees and approves policies ensuring effective implementation across the Group.

The Disclosure Panel

oversees potential price sensitive information and evaluation to ensure prompt disclosure, reporting up to the Disclosure Committee, as appropriate.

Board and Committee performance evaluation

Cobham engaged the services of Lintstock to assist with the 2018 evaluation of Board performance. Lintstock is a corporate governance advisory firm that specialises in facilitating board reviews. The first stage of the evaluation involved Lintstock engaging with the Chairman and Company Secretary to set the context for the evaluation and to tailor the survey content to the specific circumstances of Cobham. All Board members were then invited to complete an online survey addressing the performance of the Board and its Committees. The anonymity of the respondents was ensured throughout the process in order to promote an open and frank exchange of views.

The process was divided into four stages



The exercise was weighted to ensure that core areas of Board and Committee performance were addressed, as well as having a particular focus on the following areas:

- The adequacy of succession plans in place for members of the Board, and the attributes and backgrounds that should be sought in future Non-executive appointments;
- The management of the agenda and the allocation of time at the Board meetings, as well as the balance struck in the choice of location;
- The quality of the Board's strategy session held in October 2018, the performance of the Company in capturing strategic opportunities and specific ways in which the Board could contribute further to strategic oversight;
- The oversight of principal risks, and the clarity of the roles of the Audit and Board Risk Committees with respect to risk management;

- The awareness of, and readiness to comply with, the new culture provision in the recently revised UK Corporate Governance Code;
- The quality and timeliness of the materials distributed in advance of Board meetings, as well as the updating of Directors on major developments between meetings; and
- The effectiveness of the Board Committees over the past 12 months, as well as the main challenges facing each Committee over the next few years.

As a result of the evaluation, the Board has – amongst other things – considered its plans for addressing the Company's strategy over the coming year, agreed to devote greater time to human resource oversight over the coming year, and identified scope for improvement in the Board's agendas.

The CAES Sector/SSA Governance

The CAES Sector participates in classified US Defence programmes. It therefore operates under a US DoD SSA as required by the US National Industrial Security Program. The SSA is designed to mitigate FOCI so that CAES can maintain the required facility security clearances to participate in certain US Government, including DoD, programmes. There are certain areas in which CAES and the wider Group operate under an Affiliate Operations Plan (AOP), pursuant to which certain services can be shared by the Group and the SSA.

The CAES Board has been refreshed during the past two years to strengthen the governance within CAES and is currently made up of:

- the Group's CEO and CFO (whose biographies can be found on pages 52 and 53) and General Michael Hagee (retired), known as Inside Directors under the SSA;
- the CAES Sector President and CFO, known as Officer Directors under the SSA; and
- a number of other individuals who have no prior relationship with Cobham plc, known as Outside Directors under the SSA, who are approved by the US DSS, and identified below:
 - General Kevin Chilton USAF (retired) – former Commander US Strategic Command and former NASA astronaut;
 - Admiral Steve Abbot USN (retired) – former Deputy Commander in Chief US European Command;
 - Cindy Moran – President and managing partner of IT consultancy, Pikes Way LLC, and former Director of Network Services, US Defense Information Systems Agency; and
 - Scott Webster – Co-founder and former Executive Director of Orbital Sciences Corporation.

Outside Directors and Officer Directors, who must be US citizens with appropriate US security clearances, also make up the Government Security Committee (GSC) of the CAES Board. The SSA does not permit Inside Directors to be members of the GSC, which is responsible for maintaining independent policies and processes facilitating insulation of CAES operations as a US cleared defence contractor from the foreign parent. The SSA restricts the level of participation that Cobham can have in certain CAES activities. For example, it limits Cobham's ability to decide matters affecting the management or operations of the US cleared defence contractor (CAES) in a manner that may

result in unauthorised access to classified information. Cobham maintains its involvement in CAES activities primarily through participation of Cobham's CEO and CFO (as Inside Directors) in the deliberations and decisions of the CAES Board and authorised committees, or interactions through a series of shared services provided pursuant to an AOP. All CAES Board Directors have a fiduciary duty to Cobham plc, as shareholder, and the Outside Directors need to perform their duties reasonably and in good faith in a manner believed to be in the best interests of the shareholder but consistent with the national security concerns of the US.

Cobham plc, as shareholder, retains the right to remove or replace any member of the CAES Board, subject to clearance from the DSS in the case of an Outside Director. In addition, under the current SSA, the CAES Board cannot carry out a number of actions without Cobham's express approval, including amongst others the following:

- Sell, lease, acquire or dispose of property or assets otherwise than in the usual course of business;
- Merge, consolidate, reorganise, dissolve or wind up the business; or
- Mergers and acquisitions.

CAES must act in a manner which is compliant with Cobham's obligations as a UK listed company.

The effectiveness of governance and assurance procedures between the Group and the CAES Sector is regularly reviewed. The main elements of these procedures include:

- CAES management signing a Letter of Representation to Cobham plc twice a year confirming that systems of risk management and internal control within CAES have operated without significant exceptions during 2018, and that procedures are broadly consistent with the Group's controls;
- the outcome of risk assessments at business unit and sector level being presented to the CAES Audit Committee;
- CAES management confirming that key controls, including the budget process, are in place to form the basis of monthly reporting;
- key oversight functions being in place, and CAES management confirming that a fully functioning GSC has operated throughout the year;
- the CAES Audit Committee charter aligning to that of the plc; and
- defining levels of authority delegated to the CAES Board, above which approvals are escalated to the plc Board.

Engaging our stakeholders and responding to their needs

Stakeholder engagement

The Board recognises the importance of engaging with its wider stakeholder base. We have set out below the actions being taken by management around the business to engage with customers, investors and employees, plus a case study on supplier management.



Customers

Why is it important to engage?

One of the Group's key priorities has been to foster closer relationships with customers at all levels. This helps Cobham provide value for money and high performance technical solutions for customers' most pressing needs. This can take the form of close partnering or collaborative engagement in technology development and production. Cobham actively engages with its customers to exchange technology roadmaps to closely align research and development and engineering resources with customers' technology and market objectives.

How do we engage?

During the year, the Group has engaged to increase key customer awareness of the full range of capabilities. This is because in some cases, customers may only do business with certain businesses or Sectors. For example, two Sectors combined to jointly engage with a top US defence contractor during the year to present Cobham's leading-edge technology to the customer's engineering and supply-chain community in an exclusive event. The engagement resulted in exchanges of technological and market information enabling Cobham to align investments more closely to this customer.

In addition, as part of a UK Government and UK trade body initiative, Cobham presented to another major US prime contractor, to increase bid opportunities. The event was successful, giving access to key individuals and insights into new programmes. This resulted in follow-on presentations to different customer business units.

In Australia, as part of its customer engagement on a major programme, the Aviation Services business holds quarterly review meetings involving key customer stakeholders. Understanding the customer's needs, the business proposed the trial and implementation of a new search and rescue technique utilising Electro Optical technology. All trial flights undertaken to date have been successful. This has enabled locating search survivors in reduced time. In addition, the technique has the potential to be applied by other international search organisations.



Investors

Why is it important to engage?

Shareholders are important providers of capital to the Group and also vote on key resolutions at the AGM. Cobham's investor relations programme aims to keep shareholders regularly informed of the Group's prospects and performance, together with developments as they occur. In addition, the programme is intended to keep Cobham's Board informed and up to date on shareholder views. This helps to inform strategic decisions and the setting of management objectives.

How do we engage?

The centrepiece of Cobham's shareholder engagement is the interim and preliminary results. These are used to update shareholders on a number of matters. Following each set of results the CEO and CFO meet with the Group's largest shareholders, where the above matters have been central topics of conversation during the year.

The Group also releases shorter Trading Updates. The first covers the first quarter of the year and this is released on the day of the AGM. The second covers the ten months to the end of October, which is released in mid-November.



Employees

Cobham has continued to prioritise engagement with its existing shareholders during the year, updating them on significant developments during a period of change. The Group also undertook a Capital Markets Day in November 2018, see the case study on page 63.

In addition to the CEO and CFO meetings with shareholders, the Chairman, Senior Independent Director and Remuneration Committee Chair engage with investors as the need arises.

Shareholders also have the opportunity to ask questions of the Board of Directors at the AGM, which is held in April.

In addition, Cobham maintains a regularly updated website at www.cobhaminvestors.com which includes a range of information relevant to shareholders; for example, current and historical financial materials, news, strategy, governance information, together with Board biographies and share price data. A specific Annual Report and Accounts section was added to the website during the year, highlighting certain sections of this document in an easily accessible way.

Why is it important to engage?

The Board recognises the importance of regularly engaging with employees. This supports the Group's cultural change and helps attract and retain talented employees, which is critical to future growth.

How do we engage?

Engagement occurs in different ways and at different levels. Business unit management teams hold regular 'all hands' meetings with local employees to instil a sense of common purpose, to update on relevant news and developments and to respond to questions. The CEO and other members of senior management also undertake 'all hands' meetings when visiting business units.

A gathering of senior managers is held annually, which is used to reinforce the Group's direction and priorities and to communicate key messages, for dissemination through the business. In addition, for the first time in 2018 quarterly meetings of the business unit General Managers commenced. This recognises their pivotal role in effecting and consolidating needed change. The meetings enable them to share common opportunities and challenges, and together decide how business units can deliver on Group priorities.

In addition, all employees have access to a dedicated intranet site, where they can find news, policies and procedures and a range of other materials of interest. A majority of Group sites also use digital displays to communicate employee information, with many sites giving employees the opportunity to make suggestions for improvement using feedback boxes.

The Group's Corporate Communications department compiles and distributes various materials to employees including a quarterly employee magazine, online news items and senior management 'blogs'. Dovetailing with this, certain business units and Group functions undertake more specialist engagement, relevant to specific businesses or functions.

Case study

Strengthening the supplier base

There has been continuing development to improve the Group's supply chain. The aim is to increase the strength of the supplier base as Cobham works towards achieving a target of 80% of its spend with 20% of its suppliers. Consolidating the supply chain with a focus on quality provision gives more confidence in the ability to deliver, and can offer economies of scale. There have been internal and external efforts towards this target.

Within Cobham, there have been many actions to support a closer and improved relationship with suppliers across all the business units:

- Improving and refining supplier management information systems;
- Introducing dedicated managers for electrical, mechanical and indirect spending to make procurement more effective and efficient;
- Entering long term agreements with key suppliers; and
- Introducing quarterly business reviews with key suppliers.

Supplier conferences were also held in the UK and US to share the Group's vision and strategic direction with key suppliers. Priorities included introducing suppliers to developments in the supply chain strategy, show them potential new areas of business, and develop stronger relationships.

Presentations on the Sectors were given with positive feedback. The majority of suppliers had little knowledge of the breadth of Cobham's business and commented on areas where there could be further development in our partnership. There was also positive feedback regarding the current supply chain strategy, which addressed areas of improvement identified in a survey undertaken with suppliers. These will be a focus in 2019.

The survey also showed that the majority of suppliers had long-standing relationships with Cobham, with 95% satisfied with the relationship overall.

A proposal to introduce supplier awards was received positively. This aim of this is to motivate suppliers to deliver products to higher quality standards, and to reward those that meet the highest standards. Overall, the conferences were a success, and the focus on motivating our suppliers will continue.

Key stakeholder events in 2018



Key dates 2019

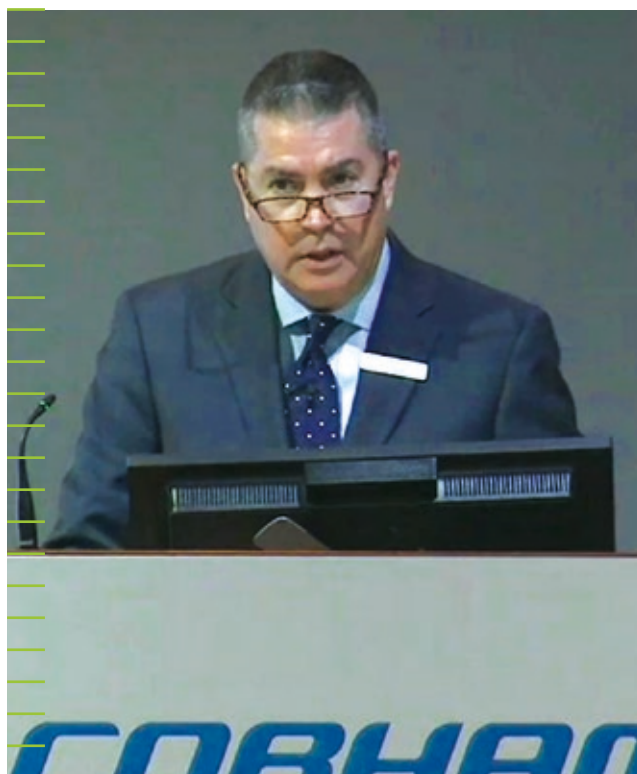
Trading update	Mid-November 2019
Interim dividend payment date	Friday 8 November 2019
Record date	Friday 11 October 2019
Ex-div date	Thursday 10 October 2019
Interim announcement (and dividend announcement)	Thursday 1 August 2019
AGM statement	Thursday 25 April 2019
AGM	Thursday 25 April 2019
Annual Report and Accounts	Friday 22 March 2019
Preliminary announcement	Thursday 7 March 2019

Results of 2018 AGM

Resolution	Total Votes For %	Total Votes Against %
1 Report & Accounts	99.82	0.18
2 Remuneration Report	98.23	1.77
3–9 Election and re-election of Board members	96.16–99.75	3.84 – 0.25
10 Re-appointment of Auditors	99.02	0.98
11 Remuneration of Auditors	99.91	0.09
12 Authority to purchase own shares	98.88	1.12
13 Authority to allot shares	84.39	15.61
14 General authority to disapply pre-emption rights	87.70	12.30
15 Additional disapplication of pre-emption rights	96.43	3.57
16 Authority to call general meetings on 14 days' notice	96.48	3.52

Substantial shareholdings as at 31 December 2018

	%
Silchester International Investors LLP	12.40
Columbia Threadneedle Investments	11.19
Causeway Capital Management LLC	11.11
Franklin Templeton Investments	4.11
BlackRock, Inc.	4.11
Artemis Fund Managers Ltd	3.59
The Vanguard Group Inc	3.31
Bestinver Gestion, S.G.I.I.C.	3.14
Aberdeen Standard Investments	3.04
Sprucegrove Investment Management	2.88
T. Rowe Price Group	2.88



Capital Markets Day

In November 2018, senior managers from the Mission Systems Sector presented to an engaged audience in London, UK with opportunities to ask questions and see some of the Sector's products in an interactive display area. The management team was led by Sector President, Jim Barber, who is seen presenting, left. In the auditorium the audience comprised some 70 analysts, shareholders and potential shareholders, plus another 40 who watched the event online. The webcast, together with the supporting presentation, is available for viewing on www.cobhaminvestors.com/reports-and-presentations/2018.

The management team set out how the Sector has a long heritage of innovation and deep technical expertise in its specialist markets. Further it described the Sector's strong market positions and attractive growth opportunities, with a focus on execution being key to growth plans and profitability. Compelling presentations followed on some of the Sector's specific growth opportunities covering its aerial refuelling, military oxygen systems and fuel tank inerting markets. The event ended with an informal opportunity to mingle with management and discuss the day's themes further.

A refreshed Board



Michael Wareing

Chairman

CMG, FCA, FCCA, MCS1

Committee members

John McAdam, Alison Wood, René Médori

Number of meetings held in 2018

4

Dear Shareholder

As we reported last year, René Médori and Norton Schwartz joined the Board with effect from 1 January 2018. René took over the role of Audit Committee Chair in April, immediately after the AGM.

We also announced the appointment of Marion Blakey on 3 August 2018. For this appointment, our specific brief was to look for a candidate with US commercial and SSA expertise. After completing a search exercise through Egon Zehnder, a long list of potential individuals was identified, from which a short list of candidates who met the agreed criteria on paper was compiled. I then interviewed candidates and took up personal references. Marion, our preferred candidate, had meetings with the majority of the current Board members and full due diligence was undertaken before her formal appointment was recommended to the Board for approval. Further details of Marion's skills and experience can be found on our website at www.cobhaminvestors.com/our-business/our-board.

In sourcing candidates for Board positions, Egon Zehnder are required to support our objective of building a diverse and inclusive board. The representation of women on the Board at 31 December 2018 was 25%.

We now have an extremely strong Board, with a good mix of backgrounds and experience to support the Executives and to provide constructive challenge. On the next page you will see the results of the skills and experience review undertaken by Egon Zehnder to support the Board refreshment programme and succession planning. Egon Zehnder have provided support for recent Board and other senior management appointments but have no other connection with the Group.

During 2018, I had surgery, which together with the recuperation period, took me away from the business for a 3 month period. In that time, John McAdam, Senior Independent Director, and an experienced Chairman in his own right, deputised as Chairman and received a relevant proportion of the Chairman's fee. In turn, I waived the Chairman's fee for the period of my absence. I thank John, and the rest of the Board, for their support through this time.

We committed to completing an in depth external Board and Committee evaluation during 2018, the last external evaluation having been undertaken in 2015, see details on page 59.

We restructured the Committee during 2018; part of this process focused on strengthening succession planning below Board level, resulting in a much clearer view of strengths and development required in our senior management team. We will build on this during 2019 as we have better data through the implementation of an enterprise wide HR Information System (excluding the CAES business). Succession has also been invigorated by a number of senior management appointments made at both Group Executive level and in their reporting line.

With the support of the Board, the executive team launched a new purpose statement and values, with a stronger focus on team working across the Group, this launch was supported by leadership assessment and development programmes and will be embedded in the business through 2019.

Having recently reviewed the performance of the Non-executive Directors and their time commitment, I am confident that we do not have an issue with overboarding with any members of our Board.

In summary, during 2018 the Nomination Committee has helped lay the foundations for much stronger talent and succession planning, and has made plans to realign the organisational culture to support the continued operational and financial performance. 2019 will focus on embedding these plans.

A handwritten signature in dark ink, appearing to read 'Mf Wareing'.

Michael Wareing

Nomination Committee Chair

7 March 2019

Board skills matrix

Committees:

A – Audit
 N – Nomination
 R – Remuneration
 K – Board Risk
 (° denotes committee chair)

	Tenure (years, months) as at 31 December 2018	Committee membership	Gender	Nationality	People development	Commercial / Product technology	Risk management	Programme management & contracting	Financial qualification/ expertise	Engineering expertise	Aerospace & defence sector	US defence experience	Foreign Ownership Control and Influence	FTSE 100/ANSE experience (NED/ED)	Other current Non-executive Director roles	International operations	Strong UK corporate governance experience
Non-executive Directors																	
Michael Wareing (Chairman)	8,0	N°,K°	M	British	✓		✓	✓	✓					✓		✓	✓
John McAdam (SID)	1,4	A,N,R	M	British	✓		✓	✓			✓			✓	✓	✓	✓
Alison Wood (NED)	7,5	R°,A,N,K	F	British		✓	✓	✓		✓	✓		✓		✓	✓	
René Médori (NED)	1,0	A°,N,K	M	French/ British	✓		✓	✓	✓					✓	✓	✓	✓
Norton Schwartz (NED)	1,0	A,K,R	M	American	✓		✓				✓	✓	✓		✓	✓	
Marion Blakey (NED)	0,5	A	F	American	✓		✓				✓	✓	✓	✓	✓	✓	
Executive Directors																	
David Lockwood (CEO)	2,1		M	British	✓	✓	✓	✓	✓		✓	✓	✓	✓		✓	✓
David Mellors (CFO)	2,0		M	British	✓	✓	✓		✓		✓	✓	✓	✓		✓	✓

Key events for 2018

- Continued oversight of the Board refresh, offering two appointments during the year;
- Reviewed the impact of the 2018 UK Corporate Governance Code and updated terms of reference accordingly;
- Reviewed the development, retention and succession plans for the Executive Directors, the Group Executive team and the Top 75 roles; and
- Completed a Board evaluation plus a composition and skills review.

Priorities for 2019

- Chairman succession;
- Oversight of succession, retention and development for the Executive Directors and the senior management team;
- Ensure the recently launched purpose and values are embedded into the business;
- Support and oversee the cultural realignment; and
- Agree and embed mechanisms for employee engagement.

The Committee's terms of reference are available on Cobham's website or by application to the Company Secretary.

Directors' professional development

On appointment, Directors undertake a structured induction programme during which they receive information about:

- The role of the Board and the matters reserved for its decision;
- The Group's corporate governance practices and procedures;
- Their duties and responsibilities as Directors of a listed company; and
- A strategic overview of the business, for the Group and by Sector.

This is supplemented by visits to key locations and meetings with, and presentations by, members of the senior management team.

As most of the Board members are newly appointed, the May 2018 meeting was devoted to a full induction session. This covered Cobham history and context, supply chain, culture and talent review, and Sector deep dives. The materials were updated and re-run for Marion Blakey on a one to one basis when she joined in August.

Development for Directors is available as required and is provided mainly by means of internal briefing from senior management or advisors and external courses. In addition, Directors' knowledge of the legal and regulatory environment is updated through the provision of information by the Group's advisors and by regular updates from the Company Secretary and the legal team.

There is also time reserved in the Board's work plan and within those of its committees to receive updates and teach-ins from advisors and subject matter experts.

Board members are required to provide details of other professional development they undergo on their own account.

A robust audit tender successfully completed



René Médori

Audit Committee Chair

Committee Members

John McAdam, Alison Wood, Norton Schwartz, Marion Blakey

Number of meetings held in 2018

7

Dear Shareholder

The second year of the turnaround has seen the Group report financial results in line with expectations, against the backdrop of a more resilient and robust balance sheet. Control improvements have continued through the year. There has been a refreshment of the Audit Committee's membership, with a successful transition to a new Committee Chair taking effect from the 2018 AGM.

Key issues for 2018:

- Focus on the key programme watchlist review process has continued, including KC-46 programme cost assertions and overdue debts, and WARP qualification status;
- Presentation and disclosures: the implementation of IFRS 15 has concluded successfully, with a restatement impact to the 2017 underlying operating profit of £2.8m. Preparation for the adoption of IFRS 16 is now complete: see note 1 to the Group Financial Statements for more details.
- Audit tender: the external audit tender was completed, with shareholders being invited to approve EY's appointment at the 2019 AGM. Details of the tender process are set out on this page.
- The Group divested its AvComm and Wireless test and measurement businesses to Viavi Solutions Inc. This gave rise to a profit on disposal of £218.4m including a review of all relevant judgements.
- Pensions: the pension deficit has reduced to £46.6m (2017: £63.2m). This is in part due to the completion of the UK triennial valuation which led to a revised deficit recovery plan.

Priorities for 2019:

- First insights and reflections from the newly appointed auditors EY who will be undertaking process walkthroughs at all main sites as part of their familiarisation;

- Talent review: to ensure appropriate succession planning is in place for all senior finance roles;
- Tracking the implications of the changes to the regulatory environment;
- Reducing the Group's most material balance sheet risks, with a focus on KC-46 and uncertain tax positions; and
- Ensuring the CAES Board and Audit Committee mirror, as far as is allowed, the Group's policies and strengthens the CAES Internal Audit function.

Audit tender

PricewaterhouseCoopers LLP (PwC) has been the auditor of the Company and Group since inception. Its performance has been reviewed annually and audit partner rotation requirements have been observed. An external audit tender was conducted in 2018 with a view to replacing PwC from the 2019 financial year onwards. PwC were not invited to participate in this audit tender process to comply with audit firm rotation requirements.

The audit tender process was completed in October 2018 when the Board concluded that EY were the most suitable firm for the role. This decision was based on the quality and industry experience of the proposed audit team, their plans for an effective audit process and approach as well as their understanding of Cobham, based on interactions with our senior management team members. Those interactions have ensured EY have already been able to spend time with those of our subsidiaries that have high transaction complexity (including our SSA) and areas of significant accounting judgements.

EY have also been able to start their transition process, including shadowing the Audit Committee. During our October hard close exercise and the 2018 year end, they have observed the PwC clearance meetings and certain PwC walkthroughs to leverage their own work from existing procedures. The EY team has performed its initial audit scoping and risk assessment, including design of a detailed transition plan for 2019.

PwC will resign after the firm has concluded the 2018 external audit process. Shareholders will be invited to appoint EY as Cobham's statutory auditor at the 2019 AGM.

Once the appointment is made, EY will host group academies to on-board their local teams and communicate the audit vision and approach to local audit partners. The engagement will start with initial insight reports which will be presented to the Audit Committee ahead of the 2019 interim closing. A successful transition is a key priority for the Audit Committee in 2019.

Conclusion of FCA investigation

As we announced in March 2017, the Enforcement and Market Oversight Division of the FCA had been investigating Cobham in relation to its compliance with the Listing Rules, Disclosure and Transparency Rules and the Market Abuse Regulations between April 2016 and February 2017.

The Company fully co-operated with this investigation throughout. The FCA informed the Company in August 2018 that it had decided to discontinue the investigation.

At the 2019 AGM, I and my fellow members of the Audit Committee will be available to respond to any questions shareholders may wish to raise on this report or the Committee's activities.

A handwritten signature in blue ink, appearing to read 'René Médori'.

René Médori

Audit Committee Chair

7 March 2019

Financial reporting and significant financial judgements

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

these matters. The Committee identified the issues below as significant in the context of the 2018 Group Financial Statements with regard to the facts and circumstances then existing, taking account of the level of materiality and the degree of judgement exercised by management.

Area of focus	Role of the Committee	Conclusion
Going concern basis for the preparation of the financial statements	The Committee considered the outcome of management's half-yearly reviews of current and forecast net debt positions and the various financing facilities and options available to the Group, including the risk and potential impact of unforeseen events.	The Committee confirmed that the application of the going concern basis for the preparation of the financial statements continued to be appropriate.
Programme watchlist	The Committee considered the estimated costs to complete, working capital levels and profitability of material development projects and production contracts. Customer performance obligations under these contracts were also considered to ensure appropriateness of accounting following the adoption of IFRS 15 effective 1 January 2018. (Refer to notes 21 and 30 to the Group Financial Statements.)	The judgements of management as regards estimated costs to complete, outcome of negotiations with customers and amounts recoverable, as well as revenue amounts recognised and related disclosures were deemed appropriate.
Revenue/contract accounting		
Provisions and material disputes	The Committee has had regular updates on the balance sheet review items from 2016, provisions and material disputes ahead of and during the year end process. (Refer to note 21 to the Group Financial Statements.)	Whilst some matters have been closed within their original estimates, the final outcome of a number of items remains uncertain. There has been appropriate control and consideration of these amounts, so that we are satisfied with their use and the year end position.
Inventory provisions	The Committee has had regular updates on balance sheet values and the levels of provisions against these. There has also been a review of the methods used for calculating provisions to improve consistency. (Refer to note 13 to the Group Financial Statements.)	Inventory remains a focus for working capital management, with a series of masterclasses having been held by management in business units to record lessons learned and improve buying and utilisation patterns in the future. Adequate provision has been made for risks identified at year end.
Uncertain tax positions and deferred tax	The Committee has reviewed the judgements made to account for uncertain tax positions. (Refer to note 7 to the Group Financial Statements.)	The Committee is satisfied that the material estimates made at the year end reflect advice that has been taken by management from relevant experts and specialists, while taking into account that there may be more than one route to settlements.
Impairment reviews	The Committee has reviewed management's computation of the present value of future cash flows from the three year plan. These have been compared to goodwill and acquired intangibles in order to test for impairment, (refer to note 10 to the Group Financial Statements) as well as the recoverability of investment in subsidiaries in the Parent Company Balance Sheet (Refer to note 6 to the Parent Company Financial Statements).	The Committee considers the management conclusion that no new impairment charges for goodwill and acquired intangibles have been required for 2018 to be appropriate. Conclusions leading to an impairment charge against the recoverability of investments in subsidiaries held by the Parent Company have also been confirmed, as necessary.
Pensions	The Committee received an update from management on the UK scheme triennial valuation and any impact of changes in assumptions for mortality, inflation and discount rates. Recent court rulings in relation to Guaranteed Minimum Pension equalisation and their potential impact for Cobham were considered. (Refer to note 23 to the Group Financial Statements.)	The Committee satisfied itself that all assumptions were within acceptable ranges, and reflected the most appropriate available data as at the year end.
Presentation, disclosures and new accounting standards	The Committee has reviewed the conclusion of the exercises for adoption of IFRS 15 and IFRS 9 and their restatement impact for the Group Financial Statements. The completeness of management exercises to identify and estimate the future impact of adopting IFRS 16 as from 1 January 2019, was also subject to evaluation.	The Group has adopted IFRS 15 and IFRS 9 from 1 January 2018 broadly in line with the estimates presented in the prior Annual Report (note 2). Adequate disclosures have been made for the impact of IFRS 16 being adopted from 1 January 2019 (note 1).

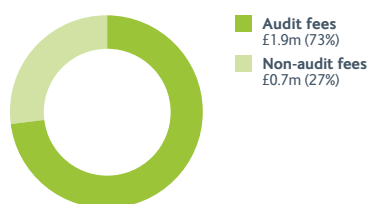
External audit

The Committee is responsible for overseeing relations with the independent, external auditors who were PwC throughout 2018, including the approval of fees. The Committee makes recommendations to the Board on the auditors' appointment and reappointment. Total fees paid to PwC in the year ended 31 December 2018 equalled £2.6m, with non-audit fees of £0.7m, representing 27% of the total. An analysis of the fees paid to the external auditors in respect of audit and non-audit work during the year can be found in note 5 to the Group Financial Statements.

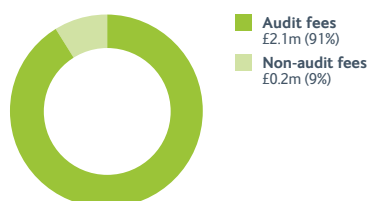
The provision of non-audit services is controlled by a policy which states that the external auditors will not be engaged to provide any element of non-audit services, without approval in advance from the CFO for fees up to £10,000, from the Chair of the Audit Committee for fees between £10,000 and £100,000 and by the Audit Committee for fees over £100,000. The Committee recognises that there may be some element of non-audit services for which the Group might wish to use the external auditors. The work must also be permitted under relevant regulations and must not impinge on the independence of the audit firm.

Corporate Governance — Audit Committee Report continued

Total fees paid to the external auditors (2018)



Total fees paid to the external auditors (2017)



Significant engagements included work related to the audit of the Form 8K filing of VIAVI Solutions Inc ('Viavi') following completion of the divestment of the AvComm and Wireless test and measurement businesses, at Viavi's request. The engagement was approved by the Audit Committee Chairman in advance of work starting and all fees, £0.6m, payable to PwC by Cobham have been recovered from Viavi.

PwC's presentation of their audit plan to the Committee set out the scope and objectives of the audit, together with an overview of the planned approach, an assessment of the Group's risks and controls, and proposed areas of audit focus. The Committee reviewed and approved the terms, areas of responsibility and scope of the December 2018 year end audit.

The external auditor is expected to report to the Committee any material departures from Group accounting policies and procedures that they identify during the course of their audit work. None were found or reported in 2018. The Independent Auditors' Report to the members of the Company can be found on page 86.

The Committee received feedback from each business unit, compiled by the Group finance function, on the performance of the external auditors through the year end process. On consideration of this feedback, the Committee confirmed that it was satisfied with the effectiveness of the external auditors.

The Committee is responsible for the development, implementation and monitoring of the Group's policies on services from external auditors, which are designed to maintain the objectivity and independence of the external auditors. These policies set out the approach to be taken when using the external auditors for non-audit work and regulate the appointment by the Group of former employees of the external auditors.

In addition to an independence review conducted by management, PwC has provided specific assurance and the Committee has considered the arrangements and safeguards that PwC has in place to maintain its independence and objectivity. The external auditors follow regulatory requirements to maintain the objectivity of the audit process; these stipulate a five year rotation policy in relation to the senior engagement auditor. Pauline Campbell was appointed lead audit partner in 2014. The Committee continues to be satisfied that PwC remains independent and objective. Details of the audit tender are set out on page 66.

Internal Audit and Assurance

The Head of Internal Audit and Assurance attended every Audit Committee meeting throughout 2018. In addition, they had ongoing contact with members of the Audit Committee throughout the year with and without management present, including private sessions with members of the Audit Committee. The Head of Internal Audit also had access to and met the Chairman of the Board without management present.

The findings of each Internal Audit review are summarised for the Committee, which focuses its discussions on unsatisfactory findings and on the action plans in place to address them. Particular areas of focus for Internal Audit during 2018 included continuation of financial control audits in line with the increased focus on control improvements, programme-related Internal Audits in line with the Programme Watchlist review process, the continuation of a specialised IT audit programme and a number of risk-based reviews focusing on the second line of defence activities.

In addition, Internal Audit has continued to maintain a programme of follow-up audits to assess the timely implementation of Internal Audit recommendations by the businesses and key matters from the Internal Audit reviews. A monthly tracking progress to ensure Audit Recommendations are addressed on a timely basis has continued throughout the year.

The Committee received regular updates against the 2018 Internal Audit Plan throughout the year.

The Committee approved the Internal Audit plan for 2019, including the proposed audit approach, coverage and allocation of resources. The 2019 plan was prepared considering a number of factors, including the principal risks of the Group. The key points of focus in the 2019 plan include:

- Continued focus on internal financial controls assurance;
- Increased focus on non-financial areas of risk; and
- Increased focus on IT controls and cyber security.

Taking account of the above, the Committee is satisfied with the performance of Internal Audit and Assurance. The next formal effectiveness review will be undertaken during 2019.

Where the operation of the SSA results in limitations of visibility when compared to other areas in the Group, the Audit Committee gains its assurance over CAES internal controls via the CAES Audit Committee of which Cobham's CFO is a member, and with Cobham plc's CEO and CFO representing Cobham on the CAES Board, in their capacity as Inside Directors. Further details can be found in the Corporate Governance Report on page 59.

Risk management and internal control systems

The Board has the ultimate responsibility for risk management and internal control systems, and has delegated to the Audit Committee responsibility for monitoring and reviewing the effectiveness of these systems in order to assist the Board in meeting this responsibility.

The Committee reviews internal financial controls, that is, the systems established to identify, assess, manage and monitor financial risks. The GE, chaired by the CEO, retains accountability for the management of operational risks, including mitigating actions. Sector Presidents are required to ensure that appropriate processes, including the maintenance of business unit and Sector risk registers, exist to identify and manage risks and to regularly carry out formal risk assessments. The Board Risk Committee, which was established during 2017, is responsible for providing assurance to the Board regarding the management of operational principal risks. The Board Risk Committee report can be found on page 70.

The Group operates under a system of internal controls which has been developed over time to meet the needs of the business and the risks and opportunities to which it is exposed, recognising differences in the nature and type of each of the Group's operations.

These controls include:

- The preparation and consideration of the three year plan;
- A comprehensive budgeting system with an annual budget which is approved by the Board;
- Review of business and financial performance in the month and year to date and monthly update of financial forecasts for the year;
- The monitoring of financial performance and key dependencies for the full year;
- The monitoring of key financial controls;
- The monitoring of project and programme management through lifecycle management; and
- The appropriate delegation of authorities to operational management.

Legacy control systems still exist from previous acquisition activity and other key control processes, including IT, are not fully standardised and implemented across the Group. The implementation and operation of certain key controls is decentralised in the business units. Sector, functional and central oversight activities and controls are in place to support this.

During the year, we have continued to embed and strengthen controls over known areas of weakness. This has included strengthened financial controls through increased independent review of the most material development contracts; extended governance and regulatory training; monthly Sector and business unit reviews by the CEO and CFO; the communication of a regularly updated delegation matrix and Letter of Representation; ongoing tracking and reporting of open and overdue audit recommendations; updates to our Minimum Standards of Financial Control and our Group Finance Manual; and an October hard close exercise, ahead of the year end.

Delegated authorities and other controls are contained in the Corporate Framework and the Group Finance Manual. Specifically with regard to the financial reporting process and the preparation of the Group Financial Statements, the system includes a semi-annual representation letter from all Sector and business units. Included in those letters are written acknowledgements that financial reporting is based on reliable data, that there is compliance with the Group's Minimum Standards of Financial Control and that the results are properly stated in accordance with Group policies. The Letter of Representation process has not highlighted any material weaknesses.

The Committee's review covers all material controls, including financial, operational and compliance controls and risk management systems, and is designed to give assurance that the day to day risk management and internal control systems which are embedded in the business, have operated effectively, with no significant failings or weaknesses identified during the review period, notwithstanding that management continues to implement plans to improve those systems.

The three principal lines of defence are outlined on page 35. The Committee receives assurance from the Inside Directors on the CAES Board on matters relating to CAES. It should be noted that due to the restrictions of the SSA, our assessment of the control environment in CAES differs from that operated elsewhere in the Group. In order to meet the requirements of the SSA and US DSS, oversight is indirect and flows primarily through the Inside Directors. Further details on how governance procedures are maintained in the SSA may be found on page 59.

Financial expert on the Committee

Given René Médori's experience as Finance Director at Anglo American plc, at The BOC Group plc, and his Audit Committee Chair experience at Petrofac and SSE plc, the Board has designated him as the financial expert on the Committee for the purposes of the Code. See page 52 Board of Directors for Committee membership and meeting attendance.

Objectives and responsibilities

The Committee's main objectives and responsibilities are set out in its terms of reference, which are available on the Group's website. The terms of reference are reviewed at least annually and were reviewed in 2018 to align more closely to best practice, and to reflect the changes required by the 2018 UK Corporate Governance Code effective 1 January 2019.

At least twice a year, immediately before a Committee meeting, the Committee meets separately with the independent lead audit partner and the Head of Internal Audit and Assurance, to give them the opportunity to discuss matters without executive management being present. In addition, regular contact is maintained between the Chairman and the Independent Lead Audit Partner and the Head of Internal Audit and Assurance between meetings, often without the presence of management.

Fair, balanced and understandable report and accounts

At the request of the Board, the Committee considered whether, in its opinion, the 2018 Annual Report and Accounts were fair, balanced and understandable. In forming its opinion, the Committee reflected on the information it had received and its discussions throughout the year. The assessment was assisted by an internal verification of the factual content by management, a review at different levels of the Group to ensure consistency and overall balance, and a comprehensive review by the senior management team.

Following its review, the Committee was of the opinion that the 2018 Annual Report and Accounts was representative of the year and presents a fair, balanced and understandable overview, providing the necessary information for shareholders to assess the Group's position and performance, business model and strategy.

In reporting on Alternative Performance Measures, the Group followed the FRC recommendation to consider the Guidelines on Alternative Performance Measures, as published by the European Securities and Markets Authority. Account has also been taken of the disclosures of our peers and current best practice.

Code of Business Conduct violations and fraud

The COBC, which incorporates the Group's whistleblowing policy, contains arrangements for an independent external service provider to receive, in confidence, complaints on suspected violations of the COBC for reporting to the Committee as appropriate. Details of the COBC are provided in the CR&S section of this report, on page 42. The Committee regularly received reports on matters relating to the COBC.

Evaluation of the effectiveness of the Committee

An external review of the effectiveness of the Board and all its Committees commenced towards the end of 2018. Feedback and input was sought from Committee members, regular meeting attendees and the independent auditors. The results were considered by the Board, see page 59, and actions required are in progress.

Legacy risk retirement confirmed as an operational priority of the Group



Michael Wareing

Chairman

CMG, FCA, FCCA, MCSI

Committee members

Alison Wood, René Médori, Norton Schwartz

Number of meetings held in 2018

3

Dear Shareholder

The Board Risk Committee was established during 2017 to provide assurance to the Board regarding the management of principal operational risks (as set out on pages 34 to 41). During 2018, the Board Risk Committee has focused on ensuring that the Group's operational risks are properly understood and defined and that the Group's risk management activities have been operating effectively to appropriately manage and mitigate the risks.

Activities during the year

During the year, the Committee considered the following main items:

- Review of the processes in place to identify operational risks throughout the Group, from a bottom-up basis through risk registers held at various levels within the Group, combined with a top-down view of the principal and strategic risks that could impact the Group in the future;
- Management of the risk mitigation activities being conducted within the Group, with a particular focus on the role of the Group Executive in mitigating the principal operational and strategic risks;
- Identification of the ability of the Group to take risks across several different resource constraints such as financial capacity, management bandwidth and technical capability; and
- Identification of the risks capable of being managed down, and the monitoring of milestones against mitigations.

Systems of risk management and internal control

The Board has ultimate accountability for the execution of risk management and internal control systems, with the Group Executive responsible for the execution of the management of risk throughout the Group.

The Board has delegated responsibility for the monitoring and reviewing of the effectiveness of the Group's risk management and internal control systems to the Audit Committee. The risk management process covers financial, operational and compliance controls, as well as the Group's Principal Risks.

The Board Risk Committee ensures that a robust assessment of the emerging and principal operational risks, including arising risks, facing the Company has been undertaken by the Group Executive, and reviews and monitors the mitigation of those risks.

Business unit, Sector and functional teams are responsible for day to day management and reporting of risks. They identify new and emerging risks, escalate where appropriate, and take action to manage risks as required.

Internal Audit provides independent and objective assurance on the adequacy and effectiveness of our risk management and internal control processes. It executes a range of risk audits across the Group.

Assessment of principal operational risks and the Group's appetite for risk

The risk data that is identified throughout the business is aggregated and analysed in order to identify the principal operational risks and uncertainties that affect the Group. The Principal Risks, which have been detailed on pages 36 to 41, represent the highest level of risk data that is used as a part of the risk management process. Each of the Principal Risks has an identified owner and a set of controls and actions that have been put in place in order to effectively mitigate them.

As part of its activities during 2018, the Board Risk Committee has also considered the capacity of the Group to accept any significant additional risks, over and above those that are either inherent to the markets in which the Group operates or those that relate to the historic activities of the Group. The Committee's assessment has been that the capacity of the Group to accept additional risk is constrained in a number of areas, and as a result, the mitigation and ultimately the retirement of these risk items remains an operational priority of the Group. As risks are retired, it is anticipated that capacity will be released which should allow the Group to accept additional risk in line with its long term appetite for risk, in support of its strategic objectives.

A handwritten signature in dark ink, appearing to read 'Mf Wareing', written in a cursive style.

Michael Wareing

Board Risk Committee Chair

7 March 2019

Remuneration outcomes reflect progress in delivering sustainable performance improvements



Alison Wood MA, MBA
Independent Non-executive Director

Committee members

John McAdam, Norton Schwartz

Number of meetings held in 2018

4 (December meeting postponed to January 2019)

Dear Shareholder

The Remuneration Committee has determined the outcome of remuneration decisions for the Executive Directors, along with how we intend to implement our Remuneration Policy in 2019. The Group has reported financial results in line with expectations. The Committee has been focused on ensuring that remuneration for our Executive Directors and senior management team is aligned with our turnaround strategy and outcomes are appropriately aligned with the overall performance of the Group. We have also considered the impact of the new remuneration provisions of the 2018 UK Corporate Governance Code and will be revisiting this area during the course of 2019.

How remuneration reflects Company performance

Based on an assessment of their financial and individual performance during the year, the CEO and CFO achieved a 2018 bonus award of 102.12% of salary, representing 68.08% of their maximum opportunity. Further details on the bonus performance measures are given on page 74. In considering performance against the financial targets, the Committee considered it appropriate to adjust targets under the 2018 Annual Incentive Plan (AIP) to reflect the divestment part way through the year of the AvComm and Wireless businesses. This ensured that performance was measured in an appropriate like for like basis with how the targets were set at the start of the year.

Determination of CEO buy-out award

As previously disclosed, under the terms of his appointment, David Lockwood received a buy-out for some of his outstanding long term incentive (LTI) awards and one deferred bonus award. The buy-out in respect of his 2016 LTI was replaced by an equivalent award of Cobham shares which would only vest subject to stretching EPS targets. This is subject to a two year holding period post-vesting. We have determined that this award will vest at 54.54% on

8 March 2019. In considering the performance under this award, we adjusted the underlying EPS targets and actuals for the divestment of the AvComm and Wireless businesses, including debt repayment, during the performance period, in order to ensure the actuals and targets were set on a like for like basis. The deferred bonus buy-out award vested in full with no performance conditions attached, as was the original award. See page 75 for details.

2019 remuneration framework

Shareholders approved a new Remuneration Policy at our AGM in April 2017. During the year, the Committee considered whether to bring forward the review of our Remuneration Policy but deemed this unnecessary to ensure alignment with the Company's strategic direction. Substantial changes are not proposed to the overall remuneration framework for the Executive Directors, which is considered to remain fit for purpose. The outcome of the 2019 salary review is a 2% increase, in line with the salary increase for the wider workforce. The 2019 AIP opportunity will remain the same at 150% of base salary for maximum achievement. Targets will be underlying operating profit, operating cash flow and key individual goals. The 2019 LTI will be awarded at 200% of base salary for the CEO, and 150% for the CFO. See page 80 for further detail.

Key issues to be addressed by the Committee in 2019

Ahead of our policy renewal at the 2020 AGM, we intend to undertake a detailed review of our current arrangements. We will review whether the current framework continues to be aligned with our return to growth strategy and drives the right behaviours. Also from a Code perspective, the review will specifically consider:

- Post-employment share ownership requirements;
- Executive Director retirement benefit arrangements; and
- Wider workforce remuneration policies and practice.

We have updated our terms of reference and work schedule to address some of the 2018 Code requirements, including our expanded remit as a Committee.

Non-executive Director fee review

After a period of 11 years without an increase in fee, the Chairman and the Executive Directors reviewed our fees against market practice and agreed to simplify our fee framework, in addition to implementing a modest increase to reflect the time commitment expected, and responsibilities of our Non-executive Directors. The Chairman's fee remains unchanged. See page 76.

Conclusion

Throughout 2018, we have sought to ensure that we exercise rigour and discipline in all remuneration decisions. In setting the 2019 AIP and LTI targets, we have reflected where we are in the turnaround and have set appropriately stretching targets for earnings and cash flow which are aligned to the delivery of sustainable margin improvement.

Alison Wood
Remuneration Committee Chair
7 March 2019

Corporate Governance — Directors' Remuneration Report continued

Our remuneration structure

Introduction

The Directors' Remuneration Policy (the Policy) set out below was approved by over 93% of our shareholders at our AGM held on 27 April 2017. The full Policy is available on the Company's website. As context for the rest of this report, the main elements of the Policy, as well as how the Policy was implemented during the year, are summarised below:

	Key elements	Key features	How it was implemented in 2018	How it will be implemented in 2019
Fixed pay	Base salary	Reviewed annually with changes effective from 1 March. Maximum salary increases typically in line with the outcomes of the annual review and typically in line with the average increase for the wider workforce.	No increase was made to the CEO's or CFO's base salary in 2018.	A 2% base salary increase, in line with the salary increase for the wider workforce, will be effective from 1 March 2019.
	Retirement benefits	The Company may make a payment into a pension scheme and/or make a cash allowance payment set as a percentage of salary.	For 2018, the CEO was paid cash in lieu of 25% and the CFO, 20%.	No change for 2019.
Annual Incentive The Annual Incentive Plan (AIP) is designed to drive and reward annual performance against financial and operational KPIs as well as individual objectives, which are directly linked to the Group's strategic plan.	Cash bonus	Maximum opportunity under the Policy is 150% of salary. For target performance, 50% of maximum bonus opportunity will be received. Measured over a one year performance period based on a combination of financial and individual metrics. Malus and clawback provisions are in place.	2018 awards: Payments of £704,630 and £531,027 have been earned by the CEO and CFO respectively. These payments amount to 102.12% of salary representing 68.08% of their maximum opportunity.	No change for 2019.
	Deferred bonus	25% of any cash award is mandatorily deferred into Company shares for a period of three years. Malus and clawback provisions are in place.	25% of each of the CEO's and CFO's AIP has been deferred into shares with a three year holding period.	No change for 2019.
Long term Incentive LTI – the Performance Share Plans (PSP) are designed to drive sustainable profitable growth and align Executive Directors' interests with shareholders' interests.	LTI – PSP	PSP allows for conditional share awards or nil-cost options up to 200% of base salary to be granted annually. Threshold level of vesting is 16.7% of maximum award. Performance assessed over more than one year, usually three years against key financial metrics. Awards are subject to a two year holding period post the end of the three year performance period. Malus and clawback provisions are in place.	Award of 200% of salary for the CEO. Award of 150% for the CFO.	Award of 200% of salary for the CEO and 150% for the CFO will be made in 2019 with performance conditions based on underlying EPS growth and cumulative free cash flow (50/50). Performance conditions are set out on page 80.
	Share Ownership Guidelines	There is a requirement to retain a percentage of salary in Company shares, which must be built up from shares vesting from executive incentive plans.	The CEO is required to build up and retain 200% of annual salary, and the CFO, 100%.	No change for 2019.
All employee share schemes	Save as You Earn/Share Incentive Plan	Both of these plans are available to all UK employees, including both the CEO and CFO on the same basis as all other employees.	Both CEO and CFO have invested in the 2017 Save as You Earn offer and commenced the Share Incentive Plan in October 2018, to the maximum allowable under each plan.	No change for 2019.

Aligning remuneration to deliver operational performance

We have taken a disciplined approach to ensure that our Policy supports Cobham's strategy and delivery of the long and short term operational and financial priorities. Our incentive framework underpins the delivery of sustainable growth in earnings and shareholder value together with the generation of free cash flow.

The annual report on remuneration

Both Executive Directors were in role throughout the year.

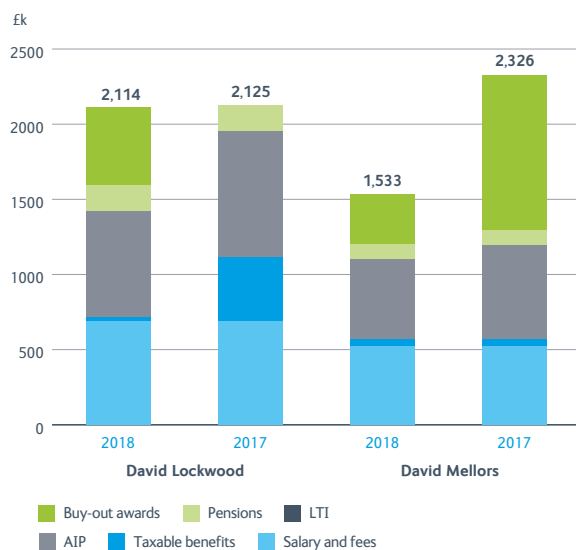
Single total figure table

£k		Salary and fees	Taxable benefits	AIP	LTI	Pensions	Buy-out awards	Total
David Lockwood	2018	690	24	705	—	173	522 ¹	2,114
	2017	690	422	840	—	173	—	2,125
David Mellors	2018	520	49	531	—	104	329 ²	1,533
	2017	520	50	621	—	104	1,031	2,326

1 The share price used to value these awards was the average mid-market share price for the last quarter of 2018, being 108.0p per share.

2 These awards vested 15 June 2018 at 126.3p per share.

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



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

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

Salary and fees

2018 Approved Policy:

Reviewed annually with changes effective from 1 March. Maximum salary increases typically in line with the outcomes of the annual review and in line with the average increase for the wider workforce.

David Lockwood receives a base salary of £690,000 and David Mellors receives a base salary of £520,000. Neither Director received an increase at the 1 March 2018 pay review.

Taxable benefits

The taxable benefit figures are as follows:

Benefit	David Lockwood £k	David Mellors £k
Car and private petrol allowance	16	17
Private medical insurance	1	2
Life cover	3	11
Income protection	3	2
Allowance to cover financial/tax advice	1	2
Travel and subsistence support in lieu of relocation ¹	—	15
Total	24	49

1 On appointment, the Committee agreed to provide funding to support the CFO's costs of working from Wimborne as he was not in a position to relocate. The travel and subsistence allowance for the CFO will be reviewed by the Committee in 2020.

Annual Incentive Plan

2018 Approved Policy:

Cash bonus	Maximum opportunity under the Policy is 150% of salary. For target performance, 50% of maximum bonus opportunity will be received. Measured over a one year performance period based on a combination of financial and individual metrics. Malus and clawback provisions are in place.
Deferred bonus	25% of any cash award mandatorily deferred into Company shares for a period of three years. Malus and clawback provisions are in place.

Awards were subject to performance measures aligned to key financial and strategic objectives of the Company over the previous 12 months. Financial measures comprised 80% of the total bonus, while key individual goals comprised the remaining 20%.

Details of the AIP measures, weightings and targets as well as performance against each of the targets are provided in the table below:

Measure ¹	Weighting	Full Year Targets			Actual Performance	Payment as a % of maximum
		Threshold	Target	Maximum		
Group operating cash flow (£m)	40%	107.3	113.0	118.6	124.7	40.0%
Group organic revenue growth (%)	20%	0.0	2.5	5.0	(2.0)	0.0%
Underlying group operating profit (£m)	20%	189.5	199.5	209.5	200.1	10.6%
Financial measures total	80%	—	—	—	—	50.6%

¹ Performance and targets are measured based on 2018 budgeted foreign exchange rates.

The targets and actuals set out above were adjusted for the divestment of the AvComm and Wireless test and measurement businesses during the performance period, in order to ensure the targets were set on an equivalent like for like basis.

As a result of the actual performance in the table above, the business element of the AIP award achieved was 50.6% of the 80% available for this element.

Given the importance to support the near term transformation goals and emerging longer term strategy, the objectives below were applied to both the CEO and CFO. Both objectives were weighted equally.

- Develop a strategy and value proposition to grow the business successfully from 2019 onwards by end of Q2 2018;
- Design and deliver an integrated positive culture change which supports organisational excellence in people and performance;
 - Detailed succession and talent pipeline for Top 75 roles
 - Aligned compensation and benefits for Top 75 linked to high performance
 - Evidence of consistent motivating leadership communications

As a result of the personal elements of the AIP, the CEO and CFO both achieved 17.5% of the 20% available for this element.

The Committee discussed at length the personal contribution of the CEO and CFO progressing the turnaround in 2018. With this context in mind, the business and personal elements achieved 68.08% payout for both the CEO and CFO.

Reflecting on these outcomes, the Committee was satisfied that they were aligned with overall business and individual performance during 2018, and there was no need to apply discretion to the outcome.

The 2018 AIP framework supported our priorities of driving continuous improvement in operational excellence and programme execution with inclusion of operational KPIs and by directly targeting organic revenue growth, underlying operating profit and operating cash flow. In addition, individual objectives were set as part of the 2018 AIP to specifically address the strategic development of the Group's portfolio.

Long term incentives

2018 Approved Policy:

PSP allows for conditional share awards or nil-cost options. Up to 200% of base salary may be granted annually.
 Performance assessed over more than one year, usually three years, against key financial metrics.
 Threshold level of vesting is 16.7% of maximum award.
 A two year holding period post the end of the three year performance period is in place.
 Malus and clawback provisions are in place.

The LTI is designed to support the creation of long term growth and value for the Group, by aligning shareholder expectations with that of performance.

PSP awards vesting in 2018

No Executive Directors hold PSP awards under the 2016-2018 cycle.

Buy-out awards vesting

As disclosed on 15 June 2018, the buy-out award of 260,636 shares issued to the CFO, David Mellors, vested on 14 June 2018. 122,814 shares were sold to cover tax and other deductions due on the vest, with the remaining 137,822 shares retained as part of the CFO's share ownership requirement.

The buy-out award of 55,842 shares issued to David Lockwood will vest on 13 March 2019. There are no performance conditions attaching to this award, as it relates to deferred shares forfeited as a consequence of joining Cobham.

The buy-out award of 782,918 shares issued to David Lockwood, will vest on 8 March 2019. The Committee applied discretion to make adjustments to the underlying EPS targets and actuals for the divestments of the AvComm and Wireless test and measurement businesses, including debt repayment, to ensure that performance was measured on an equivalent like for like basis. This resulted in adjusted targets of 5.1p at threshold, 5.6p at target and 6.7p at maximum and an adjusted 2018 underlying EPS of 5.7p equating to just over target vesting level of 54.54%. For completeness, the unadjusted targets were 5.6p threshold, 6.1p at target and 7.3p at maximum. This results in 427,046 shares, which are subject to a two year holding period post-vesting. The total value of these two awards is shown in the single figure table for 2018 on page 73.

Long term incentives awarded during the financial year (audited information)

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

	David Lockwood	David Mellors
Type of award	PSP	PSP
Basis on which award is made	200% of base salary	150% of base salary
Date of award	16 May 2018	16 May 2018
Face value of award	£1,380,000	£780,000
Number of shares awarded	1,166,361	659,247
Performance period	1 January 2018 to 31 December 2020	1 January 2018 to 31 December 2020
	A further two year holding period is applicable	A further two year holding period is applicable

- The award has been made in accordance with the relevant plan rules.
- The face value has been calculated by multiplying the number of shares awarded by the mid-market price of those shares for the three trading days immediately preceding the date of the award, being 118.1p.

Performance conditions for the PSP awarded in 2018 are set out in the table below:

Metric	Weighting %	Performance	Award vesting at
Free cash flow	50	Threshold	16.7
		Mid-point	50
		Maximum	100
EPS	50	Threshold	16.7
		Mid-point	50
		Maximum	100

At this stage the Committee considers that the actual targets remain commercially sensitive, but full disclosure will be provided at the end of the performance period.

As a result of the 2017 AIP, 25% of the cash awards made to the CEO and CFO were deferred into shares with a three year holding period, resulting in 89,538 shares being awarded to the CEO, David Lockwood, and 66,230 shares being awarded to the CFO, David Mellors. The resulting shares form part of the shares held against each of the Directors' share ownership requirement.

Retirement benefits

2018 Approved Policy:

The Company may make a payment into a pension scheme (e.g. a defined contribution plan) and/or make a cash allowance payment set as a percentage of salary.

David Lockwood's pension contributions are paid as a cash in lieu amount, which equates to 25% of his base salary. The amount paid during 2018 was £172,500. David Mellors' pension contributions are paid as a cash in lieu amount, which equates to 20% of his base salary. The amount paid during 2018 was £104,000.

Our UK employees may receive a maximum employer contribution of 12%, subject to their level of employee contribution. The UK senior management team has a range of employer contributions from 15 to 20%.

The Committee intends to review pension provision during 2019 as part of our response to the 2018 Code, and will provide further details in due course.

Non-executive Directors (audited information)

Changes to the Board membership during 2018 were the appointments of René Médori, Norton Schwartz and Marion Blakey as Non-executive Directors, and the retirement of Michael Hagee, Birgit Nørgaard and Alan Semple who stepped down as Non-executive Directors following the AGM in April 2018.

The 2018 remuneration of the Non-executive Directors, including the Chairman, are stated below:

£k	Total payable	
	2018	2017
Michael Wareing (Chairman) ¹	216	270
John McAdam ²	109	28
Alison Wood	65	65
René Médori ³	63	–
Norton Schwartz ³	63	–
Marion Blakey ⁴	26	–
Michael Hagee ⁵	23	65
Birgit Nørgaard ⁵	18	58
Alan Semple ⁵	25	70
(David) Jonathan Flint ⁶	–	40
Total	608	596

1 The Chairman, Michael Wareing, received taxable benefits of £8,314 during the year related to reimbursed travel expenses to the Wimborne and London offices, which are considered to be his permanent places of work. He waived his Chairman's fee for three months, due to surgery and recuperation.

2 John McAdam joined the Board on 3 August 2017. He was paid a fee for three months relating to additional responsibilities undertaken in the Chairman's absence due to surgery and recuperation.

3 René Médori and Norton Schwartz joined the Board on 1 January 2018.

4 Marion Blakey joined the Board on 3 August 2018.

5 Michael Hagee, Birgit Nørgaard and Alan Semple stepped down from the Board following the 2018 AGM.

6 (David) Jonathan Flint retired from the Board on 3 August 2017.

Non-executive Directors do not have a permanent place of work specified in their service contract. All reasonable and properly incurred expenses claimed in performance of duties as Board members are reimbursed by the Company.

We have taken the opportunity to simplify our Non-executive Director fee structure. Since 2008, Non-executive Directors have been paid a base fee of £55,000, plus £2,500 per annum for committee membership. Directors travelling from the US were paid a travel allowance of £5,000 per annum. A £10,000 annual fee was paid to each of the Chair of the Audit and Remuneration Committees and to the Senior Independent Director. With effect from 1 October 2018, the Non-executive Directors' base fee was increased from £55,000 to £60,000 and the separate Committee membership fee has been removed. The £10,000 annual fee paid to each of the Chair of the Audit and Remuneration Committees and to the Senior Independent Director has been increased to £12,500. This simplifies the fee structure and recognises the refreshment and realignment of Board skills to match the complexity of the Group and the enhanced role of the Non-executive Directors, where some Board members sit on multiple Board committees. The revised fee structure is shown at the top of the next page for ease of reference:

	2018	Previous fee structure
Non-executive Director base fee	£60,000	£55,000
Audit and Remuneration Committee Chair & Senior Independent Director fee	£12,500	£10,000
Travel Allowance payable to Directors travelling from the US	£2,000 per trip	£5,000
Committee membership fee	Removed	£2,500

The fee payable to the Chairman was unchanged through 2018.

Total aggregate Directors' fees for the year, including the Executive Director fees as per the single figure table on page 73, amount to £4,255,000 (2017: £5,047,000).

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

The interests of the Directors and their families in ordinary shares were:

	2018	2017
Michael Wareing	60,500	60,500
John McAdam	5,000	5,000
Alison Wood	10,500	10,500
René Médori	5,000	N/A
Norton Schwartz	5,000	N/A
Marion Blakey	5,000	N/A
David Lockwood	134,540	44,578
David Mellors	278,534	74,058
Michael Hagee	N/A	10,500
Birgit Nørgaard	N/A	10,500
Alan Semple	N/A	10,500

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

Executive Directors' share interests

The interests of the Executive Directors in share awards or share options at 31 December 2018 are shown below:

	Award	Share awards subject to performance conditions	Share awards subject to continued employment	Unvested options subject to performance awards	All employee Save As You Earn plan
David Lockwood	PSP 2017	—	—	982,206	—
	PSP 2018	—	—	1,166,361	—
	PSP 2017 Buy-out	—	—	782,918	—
	PSP 2018 Buy-out ¹	—	—	55,842	—
	2017 Save As You Earn	—	—	—	27,272
Total		—	—	2,987,327	27,272
David Mellors	PSP 2017	—	—	555,160	—
	PSP 2018	—	—	659,247	—
	Restricted Share Plan Buy-out	—	123,499	—	—
	2017 Save As You Earn	—	—	—	27,272
Total		—	123,499	1,214,407	27,272

¹ A buy-out award was granted to the CEO David Lockwood on 16 May 2018, which represented the deferred share portion of his 2015 bonus forfeited on joining Cobham. The award had a face value of £66,017, resulting in 55,842 shares being awarded. This award will vest on 13 March 2019, on a comparable basis to those of his forfeited arrangements.

Corporate Governance — Directors' Remuneration Report

Share ownership requirements

2018 Approved Policy:

Executive Directors are required to retain a percentage of salary in shares, which must be built up from shares vesting from LTI plans.

Share ownership requirements apply to Executive Directors who are obliged to hold ordinary shares. These requirements state that the CEO is to retain the value of at least two years' salary, and the CFO is to retain the value of at least one year's salary. In addition, the CEO and CFO are to retain a minimum of 50% of net vested PSP shares until the relevant shareholding level is met. There is no time frame over which the requirements are to be met.

Percentage of salary held by Executive Directors in shares



Interests at 7 March 2019, being a date no more than one month prior to the date of the notice convening the AGM, were increased by investments in the Company's Share Incentive Plan, resulting in the shareholding of each of the CEO and CFO increasing by 276 shares.

The market price of the ordinary shares as at 31 December 2018 was 119.0p per share and the closing price range during the year was 97.4p to 136.4p.

Dilution

The Company's share schemes are currently funded through shares purchased in the market and have been since November 2010, prior to which they were funded through new issue shares. Funding of awards through new issue shares is subject to an overall dilution limit of 10% of issued share capital in any ten year period. Of this, 5% may be used in connection with the Company's discretionary share schemes. As of 31 December 2018, there were no shares which had been issued pursuant to awards made in the previous ten years in connection with all share schemes and discretionary schemes respectively.

Payments to past Directors and payment for loss of office (audited information)

Mr Nicholls, the previous CFO, had an outstanding payment of bonus which had been withheld pending the outcome of the FCA investigation. On receipt of the notice confirming the FCA had discontinued this investigation, this payment was made at the gross amount of £36,667.

There were no payments made to past Directors for loss of office during the year.

Historic CEO total remuneration

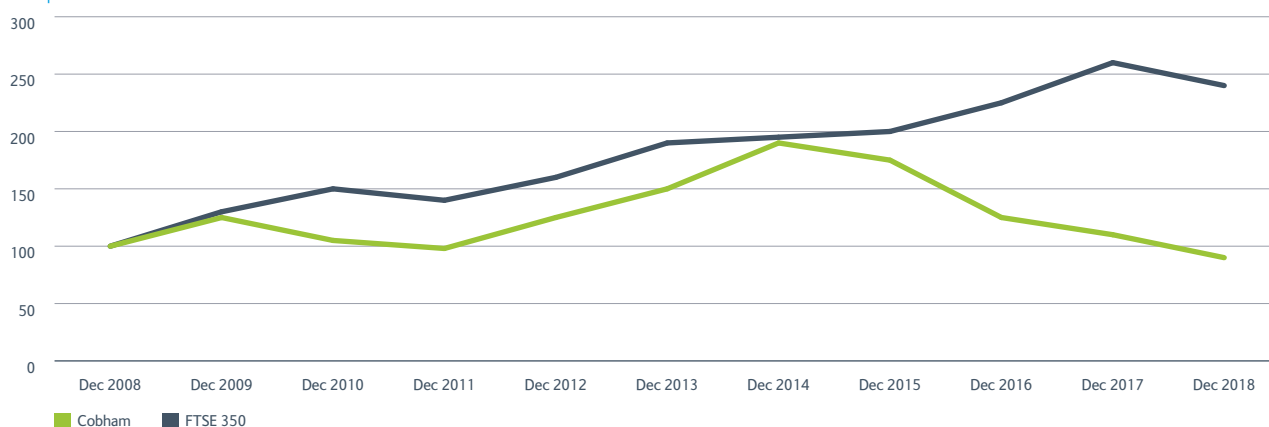
The table below shows historic CEO total remuneration, calculated on the same basis as that used in the single figure table on page 73.

Year	CEO	CEO single figure of total remuneration (£k)	Annual bonus payout against maximum opportunity % (£k)	Long term incentive vesting rates against maximum opportunity % (£k)
2018	CEO4 David Lockwood	2,114	68.1 (705)	N/A
2017	CEO4 David Lockwood	2,125	81.1 (840)	N/A
2016	CEO4 David Lockwood	60	Nil	N/A
2016	CEO3 Robert Murphy	1,518	Nil	N/A
2015	CEO3 Robert Murphy	1,364	18.4 (209)	N/A
2014	CEO3 Robert Murphy	1,196	Nil	N/A
2013	CEO3 Robert Murphy	2,058	34.3 (280)	N/A
2012	CEO3 Robert Murphy	753	48.5 (182)	N/A
2012	CEO2 Andrew Stevens	1,283	45.0 (267)	58.0 (202)
2011	CEO2 Andrew Stevens	1,916	92.5 (555)	85.0 (546)
2010	CEO2 Andrew Stevens	1,478	33.5 (201)	87.0 (471)
2009	CEO1 Allan Cook	1,496	93.0 (567)	100.0 (238)

Performance graph

The graph below illustrates the Total Shareholder Return (TSR) performance (share price growth plus dividends) of Cobham against the FTSE 350 Index over the past nine years.

TSR performance Cobham vs FTSE 350



The graph shows the value of £100 invested over the nine year period ending 31 December 2018. The FTSE 350 Index was chosen as it is a recognised broad equity market index of which Cobham was a member during 2018 and is currently, as at 7 March 2019, ranked at 137th.

Percentage change in remuneration of CEO

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

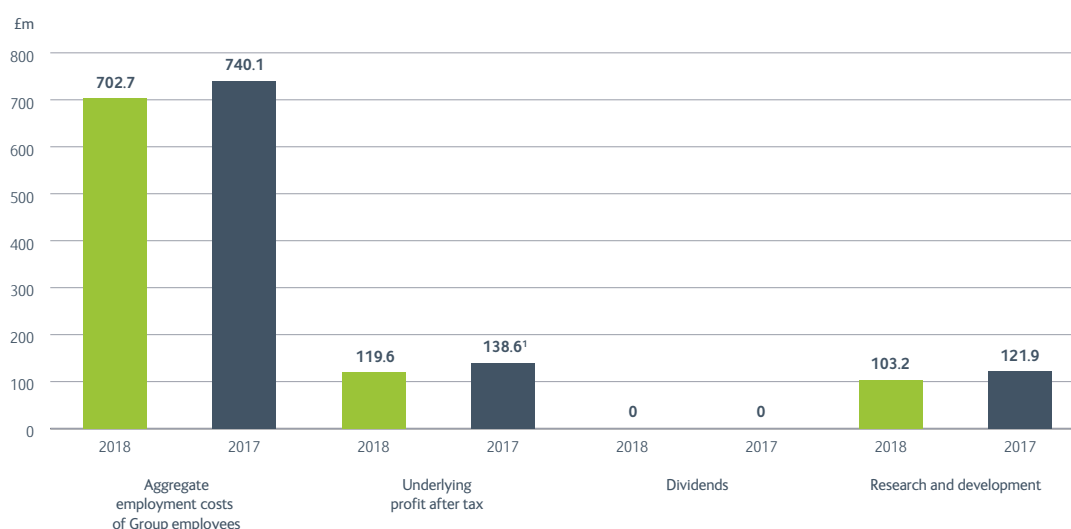
Remuneration element	CEO	Average employee per capita figure
Salary	2%	2%
Benefits	(94)%	(28)%
AIP	68%	13%

The UK payroll has been chosen for comparison as this is the location of the head office.

The large year on year benefits reduction relating to the average employee per capita figure can be attributed to better cost control and purchasing efficiency gains from benefit providers.

Relative importance of spend on pay

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



¹ This figure has been restated

The aggregate employment cost of Group employees is detailed at note 5 to the Group Financial Statements and includes employers' social security and similar costs. Group underlying profit after tax is shown above as this is the measure used by the Board to monitor financial performance, refer to note 3. No dividends have been paid in the year, refer to note 8. For research and development, refer to note 5.

Corporate Governance — Directors' Remuneration Report

Statement of implementation of remuneration policy in 2019

Base salary

The base salaries of the CEO and CFO have been reviewed and increased by 2%, resulting in a 2019 base salary of £703,800 for the CEO, and £530,400 for the CFO. This percentage increase is in line with increases awarded to the wider workforce. There was no salary increase in 2018.

Benefits

The CEO and CFO will continue to receive benefits in line with those provided for under the Remuneration Policy.

Retirement benefits

The pension contributions for the CEO and CFO are paid as a cash in lieu amount, which equate to 25% of salary for the CEO and 20% of salary for the CFO, both of which are below the 30% maximum set under the Remuneration Policy. These amounts are unchanged from 2018. The Committee intends to review pension provision during 2019 as part of our response to the 2018 Code.

2019 AIP

The maximum opportunities for the CEO and CFO will remain unchanged at 150% of base salary. The key financial metrics for the 2019 award have been amended by the removal of organic revenue growth, with underlying operating profit and operating cash flow remaining.

2019 PSP awards

PSP awards will be made to the CEO and CFO with a face value of 200% of salary and 150% of salary respectively, and will be subject to an additional two year holding period following the end of the performance period. The metrics remain unchanged at 50% underlying EPS and 50% free cash flow. The targets for underlying EPS in 2021 will be threshold vesting at 16.7% with a target of 8.2 pence and maximum vesting at 100% of 9.0 pence. The free cash flow targets are considered to be commercially sensitive at this stage and will be disclosed at the end of the performance period.

Advisors to the Remuneration Committee

Advisor	Appointed by	Services provided to the Committee	Other services provided to the Company
Deloitte LLP	Remuneration Committee in November 2009, and reappointed following a tender exercise conducted in 2016	Remuneration strategy Incentive design Market data	Immigration, international mobility and tax advice Corporate tax advice

The Committee received advice during the year from Deloitte LLP, who comply with the Code of Conduct of the Remuneration Consultants Group. Deloitte's performance was considered by the Committee as part of the tender process undertaken in 2016. The Committee is satisfied that the advice they have received has been objective and independent. Total fees for advice provided to the Committee during the year amounted to £43,718 (2017: £64,933) and were provided on a time/cost basis. Additional advice was received from the Executive Vice President Human Resources and Communications, Senior Vice President Compensation and Benefits, and Company Secretary.

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

2018 voting at the Annual General Meeting

At the AGM held on 26 April 2018, shareholders voted on the Directors' Remuneration Report for the year ended 31 December 2017. The votes 'for' include discretionary votes given to the Chairman of the Board. The Director's Remuneration Policy was approved by shareholders at the AGM held on 27 April 2017. Below are the results in respect of these resolutions.

Directors' Remuneration Report

Votes for	%	Votes against	%
51,634,096	98.23	929,355	1.77

Votes withheld: 10,616

Directors' Remuneration Policy

Votes for	%	Votes against	%
32,316,198	93.62	2,200,906	6.38

Votes withheld: 2,542

Corporate Governance — Other Statutory Information (Directors' Report)

Dividends

As previously communicated to the market, no dividend will be declared with the 2018 results. The Board has agreed a capital allocation policy, which, based on expectations for 2019, may result in an interim dividend being declared with the 2019 interim results.

Directors' indemnity arrangements

The Directors have the benefit of a Directors' and Officers' liability insurance policy and the Company has entered into qualifying third party indemnity arrangements with them, as permitted by the Companies Act 2006. The policy was in force through 2018, at the year end and continues in force at the date of this report. The Directors are permitted to take independent legal advice at the Company's expense within set limits in furtherance of their duties.

Directors' interests

None of the Directors are or were materially interested in any significant contract during or at the end of the financial year, particulars of which are required to be disclosed by the Listing Rules of the UK Listing Authority. Details of Directors' share interests and of their rights to subscribe for shares are shown in the Directors' Remuneration Report on page 77.

Share capital

The Company has one class of ordinary shares with a nominal value of 2.5 pence, which carry no right to fixed income, representing 99.9% of the total issued share capital.

In addition, 19,700 non-redeemable 6% second cumulative preference shares with a nominal value of £1 have been issued, which represent 0.1% of the total issued share capital.

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

At the AGM held on 26 April 2018, the Company was authorised to purchase up to 239,100,939 ordinary shares. This authority will expire at the conclusion of the 2019 AGM. A special resolution will be put to shareholders at the 2019 AGM to renew the authority to make market purchases of the Company's shares up to a maximum of 10% of the share capital of the Company.

The Directors have been authorised to allot and issue ordinary shares. These powers are exercised under the authority of resolutions passed at the Company's AGM.

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

Voting rights and restrictions on transfer of shares

The rights and obligations attaching to the ordinary shares and 6% second cumulative preference shares in the capital of the Company are set out in the Articles. On a show of hands at a general meeting of the Company, every holder of shares present in person or by proxy and entitled to vote has one vote, and on a poll every member present in person or by proxy and entitled to vote has one vote for every £1 in nominal value of the shares of which they are the holder. None of the ordinary or preference shares carry any special rights with regard to control of the Company.

There are no restrictions on transfers of shares other than:

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

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

Significant arrangements – change of control

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

- The Company has entered into a number of credit agreements with banks, and has issued senior notes under private placements. The total amount owing under such agreements at the year end date is shown in note 19 to the Group Financial Statements. Borrowing agreements contain clauses that in the event of a change of control require the Company to notify lenders of the change of control and either simultaneously offer to prepay all outstanding amounts or repay all outstanding amounts if the lenders so require. Both the offer to prepay and obligation to repay on request are subject to time limits;
- Under the Sentinel contract, entered into in March 2006, Surveillance Australia Pty Ltd (SAPL), a subsidiary of the Company, must seek approval for any material change in the shareholding of SAPL. There is an ancillary aircraft lease agreement under which a change of control may result in the termination of the lease if such event is likely to have a material adverse effect on SAPL's ability to perform its obligations under the lease;
- Under the Future Strategic Tanker Aircraft (FSTA) agreement entered into in June 2008, a change of control of the Company may result in a required sale of the Company's shares in FSTA to the other shareholders;
- Under the Australian Maritime Safety Authority (AMSA) contract for Dedicated Airborne Search and Rescue Services entered into in October 2014, a default of contract occurs where there is a change of control of Cobham SAR Services Pty Limited. AMSA's termination right is not automatic;
- Under contracts with Airbus for the supply of radio and audio integrated management systems, and satellite communications systems, both announced in June 2016, if a change in control reasonably appears to the purchaser to materially affect the ability of the supplier to discharge its obligations under the contract or if such change in control is in favour of a party which is strategically unacceptable to the purchaser because of

Corporate Governance — Other Statutory Information (Directors' Report) continued

existing, latent or potential conflict of interest, the purchaser shall be entitled to terminate the contract and any order in connection therewith; and

- Under the Qantas B717 Master Operating Agreement, entered into in June 2016, a default occurs where there is any change in the direct or indirect beneficial ownership or control of National Jet Systems Pty Limited, or a change of control without prior consent of Cobham Aviation Services Australia Pty Ltd.

Employee share schemes – rights of control

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

The trustee will not vote in respect of any shares held in the SIP in respect of which it has received no directions nor will the trustee vote in respect of any shares which are unallocated under the SIP. The trustees of the Employee Benefit Trust, which holds ordinary shares to be used for settlement of long term incentives and share option schemes, waive all rights to vote in respect of any shares they hold within the Trust.

Further information relating to change of control under the LTI arrangements appears within the Remuneration Policy available on the Company's website.

Major interests in shares

During 2018, the Company had been notified of the following interests in the ordinary shares:

	Number of shares at the date of notification	Percentage at date of notification
Silchester International Investors LLP	286,944,859	12.00
Lancaster Investment Management LLP	72,405,653	3.02
Causeway Capital Management LLC	191,536,103	8.01
Newton Investment Management Limited	118,797,152	4.97
Ameriprise Financial, Inc. and its Group	263,985,081	11.04
BlackRock, Inc.	Not reported	Below 5%

Since the year end and up to 7 March 2019, being a date not more than a month prior to the date of the AGM Notice, the Company had been notified of the following interests in the ordinary shares in accordance with DTR 5:

	Number of shares at the date of notification	Percentage at date of notification
Lancaster Investment Management LLP	70,721,288	2.95
Silchester International Investors LLP	286,659,138	11.99

Financial instruments

Notes 14, 22, and 24 to the Group Financial Statements and note 13 to the Parent Company Financial Statements contain disclosures relating to the use of financial instruments. The Group uses derivative financial instruments in its management of financial risks and does not trade in financial instruments or use complex financial instruments.

People

Please refer to pages 44 and 45 for details of the social dimension of our CR&S initiatives as they relate to our people, particularly in relation to diversity and inclusion, employee health and safety, and human rights.

Cobham is committed to providing all its employees with equal opportunities in a workplace free from discrimination. Applications for employment from persons with a disability are welcomed and given full and fair consideration. With regard to employees who become disabled during their employment, the Company takes all reasonable steps, including retraining, to enable them to continue their employment and career development within Cobham.

The Company maintains an independent Ethics Helpline: further details are on page 44.

Please refer to page 61, which identifies how we provide employees with information on matters which may concern them and how we consult with them, and which provides details of the Company's performance.

We offer Save As You Earn and Share Incentive Plans to all UK employees. The widening of the offer of employee share plans in other countries where we have large numbers of employees, is under consideration.

Research and development

The Group continues to invest in the important area of research and development; further details can be found in note 5 on page 113. During the year, the Group expended £103.2m (2017: £121.9m) on non-customer funded research and development.

Events after the balance sheet date

On 19 February 2019, Cobham announced that it had reached an agreement with Boeing on damages assertions, relating to the KC-46 programme. See note 3 on page 107 and note 32 on page 147.

Political donations and expenditure

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

Greenhouse gas emissions

The majority of Cobham's greenhouse gas (GHG) emissions come from aviation activity. There was an overall decrease in GHG emissions from aviation in 2018, due to a decrease in training and testing activities in CAVS UK. There has also been a significant decrease in electricity usage for the Group this year, due to the divestment of the AvComm and Wireless test and measurement businesses, as well as some energy efficiency initiatives, such as the installation of LED lightbulbs in the Davenport site.

Please note that the proportion of aviation fuel use and subsequent emissions in Scope 1 vs Scope 3 does not correlate directly to the figures presented in the 2017 report; this is because a certain number of flights in CAVS Australia which had previously been classified as producing Scope 3 emissions are now being redefined by the business as Scope 1 (see definitions below), and these flights have been reclassified retrospectively.

Definitions

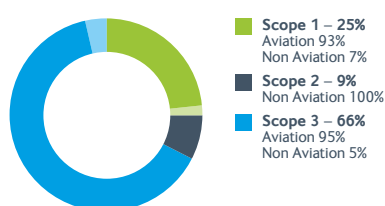
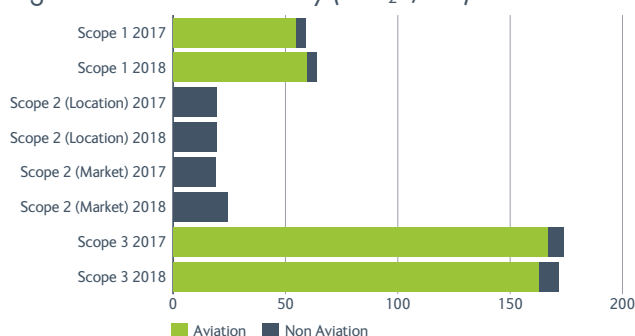
Scope 1 comprises direct emissions from Cobham owned and controlled plant and equipment, including: some aviation fuel, natural gas, heating oil, non-automotive diesel, fugitive emissions, solvent emissions and automotive fuel.

Scope 2 comprises indirect emissions from purchased renewable and non-renewable electricity using a location based or market based calculation method, and indirect emissions from purchased district heating.

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

Figure 1: 2018 GHG emissions (tCO₂e %)

Scope	Year	Aviation	Aviation %	Non Aviation	Non Aviation %	% Total change
Scope 1	2018	110,659	93.02	8,298	6.98	(3.00)
	2017	114,322	92.98	8,632	7.02	
Scope 2 (market)	2018	–	–	45,521	100.00	15.70
	2017	–	–	39,345	100.00	
Scope 2 (location)	2018	–	–	35,927	100.00	(11.00)
	2017	–	–	40,540	100.00	
Scope 3	2018	303,289	94.75	16,798	5.25	(12.00)
	2017	348,488	95.70	15,666	4.30	
Total	2018	413,949	85.43	70,617	14.57	(8.00)
	2017	462,810	87.91	63,643	12.09	

Figure 2: 2018 GHG emissions (tCO₂e%)Figure 3: Emissions intensity (tCO₂e/£m)Figure 4: 2018 Emissions intensity (tCO₂e/£m)

Scope	Year	Aviation tCO ₂ e/£m	Non Aviation tCO ₂ e/£m	Total tCO ₂ e/£m	% Total change
Scope 1	2018	59.39	4.45	63.84	8.60
	2017	54.66	4.13	58.79	
Scope 2 (location)	2018	–	19.28	19.28	(0.52)
	2017	–	19.38	19.38	
Scope 2 (market)	2018	–	24.43	24.43	29.87
	2017	–	18.81	18.81	
Scope 3	2018	162.77	9.02	171.78	(1.33)
	2017	166.62	7.49	174.11	

Figure 5: 2018 Energy usage (GWh)

Scope	Year	Aviation (GWh)	Aviation %	Non Aviation (GWh)	Non Aviation %	% Total change
Scope 1	2018	467.29	91.83	41.60	8.17	(2.78)
	2017	482.32	92.15	41.10	7.85	
Scope 2	2018	–	–	97.97	100.00	(7.97)
	2017	–	–	106.46	100.00	
Total	2018	467.29	77.00	139.57	23.00	(3.65)
	2017	482.32	76.57	147.55	23.43	

Energy usage

Under the new Streamlined Carbon Reporting framework, set to be put before Parliament this year, Cobham has begun reporting global energy use across all sources for Scope 1 and Scope 2 energy consumption. To compile this data, we have used the same boundaries and exclusions as we do for our GHG reporting, including the categorisation of some aircraft fuel from Scope 3 to Scope 1 in 2018.

Environmental initiatives

During 2018, Cobham signed off a new GHG target for the Group using science based methodology. This new target is to reduce total facility GHG emissions by 15% by the end of 2022, compared to 2016 emissions.

Cobham undertook a number of energy efficiency initiatives during 2018, the effects of which are starting to be seen and will continue to deliver results in 2019. As an example, we have put various efficiency measures in place at our Davenport site. These include: upgrading to LED lighting, replacing old cooling towers with a new, more energy efficient one and removing HVAC units. We have also implemented diesel-saving initiatives for our airline tractors in CAVS Australia through fuel-efficient driving. We successfully reduced natural gas usage at our Annemasse site, and are incorporating energy efficiency improvements into the renovation of the six buildings at our San Diego campus.

Methodology and data verification

The Group collects GHG emission data annually from its wholly owned operational subsidiaries. Cobham uses the following standards to report its GHG emissions: the World Business Council for Sustainable Development; the World Resources Institute Greenhouse Gas Protocol method as of 31 December 2014; the GHG Protocol Scope 2 Guidance; the International Aerospace Environmental Group GHG Reporting Guidance for the Aerospace Industry; a supplement of the GHG Protocol; and the Carbon Disclosure Standards Board. Cobham defines its emissions boundary as those under its direct operational control.

Reported data excludes joint ventures not under the Group's operational control, sites with fewer than five people, sites leased to tenants, vacant properties awaiting disposal, and any non-reported data for business units that have been closed or divested during 2018.

Further information about reported data is provided at www.cobham.com/the-group/corporate-responsibility-and-sustainability

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

Data assurance

Bureau Veritas UK Limited has been engaged by Cobham to provide limited assurance over selected sustainability performance indicators for inclusion in its Annual Report and Accounts and website. This Assurance Statement applies to the related information included within the scope of work described below, for the period 1 January to 31 December 2018: energy usage; Scope 1 GHG emissions; Scope 2 GHG emissions (market and location).

On the basis of the methodology and activities described above, Bureau Veritas concludes that there is no evidence to suggest that the data presented here is not materially correct and a fair representation of the Group's GHG emissions and energy data. A full verification statement including methodology, limitations and exclusions and the reporting criteria can be found on the Group's website www.cobham.com/the-group/corporate-responsibility-and-sustainability/performance-data-policies/performance-data.

Compliance with Listing Rule 9.8.4R

The majority of the disclosures required under Listing Rule 9.8.4R are not applicable to the Company. The table below gives the location of information required to be included in the Annual Report and Accounts that are applicable.

Listing Rule	Information	Response
LR 9.8.4 (12)	Details of any arrangement under which a shareholder has waived or agreed to waive any dividends.	The trustees of the SIP and the Employee Benefit Trust have elected to waive dividends, except in circumstances where they may be holding shares beneficially owned by participants. Refer to page 82 for further details.
(13)	Details of any arrangement under which a shareholder has agreed to waive future dividends.	As noted above.

The Corporate Governance Compliance Statement on page 55; likely future developments in the business or its subsidiaries on pages 10 and 11; details of persons with a significant shareholding on page 63; and rules on appointment of directors on page 56 all form part of this Directors' Report and are incorporated by reference.

Annual General Meeting

The Company's AGM will be held at 2:00pm on Thursday, 25 April 2019 at the offices of J. P. Morgan Cazenove, 60 Victoria Embankment, London EC4Y 0JP.

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

By order of the Board



Lyn Colloff

Company Secretary

7 March 2019

Corporate Governance — Statement of Directors' Responsibility

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

Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors have prepared the Group Financial Statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and Parent Company Financial Statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising Financial Reporting Standard 101, Reduced Disclosure Framework (FRS 101), and applicable law). Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company, and of the profit or loss of the Group and the Parent Company for that period.

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

- Select suitable accounting policies and then apply them consistently;
- State whether applicable IFRS, as adopted by the EU have been followed for the Group Financial Statements, and United Kingdom Accounting Standards, comprising FRS 101, have been followed for the Parent Company Financial Statements, subject to any material departures disclosed and explained in the financial statements;
- Make judgements and accounting estimates that are reasonable and prudent; and
- Prepare the Group and Parent Company Financial Statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

They are also responsible for safeguarding the assets of the Group and Parent Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Parent Company and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation.

The Directors are responsible for the maintenance and integrity of the Parent Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' Responsibility Statement

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

Each of the Directors, whose names and functions are listed on pages 52 and 53, confirms that, to the best of their knowledge:

- The Group Financial Statements, which have been prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group;
- The Parent Company Financial Statements, which have been prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising Financial Reporting Standard 101, Reduced Disclosure Framework (FRS 101), and applicable law), give a true and fair view of the assets, liabilities, financial position and results of the Parent Company; and
- The Strategic Report includes a fair review of the development and performance of the business and the position of the Group and Parent Company, together with a description of the principal risks and uncertainties that the Group faces.

Directors' declaration in relation to relevant audit information

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

- So far as the Director is aware, there is no relevant audit information of which the Group's auditors were unaware; and
- They have taken all the 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 and Parent Company's auditors are aware of that information.

The Responsibility Statement was approved by the Board of Directors on 7 March 2019 and signed on its behalf by:



David Lockwood
Chief Executive Officer
7 March 2019



David Mellors
Chief Financial Officer
7 March 2019

Independent Auditors' Report to the members of Cobham plc

Report on the audit of the Financial Statements

Opinion

In our opinion:

- Cobham plc's Group Financial Statements and Parent Company Financial Statements (together, the Financial Statements) give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2018 and of the Group's profit and cash flows for the year then ended;
- the Group Financial Statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the Parent Company Financial Statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101, Reduced Disclosure Framework, and applicable law); and
- the Financial Statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation.

We have audited the Financial Statements, included within the Annual Report and Accounts (the Annual Report), which comprise: the Consolidated and Parent Company Balance Sheets as at 31 December 2018; the Consolidated Income Statement and Consolidated Statement of Comprehensive Income; the Consolidated Cash Flow Statement; the Consolidated and Parent Company Statements of Changes in Equity for the year then ended; and the Notes to the Financial Statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the Financial Statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the Group and Parent Company in accordance with the ethical requirements that are relevant to our audit of the Financial Statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Parent Company.

Other than those disclosed in note 5 to the Group Financial Statements, we have provided no non-audit services to the Group or the Parent Company in the period from 1 January 2018 to 31 December 2018.

Our audit approach

Overview

Materiality

- Overall Group materiality: £7.7m (2017: £8.7m), based on 5% of underlying profit before tax.
- Overall Parent Company materiality: £37.4m (2017: £39.7m), based on 1% of total assets. We applied a lower materiality of £5.0m to all line items, account balances and disclosures that were in scope for the audit of the Group Financial Statements.
- In response to the level of historical adjustments arising within inventory and contract balances, we have used a specific materiality level of £5.0m for these two areas.

Audit scope

- Cobham plc has 53 reporting units which fall into four reporting Sectors. Of the 53 reporting units, 17 were subject to a full scope audit due to their size.
- Specific audit procedures were performed on certain balances and transactions in respect of other operating units.
- We visited three of four overseas locations to directly supervise the work of component auditors. For each of the four locations in which work was performed by overseas teams, we reviewed the working papers and maintained regular dialogue throughout the audit process.

Key audit matters:

- Revenue and profit recognition on contracts (Group);
- Goodwill and acquired intangible asset impairment assessments (Group);
- Accounting for uncertain tax provisions (Group);
- Inventory provisioning (Group); and
- Carrying value of investments in subsidiaries (Parent).

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the Financial Statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

Capability of the audit in detecting irregularities, including fraud

Based on our understanding of the Group and its industry, we identified that the principal risks of non-compliance with laws and regulations related to the Special Security Agreement regulation for the Advanced Electronic Solutions Sector, being the most significant regulatory framework, the Pensions Regulator legislation and the UK and US tax legislation, and we considered the extent to which non-compliance might have a material effect on the Financial Statements. We also considered those laws and regulations that have a direct impact on the preparation of the Financial Statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the Financial Statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries to increase revenue or reduce expenditure, and management bias in accounting estimates. The Group engagement team shared this risk assessment with the component auditors so that they could include appropriate audit procedures in response to such risks in their work. Audit procedures performed by the Group engagement team and/or component auditors included:

- Discussions with management, internal audit and the Group's legal advisors, including consideration of known or suspected instances of non-compliance with laws and regulation and fraud;
- Assessment of matters reported on the Group's whistleblowing helpline and the results of management's investigation of such matters;
- Reviewing correspondence with and reports to relevant regulatory authorities;
- Challenging assumptions and judgements made by management in their significant accounting estimates, in particular in relation to impairment of goodwill and acquired intangible assets and the carrying value of investments in subsidiaries;
- Identifying and testing journal entries, in particular any journal entries posted with unusual account combinations or posted by senior management; and
- Incorporating elements of unpredictability into the audit procedures performed.

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the Financial Statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the Financial Statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the Financial Statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.

Independent Auditors' Report to the members of Cobham plc

continued

Key audit matter

Revenue and profit recognition on contracts (Group)

Refer to page 67 (Audit Committee Report – Programme watchlist and Revenue/contract accounting) and page 98 (Note 1 – Accounting policies and related information – Assumptions and estimation uncertainties – Revenue recognition, contract assets and liabilities and contract loss provisions).

For revenue arising from the sale of goods, we have specifically identified risks that revenue transactions recorded in the period prior to year end may not have been recognised in line with the relevant Incoterms, particularly given material transactions can arise during this period.

The Group also has a number of significant contracts that span more than one accounting period. These contracts are subject to a high level of scrutiny by management. In particular, we focused on complex development and production contracts including those on aerial refuelling programmes such as KC-46.

The nature of much of the contracting work done by the Group means that there are reasonably frequent contractual issues, variations and renegotiations that arise in the ordinary course of business, for which the resolution is uncertain. Costs incurred can significantly exceed amounts estimated at inception as a result of material enhancements to the specifications originally assumed under the contracts. For selected contracts, we focused on:

- The amount of revenue assumed as recoverable from customers, which is based on contractual entitlement but subject to commercial negotiation;
- The estimation of costs to complete the contract;
- Whether contracts with the same customer should be accounted for as separate or linked;
- The profit recognised on revenue in the year and if this is appropriate based on the work completed and expected contract outcome;
- Whether the associated contract assets held on the Balance Sheet are recoverable or whether a contract loss provision should be recorded; and
- Whether additional cost contingency meets the definition for recognition and measurement within the contract balances or as a provision.

The Financial Statements include a charge of £200m which is disclosed as non-underlying. There is no definition of 'underlying' or 'non underlying' within International Financial Reporting Standards, so judgement is required around the treatment of items within the Directors' definition. Consistency in identifying and disclosing items defined as, and to be excluded from, underlying operating profit is important to maintain comparability of results year on year.

How our audit addressed the key audit matter

We tested revenue transactions in the period before year end to establish whether they were recognised in the correct period, through agreement to external shipping evidence, shipping terms and authorised milestone documentation with customer acceptance where appropriate. No material misstatements were identified.

We assessed the basis of profit or loss recognition on the Group's significant contracts, together with whether it was appropriate to account for them as separate or linked contracts. We evaluated the accounting in the context of the Group accounting policies, contract terms and accounting standards and identified no material misstatements in this respect.

For significant new contracts, we read the key contract terms and, for ongoing contracts, we understood any change clauses or amendments agreed in the year, considering whether any areas were subject to interpretation or dispute. We looked at the track record of customer behaviour, and any relevant correspondence, in order to obtain evidence of how terms were being interpreted. We found the accounting, in all material respects, to be in accordance with our understanding of the customer arrangements in place.

We challenged the reasonableness of the assumptions behind estimated costs to complete by meeting with engineering staff to enquire about project estimates, checking the basis of overhead rates used and, on a sample basis, checking purchase orders for materials. We also inspected risk registers and the process by which risk was included within the cost to complete estimate. Where there was insufficient evidence, we reviewed management's assessment of the historical forecasting accuracy to understand if the estimate was supportable. No material differences were identified.

We agreed total contracted revenue to original signed customer contracts, approved change orders or to evidence of customer discussions and agreements. We evaluated the reasonableness of estimated revenue through a review of, and discussion about, commercial negotiations taking place with customers. No material exceptions were found.

We assessed the recoverability of the contract assets held by reference to agreements with customers regarding payment or billing profiles. No material exceptions were found.

We agreed contract loss provisions recorded through a combination of the procedures above in respect of the overall outcome anticipated on the contracts. No material exceptions were found.

We read the disclosures relating to key estimates and judgements in the Financial Statements and are satisfied that the disclosures made are appropriate.

We also tested the presentation of non-underlying costs by assessing whether the classification was in line with the Group's accounting policy for such items, as per page 107 of the Financial Statements. We have considered management's definition of 'exceptional' and whether it has been appropriately disclosed, given that it is a non-GAAP measure and relates to items that could be considered as part of ongoing trading. We did not identify any material issues arising from these procedures.

Key audit matter

Goodwill and acquired intangible asset impairment assessments (Group)
Refer to page 67 (Audit Committee Report – Impairment reviews), page 98 (Note 1 – Accounting policies and related information – Assumptions and estimation uncertainties – Impairment of goodwill and intangible assets) and pages 120 to 122 (Note 10 – Intangible assets).

Management conducts an annual impairment assessment to test whether the carrying value of goodwill and acquired intangible assets exceeds the present value of the cash flows of the Cash Generating Units (CGUs) to which it relates.

The impairment assessments used to support the carrying value of each CGU involves the application of subjective judgement about future business performance. We considered the key assumptions made by management within the impairment assessments to be key areas of judgement, including the future cash flow forecasts, the discount rates and the long term growth rates applied.

How our audit addressed the key audit matter

We evaluated management's cash flow forecasts relating to each of the four CGUs with goodwill balances and the process by which they were determined and approved. This included confirming that the forecasts were consistent with the latest Board approved budgets (and the estimates underpinning assessments in respect of going concern and the recoverability of deferred tax assets) and the mathematical accuracy of the underlying calculations, with no exceptions identified.

We assessed the methodology used and key assumptions made within the forecasts as follows:

- Future cash flow forecasts: we evaluated the reasonableness of future cash flow forecasts based on management's historic accuracy of forecasting and our knowledge of the businesses (and assessed whether the forecasts only included cash flows as allowed by IAS 36);
- Discount rates: to assess the discount rates used in the model, we used an internally developed range of acceptable discount rates for valuing CGUs, which is based on our view of economic indicators. Each of the discount rates used fell within the range expected for all territories; and
- Long term growth rates: we compared the rates applied in the model against our own internally developed rates. No inconsistencies were noted.

For each CGU, we performed sensitivity analysis around the key assumptions in order to ascertain the extent of change in those assumptions required individually or collectively to result in an impairment of goodwill or acquired intangible assets. For those CGUs which were most sensitive, we discussed the basis for the cash flows with senior management, obtaining corroboratory evidence where available, and concluded that no impairment was required.

Management's disclosure in note 10 of the Financial Statements includes sensitivities at a CGU level. This is compliant with IAS 36 which requires disclosure of possible changes in key assumptions prospectively, during the period in which the impairment assessment for goodwill and acquired intangible assets will be monitored.

Through review of the impairment assessment performed by management and the disclosures made, we did not identify any material misstatements.

Accounting for uncertain tax provisions (Group)

Refer to page 67 (Audit Committee Report – Uncertain tax positions and deferred tax), page 98 (Note 1 – Accounting policies and related information – Assumptions and estimation uncertainties – Uncertain tax positions and deferred tax assets), pages 114 to 117 (Note 7 – Taxation) and page 147 (Note 30 – Contingent liabilities).

The Group has a wide geographical footprint and is subject to tax laws in a number of jurisdictions. The Group has a number of open tax enquiries and has recognised a number of provisions against uncertain tax positions, the valuation of which is a highly judgemental area. Where tax positions have not yet been settled with the relevant tax authorities, the Directors consider a number of factors, including precedent, the current intentions of the Board to resolve these matters and, where necessary, the advice of external experts.

We discussed with management the known uncertain tax positions and read correspondence from tax authorities, management's tax advisors and external legal counsel on open tax enquiries, where relevant. We also reviewed Board minutes to corroborate that the accounting was consistent with the Directors' intended plan to resolve these enquiries.

We assessed the adequacy of the Directors' taxation provisions by considering factors such as the risk profile of each matter, management's appetite for settlement and whether the provision addresses possible penalties and interest.

We met with senior management and challenged the judgements made in relation to a range of outcomes in respect of open enquiries. We assessed the risk that the final determination made by the relevant tax authorities is materially different to the provisions recognised by comparing management's assessment against our own views based on all available evidence and our use of relevant specialists.

We reviewed the disclosures made in respect of tax, in particular around key estimation uncertainties, as well as contingent liabilities, and are satisfied that the disclosures made are appropriate.

Independent Auditors' Report to the members of Cobham plc

continued

Key audit matter

Inventory provisioning (Group)

Refer to page 67 (Audit Committee Report – Inventory provisions), page 98 (Note 1 – Accounting policies and related information – Assumptions and estimation uncertainties – Inventory provisions) and page 124 (Note 13 – Inventories).

The nature of the business performed by the Group means that some of the products held can become obsolete. There may be long lead times on the supply of materials which results in the holding of inventory to meet the required delivery dates of customers. There may also be instances where specialised inventory has been purchased in respect of contracts which have subsequently not been won, or have been delayed. It is also necessary to hold spare parts in order to support key customers and programmes should the products require replacement or servicing.

The Group has gross inventory of £363.8m and provisions for obsolescence of £87.8m on its Balance Sheet. The level of inventory held and its ageing profile remain an area of focus for management.

We have considered inventory provisioning due to the estimates involved in the calculations, which are often dependent on assumptions concerning future realisable value and usage. Furthermore, with the delay in some of the aforementioned programmes, inventory is becoming more aged and is at risk of being damaged or subject to a new level of conformity.

Carrying value of investments in subsidiaries (Parent)

Refer to page 67 (Audit Committee Report – Impairment reviews), page 153 (Note 1 – Parent Company accounting policies – Assumptions and estimation uncertainties – Carrying value of investments) and pages 156 to 157 (Note 6 – Investments in Group undertakings).

Determining whether the carrying value of investments is impaired requires management to make significant assumptions, including the forecast operating cash flows, discount rates and long term growth rates. This is highly judgemental and changes in these could result in a material change in the carrying value of investments.

The impairment assessment performed has resulted in an impairment charge of £273.8m being recognised in the Parent Company Balance Sheet, reducing the total investments in subsidiaries held to £3,231.3m.

How our audit addressed the key audit matter

We assessed the process, methods and assumptions used to develop the provision for excess, obsolete or slow moving items. This included ensuring the provision has been calculated in line with the relevant methodology, as well as assess the historical forecasting accuracy of management where forecast demands were used in the assessment. In situations where there was evidence that management forecasts had not been achieved, we assessed the sensitivity of the provision to the failure to meet future forecasts.

We also considered whether there was any indication of management bias, such as management overrides, to the established methodology. These overrides are typically applied in respect of spares held for the servicing of products on aircraft which have a long service life or where the business has purchased 'last time buys' for components which would no longer be available for purchase after a specific date. Where the overrides were material, we considered the appropriateness of management's judgements based on historical demand and future usage expectations. No material misstatements were identified.

We tested the mechanical accuracy of the impairment model used by management for Parent Company investments and also consistency with the model utilised for goodwill impairment within the Group Financial Statements.

We challenged management on the inputs into the impairment assessment calculations, including:

- assessing whether cash flow forecasts only include cash flows as allowed by IAS 36;
- assessing the key assumptions for sales growth used and agreeing these to the Board approved budget; and
- assessing the cash flows within the model including a reasonable allocation of Parent Company costs expected to be incurred in generating the future cash flows for each investment balance, and known subsequent events.

We assessed the appropriateness of the key sensitivities applied by management to the impairment model and whether the scenarios represented likely alternative outcomes from changes in key assumptions.

We reviewed whether disclosures are appropriately made, in accordance with the applicable accounting framework and are satisfied that these disclosures are appropriate.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the Financial Statements as a whole, taking into account the structure of the Group and the Parent Company, the accounting processes and controls, and the industry in which they operate.

Of the Group's 53 reporting units, we performed audits of complete financial information at 17 reporting units in the UK, Australia, Denmark and France. At five US reporting units, we performed audit procedures on certain balances and transactions rather than an audit of their complete financial information. In addition to the above, we performed analytical procedures on the remaining 31 reporting units to understand key balances and transactions in the year and performed additional procedures on any unusual balances identified.

The Group is structured along four reported Sectors, being Advanced Electronic Solutions, Aviation Services, Communications and Connectivity and Mission Systems. The Group Financial Statements are a consolidation of 53 reporting units within these Sectors, comprising the Group's operating businesses and centralised functions. The Advanced Electronic Solutions Sector operates under a Special Security Agreement (SSA), with this being required to carry out business with the US Department of Defence. The SSA places certain restrictions on access to, and communication of, information outside of US borders. We therefore planned our audit to ensure US personnel completed the audit work on the three reporting units affected by these restrictions. We maintained regular dialogue throughout the audit process with our US team, including a face to face meeting at the planning stage to communicate, discuss and agree the

audit plan. We also supervised the work performed through regular dialogue and a review of the US team's working papers following our interim procedures and at the year end and we agreed the format and content of the required communications. There are three reporting units within the SSA that were included in our audit scope. These reporting units were subject to directed scope procedures, providing reporting to us on specified financial statement line items including revenue, contract assets and cash, as well as specified procedures on other key areas such as manual journals and inventory provisioning. We also performed specific procedures relating to US taxation.

81% of the Group's revenue is accounted for by reporting units where we performed audits of their complete financial information or performed specific audit procedures over revenue. 62% of the Group's underlying profit before taxation is accounted for by the 17 reporting units where we performed audits of their complete financial information. In combination with the other work referred to above, together with additional procedures performed at a Group level, including testing of significant journals posted within the Sector and Group consolidations, as well as significant adjustments made to the Financial Statements, this gave us the evidence we needed for our opinion on the Financial Statements as a whole.

Where the work was performed by component audit teams, we determined the level of involvement we needed to have in the audit work at those reporting units to be able to conclude whether sufficient appropriate evidence had been obtained as a basis for our opinion on the Financial Statements as a whole. There are seven in scope reporting units for which the audit work was performed by overseas teams, with visits by members of the Group team made to the territories in which these are located (being Denmark, France and the US). We held briefing calls with all of our overseas teams prior to the commencement of the audit to discuss key areas of audit focus. We reviewed the working papers of our Australian team remotely at year end. We visited Denmark at the planning stage and met with both our audit team and local management, with a review of the working papers of our Danish audit team being performed remotely at year end. We visited France at year end to meet our audit team and perform a review of their working papers. As detailed above, we met with our US team twice, being a visit at the planning stage to discuss and agree the audit plan and a visit at year end to review their working papers. We also maintained regular dialogue with all component teams throughout the audit and attended clearance calls on all in scope components. In addition, members of the Group audit team led, or formed part of, a number of significant component teams on the audit, including the two key reporting units with the aerial refuelling development and production contracts.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the Financial Statements as a whole.

Based on our professional judgement, we determined materiality for the Financial Statements as a whole as follows:

Group Financial Statements	Parent Company Financial Statements
Overall materiality £7.7m (2017: £8.7m).	£37.4m (2017: £39.7m).
How we determined it Based on 5% of underlying profit before tax.	Based on 1% of total assets.
Rationale for benchmark applied Underlying profit before tax is defined in the Annual Report on page 107. We believe that underlying profit before tax represents an appropriate metric for assessing the performance of the Group and provides us with a consistent year on year basis for determining materiality. It is the amount reported by management both internally and externally to the market. We also considered our overall Group materiality in the context of the Group's revenue, noting that it represents less than 0.5%.	We believe that total assets is an appropriate metric for assessing the Parent Company as it holds the investments and financial instruments of the Group. We applied a lower materiality of £5.0m to all items, account balances and disclosures that were in scope for the audit of the Group Financial Statements.
In response to the level of historical adjustments raised within inventory and contract balances, we have used a specific materiality level of £5.0m for these two areas. This level of materiality was determined to reflect the level of historical adjustment for these balances in prior years and the continuing heightened risk of misstatement.	

For each component in the scope of our Group audit, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £1m and £5m. Certain components were audited to a local statutory audit materiality that was also less than our overall Group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £380,000 (Group audit) (2017: £200,000) and £380,000 (Parent Company audit) (2017: £200,000) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Independent Auditors' Report to the members of Cobham plc

continued

Going concern

In accordance with ISAs (UK) we report as follows:

Reporting obligation	Outcome
We are required to report if we have anything material to add or draw attention to in respect of the Directors' statement in the Financial Statements about whether the Directors considered it appropriate to adopt the going concern basis of accounting in preparing the Financial Statements and the Directors' identification of any material uncertainties to the Group's and the Parent Company's ability to continue as a going concern over a period of at least twelve months from the date of approval of the Financial Statements.	We have nothing material to add or to draw attention to. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's and Parent Company's ability to continue as a going concern. For example, the terms on which the United Kingdom may withdraw from the European Union, which is currently due to occur on 29 March 2019, are not clear, and it is difficult to evaluate all of the potential implications on the company's trade, customers, suppliers and the wider economy.
We are required to report if the Directors' statement relating to Going Concern in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.	We have nothing to report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the Financial Statements and our auditors' report thereon. The Directors are responsible for the other information. Our opinion on the Financial Statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the Financial Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Financial Statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the Financial Statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' Report, we also considered whether the disclosures required by the UK Companies Act 2006 (CA06), have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, CA06, ISAs (UK) and the Listing Rules of the Financial Conduct Authority (FCA) require us also to report certain opinions and matters as described below (required by ISAs (UK) unless otherwise stated).

Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 31 December 2018 is consistent with the Financial Statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the Group and Parent Company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report. (CA06)

The Directors' assessment of the prospects of the Group and of the principal risks that would threaten the solvency or liquidity of the Group

We have nothing material to add or draw attention to regarding:

- The Directors' confirmation on page 54 of the Annual Report that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.
- The disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.
- The Directors' explanation on page 35 of the Annual Report as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We have nothing to report having performed a review of the Directors' statement that they have carried out a robust assessment of the principal risks facing the Group and statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the UK Corporate Governance Code (the Code); and considering whether the statements are consistent with the knowledge and understanding of the Group and parent company and their environment obtained in the course of the audit. (Listing Rules)

Other Code Provisions

We have nothing to report in respect of our responsibility to report when:

- The statement given by the Directors, on page 54, that they consider the Annual Report taken as a whole to be fair, balanced and understandable, and provides the information necessary for the members to assess the Group's and Parent Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and Parent company obtained in the course of performing our audit.
- The section of the Annual Report on page 66 describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.
- The Directors' statement relating to the Parent Company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified, under the Listing Rules, for review by the auditors.

Directors' Remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006. (CA06)

Responsibilities for the Financial Statements and the audit

Responsibilities of the Directors for the Financial Statements

As explained more fully in the Statement of Directors' Responsibility set out on page 85, the Directors are responsible for the preparation of the Financial Statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The Directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the Financial Statements, the Directors are responsible for assessing the Group's and the Parent Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or the Parent Company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the Financial Statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Financial Statements.

A further description of our responsibilities for the audit of the Financial Statements is located on the FRC's website at:

www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

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

Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- the Parent Company Financial Statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the Audit Committee, we have been appointed by the Directors to audit the Financial Statements since at least the year ended 31 December 1973 and subsequent financial periods. The period of total uninterrupted engagement is at least 46 years, covering up to the year ended 31 December 2018.



Pauline Campbell (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

London

7 March 2019

Consolidated Income Statement

For the year ended 31 December 2018

£m	Note	2018	2017 (restated)
Revenue	4	1,863.3	2,091.6
Cost of sales		(1,539.9)	(1,494.8)
Gross profit		323.4	596.8
Operating costs		(438.5)	(491.0)
Profit on divestments	28	227.0	1.1
Operating profit		111.9	106.9
Finance income	6	10.5	6.1
Finance costs	6	(51.4)	(43.3)
Profit before taxation		71.0	69.7
Taxation	7	2.7	14.4
Profit after taxation for the year		73.7	84.1
Attributable to:			
Owners of the parent		73.5	83.9
Non-controlling interests		0.2	0.2
		73.7	84.1

Further details of the restatement of the 2017 Income Statement, due to the implementation of IFRS 15, Revenue from Contracts with Customers, can be found in note 2.

Earnings per ordinary share	3		
Basic		3.1p	3.7p
Diluted		3.1p	3.7p

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2018

£m	Note	2018	2017 (restated)
Profit after taxation for the year		73.7	84.1
Items that will not be reclassified subsequently to profit or loss			
Remeasurement of fair value of other financial assets	17	(5.6)	–
Remeasurement of defined benefit retirement benefit obligations	23	8.9	7.4
Actuarial loss on other retirement benefit obligations	23	(1.0)	–
Tax effects	7	(1.6)	(1.4)
		0.7	6.0
Items that may subsequently be reclassified to profit or loss			
Net translation differences on investments in overseas subsidiaries	26	57.2	(51.4)
Reclassification of foreign exchange on divestment of overseas operations	26	(15.8)	–
Reclassification of cash flow hedge fair values	26	(0.3)	0.5
Hedge accounted derivative financial instruments	26	(0.8)	0.9
Tax effects	7	(0.1)	(0.1)
		40.2	(50.1)
Other comprehensive income/(expense) for the year		40.9	(44.1)
Total comprehensive income for the year		114.6	40.0
Attributable to:			
Owners of the parent		114.4	39.8
Non-controlling interests		0.2	0.2
		114.6	40.0

Consolidated Balance Sheet

As at 31 December 2018

fm	Note	2018	2017 (restated)	1 January 2017 (restated)
Assets				
Non-current assets				
Intangible assets	10	821.2	893.8	1,165.9
Property, plant and equipment	11	388.2	380.9	422.9
Investment properties	12	2.3	2.4	3.6
Investments in joint ventures and associates		4.1	3.6	3.6
Contract assets	15	55.9	64.3	56.2
Trade and other receivables	16	28.4	28.5	33.2
Other financial assets	17	39.5	6.1	6.1
Deferred tax	7	89.8	58.8	43.9
Derivative financial instruments	22	23.0	25.0	19.7
		1,452.4	1,463.4	1,755.1
Current assets				
Inventories	13	276.0	254.2	284.0
Contract assets	15	131.0	125.9	116.8
Trade and other receivables	16	322.2	293.8	367.1
Current tax receivables	7	7.8	7.2	3.1
Derivative financial instruments	22	1.6	10.4	8.5
Cash and cash equivalents	19	406.9	451.9	236.2
Assets classified as held for sale	18	—	171.7	—
		1,145.5	1,315.1	1,015.7
Liabilities				
Current liabilities				
Borrowings	19	(58.6)	(0.1)	(60.9)
Contract liabilities	15	(180.9)	(105.2)	(104.3)
Trade and other payables	20	(376.7)	(347.8)	(351.5)
Provisions	21	(93.1)	(121.7)	(139.2)
Current tax liabilities	7	(136.7)	(135.8)	(141.6)
Derivative financial instruments	22	(16.4)	(12.2)	(42.2)
Liabilities associated with assets classified as held for sale	18	—	(49.1)	—
		(862.4)	(771.9)	(839.7)
Non-current liabilities				
Borrowings	19	(338.0)	(835.3)	(1,203.5)
Trade and other payables	20	(18.7)	(11.6)	(12.1)
Provisions	21	(107.6)	(30.6)	(73.0)
Deferred tax	7	(5.1)	(6.3)	(33.6)
Derivative financial instruments	22	(27.8)	(27.2)	(32.2)
Retirement benefit obligations	23	(46.6)	(63.2)	(87.0)
		(543.8)	(974.2)	(1,441.4)
Net assets		1,191.7	1,032.4	489.7
Equity				
Share capital	25	61.7	61.7	44.6
Share premium	25	1,257.9	1,257.9	778.3
Other reserves	26	32.3	(9.6)	37.9
Retained earnings		(161.7)	(278.9)	(372.2)
Total equity attributable to owners of the parent		1,190.2	1,031.1	488.6
Non-controlling interests in equity		1.5	1.3	1.1
Total equity		1,191.7	1,032.4	489.7

Further details of the restatement of the comparative Balance Sheets, due to the implementation of IFRS 15, Revenue from Contracts with Customers, can be found in note 2.

The financial statements on pages 94 to 150 were approved by a duly appointed and authorised committee of the Board on 7 March 2019 and signed on its behalf by:



David Lockwood
Directors



David Mellors

Consolidated Statement of Changes in Equity

For the year ended 31 December 2018

£m	Share capital	Share premium	Other reserves (note 26)	Retained earnings	Total attributable to owners of the parent	Non-controlling interests	Total equity
Total equity at 31 December 2017 (as originally stated)	61.7	1,257.9	(8.6)	(284.0)	1,027.0	1.3	1,028.3
Change in accounting policy – IFRS 15 (note 2)	–	–	(1.0)	5.1	4.1	–	4.1
Total equity at 31 December 2017 (restated)	61.7	1,257.9	(9.6)	(278.9)	1,031.1	1.3	1,032.4
Change in accounting policy – IFRS 9 (note 2)	–	–	–	39.0	39.0	–	39.0
Total equity at 1 January 2018	61.7	1,257.9	(9.6)	(239.9)	1,070.1	1.3	1,071.4
Profit for the year	–	–	–	73.5	73.5	0.2	73.7
Other comprehensive income	–	–	40.2	0.7	40.9	–	40.9
Total comprehensive income for the year	–	–	40.2	74.2	114.4	0.2	114.6
Share based payments (note 27)	–	–	5.8	–	5.8	–	5.8
Transfer of other reserves to retained earnings	–	–	(4.0)	4.0	–	–	–
Tax effects (note 7)	–	–	(0.1)	–	(0.1)	–	(0.1)
Total equity at 31 December 2018	61.7	1,257.9	32.3	(161.7)	1,190.2	1.5	1,191.7
Total equity at 1 January 2017 (as originally stated)	44.6	778.3	37.9	(372.0)	488.8	1.1	489.9
Change in accounting policy – IFRS 15 (note 2)	–	–	–	(0.2)	(0.2)	–	(0.2)
Total equity at 1 January 2017 (restated)	44.6	778.3	37.9	(372.2)	488.6	1.1	489.7
Profit for the year (restated)	–	–	–	83.9	83.9	0.2	84.1
Other comprehensive income/(expense) (restated)	–	–	(50.1)	6.0	(44.1)	–	(44.1)
Total comprehensive income/(expense) for the year (restated)	–	–	(50.1)	89.9	39.8	0.2	40.0
Issue of shares, net of costs (note 25)	17.1	479.6	–	–	496.7	–	496.7
Proceeds on allocation of treasury shares	–	–	–	0.5	0.5	–	0.5
Share based payments (note 27)	–	–	5.5	–	5.5	–	5.5
Transfer of other reserves to retained earnings	–	–	(2.9)	2.9	–	–	–
Total equity at 31 December 2017 (restated)	61.7	1,257.9	(9.6)	(278.9)	1,031.1	1.3	1,032.4

Consolidated Cash Flow Statement

For the year ended 31 December 2018

£m	Note	2018	2017
Cash generated from operations		186.1	282.3
Tax paid		(25.5)	(32.2)
Interest paid		(43.5)	(41.6)
Interest received		8.2	6.7
Net cash from operating activities	9	125.3	215.2
Cash flows from investing activities			
Purchase of property, plant and equipment		(63.4)	(69.0)
Purchase of intangible assets		(6.1)	(10.8)
Proceeds on disposal of property, plant and equipment and intangible assets		6.8	5.1
Acquisition of subsidiaries net of cash or debt acquired		—	(0.3)
Proceeds from/(costs of) business divestments		324.7	(0.5)
Net cash from/(used in) investing activities		262.0	(75.5)
Cash flows from financing activities			
Issue of share capital		—	496.7
Dividends paid to non-controlling interests	8	—	(0.1)
Proceeds on allocation of treasury shares		—	0.5
Repayment of borrowings	19	(470.3)	(359.6)
Net cash (used in)/from financing activities		(470.3)	137.5
Net (decrease)/increase in cash and cash equivalents		(83.0)	277.2
Exchange movements		27.8	(61.5)
Cash and cash equivalents at start of year		451.9	236.2
Cash and cash equivalents at end of year		396.7	451.9

Reconciliation of cash and cash equivalents and net cash/(debt)

£m	Note	2018	2017
Cash and cash equivalents per Cash Flow Statement		396.7	451.9
Bank overdrafts		10.2	—
Cash and cash equivalents per Balance Sheet		406.9	451.9
Borrowings – current liabilities	19	(58.6)	(0.1)
Borrowings – non-current liabilities	19	(338.0)	(835.3)
Net cash/(debt) at 31 December		10.3	(383.5)

A reconciliation of the movements in net cash/(debt) can be found in note 19.

Note 14 includes details of the offsetting of overdrafts with cash and cash equivalents and other financial instruments.

Notes to the Group Financial Statements

1. Accounting policies and related information

1.1 General information

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

1.2 Basis of preparation

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

These financial statements have been prepared on the going concern basis under the historical cost convention, unless otherwise stated.

1.3 Management judgement and estimation uncertainty

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

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

1.3.1 Significant judgements in applying accounting policies

The following are the judgements, apart from those involving estimations, that the Directors have made in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognised in the financial statements:

a. Consolidation of Cobham Advanced Electronic Solutions Sector

The Cobham Advanced Electronic Solutions Sector operates under an SSA with the US Government due to the nature of its work on classified US DoD programmes. The results of this Sector have been consolidated based on a judgement that, whilst the day to day operation of this Sector is managed by the SSA Board, the Cobham plc Board retains the right to variable returns and the ability to affect those returns. Further details can be found in the Corporate Governance section on page 59;

b. Revenue recognition and contract accounting

The Group has a number of contracts related to long term development programmes. For the majority of these contracts revenue is recognised over time on a percentage of completion basis. This is where a portion of the contract revenue is recognised based on contract costs incurred to date compared with total estimated costs at completion. There are three principal judgements associated with this method of contract accounting:

- Performance obligations: Judgement is applied in determining how many performance obligations there are within each contract and whether the development phase represents a separate obligation. In most cases, the development phase is not considered to be distinct as the customer does not benefit from the development activities alone. It is instead combined with the early contracted production phases such as low rate initial production (LRIP) which are considered a key part of the development cycle;

- Modifications and claims: Judgement is applied in determining whether claims to or from the customer are likely to be successful. Estimation techniques are then used to quantify the impact (see 1.3.2d below);
- Costs to fulfil a contract: For some contracts, where revenue is recognised at a point in time (rather than over time), the Group incurs development costs in order to meet its performance obligation and these costs are recognised as an asset. The asset is then amortised to cost of sales as revenue is recognised. Judgement is applied in assessing whether these costs are costs to fulfil a contract or internally generated intangible assets. This judgement will depend on management's assessment of the nature of the underlying costs and whether they principally relate to a particular contract.

c. Capitalisation of development costs

The Group undertakes significant levels of development work which is largely expensed to the Income Statement. Judgement is exercised in determining whether the criteria for capitalisation as described in IAS 38, Intangible Assets are met; in particular in applying the appropriate level of caution to the requirement for the product to be technically feasible and capable of generating a financial return. If these tests are met, further costs are capitalised as an intangible asset until the intangible asset is readily available for use and is then amortised.

1.3.2 Assumptions and estimation uncertainties

Management consider that there are a number of assumptions concerning the future and other major sources of estimation uncertainty at the balance sheet date, which have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. Those key assumptions and estimation uncertainties are as follows:

a. Uncertain tax positions and deferred tax assets (note 7)

Recognition and measurement of amounts provided in respect of uncertain tax positions are included within net current tax liabilities in the Balance Sheet. The recoverability of deferred tax assets is assessed by reference to estimated future profits in each territory;

b. Impairment of goodwill and intangible assets (note 10)

Determination of the value in use of Cash Generating Units (CGUs) as assessed in relation to the annual review of goodwill and any subsequent impairment of goodwill and intangible assets, or reversal of previously impaired intangible assets relies on estimated cash flows, discounted to present value;

c. Inventory provisions (note 13)

Recognition and measurement of provisions for obsolete, slow moving and defective items of inventory;

d. Revenue recognition (note 4), contract assets and liabilities (note 15) and contract loss provisions (note 21)

Recognition and measurement of revenue on long term contracts, associated contract assets and liabilities and contract loss provisions, including those relating to the KC-46 programme, requires estimation of the costs to complete the contracts including some contingencies for the risks identified, the final costs of technical solutions, the outcome of negotiations with customers (including modifications) and the amounts recoverable under these contracts;

- e. Pension assets and liabilities (note 23)
Assumptions are made in assessing the costs and present value of the pension assets and liabilities, which include the discount rate, inflation and mortality rates; and
- f. Valuation of the Parent Company's minority shareholdings (note 17)
Fair value is determined based on the estimated cash flows expected to be received, discounted to present value.

1.4 Underlying measures (note 3)

Definitions and a description of the use of the non-GAAP measures can be found in note 3 on page 107.

1.5 Operating segments (note 4)

The chief operating decision making body for the Group has been identified as the Board. It reviews the Group's internal reporting in order to assess performance and allocate resources. Details of the composition and purpose of the Board can be found on pages 52 and 53.

The Group reports four operating segments whose revenue and results are reported to the Board. These are the Communications and Connectivity, Mission Systems, Advanced Electronic Solutions and Aviation Services Sectors. All operating segments meet the definition of reportable segments as defined in IFRS 8. Costs of the corporate head office and Group functions are allocated across the operating segments. The principal activities of these segments are described on pages 20 to 27.

The Board assesses the trading performance of operating segments based on revenue and underlying operating profit as defined in note 3. Finance income, finance costs and taxation are not segmented and are reviewed by the Board on a consolidated basis. Segment net assets are disclosed in note 4 and include intangible assets, property, plant and equipment, investment properties, inventory, contract assets and liabilities, trade and other receivables, trade and other payables and provisions. They do not include tax, net cash/(debt), derivative financial instruments, contingent consideration payable or retirement benefit obligations.

1.6 Principal accounting policies

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

1.6.1 Basis of consolidation

The Group Financial Statements include the financial statements of the Parent Company, Cobham plc, and of all its subsidiaries.

Subsidiaries are all entities over which the Group has control, which is defined as the right to variable returns and the ability to affect those returns. Subsidiaries are fully consolidated from the date on which control is transferred to the Group until the date that control ceases. Joint ventures and associates are not consolidated but are accounted for using the equity method.

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

As noted in section 1.3.1 above, the consolidation of the Cobham Advanced Electronic Solutions Sector is the subject of a significant judgement.

1.6.2 Foreign currencies

The presentation currency of the Group is sterling. Most Group companies, including the Parent Company, use their local currency as their functional currency. Transactions in currencies other than the functional currency are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in non-functional currencies are

retranslated at the exchange rate ruling at the balance sheet date and any exchange differences arising are taken to the Income Statement.

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

1.6.3 Revenue recognition

IFRS 15, Revenue from Contracts with Customers, has been applied for the first time in these financial statements. Full details on the impact of this new standard are set out in note 2.

A five-step process must be applied before revenue can be recognised:

1. Identify contracts with customers;
2. Identify the separate performance obligations;
3. Determine the transaction price of the contract;
4. Allocate the transaction price to each of the separate performance obligations; and
5. Recognise the revenue as each performance obligation is satisfied.

The transaction price is measured based on the consideration specified in a contract with a customer and, where applicable, the best estimate of any consideration related to modifications to the contract which has yet to be agreed. Any amounts expected to be paid to the customer, such as penalties for late delivery, are deducted from the consideration. Where a transaction price has to be allocated between multiple performance obligations, this is generally achieved through allocating a proportion of total price against each using either standard list sales prices or an estimated costs methodology.

Revenue related to the sale of short cycle catalogue items, mostly seen in the Communications and Connectivity Sector is recognised when control of the product passes to the customer. This may be on delivery or on dispatch depending on the specific terms of the contract. There is generally a low level of returns experienced across the short cycle businesses and therefore no returns provision is recorded.

Most of the revenue in the Aviation Services Sector is generated from providing services to customers. Revenue is recognised over time as the services are enjoyed. Contracts within this Sector can include variable consideration associated with the level of services provided, for example, flying hours. This is generally straightforward to estimate and is invoiced to the customer on a regular basis.

The Group has a number of long term development programmes, particularly within the Mission Systems Sector. For the majority of these contracts revenue is recognised over time on a percentage of completion basis. This is where a portion of the contract revenue is recognised based on contract costs incurred to date compared with total estimated costs at completion. This method is considered to most faithfully depict the transfer of goods and services to the customer over the life of the performance obligation. As these products come out of the development phase and into full rate production, revenue is recognised at a point in time where there is an alternative use. For some programme specific products, markets may not be sufficiently mature to offer an alternative use and in these circumstances, where there is also a right to payment at all times, revenue is recognised over time based on a percentage of completion basis using costs as the measure of progress. For development and production contracts where there is not considered to be a right to payment at all times through the contract, these

Notes to the Group Financial Statements

continued

are accounted for at a point in time, with revenue recognised when control transfers to the customer, typically on delivery of the production units.

The Group has a number of contracts with government bodies, in particular within the Advanced Electronic Solutions Sector, for which control is transferred to the customer as the product is being manufactured or as the services are being provided. For these contracts, revenue is recognised over time on a percentage of completion basis, using cost to measure progress (as above for Mission Systems contracts). For 'cost-plus' contracts (typically with government departments and agencies), revenue is recognised to the extent of reimbursable costs incurred, plus a proportionate amount of the estimated fee earned.

The timing of payment from customers is generally aligned to revenue recognition, subject to agreed invoice terms. The majority of development programmes have payment terms based on contractual milestones, which are not necessarily aligned to when revenue is recognised, particularly for those contracts recognised over time using percentage of completion methodology. This generally leads to recognition of revenue in advance of customer billings, for which a contract asset is recognised. Where cash is received from the customer in advance of recognising revenue under a contract, a contract liability is recorded (advance payments from customers).

The practical expedient available under IFRS 15 has been taken whereby any financing element of the contract price has been ignored if the timing difference between the satisfaction of the obligations under the contract and the receipt of payment due under the contract are expected to be one year or less.

Where incremental costs of obtaining a contract are incurred, such as sales commissions, the Group has taken advantage of the practical expedient to recognise these costs as expensed when incurred rather than capitalising them as an asset, on the basis that the amortisation period would typically be one year or less. Other costs to obtain a contract, such as bid costs, that would have been incurred regardless of whether the contract was awarded are expensed as incurred because they are not recoverable from the customer in the event of an unsuccessful bid.

Costs incurred in fulfilling a contract with a customer are capitalised where: they are directly related to a contract; they generate or enhance the resources of the Group in fulfilling the contract; and they are recoverable. Such costs are then amortised to cost of sales over a consistent period as the associated revenue is recognised.

1. 6. 4 Taxation (note 7)

The tax expense is the sum of current tax and deferred tax. Tax is charged or credited to the Income Statement except when it relates to items recognised in OCI or directly in equity, in which case the tax is also dealt with in OCI or in equity respectively.

Current tax is provided at the amounts expected to be paid, using rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying values in the consolidated financial statements. It is calculated using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and that are expected to apply to the period when the asset is realised or the liability is settled.

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

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

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

1. 6. 5 Intangible assets (note 10)

Goodwill

Goodwill arises on business combinations and represents the excess of the fair value of consideration transferred over the fair value of the Group's share of the identifiable net assets acquired. Goodwill is allocated at acquisition to the CGUs that are expected to benefit from that business combination. CGUs represent the lowest level within the Group at which the goodwill is monitored for internal management purposes.

On divestment of a business the attributable amount of goodwill is included in the determination of the profit or loss on divestment.

Other intangible assets

Intangible assets other than goodwill which are acquired by the Group are stated at cost less accumulated amortisation and impairment losses. These include customer relationships, technology and software, trademarks, licences and patents. The only internally generated intangible assets are development costs which are capitalised as described below and internally developed software where asset recognition criteria are met.

These intangible assets are amortised over the asset's estimated useful life on a straight-line basis as follows:

Customer relationships	5 to 15 years
Technology based assets	5 to 15 years
Development costs	2 to 10 years
Order book and trade names	6 months to 10 years
Software and other	2 to 10 years

Useful lives are assessed for each asset on an individual basis, taking into account the specific characteristics of the asset.

Research and development

Development costs are capitalised when it can be demonstrated that the conditions for capitalisation as described in IAS 38, Intangible Assets are met, paying particular attention to the requirements for the product to be technically feasible and capable of generating a financial return. At that point, further costs are capitalised as an intangible asset until the intangible asset is readily available for use and it is then amortised as described above. All development costs not capitalised are written off as incurred together with all research costs.

1.6.6 Property, plant and equipment (note 11)

Freehold and leasehold land and buildings, plant and machinery, and fixtures, fittings, tools and equipment are held at historic cost less accumulated depreciation and any recognised impairment losses. Cost comprises the purchase price and any costs directly attributable to the asset.

All property, plant and equipment other than land and assets under construction is depreciated on a straight-line basis to the estimated residual values over the estimated useful lives. These lives are as follows:

Freehold buildings	50 years
Leasehold properties	Period to next break clause
Plant and machinery	3 to 15 years
Fixtures, fittings, tools and equipment	3 to 15 years

Estimated residual values and the estimated useful lives are reviewed annually and adjusted where necessary. Freehold land is not depreciated, and is reviewed for impairment at least annually.

Assets under construction are held at cost and transferred to the appropriate category of property, plant and equipment once construction is complete and they enter into service. They are depreciated from this point in accordance with the policies described above.

Assets held under finance leases are depreciated over the term of the relevant lease.

Major overhaul expenditure on owned aircraft is capitalised when incurred and the resultant property, plant and equipment is depreciated over its useful economic life.

1.6.7 Investment properties (note 12)

Investment properties, which are properties held to earn rentals or for capital appreciation, are stated at cost in the Balance Sheet. They are depreciated on a straight-line basis to their estimated residual value over their estimated useful lives of up to 50 years.

Rental income is recognised as revenue on a straight-line basis.

1.6.8 Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets are reviewed at least annually to determine whether there is any indication of impairment. Where there is an indication of impairment, the asset's recoverable amount is estimated. The recoverable amount is the higher of fair value less costs of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

An impairment loss is recognised where the recoverable amount of an asset is lower than its carrying amount. All impairment losses are recognised in operating costs in the Income Statement.

An impairment loss, other than arising on goodwill, is reversed only after a change in the estimates used to assess the recoverable amount is identified and only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. Any reversal is recognised in operating costs in the Income Statement.

1.6.9 Leasing (notes 19 and 29)

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Rentals payable under operating leases are charged to the Income Statement on a straight-line basis over the term of the relevant lease. Benefits receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

1.6.10 Inventories (note 13)

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the first-in, first-out method. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution. Provision is made where necessary for obsolete, slow moving and defective items.

1.6.11 Non-current assets and disposal groups held for sale (note 18)

Non-current assets and disposal groups classified as held for sale are stated at the lower of carrying amount and fair value less costs of disposal. No further depreciation is charged in respect of non-current assets classified as held for sale.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and expected to be completed within a year of the balance sheet date. The asset or disposal group should be available for immediate sale in its present condition and actively marketed at a price that is reasonable in relation to its current fair value.

1.6.12 Fair values

The fair value of an asset or liability is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the balance sheet date. Fair value measurements are used on a recurring basis except where used in the measurement of net assets classified as held for sale and in the valuation of assets and liabilities in a business combination.

The fair values of derivative financial instruments have been determined by the use of valuation techniques, primarily discounted cash flows, based on assumptions that are supported by observable market prices or rates. The fair values of non-financial assets and liabilities, which includes net assets classified as held for sale, are based on observable market prices or rates. For non-financial assets, the fair value takes into account the highest and best use of the assets. These measurements fall within Level 2 of the fair value hierarchy as described in IFRS 13.

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For financial assets and liabilities which are not held at fair value in the Balance Sheet, the carrying values of these items are assumed to approximate to fair value due to their short term nature.

There have been no changes to the valuation techniques used during the year. The Group's policy is to recognise transfers in and transfers out of fair value hierarchy levels as at the date of the event or change in circumstances that caused the transfer, although there have been no such transfers during the current or comparative periods.

1. 6. 13 Financial instruments (note 14)

Financial assets and financial liabilities are recognised on the Group's Balance Sheet when the Group becomes a party to the contractual provisions of the instrument and are initially recognised at fair value at trade date.

All financial assets and liabilities are classified as current or non-current dependent upon the maturity date of the instruments. Financial assets and liabilities are presented on an offset basis when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis.

Accounting policies applied from 1 January 2018

IFRS 9, Financial Instruments, has been applied for the first time in these financial statements. IFRS 9 has replaced the multiple classification and measurement models in IAS 39, Financial instruments: Recognition and Measurement with a single model that has initially only two classification categories: amortised cost and fair value. Full details on the impact of this new standard are set out in note 2.

Accounting policies applied prior to 1 January 2018

The Group has applied IFRS 9 retrospectively but has elected not to restate comparative information. As a result, the accounting policies as presented in previous years continue to apply to the comparative information. As there were no significant changes arising from the implementation of IFRS 9 other than the measurement of equity investments as detailed below (financial assets), these policies have not been repeated in these financial statements.

Financial assets (note 14)

On initial recognition, financial assets are classified as being subsequently measured at either amortised cost or fair value dependent upon the Group's business model for managing the asset and its cash flow characteristics. Financial assets are not reclassified following initial recognition unless the Group changes its business model for managing financial assets.

Financial assets are deemed to be held under one of three business models:

1. Hold to collect, where the business objective is to hold the asset to collect the contractual cash flows;
2. Hold to collect and sell, where the business objective is to hold the asset to collect the contractual cash flows and to sell the financial assets; and
3. Other.

Unless specifically designated to be held at fair value through profit or loss, a financial asset is measured at amortised cost if it is held within a hold to collect business model and its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets held within a hold to collect and sell business model are measured at fair value through OCI if the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. The Group does not currently have any such assets.

Equity investments not held for trading (such as the Group's AirTanker investments) are held at fair value and the Group has elected to present subsequent changes in the investment's fair value in OCI. Dividends on these investments are recognised in profit or loss when the Group's right to receive the dividends is established, it is probable that they will be paid and the amount can be measured reliably. This dividend income is included in operating costs in the Income Statement.

All other financial assets, including derivative financial instruments, are held at fair value through profit or loss.

Amortised cost is measured using the effective interest method. Transaction costs of financial assets carried at fair value through profit or loss are expensed in the Income Statement.

Impairment of financial assets

The Group recognises lifetime expected credit losses at the point of initial recognition for trade receivables, contract assets (under IFRS 15) and lease receivables. These are assessed with reference to past default rates, also reflecting forward looking information such as local economic or market conditions and using a provision matrix where appropriate.

For other financial assets, a loss allowance is recognised for expected credit losses taking into account changes in the level of credit risk. Where credit risk is considered to be low, the loss allowance is limited to expected losses arising from default events that are possible within 12 months from the balance sheet date.

No impairment loss is recognised for investments in equity instruments.

Impairments are charged to operating costs in the Income Statement.

Financial liabilities (note 14)

Subsequent to initial recognition, financial liabilities are classified as measured at fair value through profit or loss, or at amortised cost using the effective interest method.

Trade and other receivables including contract assets (notes 15 and 16)
Trade and other receivables and contract assets are stated at their amortised cost, net of impairment loss allowances. All trade receivables which are more than six months overdue are provided for by reference to past default experience. Where there is clear evidence that the receivable will not be recovered, and generally where receivables are in excess of 12 months old, the balance is written off in full.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and bank deposits with an original maturity of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the Cash Flow Statement.

Bank borrowings (note 19)

Interest bearing bank loans and overdrafts are recorded at the amount of proceeds received, net of direct issue costs. Borrowing costs, net of amounts capitalised, are accounted for on an accruals basis and charged to the Income Statement as incurred. Premiums payable on settlement or redemption and direct issue costs are capitalised and amortised over the period of the facility. Borrowing costs that are directly attributable to relevant property, plant and equipment are capitalised as part of the cost of that asset.

Trade payables (note 20)

Trade payables do not carry any interest and are stated at their nominal value.

Derivative financial instruments and hedge accounting (note 22)

The majority of foreign exchange contracts entered into by the Group are used to mitigate foreign exchange impacts of trading in non-functional currencies. These are not accounted for using hedge accounting principles.

A limited number of specific foreign exchange contracts are designated as hedging instruments in cash flow and net investment hedges, and hedge accounting is applied. The effective portion of changes in fair value is recognised in OCI through the hedge reserve and the gain or loss relating to the ineffective portion is recognised immediately in the Income Statement. Amounts accumulated in OCI are reclassified to finance income or finance costs in the Income Statement in the periods when the hedged item affects profit or loss.

Foreign currency borrowings are also used to hedge the effects of changes in the Group's net investment in foreign operations. These borrowings either provide a natural economic hedge through the use of intercompany debt or are designated as net investment hedges. Where net investment hedging applies, the borrowings are designated as fair value hedges of the foreign currency risk attributable to the foreign equity investment. The exchange differences arising are recognised in OCI and through profit and loss on disposal of the foreign operation.

Where hedge accounting is not applied, movements in fair value of the derivative instruments are included in the Income Statement within operating costs.

The fair value of derivative financial instruments is classified as a current or non-current asset or liability dependent upon the maturity date of the financial instrument or hedged item as appropriate.

1. 6. 14 Provisions (note 21)

A provision is required when the Group has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required and where the amount can be reliably measured. No provision is recognised where the existence of an obligation is possible but will only be confirmed by uncertain future events.

Contract loss provisions are recognised for onerous contracts when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

Restructuring provisions are made where there is an approved and detailed formal plan. There will also be a valid expectation in those affected that the restructuring will be carried out because it has been started or announced. The amount provided includes only the direct expenditures arising from the restructuring.

Provisions for warranty costs are recognised at the date of sale of the relevant products, at management's best estimate of the expenditure required to settle the Group's liabilities, based on past experience and industry averages for defective products.

Provisions for claims made against the Group and commitments made under performance guarantees are recognised at management's best estimate of the expenditure required to settle the Group's liabilities.

Aircraft maintenance provisions are established in respect of significant periodic maintenance costs, where maintenance activity is required on leased operational aircraft or engines on a cycle greater than 12 months. Costs are charged to the Income Statement on the basis of utilisation of the aircraft and are credited to the provision. The provision is then utilised by absorbing the actual costs incurred in carrying out the maintenance activity. Maintenance carried out on a cycle of 12 months or less is charged to the Income Statement as incurred.

Provisions are discounted at an appropriate risk free rate when the impact is material.

1. 6. 15 Retirement benefit schemes (note 23)

For defined benefit schemes, current service costs and costs related to the administration of the schemes are charged to operating profit. Gains and losses on settlements and curtailments arising on a business divestment are included in profit on divestment. Past service costs are recognised in the Income Statement. The interest on net assets or liabilities is shown within finance income and costs. Actuarial remeasurements are recognised in OCI.

Defined benefit schemes are funded, with the assets of the scheme held separately from those of the Group, in separate trustee administered funds. Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting net defined benefit asset or liability is presented separately on the Balance Sheet.

For defined contribution schemes, contributions are charged to the Income Statement as they fall due.

1. 6. 16 Treasury shares (note 25)

When ordinary share capital recognised as equity is acquired by the Company the shares are held as treasury shares.

1. 6. 17 Share based payments (note 27)

For grants made under the Group's equity settled share based payment schemes, amounts which reflect the fair value of awards at the time of grant are charged to the Income Statement over the relevant vesting periods, taking into account management's best estimate of the number of awards expected to vest. The Group reviews and updates the vesting estimate, which includes progress against non-market related performance conditions, at each balance sheet date.

The valuation methodology for all schemes is based on the Black-Scholes model, modified where required to allow for the impact of market related performance criteria and taking into account all non-vesting conditions.

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1.7 Current and future accounting developments

Two new standards have been adopted on 1 January 2018, IFRS 15, Revenue from Contracts with Customers (1.6.3) and IFRS 9, Financial Instruments (1.6.13). Details of the restatement arising from these changes can be found in note 2.

The following additional amendments to standards and interpretations of the IFRS Interpretations Committee have been adopted with effect from 1 January 2018:

- Amendments to IFRS 2, Share Based Payment Transactions. The amendments clarify the measurement basis for cash settled share based payments and the accounting for modifications that change an award from cash settled to equity settled. They also introduce an exception to the classification principles in IFRS 2 associated with the treatment of employee's tax obligations;
- Amendments to IAS 40, Investment Property. The amendments clarify that transfers to, or from, investment property can only be made if there has been a change in use that is supported by evidence;
- IFRIC 22, Foreign Currency Transactions and Advance Consideration. The interpretation clarifies how to determine the date of transaction for the exchange rate to be used on initial recognition of a related asset, expense or income where an entity pays or receives consideration in advance for foreign currency denominated contracts; and
- Annual Improvements 2014-2016 cycle.

No changes to previously published accounting policies or other adjustments were required on the adoption of these amendments.

A number of new standards and amendments have been published that are mandatory for future accounting periods:

IFRS 16, Leases

The Group will adopt IFRS 16, Leases, with effect from 1 January 2019. It will result in almost all leases being recognised on the Balance Sheet by lessees, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short term and low value leases.

The Group intends to take the fully retrospective approach and restate its Balance Sheet and Income Statement as if the new standard had always been applied.

A detailed review of all lease arrangements has been undertaken. The Group expects to recognise right-of-use assets of approximately £100m on 1 January 2019 and lease liabilities of approximately £140m.

The Group expects that profit before tax and EPS for 2018 will not change significantly as a result of adopting the new rules. Underlying operating profit used to measure segment results is expected to increase by approximately £7m. Previously the operating lease payments were included in underlying operating profit. Going forward only the amortisation of the right-of-use assets will be included whereas interest on the lease liability is excluded from this measure.

Total cash flows are not impacted.

IFRIC 23, Uncertainty over Income Tax Treatments

The interpretation, which is effective from 1 January 2019, explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment. In particular, it discusses that the impact of the uncertainty should be measured using either the most likely amount or the expected value method, depending on which method better predicts the resolution of the uncertainty. It also discusses that the entity should assume a tax authority will examine the uncertain tax treatments and have full knowledge of all related information (i.e. that detection risk should be ignored). No new disclosure requirements are introduced by this interpretation.

The Group has performed a review of its uncertain tax positions in light of this new interpretation and does not expect the additional guidance to have a material impact on the Group's financial reporting.

Other future changes

There are also a number of amendments to existing standards including Annual Improvements and interpretations which, once endorsed by the EU, will be effective from 1 January 2019 or later years.

None of these are expected to have a material impact on the Group's financial reporting.

2. Impact of new accounting standards

As previously identified, the Group adopted IFRS 9, Financial Instruments and IFRS 15, Revenue from Contracts with Customers, on 1 January 2018.

IFRS 15, Revenue from Contracts with Customers

Under IFRS 15, revenue is recognised over time for contracts where there is no alternate use for the product and there is a right to payment at all times throughout the contract. A number of long term development programmes, notably within the Mission Systems Sector, meet these criteria. Revenue is also recognised over time for contracts where control transfers as the product is being manufactured. This occurs on some contracts directly with government bodies, most notably in the Advanced Electronic Solutions Sector. On both types of contract, where revenue is now recognised over time, the amounts previously included within inventories as work in progress or finished goods are now recognised, including margin, as a contract asset described as unbilled receivables.

Under IAS 18 it was appropriate, in certain situations, to combine related contracts. Under IFRS 15 the circumstances where this is allowed are more clearly defined and therefore some customer delivery obligations have been treated as separate obligations which impacts the timing of revenue and profit recognition.

On transition to IFRS 15, in addition to the matters described above, the balance sheet presentation has changed in a number of areas. Where there has been no change to the revenue recognition basis arising from IFRS 15, any remaining accrued income balances that were previously included within trade and other receivables are now shown as a contract asset (described as unbilled receivables). Deferred income (where the customer has paid upfront but revenue has not yet been recognised) was previously included in trade and other payables and is now recognised separately as a contract liability (described as advance payments from customers). Costs to fulfil a contract were previously included within inventories as work in progress.

IFRS 15 has been applied retrospectively and therefore comparative information presented in these financial statements has been restated as disclosed in the tables below. A summary of the impact of adopting IFRS 15, as described above, is as follows:

£m	Total equity
At 31 December 2016 (as originally stated)	489.9
Adjustments to retained earnings on adoption of IFRS 15	(0.2)
At 1 January 2017 (restated)	489.7
At 31 December 2017 (as originally stated)	1,028.3
Contracts where revenue is recognised over time rather than at a point in time	18.4
Contracts where performance obligations are now accounted for separately	(11.4)
Deferred tax impact	(2.9)
Adjustments to retained earnings on adoption of IFRS 15	4.1
At 31 December 2017 (restated)	1,032.4

The full impact on the Balance Sheets as at 1 January 2017 and 31 December 2017 and on the Income Statement for the year ended 31 December 2017 are as below:

Impact on Balance Sheet at 1 January 2017

£m	As originally stated	IFRS 15 adjustments	Restated
Assets			
Inventories	405.3	(121.3)	284.0
Contract assets	–	173.0	173.0
Trade and other receivables	475.8	(75.5)	400.3
Other assets	1,913.5	–	1,913.5
	2,794.6	(23.8)	2,770.8
Liabilities			
Contract liabilities	–	(104.3)	(104.3)
Trade and other payables	(471.8)	108.2	(363.6)
Provisions	(237.9)	25.7	(212.2)
Deferred tax	(27.6)	(6.0)	(33.6)
Other liabilities	(1,567.4)	–	(1,567.4)
	(2,304.7)	23.6	(2,281.1)
Net assets	489.9	(0.2)	489.7

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Impact on Balance Sheet at 31 December 2017

£m	As originally stated	IFRS 15 adjustments	Restated
Assets			
Inventories	389.4	(135.2)	254.2
Contract assets	–	190.2	190.2
Trade and other receivables	393.5	(71.2)	322.3
Other assets	2,010.5	1.3	2,011.8
	2,793.4	(14.9)	2,778.5
Liabilities			
Contract liabilities	–	(105.2)	(105.2)
Trade and other payables	(484.3)	124.9	(359.4)
Provisions	(155.8)	3.5	(152.3)
Deferred tax	(2.1)	(4.2)	(6.3)
Other liabilities	(1,122.9)	–	(1,122.9)
	(1,765.1)	19.0	(1,746.1)
Net assets	1,028.3	4.1	1,032.4

Impact on Income Statement for the year ended 31 December 2017

£m	As originally stated	IFRS 15 adjustments	Restated
Revenue	2,052.5	39.1	2,091.6
Cost of sales	(1,457.9)	(36.9)	(1,494.8)
Gross profit	594.6	2.2	596.8
Operating costs	(491.6)	0.6	(491.0)
Profit on divestments	1.1	–	1.1
Operating profit	104.1	2.8	106.9
Finance income	6.1	–	6.1
Finance costs	(43.3)	–	(43.3)
Profit before taxation	66.9	2.8	69.7
Taxation	11.9	2.5	14.4
Profit after taxation for the year	78.8	5.3	84.1
Attributable to:			
Owners of the parent	78.6	5.3	83.9
Non-controlling interests	0.2	–	0.2
	78.8	5.3	84.1
Earnings per ordinary share			
Basic	3.5p		3.7p
Diluted	3.5p		3.7p

IFRS 9, Financial Instruments

Following the adoption of IFRS 9, the accounting policies for financial instruments applied during the year ended 31 December 2017 are, on a practical level, largely unchanged.

Retained earnings and other financial assets at 1 January 2018 have been restated by £39.0m as a result of the transition to this new standard. There was, however no impact on the consolidated income statement, other balance sheet line items or the consolidated cash flows of the Group, nor on EPS. In accordance with the transitional provisions, comparative figures have not been restated.

The restatement relates to Cobham plc's minority shareholdings in equity investments which were accounted for as trade investments and categorised as available for sale under IAS 39. Under IFRS 9, these investments are held at fair value, using a present value methodology. The Company has elected to present movements in fair value in OCI. Further details are shown in note 17.

Reclassification of financial assets into the IFRS 9 categories had no overall impact on the measurement basis applied. The table below provides details of the classification and measurement of financial assets and liabilities under IAS 39 and IFRS 9 at 1 January 2018, the date of initial application, after taking into account the impact of IFRS 15 as described above.

£m	Original IAS 39 measurement category	Revised IFRS 9 measurement category	IAS 39 carrying amount	IFRS 9 carrying amount
Financial assets				
Trade receivables, other receivables, cash and cash equivalents	Loans and receivables (amortised cost)	Financial assets at amortised cost	938.5	938.5
Derivative contracts (not hedge accounted)	Fair value through profit or loss	Financial assets at fair value through profit or loss	13.2	13.2
Other financial assets	Amortised cost	Financial assets at fair value through OCI	6.1	45.1
Financial liabilities				
Borrowings, trade payables, accruals, other financial liabilities	Amortised cost	Financial liabilities at amortised cost	(1,274.6)	(1,274.6)
Derivative contracts (not hedge accounted)	Fair value through profit or loss	Financial liabilities at fair value through profit or loss	(17.4)	(17.4)
Hedging instruments				
Assets	Derivatives used for hedging	Derivatives used for hedging	22.2	22.2
Liabilities	Derivatives used for hedging	Derivatives used for hedging	(22.0)	(22.0)
Net financial liabilities at 1 January 2018			(334.0)	(295.0)

3. Underlying measures, EPS and specific adjusting items

Use of underlying measures

To assist with the understanding of earnings trends, the Group has included within its published financial statements non-GAAP alternative performance measures including underlying operating profit and underlying profit.

The non-GAAP measures used are not defined terms under IFRS and therefore may not be comparable to similar measures used by other companies. They are not intended to be a substitute for, or superior to, GAAP measures.

Management use underlying measures to assess the operating performance of the Group, having adjusted for specific items as defined below. They form the basis of internal management accounts and are used for decision making including capital allocation, and a subset also forms the basis of internal incentive arrangements. By using underlying measures in our segmental reporting, this further ensures readers of the financial statements can recognise how incentive performance is targeted. Underlying measures are also presented in this report because the Directors believe they provide additional useful information to shareholders on comparative trends over time. Finally, this presentation allows for separate disclosure and specific narrative to be included concerning the adjusting items; this helps to ensure performance in any one year can be more clearly understood by users of the financial statements.

In 2016, certain exceptional items were adjusted for and excluded from underlying measures due to their unusual size and incidence. These arose from the January 2017 Balance Sheet review and included revisions to the carrying value of assets, additional contract loss provisions, and legal and other provisions. Where relevant, updates to, and the final outcome of, these items are presented consistently with this treatment as exceptional charges or credits as appropriate.

Definitions of underlying measures

All underlying measures include the operational results of all businesses including those held for sale until the point of sale. These definitions are applied consistently on a year to year basis.

Underlying operating profit

Underlying operating profit has been defined as operating profit from continuing operations excluding the impacts of business acquisition and divestment related activity and prior periods' business restructuring costs as detailed below. Also excluded are changes in the marking to market of non-hedge accounted derivative financial instruments, gains and losses arising on dividend related foreign exchange contracts and other items deemed by the Directors to be of a non-operating nature including the impairment of intangible assets. Changes in items previously treated as exceptional in 2016 will also be adjusted.

Underlying profit

Underlying profit before taxation is defined as underlying operating profit less net underlying finance costs, which exclude business acquisition and divestment related items and specific finance costs.

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Income Statement including underlying results

£m	Note	2018			2017 (restated)		
		Underlying	Specific adjusting items	Total	Underlying	Specific adjusting items	Total
Revenue	4	1,863.3	–	1,863.3	2,091.6	–	2,091.6
Cost of sales		(1,339.9)	(200.0)	(1,539.9)	(1,494.8)	–	(1,494.8)
Gross profit		523.4	(200.0)	323.4	596.8	–	596.8
Operating costs		(327.3)	(111.2)	(438.5)	(383.7)	(107.3)	(491.0)
Profit on divestments	28	–	227.0	227.0	–	1.1	1.1
Operating profit/(loss)		196.1	(84.2)	111.9	213.1	(106.2)	106.9
Finance income	6	10.5	–	10.5	6.1	–	6.1
Finance costs	6	(51.4)	–	(51.4)	(43.3)	–	(43.3)
Profit/(loss) before taxation		155.2	(84.2)	71.0	175.9	(106.2)	69.7
Taxation	7	(35.6)	38.3	2.7	(37.3)	51.7	14.4
Profit/(loss) after taxation for the year		119.6	(45.9)	73.7	138.6	(54.5)	84.1

Earnings per ordinary share

£m	2018			2017 (restated)		
	Underlying	Specific adjusting items	Total	Underlying	Specific adjusting items	Total
Profit/(loss) after taxation for the year	119.6	(45.9)	73.7	138.6	(54.5)	84.1
Amount attributable to non-controlling interests	(0.2)	–	(0.2)	(0.2)	–	(0.2)
Earnings attributable to owners of the parent	119.4	(45.9)	73.5	138.4	(54.5)	83.9
Weighted average number of shares (million)	2,379.8		2,379.8	2,231.8		2,231.8
Effect of dilutive securities (million)	4.3		4.3	3.5		3.5
Diluted weighted average number of shares (million)	2,384.1		2,384.1	2,235.3		2,235.3
Basic EPS	5.0p		3.1p	6.2p		3.7p
Diluted EPS	5.0p		3.1p	6.2p		3.7p

Potentially dilutive securities are unvested awards under the Group's share based payment schemes described in note 27.

Details of the restatement can be found in note 2.

Details of specific adjusting items

The specific adjusting items excluded from underlying profit can be analysed as follows:

fm	Note	2018	2017
Cost of sales			
Estimates of fixed price contract profitability		200.0	–
Operating costs			
Derivative financial instruments	22	19.7	(28.9)
Net pension adjustments		3.4	–
Business acquisition and divestment related items			
Amortisation of intangible assets arising on business combinations	10	89.8	138.9
Other M&A related costs		–	0.3
Impairment of goodwill and other intangible assets	10	–	33.5
Reversal of impairment of intangible assets	10	–	(31.8)
Other items provided as exceptional items at 31 December 2016			
Adjustments to revisions of the carrying values of other assets		–	(1.4)
Assessment of legal and other provisions		(1.7)	(8.0)
Amounts related to prior periods restructuring programmes		–	4.7
		111.2	107.3
Profit on divestments			
Profit on divestments	28	(227.0)	(1.1)
Taxation			
Tax credit on specific adjusting items	7	(38.3)	(51.7)

Explanation of specific adjusting items

Estimates of fixed price contract profitability

A charge of £200.0m has been taken against increased estimates of cost to complete and recovery on the KC-46 contract comprising £40.0m recorded in the half year and a further £160.0m recorded following the announcement on 19 February 2019. This reflects an adjustment to an item previously disclosed as exceptional and hence it has been presented as a specific adjusting item. The Board recognises that making estimates on complex contracts is inherently judgemental and therefore whilst it has made a best estimate of contract positions at present, the final outcome of the contracts could be more or less favourable than the position taken.

Derivative financial instruments

The impact of derivative financial instruments excluded from underlying results includes changes in the marking to market of non-hedge accounted derivative financial instruments other than fair value gains or losses arising on currency swaps which offset movements in currency balances held. These amounts relate to foreign currency exchange contracts and would not impact operating results had the Group chosen to comply with IFRS 9 requirements to enable these contracts to be hedge accounted. These impacts are excluded as market volatility can result in material changes in fair value, both positive and negative, which distort the underlying results.

Pension adjustments

In October 2018, the English High Court determined that UK defined benefit pension schemes with Guaranteed Minimum Pensions (GMP) must be equalised between men and women. The impact of this ruling on the UK schemes has been estimated at £5.5m and recognised as a past service cost. This has been calculated using the 'C2' method as the Company's current best estimate; the actual method of satisfying the obligations to the members of the pension plans will ultimately need to be agreed by the Company and the trustees of the pension plans. This additional cost has been excluded from underlying measures to reflect the highly unusual nature of this cost which relates to service cost generated many years ago.

Offset against the GMP charge is a gain on curtailment of £2.1m arising from the closure of the US defined benefit pension scheme to future accrual. While this gain arose due to management decisions in the year, such an event is also considered to be unusual and warrants separate disclosure.

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Business acquisition and divestment related items

The Group has been acquisitive over time and also divests businesses in accordance with its strategy. Accounting adjustments that arise as a result of business combinations and divestments are not considered to result from the underlying business activity and have therefore been excluded from underlying measures.

These adjustments include the amortisation of intangible assets arising on business combinations, gains or losses arising on business divestments, adjustments to businesses held for sale, the writing off of the pre-acquisition profit element of inventory written up on acquisition, revaluation gains and losses arising on the original equity interests on stepped acquisitions, other direct costs associated with business combinations and terminated divestments, and adjustments to contingent consideration related to previously acquired businesses. Amortisation of intangible assets arises as a result of the purchase price allocation on business combinations and includes customer lists, technology based assets, and order book and trade names. It is excluded from underlying measures because it does not relate to the in year operational performance of the business, being driven by the timing and amount of investment in business combinations. Likewise impairments of goodwill and other intangible assets arising on business combinations, together with any reversal of impairment of intangible assets, are treated as specific adjusting items as these assets arose from business acquisitions in prior periods. The amortisation of internally generated intangible assets such as software and development costs is included within underlying measures.

Other M&A related costs reflect the finalisation of costs related to acquisitions and divestments in prior years.

Other items

The assessment of legal and other provisions of £1.7m (2017: £8.0m) relates to provisions made at 31 December 2016 which have been reassessed and, in some instances, settled. These provision releases are treated as adjusting items consistent with the treatment of the original provisions.

The 2017 adjustments to revisions of the carrying value of other assets provided at 31 December 2016 related to a provision against aged receivables which was considered doubtful at 31 December 2016 but which was subsequently recovered with only a small loss. The release of this provision was treated as an adjusting item consistent with the treatment of the original provision.

Amounts related to prior periods restructuring programmes

Amounts related to prior periods restructuring programmes were deemed as incremental to normal operations. These costs relate to the integration of the Aeroflex businesses acquired in 2014. This programme is now closed and no further amounts are expected.

4. Revenue and segmental information

Revenue

Revenue comprises income from the sale of goods and services during the year and can be analysed as follows:

£m	Communications and Connectivity	Mission Systems	Advanced Electronic Solutions	Aviation Services	Total 2018
External revenue by market					
US defence/security	43.1	195.0	471.6	–	709.7
UK, RoW defence/security	109.6	162.4	31.7	171.3	475.0
Commercial	398.4	45.3	91.3	143.6	678.6
	551.1	402.7	594.6	314.9	1,863.3
External revenue by customer geography					
USA	155.6	288.9	546.2	–	990.7
UK	35.2	21.5	7.7	78.5	142.9
Other EU	219.7	59.2	13.3	5.6	297.8
Australia	5.8	5.0	0.4	206.1	217.3
Asia	91.0	19.2	15.6	17.9	143.7
Rest of the world	43.8	8.9	11.4	6.8	70.9
	551.1	402.7	594.6	314.9	1,863.3
External revenue by revenue recognition category					
Goods transferred at a point in time	485.3	346.7	339.5	–	1,171.5
Goods transferred over time	14.1	(11.3)	227.6	–	230.4
Services transferred over time	31.2	35.9	19.4	308.8	395.3
Services transferred at a point in time	20.5	31.4	8.1	6.1	66.1
	551.1	402.7	594.6	314.9	1,863.3

As announced on 19 February 2019, agreement has been reached with Boeing to settle damages assertions, and estimates of cost to complete have been increased, on the KC-46 contract. A further non-underlying charge of £160.0m has been taken, within the Mission Systems segment, in addition to the £40.0m recorded in the first half of the year as announced on 26 July 2018. This agreement has reduced both the total value of the contract and the percentage of completion, resulting in a derecognition of £79.8m of revenue. This has been accounted for in the current year as the underlying events occurred during 2018. Whilst some of the revenue related to prior periods, our programme accounting takes into account the facts and circumstances reasonably known at the time.

Revenue by customer geography is revenue from external customers analysed by their geographic location, irrespective of the origin of the goods and services. Revenue from customers in individual countries within the EU (except the UK) and the rest of the world is not considered to be individually material.

£m	Communications and Connectivity	Mission Systems	Advanced Electronic Solutions	Aviation Services	Total 2017 (restated)
External revenue by market					
US defence/security	52.0	253.1	471.3	–	776.4
UK, RoW defence/security	112.9	137.9	27.2	209.5	487.5
Commercial	534.4	40.8	95.4	157.1	827.7
	699.3	431.8	593.9	366.6	2,091.6
External revenue by customer geography					
USA	194.0	332.7	539.9	–	1,066.6
UK	45.3	18.4	8.4	114.3	186.4
Other EU	262.0	53.3	16.4	7.2	338.9
Australia	8.4	4.9	0.5	215.6	229.4
Asia	134.0	14.4	24.3	21.4	194.1
Rest of the world	55.6	8.1	4.4	8.1	76.2
	699.3	431.8	593.9	366.6	2,091.6
External revenue by revenue recognition category					
Goods transferred at a point in time	597.7	279.5	390.1	–	1,267.3
Goods transferred over time	16.8	90.0	175.4	–	282.2
Services transferred over time	32.1	35.6	10.3	300.1	378.1
Services transferred at a point in time	52.7	26.7	18.1	66.5	164.0
	699.3	431.8	593.9	366.6	2,091.6

Details of the restatement can be found in note 2.

Notes to the Group Financial Statements

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Revenue to be recognised in the future related to agreed performance obligations that are unsatisfied or partially satisfied is as follows:

£m	2019	2020	Later	Total
Communications and Connectivity	215.1	40.7	22.1	277.9
Mission Systems	397.3	147.9	202.3	747.5
Advanced Electronic Solutions	477.4	152.1	24.2	653.7
Aviation Services	248.9	204.5	537.4	990.8
	1,338.7	545.2	786.0	2,669.9

Revenue to be recognised in the future, related to agreed performance obligations that are unsatisfied or partially satisfied as at 31 December 2017, was as follows:

£m	2018	2019	Later	Total
Communications and Connectivity	210.8	31.1	24.7	266.6
Mission Systems	431.9	191.4	98.3	721.6
Advanced Electronic Solutions	362.5	119.4	11.8	493.7
Aviation Services	241.1	200.3	673.5	1,114.9
	1,246.3	542.2	808.3	2,596.8

The tables above refer to external performance obligations; order book values disclosed in the Strategic Report use the same data and also include inter-sector revenue.

Operating segments

£m	Total revenue		Underlying operating profit		Segment net assets	
	2018	2017 (restated)	2018	2017 (restated)	2018	2017 (restated)
Communications and Connectivity	552.0	700.7	55.9	69.0	373.8	522.7
Mission Systems	402.7	431.8	75.3	55.2	78.7	191.8
Advanced Electronic Solutions	595.0	594.7	52.9	66.1	579.9	607.2
Aviation Services	315.1	366.6	12.0	22.8	210.6	222.2
Elimination of inter-segment items and head office	(1.5)	(2.2)	—	—	63.1	22.3
Total Group	1,863.3	2,091.6	196.1	213.1	1,306.1	1,566.2
Interests in joint ventures and associates					4.1	3.6
Unallocated liabilities					(118.5)	(537.4)
Total net assets					1,191.7	1,032.4

Details of the restatement can be found in note 2.

Underlying operating profit is reconciled to the profit before taxation as follows:

£m	Note	2018	2017 (restated)
Underlying operating profit		196.1	213.1
Specific adjusting items included within:			
Cost of sales	3	(200.0)	—
Operating costs	3	(111.2)	(107.3)
Profit on divestments	3	227.0	1.1
Net finance costs	6	(40.9)	(37.2)
Profit before taxation		71.0	69.7

Depreciation of property, plant and equipment, investment properties and amortisation of internally generated intangibles included in the calculation of underlying operating profit can be analysed by segment as follows:

£m	2018	2017
Communications and Connectivity	8.0	15.2
Mission Systems	7.4	6.8
Advanced Electronic Solutions	14.5	16.0
Aviation Services	38.2	37.6
Head office and other activities	11.3	9.4
Total Group	79.4	85.0

Details of employees analysed by operating segment can be found in note 5.

Geographical information

Non-current assets are analysed by the physical location of the assets and exclude financial instruments and deferred tax assets.

£m	2018	2017 (restated)
USA	614.1	647.3
UK	152.1	172.1
Other EU	282.6	294.8
Australia	147.4	146.1
Rest of the world	19.6	20.4
	1,215.8	1,280.7

5. Other income statement disclosures

The following costs are included in operating profit:

£m	Note	2018	2017
Materials costs within cost of sales		596.3	645.4
Restructuring costs included within underlying profit		12.3	7.5
Amounts related to prior periods restructuring programmes excluded from underlying profit	3	—	4.7
Company funded research and development		103.2	121.9

Operating profit also includes dividends of £9.9m (2017: £0.6m) received from the AirTanker investments, see note 17.

Employment costs and employee numbers

The aggregate employment costs are as follows:

£m	Note	2018	2017
Wages and salaries		614.1	644.9
Social security costs		47.0	51.6
Pension costs	23	35.8	38.1
Share based payments	27	5.8	5.5
		702.7	740.1

Employee numbers, analysed by segment, are as follows:

	Monthly average number of employees		As at 31 December	
	2018	2017	2018	2017
Communications and Connectivity	2,726	3,300	2,394	3,197
Mission Systems	1,896	1,682	1,981	1,774
Advanced Electronic Solutions	3,543	3,202	3,602	3,393
Aviation Services	1,826	2,181	1,718	2,072
Head office and other activities	368	371	374	377
Total Group	10,359	10,736	10,069	10,813

Compensation of key management personnel

The remuneration of the Group Executive Committee, as referred to on page 58, was as follows:

£m	2018	2017
Salaries and short term employee benefits	7.4	7.9
Post employment benefits	0.2	0.3
Termination benefits	0.7	1.8
Share based payments	1.5	1.1
	9.8	11.1

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Audit fees

During the year, the Group obtained the following services from the Company's auditors, PricewaterhouseCoopers LLP and its associates:

£m	2018	2017
Annual audit of the Parent Company and Group Financial Statements	1.0	1.0
Audit of the Company's subsidiaries	0.9	1.1
Fees payable for audit services	1.9	2.1
Other assurance services	0.7	0.2
Fees payable for other services	0.7	0.2
Total fees payable to the auditors	2.6	2.3

Other assurance services include £0.6m relating to work undertaken to support the regulatory filings by Viavi following their acquisition of the Group's AvComm and Wireless test and measurement businesses, for which Cobham received reimbursement in full.

6. Finance income and costs

£m	Note	2018	2017
Bank interest		4.5	3.9
Other finance income		6.0	2.2
Total finance income		10.5	6.1
Interest on bank overdrafts and loans		(20.1)	(38.3)
Interest on obligations under finance leases		(0.4)	–
Interest on net pension scheme liabilities	23	(1.5)	(2.3)
Other finance expense		(29.4)	(2.7)
Total finance costs		(51.4)	(43.3)
Net finance costs		(40.9)	(37.2)

Other finance expense for 2018 includes £20.4m of make-whole fees payable in connection with the early repayment of borrowings during the year as detailed in note 19, together with £7.8m related to interest on uncertain tax positions as shown in note 20.

7. Taxation

Tax included in Income Statement

£m	2018	2017 (restated)
Charge for the year	6.8	22.0
Adjustments to tax charge in respect of prior years	24.4	–
Current tax	31.2	22.0
Credit for the year	(17.2)	(39.8)
Impact of change in tax rates	(0.8)	0.1
Adjustments to tax charge in respect of prior years	(15.9)	3.3
Deferred tax	(33.9)	(36.4)
Total tax credit for the year	(2.7)	(14.4)

Details of the restatement can be found in note 2

Income tax is calculated on the estimated assessable profit for the year at the rates prevailing in the relevant tax jurisdiction. The total tax credit for the year includes a credit of £4.8m (2017: £8.6m) for the UK.

The total tax charge/(credit) for the year can be reconciled to the accounting result as follows:

£m	2018			2017 (restated)		
	Underlying	Specific adjusting items*	Total	Underlying	Specific adjusting items*	Total
Profit/(loss) before tax	155.2	(84.2)	71.0	175.9	(106.2)	69.7
Tax thereon at the UK income tax rate of 19% (2017: 19.25%)	29.5	(16.0)	13.5	33.9	(20.4)	13.5
Effect of differences in overseas tax rates	7.6	(2.6)	5.0	7.7	(15.1)	(7.4)
Impact of tax treatment of divestments	–	(31.6)	(31.6)	–	(11.9)	(11.9)
Impact of change in tax rates	(0.8)	–	(0.8)	0.1	–	0.1
Expenditure qualifying for additional R&D tax relief	(2.0)	–	(2.0)	(1.9)	–	(1.9)
Adjustments to tax charge in respect of prior years	8.5	–	8.5	3.3	–	3.3
Impact of other items	(7.2)	11.9	4.7	(5.8)	(4.3)	(10.1)
Total tax charge/(credit) for the year	35.6	(38.3)	(2.7)	37.3	(51.7)	(14.4)
Effective tax rate	23.0%		(3.8%)	21.2%		(20.7%)

* Details of specific adjusting items can be found in note 3.

Adjustments to tax charge in respect of prior years arise from differences in the filed tax returns compared to the estimates made in December 2017. Impact of other items primarily relates to interest taxed at a reduced rate in addition to amounts related to the KC-46 programme.

The adoption of IFRS 15 means that the restated Balance Sheet at 31 December 2017 includes the cumulative impact of earlier profit recognition on some US based contracts. The associated deferred tax liabilities were reduced when the US tax rate change of 35% to 21% was substantially enacted in 2017. This led to a one-time credit in 2017, which is disclosed here as part of the IFRS 15 restatement impact. The 2017 effective tax rate charge is restated to reflect this, but that in year reduction will not be repeated in future periods. Prior to this restatement, the 2017 underlying effective tax rate was 23%.

The UK corporation tax rate reduced from 20% to 19% on 1 April 2017. It will reduce further to 17% from 1 April 2020. UK deferred taxes have been calculated at 19%, or 17% where the impact is expected to crystallise after 1 April 2020.

The US corporation tax rate reduced from 35% to 21% on 1 January 2018.

Tax included in OCI

£m	2018	2017
Items that will not be reclassified subsequently to profit or loss		
Actuarial gain on retirement benefit obligations	1.7	1.4
Actuarial loss on other retirement benefit obligations	(0.1)	–
	1.6	1.4
Items that may subsequently be reclassified to profit or loss		
Hedge accounted derivative financial instruments	0.1	0.1

Tax included in equity

£m	2018	2017
Share based payments	0.1	–

Current tax assets and liabilities

£m	2018	2017
Current tax receivables	7.8	7.2
Current tax liabilities	(136.7)	(135.8)
	(128.9)	(128.6)

Notes to the Group Financial Statements

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Current tax risks (key estimation uncertainty)

The Group is subject to corporate and other tax rules in the jurisdictions where it conducts its business operations. Changes in tax rates, tax reliefs and tax laws, changes in practice or interpretation of the law by the relevant tax authorities, increasing challenges by relevant tax authorities on transfer pricing and other matters, or any failure to manage tax risks adequately could result in increased charges, financial loss, penalties and reputational damage, which may materially adversely affect the Group's financial condition and results of operations.

In addition, tax enforcement has become a higher priority for many tax authorities in jurisdictions in which the Group operates, which has led to an increase in tax audits, enquiries and challenges, or the testing through litigation of the boundaries of the correct interpretation of legislation. Tax authorities may also actively pursue additional taxes based on retroactive changes to tax laws and the Group may have disagreements with tax authorities which could result in a material restatement to the tax position. For example, the availability of certain interest deductions on one of the Group's internal financing arrangements, principally as a result of various US acquisitions, has been under challenge for some time. Over the life of this internal financing arrangement, the aggregate tax value of the interest deductions amounted to approximately £130m. If decided adversely to the Group, this could lead to increased tax liabilities in excess of those provided in the Group's Balance Sheet, and result in a substantial tax payment becoming due. That payment may also result in an additional interest charge from the relevant authority. The Group is actively involved in attempting to resolve this matter ahead of a Tribunal hearing, which is scheduled for autumn 2019.

The European Commission (EC) has opened an investigation into the UK's controlled foreign company (CFC) rules. The CFC rules levy a charge on foreign entities controlled by the UK that are subject to a lower rate of tax; however there is currently an exemption available for 75% of this charge if the activities being undertaken by the CFC relate to financing. The EC is investigating whether this exemption is in breach of EU State Aid rules, but it is too early to assess what the conclusions of this investigation might be. If there is an adverse final determination on the UK's CFC legislation, the Group estimates that its maximum exposure on this matter is approximately £60m.

The Group has accrued £146.8m (2017: £126.4m) in respect of uncertain tax positions in the UK, US and other tax jurisdictions, together with £18.4m (2017: £10.6m) related to interest on uncertain tax positions as shown in note 20. Final resolutions will affect the amounts settled and the timing of any settlements. Whilst resolution remains uncertain, these amounts are included in current liabilities.

Deferred tax assets and liabilities

£m	2018	2017 (restated)	1 January 2017 (restated)
Deferred tax assets			
Recoverable within one year	(63.9)	(54.8)	(26.5)
Recoverable after one year	(25.9)	(4.0)	(17.4)
	(89.8)	(58.8)	(43.9)
Deferred tax liabilities			
Falling due within one year	5.1	3.7	0.5
Falling due after one year	–	2.6	33.1
	5.1	6.3	33.6
Net deferred tax assets	(84.7)	(52.5)	(10.3)

Further details of the restatement of the comparative Balance Sheets, due to the implementation of IFRS 15, Revenue from Contracts with Customers, can be found in note 2.

The following are the major deferred tax assets and liabilities recognised by the Group and the movements thereon:

£m	Intangible assets	Property, plant and equipment	Retirement benefit obligations	Tax losses	Other	Total
At 31 December 2016 (as originally stated)	164.0	24.6	(17.4)	(28.9)	(158.6)	(16.3)
Change in accounting policy – IFRS 15 (note 2)	–	–	–	–	6.0	6.0
At 1 January 2017 (restated)	164.0	24.6	(17.4)	(28.9)	(152.6)	(10.3)
(Credit)/charge to income statement	(71.5)	(5.1)	2.6	(18.1)	55.7	(36.4)
Credit to OCI	–	–	1.4	–	0.1	1.5
Charge to equity	–	–	–	–	0.1	0.1
Reclassified as held for sale	(10.7)	0.8	–	–	3.1	(6.8)
Foreign exchange adjustments	(9.5)	(1.0)	0.3	0.6	9.0	(0.6)
At 31 December 2017 (restated)	72.3	19.3	(13.1)	(46.4)	(84.6)	(52.5)
(Credit)/charge to income statement	(12.8)	4.0	1.8	(21.6)	(5.3)	(33.9)
Charge to OCI	–	–	1.6	–	0.2	1.8
Charge to equity	–	–	–	–	0.1	0.1
Business divestments	4.3	0.2	–	–	(4.9)	(0.4)
Foreign exchange adjustments	4.1	0.3	(0.1)	(0.4)	(3.7)	0.2
At 31 December 2018	67.9	23.8	(9.8)	(68.4)	(98.2)	(84.7)

Other deferred tax assets and liabilities shown above include balances arising from temporary differences in relation to provisions and accruals of £47.8m (2017: £56.9m) and disallowed interest of £41.3m (2017: £31.3m).

Tax losses (key estimation uncertainty)

Tax losses of £51.5m (2017: £29.6m) arising in the UK and £10.5m (2017: £5.8m) arising in Denmark have been recognised on the basis of UK and Danish forecasted future taxable profits, using projections prepared by management and reviewed by the Board. The recognition of these tax losses can be sensitive to movement in these forecasted profits. As an indication of sensitivity, a 33% reduction in the estimated profits would not impact the recognition of these tax losses. Capital losses in the US of £10.9m were used on completion of the divestment of the AvComm business.

At the balance sheet date, the Group has unused capital losses of £61.1m (2017: £85.9m) potentially available for offset against future capital profits in certain circumstances. No deferred tax asset has been recognised in respect of this amount because of the unpredictability of future qualifying profit streams. These losses can be carried forward indefinitely.

Unremitted earnings

The unprovided tax on unremitted earnings as at 31 December 2018 is considered to be immaterial.

8. Dividends

No dividends have been paid or approved by Cobham plc during the current or prior year. Further details of Cobham plc's dividend policy can be found in note 24.

A dividend of £0.1m was paid to the holders of non-controlling interests in TEAM SA, a subsidiary of Cobham plc, during the year ended 31 December 2017.

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9. Cash flow from operations

£m	Note	2018	2017 (restated)
Operating profit		111.9	106.9
Non-cash items:			
Share of post-tax results of joint ventures and associates		(0.5)	0.2
Depreciation and amortisation		169.2	223.9
Impairment of goodwill and intangible assets	10	–	33.5
Reversal of impairment provision		–	(31.8)
Profit on sale of property, plant and equipment and intangible assets		(0.4)	(0.2)
Profit on divestments	28	(227.0)	(0.8)
Derivative financial instruments	22	19.7	(28.9)
Adjustments to revisions of the carrying values of other assets	3	–	(1.4)
Assessment of legal and other provisions	3	(1.7)	(8.0)
Pension contributions in excess of pension charges		(10.1)	(17.3)
Share based payments	27	5.8	5.5
Operating cash movements:			
Increase in inventories		(10.9)	(4.2)
Decrease/(increase) in contract assets		8.2	(28.8)
(Increase)/decrease in trade and other receivables		(13.9)	26.5
Increase in contract liabilities		67.7	18.4
Increase in trade and other payables		20.7	31.0
Increase/(decrease) in provisions		47.4	(42.2)
Cash generated from operations		186.1	282.3
Tax paid		(25.5)	(32.2)
Interest paid including make-whole fees		(43.5)	(41.6)
Interest received		8.2	6.7
Net cash from operating activities		125.3	215.2

Use of alternative cash flow performance measures

Free cash flow and operating cash flow are considered to provide a consistent measure of the operating cash flow of the Group's business. These alternative performance measures are used in internal management accounts and for decision making including capital allocation. In addition to underlying profit measures, underlying cash conversion is also used for internal incentive arrangements, and presenting this information allows users of the financial statements to better understand the way in which performance is targeted.

Definitions of operating cash flow measures

Free cash flow

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

Operating cash flow

Operating cash flow is free cash flow before payment of tax, interest and restructuring costs.

Reconciliation of operating cash flow measures

The Cash Flow Statement subtotal of net cash from operating activities is reconciled to alternative measures of cash flow, free cash flow and operating cash flow as follows:

£m	2018	2017
Net cash from operating activities per Cash Flow Statement	125.3	215.2
Purchase of property, plant and equipment	(63.4)	(69.0)
Purchase of intangible assets	(6.1)	(10.8)
Proceeds on disposal of property, plant and equipment	6.8	5.1
Business acquisition and divestment related costs paid	–	0.1
Free cash flow	62.6	140.6
Amounts related to prior periods restructuring programmes	–	9.9
Tax paid	25.5	32.2
Net finance costs paid	35.3	34.9
Operating cash flow	123.4	217.6

The operating cash conversion ratio is operating cash flow divided by underlying operating profit, excluding the share of post-tax results of joint ventures and associates:

£m	2018	2017 (restated)
Underlying operating profit excluding the share of post-tax results of joint ventures	195.6	213.3
Operating cash flow	123.4	217.6
Cash flow on exceptional items provided at 31 December 2016	103.0	66.6
Operating cash flow before net cash flow on exceptional items	226.4	284.2
Operating cash conversion including net cash flow on exceptional items	63%	102%
Operating cash conversion before net cash flow on exceptional items	116%	133%

The cash flow on exceptional items principally relates to the KC-46 contract.

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10. Intangible assets

	Arising on business combinations					
£m	Goodwill	Customer relationships	Technology based assets	Order book and trade names	Software and other	Total
Cost						
At 1 January 2017	1,318.4	623.9	279.1	5.1	99.9	2,326.4
Additions	—	—	—	—	10.6	10.6
Reclassified as held for sale	(186.0)	(93.5)	(94.9)	—	(1.3)	(375.7)
Derecognitions and disposals	—	(20.3)	(24.6)	(0.3)	(1.7)	(46.9)
Foreign exchange adjustments	(57.5)	(31.7)	(15.5)	(0.4)	(3.7)	(108.8)
Reclassifications	—	—	—	—	0.8	0.8
At 31 December 2017	1,074.9	478.4	144.1	4.4	104.6	1,806.4
Additions	—	—	—	—	6.6	6.6
Business divestments	(2.2)	—	—	—	(0.6)	(2.8)
Derecognitions and disposals	—	(74.4)	—	(0.3)	(3.5)	(78.2)
Foreign exchange adjustments	41.9	20.7	8.7	0.2	2.0	73.5
Reclassifications	—	—	—	—	1.5	1.5
At 31 December 2018	1,114.6	424.7	152.8	4.3	110.6	1,807.0
Accumulated amortisation and impairment						
At 1 January 2017	593.2	354.9	160.5	3.0	48.9	1,160.5
Amortisation charge for the year	—	101.5	36.7	0.7	10.8	149.7
Impairment provision	33.5	—	—	—	—	33.5
Reversal of impairment provision	—	(19.7)	(12.1)	—	—	(31.8)
Reclassified as held for sale	(152.9)	(61.3)	(72.3)	—	(1.1)	(287.6)
Derecognitions and disposals	—	(20.3)	(24.6)	(0.3)	(1.7)	(46.9)
Foreign exchange adjustments	(35.9)	(18.6)	(7.5)	(0.2)	(2.8)	(65.0)
Reclassifications	—	—	—	—	0.2	0.2
At 31 December 2017	437.9	336.5	80.7	3.2	54.3	912.6
Amortisation charge for the year	—	67.5	21.6	0.7	13.9	103.7
Eliminated on business divestments	—	—	—	—	(0.1)	(0.1)
Derecognitions and disposals	—	(74.4)	—	(0.4)	(3.2)	(78.0)
Foreign exchange adjustments	23.5	16.1	5.9	0.3	1.8	47.6
At 31 December 2018	461.4	345.7	108.2	3.8	66.7	985.8
Carrying amount						
At 31 December 2018	653.2	79.0	44.6	0.5	43.9	821.2
At 31 December 2017	637.0	141.9	63.4	1.2	50.3	893.8
At 1 January 2017	725.2	269.0	118.6	2.1	51.0	1,165.9

Customer relationships represent customer lists, customer contracts and the associated benefits of customer relationships recognised on acquisition.

Technology based assets represent trade secrets and processes, patented and unpatented technology, and know-how recognised on acquisition. Software and other intangible assets include both internally generated and purchased software together with purchased patents, licences, trademarks and also includes capitalised development costs with a carrying amount of £0.1m (2017: £0.1m).

Derecognition of intangible assets recognised on business combinations occurs when assets are fully amortised. Amortisation charged during the year relating to intangible assets recognised on business combinations was £89.8m (2017: £138.9m). This amortisation, together with the impairment provision of £33.5m and reversal of impairment of £31.8m in 2017, has been excluded from underlying measures as described in note 3. All amortisation charges are included within operating costs in the Income Statement.

Goodwill

Goodwill represents the premium paid on acquisitions in anticipation of future economic benefits from assets that are not capable of being separately identified and separately recognised, such as the value of the workforce, and is the only indefinite life intangible asset held by the Group. Goodwill must be allocated to CGUs for the purposes of reporting and accounting. CGUs are defined at the Sector level.

The carrying value of goodwill is allocated to the following Sectors:

£m	2018	2017
Communications and Connectivity	279.1	278.8
Mission Systems	91.5	89.8
Advanced Electronic Solutions	237.3	225.1
Aviation Services	45.3	43.3
Total	653.2	637.0

Annual impairment review (key estimation uncertainty)

A review of the carrying value of goodwill is completed at least once a year to ensure that it is not impaired. This requires estimation of the recoverable amounts of the CGUs to which the goodwill is allocated. This is determined from value in use calculations unless specific conditions at a CGU dictate otherwise.

Impairment tests on other intangible assets are undertaken if events occur which may indicate that these assets may be impaired. The carrying value of intangible assets is considered annually as part of the goodwill impairment exercise with reference to the value in use calculation of each CGU.

Estimating value in use requires the Group to make an estimate of the expected future cash flows from the CGUs and also to choose a suitable discount rate in order to calculate the present value of those cash flows. This is considered to be a source of estimation uncertainty at the balance sheet date, which may have a significant risk of causing a material adjustment to the carrying amount of intangible assets within the next financial year.

Key assumptions

The calculation of recoverable value for CGUs based on value in use includes the following key assumptions:

- Cash flow forecasts prepared by management and reviewed by the Board covering a three year period, updated where appropriate for more recent forecasts. These forecasts take into account the current and expected economic environment including factors such as continued uncertainty (e.g. Brexit), within some markets in which we operate. They also make assumptions about the demand for our products in our primary geographical markets, based on historic experience, available government spending and key current and future programme platforms. These cash flow projections do not include benefits or costs expected to arise from future restructuring or initiatives to enhance performance which have not yet commenced;
- Growth rates assumed after this period are based on long term GDP projections of the primary market for each business. The long term projections used are in the range 1.6% to 2.5% (2017: 1.5% to 2.5%);
- Cash flows are discounted using the Group's WACC, adjusted for country, cash flow and currency risks in the principal territories in which the CGU operates. These pre-tax discount rates are within the range 8.6% to 10.7% (2017: 8.6% to 10.5%);
- Cash flows include the impact of working capital and fixed asset requirements; and
- Cash flows include management charges which allocate central overheads to the CGUs.

There were no impairments in 2018. In 2017, £31.8m of a previous impairment of intangible assets held in the Communications and Connectivity sector was reversed with reference to the expected sale proceeds less costs to sell for the AvComm and Wireless test and measurement businesses. An impairment of £33.5m was made in 2017 in Aviation Services driven principally from the loss of the UK Defence Helicopter Flying School contract which expired during 2018.

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Sensitivity analysis

Sensitivity analysis has been performed on the CGUs, as described below:

	Background	Key financial assumptions	Cash flow dependencies	Sensitivity analysis
Communications and Connectivity	The largest elements of goodwill in Communications and Connectivity arose on the acquisition of Thrane & Thrane in 2012 and a number of Aerospace Communications businesses.	Projected cash flows for the next three years, with subsequent growth assumed at a rate of 1.9% were discounted at a pre-tax rate of 8.8%.	Cash flow projections assume growth in the satellite communications market for maritime products driven by availability of satellite capacity and aerospace products from regulatory changes and passenger connectivity demands.	If cash flows reduced by 20%, the discount rate increased by 200 basis points, or if the growth rate was zero, then no impairment losses would arise.
Mission Systems	Mission Systems' goodwill primarily arose on the acquisition of Carleton Technologies in 1987, Conax in 1998 and Koch in 2005.	Projected cash flows for the next three years, with subsequent growth assumed at a rate of 2.1% were discounted at a pre-tax rate of 10.2%.	Cash flow projections assume that major cash outflows associated with development programmes will finish within the next few years and be replaced with cash inflows from full rate production.	If cash flows reduced by 20%, the discount rate increased by 200 basis points, or if the growth rate was zero, then no impairment losses would arise.
Advanced Electronic Solutions	Advanced Electronic Solutions' goodwill includes part of the Aeroflex business acquired in 2014, the Trivec business acquired in 2011, the Lansdale business and the former M/A-COM businesses acquired in 2008, and the REMEC business acquired in 2005.	Projected cash flows for the next three years, with subsequent growth assumed at a rate of 2.1% were discounted at a pre-tax rate of 10.7%.	Cash flow projections assume a production ramp up on development programmes and successful execution of order backlog.	If cash flows reduced by 20%, the discount rate increased by 200 basis points, or if the growth rate was zero, then no impairment losses would arise.
Aviation Services	Aviation Services' goodwill includes that arising on the acquisition of FR Aviation together with the remaining goodwill, after the impairment charge made in 2017, that arose on the acquisition of the FB Group in 2013.	Projected cash flows for the next three years, with subsequent growth assumed at a rate of 2.4% were discounted at a pre-tax rate of 9.4%.	Cash flow projections assume that major contract bids or extensions, including Operational Awareness Training in the UK and Coastwatch in Australia, are successful.	If cash flows reduced by 20%, the discount rate increased by 200 basis points, or if the growth rate was zero, then no impairment losses would arise.

11. Property, plant and equipment

	Land and buildings			Plant and machinery (including aircraft and vehicles)	Fixtures, fittings, tools and equipment	Assets under construction	Total
£m	Freehold	Long leases	Short leases				
Cost							
At 1 January 2017	109.5	33.9	4.3	734.5	104.4	70.1	1,056.7
Additions	3.9	2.6	0.1	43.3	5.3	14.2	69.4
Disposals	(0.6)	—	—	(24.5)	(5.0)	(0.6)	(30.7)
Reclassified as held for sale	(7.1)	—	—	(33.4)	(2.8)	(0.2)	(43.5)
Foreign exchange adjustments	(6.0)	(1.6)	(0.2)	(19.8)	(3.6)	(0.9)	(32.1)
Reclassifications	2.0	(0.3)	—	49.3	0.9	(52.7)	(0.8)
At 31 December 2017	101.7	34.6	4.2	749.4	99.2	29.9	1,019.0
Additions	0.2	4.4	0.1	41.6	5.4	26.9	78.6
Business divestments	—	(0.8)	—	(0.1)	(0.2)	(0.1)	(1.2)
Disposals	(0.2)	—	—	(38.3)	(6.9)	(0.3)	(45.7)
Foreign exchange adjustments	3.4	1.4	0.2	(1.9)	1.4	0.9	5.4
Reclassifications	3.2	1.3	—	9.3	4.2	(19.5)	(1.5)
At 31 December 2018	108.3	40.9	4.5	760.0	103.1	37.8	1,054.6
Accumulated depreciation							
At 1 January 2017	37.7	21.2	3.3	499.2	72.4	—	633.8
Depreciation charge for the year	4.5	1.4	0.4	58.0	9.7	—	74.0
Eliminated on disposals	(0.5)	—	—	(20.8)	(4.9)	—	(26.2)
Reclassified as held for sale	(0.9)	0.1	—	(22.7)	(1.7)	—	(25.2)
Foreign exchange adjustments	(2.0)	(1.2)	(0.2)	(12.5)	(2.2)	—	(18.1)
Reclassifications	—	—	—	—	(0.2)	—	(0.2)
At 31 December 2017	38.8	21.5	3.5	501.2	73.1	—	638.1
Depreciation charge for the year	4.0	1.4	0.4	49.2	10.4	—	65.4
Eliminated on business divestments	—	(0.7)	—	(0.1)	(0.2)	—	(1.0)
Eliminated on disposals	(0.2)	—	—	(32.8)	(6.6)	—	(39.6)
Foreign exchange adjustments	1.1	0.8	0.2	0.3	1.1	—	3.5
At 31 December 2018	43.7	23.0	4.1	517.8	77.8	—	666.4
Carrying amount							
At 31 December 2018	64.6	17.9	0.4	242.2	25.3	37.8	388.2
At 31 December 2017	62.9	13.1	0.7	248.2	26.1	29.9	380.9
At 1 January 2017	71.8	12.7	1.0	235.3	32.0	70.1	422.9

At 31 December 2018, the Group had commitments for the acquisition of property, plant and equipment of £13.6m (2017: £13.8m).

The carrying amount of the Group's property, plant and equipment includes an amount of £12.5m (2017: £nil) in respect of aircraft held under finance leases. These assets are held as security against the finance lease liabilities as shown in note 19.

12. Investment properties

£m	2018	2017
Carrying amount at 1 January	2.4	3.6
Depreciation	(0.1)	(0.2)
Disposals	–	(0.4)
Reclassified as held for sale	–	(0.6)
Carrying amount at 31 December	2.3	2.4

The fair value of the Group's investment properties has been assessed to be £5.0m (2017: £5.0m). These values are based on management estimates using observable market data, taking into account current lease terms.

Property rental income earned by the Group from its investment properties amounted to £0.5m (2017: £0.7m), which is net of all direct costs associated with leasing the properties other than depreciation. The buildings held at 31 December 2018 are leased to commercial users under an operating lease with a 25 year term which expires in 2023.

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13. Inventories

£m	2018	2017 (restated)	1 January 2017 (restated)
Raw materials and consumables	174.5	182.3	210.7
Work in progress	141.2	118.5	116.9
Finished goods and goods for resale	48.1	39.8	42.5
Allowance for obsolescence	(87.8)	(86.4)	(86.1)
	276.0	254.2	284.0

Details of the restatement are set out in note 2.

All inventory is expected to be realised within the normal operating cycle of the businesses.

Obsolescence provision (key estimation uncertainty)

The nature of much of the Group's business means that inventory held can become technically obsolete. It is also necessary to hold additional spare parts in order to support key customers and programmes. Assessing the level of provision required for obsolete, slow moving and defective items of inventory is an area of estimation uncertainty which may have a significant effect on the carrying amount of inventory within the next financial year.

This allowance is reviewed by management on a regular basis and further amounts are provided or released as considered necessary. The amounts are generally determined based on factors which include ageing and known demand, reflecting assumptions concerning future orders and revenue streams. Subsequent events may give rise to these estimates being revised and, consequently, to the reversal of amounts previously provided.

During the year £14.2m (2017: £21.2m) was provided, £8.7m (2017: £4.5m) was utilised and £6.0m (2017: £6.2m) of the allowance for obsolescence was reversed.

The amount provided in the year represents the outcome of the key sensitivity, being changes in forecast customer demand against which production has been planned or undertaken. A 10% deterioration in the assumed immediate forecast demand would lead to an increased provision in the order of £5m (2017: £4m).

14. Financial instruments

The Group's financial assets and liabilities are categorised as follows:

£m	Note	At amortised cost	Fair value through profit or loss	At fair value through OCI	Derivatives used for hedging	Total carrying amount	Fair value
Financial assets							
Contract assets	15	186.9	—	—	—	186.9	186.9
Trade receivables	16	259.1	—	—	—	259.1	259.1
Loans and other receivables	16	62.6	—	—	—	62.6	62.6
Cash and cash equivalents	19	406.9	—	—	—	406.9	406.9
Derivative contracts (not hedge accounted)	22	—	1.8	—	—	1.8	1.8
Other financial assets	17	—	—	39.5	—	39.5	39.5
Financial liabilities							
Borrowings	19	(396.6)	—	—	—	(396.6)	(409.0)
Contract liabilities	15	(180.9)	—	—	—	(180.9)	(180.9)
Trade payables	20	(171.8)	—	—	—	(171.8)	(171.8)
Accruals	20	(127.3)	—	—	—	(127.3)	(127.3)
Other financial liabilities	20	(67.7)	—	—	—	(67.7)	(67.7)
Derivative contracts (not hedge accounted)	22	—	(20.8)	—	—	(20.8)	(20.8)
Hedging instruments							
Assets	22	—	—	—	22.8	22.8	22.8
Liabilities	22	—	—	—	(23.4)	(23.4)	(23.4)
Net financial liabilities at 31 December 2018						(8.9)	(21.3)
Financial assets							
Contract assets	15	190.2	—	—	—	190.2	190.2
Trade receivables	16	235.9	—	—	—	235.9	235.9
Loans and other receivables	16	60.5	—	—	—	60.5	60.5
Cash and cash equivalents	19	451.9	—	—	—	451.9	451.9
Derivative contracts (not hedge accounted)	22	—	13.2	—	—	13.2	13.2
Other financial assets	17	—	—	6.1	—	6.1	6.1
Financial liabilities							
Borrowings	19	(835.4)	—	—	—	(835.4)	(893.1)
Contract liabilities	15	(105.2)	—	—	—	(105.2)	(105.2)
Trade payables	20	(140.2)	—	—	—	(140.2)	(140.2)
Accruals	20	(140.9)	—	—	—	(140.9)	(140.9)
Other financial liabilities	20	(52.9)	—	—	—	(52.9)	(52.9)
Derivative contracts (not hedge accounted)	22	—	(17.4)	—	—	(17.4)	(17.4)
Hedging instruments							
Assets	22	—	—	—	22.2	22.2	22.2
Liabilities	22	—	—	—	(22.0)	(22.0)	(22.0)
Net financial liabilities at 31 December 2017 (restated)						(334.0)	(391.7)

Details of the restatement can be found in note 2.

Borrowings are held at amortised cost which equates to fair value except for the Group's fixed rate borrowings. At 31 December 2018, the fair value of those borrowings was £233.6m (2017: £743.7m) compared to their book value of £221.2m (2017: £686.0m). The fair value of the fixed rate borrowings and derivative financial instruments have been determined by reference to observable market prices and rates.

Gains and losses on derivative financial assets and liabilities held at fair value through profit or loss are shown in note 22.

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Offsetting financial assets and liabilities

Cash and cash equivalents as shown in the Balance Sheet include overdraft balances on currency cash pooling accounts which have been offset as the accounts will be settled on a net basis as described in note 24. Master netting agreements also cover all bank balances and derivative balances with the same counterparty. These do not meet the criteria for offsetting because the right to offset is only enforceable on the occurrence of future events such as a default and amounts presented in the Balance Sheet are therefore presented on a gross basis.

If full offsetting by counterparty were to be applied, the resulting net amounts would be as follows:

£m	Gross amounts before set off	Amounts set off in the Balance Sheet	Amounts as presented in the Balance Sheet	Amounts not set off in the Balance Sheet	Net amount
Financial assets					
Cash and cash equivalents	832.2	(425.3)	406.9	(17.4)	389.5
Derivative financial assets	24.6	–	24.6	(24.6)	–
Financial liabilities					
Bank overdrafts	(435.5)	425.3	(10.2)	10.2	–
Derivative financial liabilities	(44.2)	–	(44.2)	31.8	(12.4)
At 31 December 2018	377.1	–	377.1	–	377.1
Financial assets					
Cash and cash equivalents	943.7	(491.8)	451.9	(3.1)	448.8
Derivative financial assets	35.4	–	35.4	(30.6)	4.8
Financial liabilities					
Bank overdrafts	(491.8)	491.8	–	–	–
Derivative financial liabilities	(39.4)	–	(39.4)	33.3	(6.1)
At 31 December 2017	447.9	–	447.9	(0.4)	447.5

15. Contract balances

Contract assets

£m	2018	2017 (restated)	1 January 2017 (restated)
Within current assets	131.0	125.9	116.8
Within non-current assets	55.9	64.3	56.2
	186.9	190.2	173.0
£m	2018	2017 (restated)	1 January 2017 (restated)
Unbilled amounts related to goods and services transferred	159.6	156.4	134.2
Costs to fulfill a contract	27.3	33.8	38.8
	186.9	190.2	173.0

Unbilled amounts related to goods and services transferred are included in contract balances until they become unconditional, at which point they are transferred to trade receivables. Unbilled amounts arise when revenue is recognised prior to an invoice being raised to the customer; typically this arises when revenue is recognised over time as payments often have milestone payments conditional on customer acceptances on progress. During the year £114.3m (2017: £82.5m) of the opening contract asset was transferred to trade receivables; additional amounts of £103.8m were recognised as a contract asset during the year (2017: £111.3m) as a result of changes in the measure of progress of the satisfaction of performance obligations.

Costs to fulfill a contract relate to costs incurred in advance of the commencement of delivering performance obligations to the customer, principally in respect of certain air-to-air refuelling contracts and additional provisioning on service delivery contracts.

Contract liabilities

£m	2018	2017 (restated)	1 January 2017 (restated)
Advance payments from customers	180.9	105.2	104.3

Advance payments from customers relate to amounts received prior to transferring goods or services to the customer. Of the amount recognised at 31 December 2017, £55.6m (2017: £53.2m) has been recognised in revenue during the year. Advance payments of £125.4m (2017: £71.7m) have been received during the year and are included in the Balance Sheet. This includes £48.7m recognised subsequent to the agreement with Boeing on the KC-46 programme.

Details of the restatements can be found in note 2.

16. Trade and other receivables

Current

£m	2018	2017 (restated)	1 January 2017 (restated)
Trade receivables (net of allowance for expected credit losses)	259.1	235.7	307.5
Accrued income	—	5.6	0.7
Loans and other receivables	34.2	26.6	29.9
Prepayments	28.9	25.9	29.0
	322.2	293.8	367.1

Non-current

£m	2018	2017 (restated)	1 January 2017 (restated)
Trade receivables (net of allowance for expected credit losses)	—	0.2	—
Loans and other receivables	28.4	28.3	33.2
	28.4	28.5	33.2

Details of the restatement of trade and other receivables can be found in note 2.

Impairment of trade receivables

£m	2018	2017
Trade receivables	266.2	240.7
Allowance for expected credit losses	(7.1)	(4.8)
Net trade receivables	259.1	235.9

Movements in the allowance for expected credit losses for trade receivables during the year are as follows:

£m	2018	2017
At 1 January	4.8	10.5
Additional provision for expected credit losses	6.6	4.5
Trade receivables written off during the year	(3.8)	(2.8)
Unused amounts reversed	(0.6)	(5.2)
Unused amounts reversed (specific adjusting item, see note 3)	—	(1.4)
Reclassified as held for sale and business divestments	—	(0.4)
Foreign exchange adjustments	0.1	(0.4)
At 31 December	7.1	4.8

Provisions for credit losses were recognised during the year in relation to amounts receivable from specific customers. Where there has been a significant increase in the risk that amounts past due will not be paid, full provision for additional credit losses is made.

The Group has limited exposure to credit risk and has not experienced significant levels of credit losses during the current or previous years. At 31 December 2018, provisions for expected credit losses were required for only 3% (2017: 3%) of gross trade receivables. Information concerning management of credit risk is shown in note 24. A significant proportion of the Group's business is directly with government agencies or in respect of large government funded military programmes, where credit risk is considered to remain low.

Trade receivables at 31 December 2018 do not include any amounts in respect of the KC-46 contract, which, as a result of the agreement reached with Boeing announced on 19 February 2019, are now being offset against amounts payable to Boeing in 2019.

Other classes of financial assets within trade and other receivables do not include any overdue or impaired assets.

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17. Other financial assets

£m	Note	2018
At 1 January 2017 and 31 December 2017		6.1
Change in accounting policy – adoption of IFRS 9	2	39.0
At 1 January 2018		45.1
Revaluation losses recognised in OCI		(5.6)
At 31 December 2018		39.5

Other financial assets represent Cobham plc's investments in the equity of AirTanker Holdings Limited and AirTanker Services Limited which relate to the Voyager (FSTA) project. These are minority shareholdings which are not held for trading and as such as are held at fair value. The Group has elected to present subsequent changes in fair value in OCI.

The fair value of these assets has been assessed using a present value methodology. The inputs to this calculation are not based on observable market data and hence they fall within level 3 of the IFRS 13 fair value hierarchy.

Valuation of other financial assets (key estimation uncertainty)

Fair value is determined based on the estimated cash flows expected to be received, discounted to present value. The estimated cash flows are calculated using an income approach reflecting the cash flows available to the Company after repayment of debt capital and interest, taking into account operating and financing cash flows. The most significant assumptions concern the anticipated usage of aircraft, including the number and types of sorties flown. The fair value would decrease with lower than anticipated usage of the aircraft or a higher discount rate. A 10% decrease in flying hours would result in a 7% reduction in fair value and a 1% increase in discount rate would reduce the fair value by 6%. Other assumptions include interest and inflation rates, repayment of debt and the residual value of the aircraft.

18. Non-current assets and disposal groups held for sale

There were no non-current assets or disposal groups held for sale at 31 December 2018.

At 31 December 2017, the following assets and liabilities of the AvComm and Wireless test and measurement businesses were classified as held for sale. They were measured on a non-recurring basis at fair value based on the agreed selling price of US\$455m, less costs to sell.

£m	2017
Total assets classified as held for sale	171.7
Total liabilities associated with assets classified as held for sale	(49.1)
Total non-current assets and disposal groups held for sale	122.6

Further details of the divestment can be found in note 28.

19. Borrowings

£m	2018	2017
Current borrowings		
Bank overdrafts	10.2	–
Senior notes	46.5	–
Finance leases	1.9	0.1
	58.6	0.1
Non-current borrowings		
Bank loans	152.4	204.3
Senior notes	174.7	630.8
Finance leases	10.9	0.2
	338.0	835.3
Total borrowings	396.6	835.4

Bank loans and overdrafts

Bank loans comprise the following:

£m	Agreement date	Maturity date	Amount drawn		Undrawn facilities	
			2018	2017	2018	2017
Fixed rates						
US\$75m credit agreement	December 2008	–	–	55.2	–	–
Floating rates						
€131m and US\$40m loan agreements	May 2015	May 2020	148.8	145.5	–	–
€4m loan agreement	May 2015	May 2022	3.6	3.6	–	–
US\$45m multi-currency revolving facility	December 2017	December 2022	–	–	35.3	33.3
US\$450m multi-currency revolving facility	December 2017	December 2023	–	–	353.3	332.6
DKK320m multi-currency revolving facility	December 2017	December 2023	–	–	38.5	38.2
			152.4	204.3	427.1	404.1

Floating rate bank loans accrue interest at LIBOR or other appropriate benchmark plus margin. The US\$75m credit agreement was repaid and cancelled in January 2018. The maturity dates of the US\$450m and DKK320m multi-currency revolving facilities were extended by one year in November 2018.

Bank overdrafts are repayable on demand and accrue interest at floating rates.

Senior notes

At 31 December 2018, senior notes with a total principal value of US\$282.2m (£221.2m) (2017: US\$855.0m; £630.8m) were outstanding as set out below:

£m	Issue date	Maturity date	2018	2017
US\$930m fixed rate original amount comprising:				
US\$59.4m (originally US\$180m)	October 2014	October 2019	46.5	132.9
US\$82.5m (originally US\$250m)		October 2021	64.7	184.4
US\$140.3m (originally US\$425m)		October 2024	110.0	313.5
			221.2	630.8

Senior notes of US\$572.8m were repaid on 17 April 2018, incurring accelerated interest costs (make-wholes) totalling £20.4m as disclosed in note 6.

Finance leases

At 31 December 2018, the Group had the following obligations under finance leases:

£m	Minimum lease payments		Present value of minimum lease payments	
	2018	2017	2018	2017
Amounts payable under finance leases:				
Within one year	2.5	0.1	1.9	0.1
In the second to fifth years inclusive	11.7	0.2	10.9	0.2
	14.2	0.3	12.8	0.3
Less: future finance charges	(1.4)	–	n/a	n/a
Present value of lease obligations	12.8	0.3	12.8	0.3
Less: amount due for settlement within 12 months (shown under current liabilities)			(1.9)	(0.1)
Amount due for settlement after 12 months			10.9	0.2

The fair value of the finance leases is the present value of the minimum lease payments and is equal to the carrying amount as shown above. The lease obligations are denominated in Australian dollars. The Group's obligations under finance leases are secured by the lessors' title to the underlying leased assets as shown in note 11.

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Reconciliation of movements in net cash/(debt)

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

£m	Cash and cash equivalents	Bank overdrafts	Liabilities from financing activities			Net cash/(debt)
			Bank loans	Senior notes	Finance leases	
At 1 January 2017	236.2	–	(475.7)	(788.2)	(0.5)	(1,028.2)
Cash flows	277.2	–	–	–	–	277.2
Repayment of borrowings	–	–	266.5	92.9	0.2	359.6
Foreign exchange adjustments	(61.5)	–	4.9	64.5	–	7.9
At 31 December 2017	451.9	–	(204.3)	(630.8)	(0.3)	(383.5)
Cash flows	(72.8)	(10.2)	–	–	–	(83.0)
New finance leases	–	–	–	–	(14.7)	(14.7)
Repayment of borrowings	–	–	53.6	415.1	1.3	470.0
Borrowings of undertakings sold	–	–	–	–	0.3	0.3
Foreign exchange adjustments	27.8	–	(1.7)	(5.5)	0.6	21.2
At 31 December 2018	406.9	(10.2)	(152.4)	(221.2)	(12.8)	10.3

Financial covenants

The various borrowing agreements include both financial and non-financial covenants but do not contain any provisions for charges over Group assets. The terms of the financial covenants are based on adjusted IFRS results, as defined in the agreements. The financial covenant calculations as presented below are as defined in the senior note borrowing agreements and are included here to allow readers of these financial statements to better understand their interpretation.

Note that the figures presented below for 2017 have not been restated for the impacts of changes in accounting policies as these covenant ratios will not be retested.

Net cash/(debt) to EBITDA

£m	Note	2018	2017
Net cash/(debt) per Balance Sheet		10.3	(383.5)
Adjust to average exchange rates		0.1	(21.8)
Net cash/(debt) for covenant purposes		10.4	(405.3)
Operating profit per Income Statement		111.9	104.1
Specific adjusting items	3	84.2	106.2
Depreciation and amortisation not included within specific adjusting items	10, 11, 12	79.4	85.0
Restructuring costs included within underlying profit	5	12.3	7.5
Other adjustments		5.6	5.7
EBITDA for covenant purposes		293.4	308.5
Net debt to EBITDA ratio as calculated for financial covenants		n/a	1.3
Covenant condition – not more than		3.5	3.5

Interest cover

£m	Note	2018	2017
Operating profit per Income Statement		111.9	104.1
Specific adjusting items	3	84.2	106.2
Amortisation not included within specific adjusting items	10	13.9	10.8
Restructuring costs included within underlying profit	5	12.3	7.5
Other adjustments		6.2	5.7
EBITA for covenant purposes		228.5	234.3
Net finance costs per Income Statement		(40.9)	(37.2)
Other adjustments		22.3	2.5
Net finance costs for covenant purposes		(18.6)	(34.7)
Interest cover as calculated for financial covenants		12.3	6.8
Covenant condition – not less than		3.0	3.0

There have been no breaches of the terms of the borrowing agreements or defaults during the current or prior year.

20. Trade and other payables

Current liabilities

£m	2018	2017 (restated)	1 January 2017 (restated)
Trade payables	171.8	140.2	154.7
Other taxes and social security	28.6	25.4	28.2
Accruals	118.9	134.4	125.0
Other liabilities	57.4	47.8	35.7
	376.7	347.8	343.6

Details of the restatement can be found in note 2. Included in other liabilities is £18.4m (2017: £10.6m) related to interest on uncertain tax positions.

Non-current liabilities

£m	2018	2017 (restated)	1 January 2017 (restated)
Trade payables	–	–	0.5
Accruals	8.4	6.5	6.0
Other liabilities	10.3	5.1	5.6
	18.7	11.6	12.1

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21. Provisions

£m	2018	2017 (restated)	1 January 2017 (restated)
Current liabilities	93.1	121.7	139.2
Non-current liabilities	107.6	30.6	73.0
	200.7	152.3	212.2

Movements in provisions during the year are as follows:

£m	Contract loss provisions	Provisions related to businesses divested	Restructuring provisions	Warranty claims	Aircraft maintenance provisions	Other	Total
At 1 January 2018 (as originally stated)	89.7	5.9	17.6	14.8	2.7	25.1	155.8
Change in accounting policy – IFRS 15	(0.5)	–	–	(3.0)	–	–	(3.5)
At 1 January 2018 (restated)	89.2	5.9	17.6	11.8	2.7	25.1	152.3
Additional provisions in the year	126.8	0.6	13.0	7.8	0.2	11.0	159.4
Utilisation of provisions	(71.7)	–	(11.0)	(3.4)	(0.3)	(9.8)	(96.2)
Provisions released	(0.9)	–	–	(1.6)	(2.2)	(13.3)	(18.0)
Reclassifications	(3.2)	–	(1.0)	(0.1)	–	4.4	0.1
Foreign exchange adjustments	1.1	–	1.1	0.3	(0.1)	0.7	3.1
At 31 December 2018	141.3	6.5	19.7	14.8	0.3	18.1	200.7

Details of the restatement can be found in note 2.

Provisions released in the year include the release of £1.7m of other provisions (2017: £4.3m of provisions for warranty claims and £3.7m of other provisions) which have been excluded from underlying earnings as shown in note 3.

Contract loss provisions (key estimation uncertainty)

Contract loss provisions are recognised for onerous contracts when the expected benefits to be derived by the Group are lower than the forecasted unavoidable cost of meeting the related contractual obligations. The assessment of the amount provided is a source of estimation uncertainty which may have a significant effect on the carrying amount of these provisions within the next financial year. The estimated costs to complete including contingencies to cover the risks identified, the outcome of negotiations with customers, the amounts recoverable under these contracts and the risk of incurring penalties for not meeting challenging delivery schedules are all areas requiring management judgement and the Group may take account of the advice of experts in quantifying the expected costs of future adverse outcomes. Due to the inherent uncertainty associated with such matters, the timing and determination of the total costs or amount of any payments under any claims could differ from the amounts provided. These provisions are expected to be utilised within four years although, where there are uncertainties surrounding the timing of utilisation, they have been disclosed as current liabilities.

There are multiple sensitivities to be considered in assessing contract loss provisions, in particular the ability to achieve development milestone dates, the accuracy of cost estimates to complete contractual work and the ability to successfully invoice and collect cash from the end customer. It is not considered practical to provide sensitivities for each of these items, and potentially misleading to suggest each one can be considered separately, so this risk is disclosed as part of our contingent liabilities in note 30.

Other categories of provisions

Provisions related to businesses divested relate to longer term warranties given on the divestments completed in 2005 and during the year. Due to uncertainties surrounding the timing of settlement of these items, they have been disclosed as current liabilities.

Restructuring provisions relate to restructuring projects announced in the year together with onerous lease provisions arising from the restructuring of the Aeroflex businesses, which is now complete. Amounts carried forward are not expected to be fully settled until 2025.

Provisions for warranty claims are expected to be utilised within three years.

Aircraft maintenance provisions relate to significant periodic maintenance costs as well as return conditions for leased aircraft and are anticipated to crystallise within five years.

Other provisions include amounts provided in respect of legal claims and environmental obligations and are mostly expected to be settled within one year.

22. Derivative financial instruments

The fair values of derivative financial instruments are as follows:

£m	Foreign exchange derivatives – not hedged	Foreign exchange derivatives – hedging instruments	Inflation swap	Total
Non-current assets	0.2	22.8	–	23.0
Current assets	1.6	–	–	1.6
Current liabilities	(16.4)	–	–	(16.4)
Non-current liabilities	(4.4)	(23.4)	–	(27.8)
Fair value at 31 December 2018	(19.0)	(0.6)	–	(19.6)
Non-current assets	2.9	22.1	–	25.0
Current assets	10.3	0.1	–	10.4
Current liabilities	(11.8)	–	(0.4)	(12.2)
Non-current liabilities	(5.2)	(22.0)	–	(27.2)
Fair value at 31 December 2017	(3.8)	0.2	(0.4)	(4.0)

The movements in the fair values of derivative financial instruments during the year and their impact on the income statement and equity are as follows:

£m	Foreign exchange derivatives – not hedged	Foreign exchange derivatives – hedging instruments	Inflation swap	Interest rate swaps	Total
At 1 January 2017	(42.9)	0.3	(1.8)	(1.8)	(46.2)
Gain through income statement – not hedged	39.1	0.1	1.4	–	40.6
Gain/(loss) reclassified to income statement	–	(0.2)	–	0.7	0.5
Ineffectiveness of net investment hedge through income statement	–	0.2	–	–	0.2
Gain/(loss) through OCI – hedged items	–	(0.2)	–	1.1	0.9
At 31 December 2017	(3.8)	0.2	(0.4)	–	(4.0)
(Loss)/gain through income statement – not hedged	(15.2)	0.2	0.4	–	(14.6)
Loss reclassified to income statement	–	(0.3)	–	–	(0.3)
Ineffectiveness of net investment hedge through income statement	–	0.1	–	–	0.1
Loss through OCI – hedged items	–	(0.8)	–	–	(0.8)
At 31 December 2018	(19.0)	(0.6)	–	–	(19.6)

The majority of foreign exchange derivatives and the inflation swap are not accounted for using hedge accounting and movements in fair values are recorded in the Income Statement within operating costs. These fair value movements are excluded from underlying measures as described in note 3, except for gains of £4.9m (2017: £11.7m gain) arising from the movement in fair values of currency swaps which offset movements in currency balances held. In 2017, gains and losses arising on foreign exchange derivatives related to dividend flows within the Group were also excluded from the underlying results.

A small number of specific foreign exchange derivatives as detailed below are designated as cash flow hedging instruments or as hedging instruments for net investment hedging purposes, and hedge accounting is applied. The foreign currency forward contracts were de-designated as hedging instruments during the year. Ineffectiveness in the cash flow hedge and net investment hedge occurs when the critical terms do not match exactly with the critical terms of the hedging instrument, this is calculated using the hypothetical derivative method.

Notes to the Group Financial Statements

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The foreign exchange derivatives which are designated as hedging instruments are included in the Balance Sheet as follows:

£m	Cross-currency swaps – net investment hedge	Cross-currency swaps – cash flow hedge	Foreign currency forward contracts – cash flow hedge	Total
Non-current assets	–	22.8	–	22.8
Non-current liabilities	(23.4)	–	–	(23.4)
Fair value at 31 December 2018	(23.4)	22.8	–	(0.6)
Non-current assets	–	22.1	–	22.1
Current assets	–	–	0.1	0.1
Non-current liabilities	(22.0)	–	–	(22.0)
Fair value at 31 December 2017	(22.0)	22.1	0.1	0.2
Notional amount – currency	DKK977.7m	EUR131.0m		
Notional amount – sterling	£95.0m	£94.9m		

There have been no changes in the cross-currency swap contracts designated as hedging instruments during the year.

The Group uses net investment hedging to manage its exposure to DKK/GBP foreign exchange risk arising on its Danish kroner functional currency foreign operations. The hedging instrument comprises cross-currency swaps (pay DKK, receive GBP) with the hedged item being the total Danish kroner net assets of the Group's operations in Denmark. There is an economic relationship between the hedged item and the hedge instrument as the net investment hedge creates a translation risk that will match the foreign exchange risk on the currency borrowing. The Group has established a hedge ratio of 1:1 as the underlying risk of the hedging instrument is broadly the same as the hedged risk component.

The Group also has in place a cash flow hedge to manage the foreign exchange risk arising out of its foreign currency borrowings. The hedging instrument comprises a cross-currency swap (pay GBP, receive EUR). The hedge item is the €131m floating rate borrowing and the hedge ratio is 1:1.

Full details of the Group's financial instrument accounting policies and risk management strategies, objectives and policies are set out in the accounting policies in note 1 and in note 24, financial risk management.

23. Retirement benefit schemes

£m	2018	2017
Defined benefit scheme assets	746.4	816.3
Defined benefit obligations	(793.0)	(879.5)
	(46.6)	(63.2)

Pension expense included in employment costs in note 5 are as follows:

£m	2018	2017
Defined benefit schemes	4.1	0.7
Defined contribution schemes	31.7	37.4
	35.8	38.1

Within the expense amounts above, £0.5m (2017: £1.4m) was outstanding in respect of defined benefit schemes but not due for payment at 31 December 2018. In addition, £0.5m (2017: £1.1m) was outstanding in respect of defined contribution schemes but not due for payment at 31 December 2018.

Defined contribution schemes

The Group operates a number of defined contribution pension arrangements. Under a defined contribution pension arrangement the Group's contribution is fixed at a set percentage of employees' pay. The contributions are recognised as an employee benefit expense as the employee provides service to the Group. There is no legal or constructive obligation to pay any additional amounts into the funds.

Defined benefit schemes

The Group also operates a number of funded defined benefit schemes (where benefits are based on employees' length of service and average final salary), the most significant being the Cobham Pension Plan (CPP). The assets of all of these schemes are held separately from those of the Group in funds under the control of trustees. However, the Group is ultimately responsible for funding any shortfall in the obligations of the schemes to their members. All defined benefit schemes have been closed to new members since 2003 and the UK schemes were closed to future accrual from 1 April 2016.

Events during the year

During the year, there have been three major events affecting the Group's defined benefit schemes:

- The CPP completed its triennial valuation. As a result, deficit contributions reduced from £17.2m to £6.0m per annum, with effect from September 2018 and payable up to March 2024;
- The US scheme was closed to future accrual resulting in a gain on curtailment of £2.1m. This gain has been presented as a specific adjusting item within note 3; and
- In October 2018, the English High Court determined that UK defined benefit pension schemes with Guaranteed Minimum Pensions (GMP) must be equalised between men and women. The impact of this ruling on the UK schemes has been estimated at £5.5m and recognised as a past service cost. This has been calculated using the 'C2' method as the Company's current best estimate; the actual method of satisfying the obligations to the members of the pension plans will ultimately need to be agreed by the Company and the trustees of the pension plans. This cost has been presented as a specific adjusting item within note 3.

Risk management

The defined benefit schemes expose the Group to a number of risks, as described below:

- Volatility of investment returns. If the investment return is lower than future funding obligations from the Company will increase;
- Inflation risk. Deferred pensions and pensions in payment are subject to inflationary increases. A higher inflation rate will lead to higher defined benefit obligations;
- Changes in bond yields. Volatility in the financial markets can have a significant impact on corporate bond yields which are used to generate a discount rate assumption. Lower corporate bond yields will lead to higher defined benefit obligations; and
- Life expectancy risk. The schemes' obligations are to provide benefits for the life of the member and therefore increases in life expectancy will lead to higher defined benefit obligations.

The trustees seek to mitigate these risks and have entered into a number of buy-in arrangements where assets are transferred to an insurance company in return for a qualifying insurance policy which provides an income stream equivalent to the obligations to pensioners covered by the arrangement. The most significant buy-in arrangement relates to pensioners of the CPP as at 1 July 2013. This eliminates all of the above risks in relation to these liabilities except for the credit risk related to the insurance provider. In addition, the trustees have invested in liability driven investments that mitigate most of the remaining bond yield and inflation risks, on a technical provision basis. This is achieved by using a portfolio of gilts and swaps supported with investment grade credit instruments. These investments introduce the risk that a call for further investment may be made if inflation decreases or the bond yield increases, which is managed by maintaining sufficient liquid investments. Leverage and counterparty risks are managed by the fund investment managers. The remaining assets include significant investment in diversified growth funds which seek to manage investment risks.

Actuarial valuations

Actuarial valuations of the present value of the defined benefit obligations for the CPP are carried out on a triennial basis by qualified independent actuaries; the most recent valuation was as at 1 April 2018 recording a deficit of £37.8m. Actuarial valuations of other schemes have been carried out at regular intervals as required by the applicable country regulations. In the UK, within 15 months of each triennial valuation, the employer and the trustees are required to agree a schedule of contributions to ensure that the plan is fully funded over time on a suitably prudent basis. A new schedule of contributions has been agreed during the year for the CPP as explained in the events section above. The valuation of plan liabilities for triennial valuations are on a more prudent basis than that required by IAS 19 and therefore the schedule of contributions will address a higher deficit than that recorded on an IAS 19 basis. The Group expects to contribute £7.5m to its defined benefit pension schemes in 2019 and, under the current schedules of contributions, £7.5m each year until March 2024.

The actuarial valuations for all schemes were updated for accounting purposes to 31 December 2018 by qualified independent actuaries.

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Assumptions (source of estimation uncertainty)

A number of assumptions are made in assessing the costs and present value of the pension assets and liabilities, which include the discount rate, inflation and mortality rates. These are considered to be major sources of estimation uncertainty as comparatively small changes in the assumptions used may have a significant effect on the Group's financial statements within the next financial year. The Group uses published indices and independent actuarial advice to select the values of critical assumptions.

The principal financial assumptions used for the purpose of the actuarial valuations were as follows:

	2018		2017	
	UK schemes	USA scheme	UK schemes	USA scheme
RPI inflation assumption (rate of increase in pensions in payment unless overridden by specific scheme rules)	3.45%	3.00%	3.35%	3.35%
CPI inflation assumption (rate of increase in deferred pensions)	2.45%	2.00%	2.35%	2.35%
Discount rate	2.70%	4.11%	2.35%	3.47%

The mortality assumptions used for the CPP are based upon actuarial tables which reflect actual recent mortality experience and also allow for future mortality improvements. The mortality tables used to estimate life expectancy are known as 'SAPS CMI 17' (2017: SAPS CMI 16). In practical terms, this is demonstrated in the table below:

	Year of birth	Year age 65	Life expectancy
Male	1953	2018	87 years
Female	1953	2018	89 years
Male	1980	2045	90 years
Female	1980	2045	91 years

At 31 December 2018, it has been assumed that members will commute on average 25% (2017: 25%) of their pension for cash at retirement.

Sensitivity analysis

The sensitivity of scheme liabilities to changes in certain key assumptions, after adjusting for liabilities covered by insurance contracts, is provided below:

	Change in assumption	Change in liabilities
Discount rate	Increase by 1.0%	-10%
Inflation rate (both RPI and CPI)	Increase by 0.5%	+3%
Life expectancy	Increase by one year	+2%

If the change in assumptions were in the opposite direction to that shown above, the impact would be approximately symmetrical.

Movements in scheme assets and scheme liabilities

A summary of the movements in the net liability and the amounts recognised in the Income Statement and OCI are as follows:

£m	2018			2017		
	Scheme assets	Defined benefit obligations	Total	Scheme assets	Defined benefit obligations	Total
Current service cost included in administrative expenses	—	(0.7)	(0.7)	—	(0.7)	(0.7)
Past service cost included in administrative expenses	—	(5.5)	(5.5)	—	—	—
Gain on curtailment included in administrative expenses	—	2.1	2.1	—	—	—
Scheme administration expenses	(0.2)	—	(0.2)	(0.2)	—	(0.2)
Amounts recognised in operating profit	(0.2)	(4.1)	(4.3)	(0.2)	(0.7)	(0.9)
Net interest	19.2	(20.7)	(1.5)	20.8	(23.1)	(2.3)
Amounts credited/(charged) to other finance expense	19.2	(20.7)	(1.5)	20.8	(23.1)	(2.3)
Actual return less interest income on pension scheme assets	(63.5)	—	(63.5)	31.0	—	31.0
Experience gains and losses arising on scheme liabilities	—	17.3	17.3	—	(0.1)	(0.1)
Actuarial gains and losses arising from changes in financial assumptions	—	41.4	41.4	—	(34.8)	(34.8)
Actuarial gains arising from changes in demographic assumptions	—	13.7	13.7	—	11.3	11.3
Amounts recognised in OCI	(63.5)	72.4	8.9	31.0	(23.6)	7.4
Employer contributions	14.4	—	14.4	18.2	—	18.2
Settlements	(4.3)	4.3	—	—	—	—
Benefits paid	(36.5)	36.5	—	(41.8)	41.8	—
Amounts included in Cash Flow Statement	(26.4)	40.8	14.4	(23.6)	41.8	18.2
Exchange differences	1.0	(1.9)	(0.9)	(1.7)	3.1	1.4
Net movement in the year	(69.9)	86.5	16.6	26.3	(2.5)	23.8
Balance at start of year	816.3	(879.5)	(63.2)	790.0	(877.0)	(87.0)
Net liability at end of year	746.4	(793.0)	(46.6)	816.3	(879.5)	(63.2)
UK schemes	731.2	(764.2)	(33.0)	796.3	(844.6)	(48.3)
US scheme	15.2	(28.8)	(13.6)	20.0	(34.9)	(14.9)
Net liability at end of year	746.4	(793.0)	(46.6)	816.3	(879.5)	(63.2)

The cumulative amount of actuarial losses recognised in OCI since transition to IFRS is £232.2m (2017: £241.4m).

Of the net actuarial gain recognised in the year, the loss from changes in financial assumptions is primarily driven by the movements in the discount rate, while the gain from changes in demographic assumptions arises from the use of the latest mortality tables.

The actual loss on scheme assets was £44.3m (2017: gain £51.8m). The loss in 2018 reflects the use of liability driven investments which reduced significantly in value as the pension liabilities decrease, and the impact of the reduced value of the insurance contracts which are linked to the value of the underlying liabilities which are insured. The weighted average duration of the scheme liabilities is estimated to be 17 years.

Settlements relate to the purchase of annuities for certain members of the US pension plan.

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Scheme assets

The fair value of major categories of scheme assets, and as a percentage of total scheme assets, is as follows:

	2018		2017	
	£m	%	£m	%
UK equity instruments	11.0	1.5%	14.4	1.8%
Global equities	87.3	11.7%	92.3	11.3%
Liability driven investments	113.9	15.3%	149.5	18.3%
Corporate bonds	76.2	10.2%	87.0	10.7%
Private credit	34.2	4.6%	27.8	3.4%
Diversified growth funds	119.2	15.9%	127.8	15.6%
Insurance contracts	274.9	36.8%	313.7	38.4%
Other assets including cash	29.7	4.0%	3.8	0.5%
	746.4	100.0%	816.3	100.0%

Scheme assets do not include any of the Group's own financial instruments, nor any property occupied by, or other assets used by the Group. None of the scheme assets are quoted in an active market. The above, except for the insurance contracts assets, are pooled investment vehicles and are valued based on bid price for funds with bid/offer spreads, or single price where there are no bid/offer spreads based on valuations provided by the investment manager. Insurance contracts are valued based on the valuation of the liabilities insured.

Other retirement benefit schemes

The assets and liabilities of other immaterial retirement benefit schemes are as follows:

£m	2018		2017	
	Assets	Liabilities	Assets	Liabilities
French indemnity schemes	—	(6.2)	—	(5.8)
German based schemes	—	—	1.0	(1.5)
Norwegian based schemes	4.0	(4.3)	4.1	(3.9)
	4.0	(10.5)	5.1	(11.2)

Given their relative values, disclosure of the full reconciliation of movements in assets and liabilities is not provided. The actuarial loss for these schemes in the year to 31 December 2018, recognised in OCI, was £1.0m (2017: £nil). The net liabilities are included in other liabilities in note 20.

24. Financial risk management

The Group's multinational operations and debt financing expose it to a variety of financial risks which include the effects of changes in foreign currency exchange rates, interest rates, liquidity risk and credit risk. The Group has in place a risk management programme that seeks to limit the adverse effects on the financial performance of the Group by using foreign currency financial instruments, debt and other instruments. Other derivative financial instruments may be used from time to time to manage exposures such as inflation risk. The financial risk management policies agreed by the Board have not changed during the year and are summarised below. The Group does not trade in financial instruments.

Foreign currency risk

Foreign currency risk exposure and risk management strategy

The Group is based in the UK, reports in sterling and has significant investment in overseas operations in the USA, Australia and other European countries. As a result, the Group's Balance Sheet, including the net cash/(debt) position, can be affected by movements in these countries' exchange rates. The Group's policy is to reduce, or eliminate where practical, both structural and transactional foreign exchange risk and, consequently, the net foreign exchange gains and losses included in the Income Statement amounted to a loss of £6.6m (2017: £12.1m gain). The Group undertakes to manage the currency mix of debt and EBITDA so that they are broadly in line to mitigate the impact of currency fluctuations on the net debt to EBITDA financial covenant. All currency exposures are reviewed regularly and all significant foreign exchange transactions are approved by Cobham plc management.

The Group has the following exposure to foreign currency denominated monetary assets and monetary liabilities in the Balance Sheet, translated into sterling at the relevant year-end exchange rates:

£m	2018		2017	
	Monetary assets	Monetary liabilities	Monetary assets	Monetary liabilities
US dollars	623.5	(298.7)	577.6	(856.1)
Euro	100.4	(152.3)	101.7	(154.8)
Australian dollars	52.0	(20.0)	48.7	(3.6)
Danish kroner	11.9	(10.9)	9.3	(3.6)
Other currencies	26.7	(5.1)	36.3	(5.7)
	814.5	(487.0)	773.6	(1,023.8)
Sterling denominated monetary assets and liabilities	129.9	(171.8)	190.8	(76.9)
	944.4	(658.8)	964.4	(1,100.7)

Foreign currency borrowings are used to mitigate the impact of foreign currency exchange differences arising from the Group's overseas net assets. Monetary liabilities in the table above include US dollar borrowings of £253.0m (2017: £717.1m) which match exposures arising from currency denominated net assets.

On consolidation, the net assets of overseas subsidiaries (which include the monetary assets and liabilities shown in the table above) are translated at closing exchange rates and exchange differences arising are accounted for in OCI through the translation reserve (note 26).

Foreign currency derivative contracts are also used to manage exposure to currency risks as detailed below.

The Group is exposed to foreign currency risk in the Income Statement where individual subsidiaries hold non-functional currency monetary assets and liabilities, and when an operating unit makes sales and purchases in currencies other than its own functional currency. The Group undertakes a formal process to actively manage and mitigate this exposure through a combination of matching non-functional currency revenues and costs, matching non-functional currency monetary assets and liabilities, and through the use of forward contracts.

Group policy is that at least 80% of the next 12 months' forecast cash flows in non-functional currencies are covered by forward foreign exchange contracts. For shorter cycle businesses, the profile of hedging is based on customer commitments which are subject to approval by the Group CFO. Where forecasted currency cash flows do not arise this will result in increased income statement exposure to foreign currency exchange differences. These are however managed at a Group level and mitigating action is taken where possible. Hedge accounting is not applied for these forward foreign exchange contracts.

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The most important exchange rates for the Group are sterling/US dollar and Danish krone/US dollar. The Group has the following forward foreign currency contracts outstanding for net sales of US dollars for sterling and Danish kroner:

	US\$m amount		Average US\$: £ exchange rate	
	2018	2017	2018	2017
Expiring within one year	98.9	119.4	1.37	1.37
Expiring within one to two years	28.4	85.3	1.38	1.36
Expiring after two years	25.1	29.5	1.49	1.50
US\$/sterling contracts outstanding at 31 December	152.4	234.2	1.39	1.38

	US\$m amount		Average US\$: DKK exchange rate	
	2018	2017	2018	2017
Expiring within one year	74.7	85.5	5.93	6.34
Expiring within one to two years	0.6	0.5	6.08	6.20
Expiring after two years	0.6	1.2	5.95	6.01
US\$/DKK contracts outstanding at 31 December	75.9	87.2	5.93	6.34

The latest expiry date of forward foreign currency contracts for sales of US dollars is June 2023 and it is the Group's current belief that the net dollar receipts by subsidiaries will exceed the level of the outstanding commitments.

Sensitivity analysis

Financial instruments denominated in a currency other than the functional currency in which they are measured create exposure to foreign currency exchange rate risk. These financial instruments include the monetary assets and liabilities and the forward foreign currency contracts shown in the tables above. The sensitivity arising on these financial instruments from a weakening in sterling against the respective foreign currency at the balance sheet date is set out below, with a negative number indicating a reduction in profit after taxation or total equity.

£m	2018			2017		
	Sensitivity	Profit or loss	Total equity	Sensitivity	Profit or loss	Total equity
US dollars to sterling	12%	(19.4)	(19.4)	12%	(23.1)	(23.1)
US dollars to Danish kroner	12%	(1.7)	(1.7)	12%	(6.1)	(6.1)
Euro to sterling	13%	(7.9)	(7.9)	12%	(10.6)	(10.6)

The sensitivities used represent management's assessment of the possible changes in foreign exchange rates, based on experience over the previous five years. These potential changes are, however, hypothetical and actual rates in future may differ significantly as a result of developments in global financial markets. This sensitivity analysis has been based on the assumption that all other variables, including interest rates, remain constant.

Use of hedging

As detailed in note 22, the Group uses net investment hedging to manage its exposure to DKK/GBP foreign exchange risk arising on its DKK functional currency foreign operations. Exposure to foreign exchange risk arising out of the Group's foreign currency borrowings is also managed using cross-currency swaps designated as hedging instruments in a cash flow hedge. Further details on the use of foreign exchange derivative financial instruments in hedge relationships can be found in note 22.

Interest rate risk

The Group has borrowings with a range of maturities at both fixed and floating rates of interest. In managing its borrowing costs, the Group monitors its exposure to movements in interest rates, having regard to prevailing market conditions and, where necessary, uses interest rate swaps to manage the interest rate risk. At 31 December 2018, the Group does not have any interest rate swaps outstanding.

All floating rate borrowings have regular repricing dates.

£m	2018	2017
Senior notes	221.2	630.8
Bank loans at fixed rate	–	55.2
Fixed rate borrowings	221.2	686.0
Bank loans and overdrafts	162.6	149.1
Finance leases	12.8	0.3
Floating rate borrowings	175.4	149.4
Total borrowings	396.6	835.4

Surplus funds are placed on short term fixed rate deposit and as such also give rise to interest rate exposure. There was no material sensitivity to changes in interest rates at the year end.

Liquidity risk

The Group's policy on managing liquidity risk throughout the year has been to maintain a mix of short, medium and long term borrowings with lenders. Overdraft and revolving credit facilities provide short term flexibility whilst the revolving credit facilities provide longer term committed funding.

As shown in note 19, at 31 December 2018 undrawn committed borrowing facilities of £427.1m (2017: £404.1m) were available to the Group in various currencies.

At an operating level, the Group has a positive cash flow from operating activities and where practical the funds generated by business units are managed on a regional basis. In the UK and USA, most business units utilise local banking facilities within a UK or US group arrangement. This allows a balance to be maintained between continuity of funding, security and flexibility.

The table below summarises the remaining contractual maturity for the Group's borrowings and other financial liabilities. The amounts shown are the contractual undiscounted cash flows which include interest, analysed by contractual maturity. The difference between the contractual cash flows and the carrying amount of these liabilities reflects the effects of interest not included in the carrying amount and discounting applied in assessing fair value.

£m	Within one year	1-2 years	2-5 years	Over 5 years	Total
Non-derivative financial liabilities					
Borrowings	72.4	159.6	94.2	114.0	440.2
Trade and other payables	490.2	22.9	23.1	9.6	545.8
	562.6	182.5	117.3	123.6	986.0
Less discounting of finance leases					(1.5)
At 31 December 2018					984.5

Derivative liabilities

Foreign exchange derivatives					
Gross cash outflows	417.1	181.7	23.5	–	622.3
Gross cash inflows	(400.7)	(156.9)	(21.0)	–	(578.6)
At 31 December 2018	16.4	24.8	2.5	–	43.7

Non-derivative financial liabilities

Borrowings	35.0	85.6	521.5	338.7	980.8
Trade and other payables (restated)	387.5	19.6	17.9	9.8	434.8
At 31 December 2017	422.5	105.2	539.4	348.5	1,415.6

Derivative liabilities

Foreign exchange derivatives					
Gross cash outflows	381.6	31.5	31.0	–	444.1
Gross cash inflows	(370.2)	(29.0)	(28.4)	–	(427.6)
Inflation swap	0.4	–	–	–	0.4
At 31 December 2017	11.8	2.5	2.6	–	16.9

Details of the restatement can be found in note 2.

Notes to the Group Financial Statements

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Credit risk

The Group's principal financial assets are bank balances, contract assets, trade and other receivables and derivative financial instruments. There are no significant concentrations of credit risk. The Group is exposed to credit risk on these balances through its operating activities as the counterparties involved may not meet their obligations under the contract or financial instrument, leading to a financial loss.

The Group has a conservative policy towards the credit risk related to liquid funds and derivative financial instruments with balances currently spread across a range of reputable financial institutions. The levels of credit risk are monitored through the Group's ongoing risk management processes, which include a regular review of the banks' credit ratings. Risk in this area is limited further by setting a maximum level for term deposits with any one counterparty.

Concentrations of credit risk with respect to trade receivables are limited due to the Group having a large customer base. Customers are typically large global companies or government agencies with long term trading relationships. The Group also has in place procedures that require appropriate credit checks on potential customers before sales are made and any requests for extended credit are approved by senior management. Letters of credit are obtained where necessary from reputable banks and financial institutions. Existing customer accounts are monitored on an ongoing basis and appropriate action is taken where necessary to minimise any credit risk. No further credit risk provision is required in excess of the provision for impaired receivables shown in note 16.

Group management monitor debtor days and the ageing of receivables which are more than one month overdue on a regular basis. At 31 December 2018, 23.5% (2017: 23.9%) of gross trade receivables were overdue including 6.8% (2017: 8.7%) which were overdue by one month or more.

The maximum exposure to credit risk at 31 December 2018 is the fair value of financial assets as disclosed in note 14.

Finance leases totalling £12.8m (2017: £0.3m) are secured against the items of property, plant and equipment that the leases are financing, as disclosed in notes 11 and 19. Group assets have not been pledged in respect of the Group's primary borrowing facilities or other financial liabilities.

Bank term balances totalling £5.8m (2017: £7.0m) have been pledged against the residual value of leased assets under an agreement which expires in 2020.

The Group has master netting arrangements in respect of bank balances in the UK. In the normal course of business, these bank accounts are settled on a net basis within each currency and as such are presented net in the Balance Sheet as shown in note 16. In the event of an automatic enforcement event, the bank balances are set off against each other to achieve a net position. Derivatives can also be offset by counterparties in the event of a default; net amounts that result on this basis are also shown in note 14.

Inflation risk

The Group's exposure to inflation is considered to be a general business risk which is mitigated through normal commercial activity. The Group has previously used an inflation swap contract to manage the inherent inflation risk in a specific operational contract which was completed during 2018. The fair value of this swap contract is included in derivative financial instruments shown in note 22.

Capital risk management

Capital is defined as total equity excluding non-controlling interests and amounted to £1,190.2m at 31 December 2018 (2017: £1,031.1m restated).

During 2018, Group policy was to maintain a strong capital base so as to maintain shareholder confidence and to sustain future development of the business.

Subsequent to the year end, the Board has agreed a capital allocation policy for the Group which will lie at the core of a disciplined approach to investment and value creation. Priorities for capital allocation are as follows:

1. Organic investment. Investing in businesses we know and understand is the best way to deliver shareholder value. We will invest for capability enhancement and growth, including in technology and people and on capital expenditure for equipment and infrastructure, as well as for the resolution of legacy items;
2. Dividends. The Board intends to reinstate an ordinary dividend payment with the 2019 interim results. It intends to follow a progressive policy which will take into consideration the profitability and underlying growth of Cobham's businesses and its capital requirements, while ensuring an appropriate level of earnings and free cash flow cover. It anticipates announcing a first full year dividend of 1.0p. Approximately 40% of the full year dividend will be paid at the interim stage;
3. Mergers and acquisitions. We will carefully consider bolt-on size business acquisitions and other investments where there is a strong strategic fit and management bandwidth to properly integrate;
4. Shareholder returns. If, after such investments and distributions there is surplus capital, the Board would look to return cash to shareholders.

The Board has previously set a net debt/EBITDA threshold of 1.5x following the need to strengthen the Balance Sheet through the rights issue in 2017. This is still considered to be the appropriate target in order to maintain the strength of the Balance Sheet.

25. Share capital

	Number of 2.5p shares	Share capital £m	Share premium £m
At 1 January 2017	1,783,815,575	44.6	778.3
Issued in the year to 31 December 2017	683,145,540	17.1	479.6
At 31 December 2018 and 2017	2,466,961,115	61.7	1,257.9

Shares were issued on 4 May 2017 as a result of a 2 for 5 fully underwritten rights issue at an issue price of 75 pence per share. Net proceeds of £496.7m were realised after costs of £15.7m.

As at 31 December 2018, 85,300,412 (2017: 88,427,023) ordinary shares were held in treasury including 9,348,688 (2017: 12,475,299) shares held in the Cobham Employee Benefit Trust. At 31 December 2018, the market value of treasury shares was £83.4m (2017: £111.7m), including shares with a market value of £9.1m (2017: £15.8m) held by the Cobham Employee Benefit Trust.

Treasury shares are used to satisfy awards and options under the Group's share based payment schemes. Receipts from option exercises are included in retained earnings and total equity.

Further details of the share capital of Cobham plc can be found in the Directors' Report on page 81.

26. Other reserves

£m	Note	Translation reserve	Hedge reserve	Share based payment reserve	Total other reserves
At 1 January 2017		16.5	(0.3)	21.7	37.9
Foreign exchange differences on translation of overseas operations (restated)		(51.4)	–	–	(51.4)
Movements on cash flow hedges – interest rate swaps	22	–	1.1	–	1.1
Movements on cash flow hedges – foreign exchange contracts		0.5	(0.7)	–	(0.2)
Reclassification of fair value of cash flow hedges to income statement		–	0.5	–	0.5
Transfer reserves on settlement of cash flow hedge contracts		0.1	(0.1)	–	–
Share based payments recognised in reserves	27	–	–	5.5	5.5
Transfer of share based payment reserve on exercise		–	–	(2.9)	(2.9)
Tax effects		–	(0.1)	–	(0.1)
At 31 December 2017 (restated)		(34.3)	0.4	24.3	(9.6)
Foreign exchange differences on translation of overseas operations		57.2	–	–	57.2
Reclassification of foreign exchange on divestment of overseas operations	28	(15.8)	–	–	(15.8)
Movements on cash flow hedges – foreign exchange contracts		(0.3)	(0.5)	–	(0.8)
Reclassification of fair value of cash flow hedges to income statement		–	(0.3)	–	(0.3)
Share based payments recognised in reserves	27	–	–	5.8	5.8
Transfer of share based payment reserve on exercise		–	–	(4.0)	(4.0)
Tax effects		(0.2)	0.1	(0.1)	(0.2)
At 31 December 2018		6.6	(0.3)	26.0	32.3

Details of the restatement can be found in note 2.

The translation reserve comprises all foreign exchange differences arising on the results and financial position of subsidiaries whose functional currencies differ from the Group's reporting currency together with foreign exchange movements arising on interest rate swaps and foreign exchange derivatives designated as hedge instruments.

The hedge reserve reflects movements in fair values on cash flow hedging derivatives as detailed in notes 22 and 24.

The share based payment reserve includes the cost of awards as assessed under IFRS 2 and detailed in note 27, together with related deferred tax provided under IAS 12. The appropriate proportion of this reserve is transferred to retained earnings following vesting or exercise.

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27. Share based payments

The Group offers a number of long term incentive schemes which provide a mix of performance based incentive and retention awards as described below and in the Directors' Remuneration Report on page 71. All schemes are equity settled.

The Long Term Incentive Plan is offered to senior executives across the Group and allows for annual grants of Performance Share Plan (PSP) or Restricted Share Plan (RSP) awards. PSP awards are conditional shares and nil-cost options with vesting conditions based on the Group's financial performance, taking into account non-market based measures such as EPS and cash conversion. In previous years, awards have also included market based conditions such as TSR growth. The scheme includes retention awards granted from time to time to specific personnel and buy-out awards granted to key new starters, vesting after a maximum of three years conditional only upon continued employment within the Group. RSP awards provide conditional shares which vest solely on continued employment within the Group over a maximum of four years.

The Group also operates a Save As You Earn (SAYE) scheme which is open to all UK employees and has previously offered share options under the Cobham Employee Share Option Scheme (ESOS) which are fully vested with exercise prices in the range £1.359 to £1.826.

The total amount included in the Income Statement arising from share based payment schemes is as follows:

£m	2018	2017
PSP	3.2	1.4
RSP	2.0	3.4
SAYE	0.6	0.7
	5.8	5.5

The number of awards outstanding at 31 December under each scheme are as follows:

Number of awards (thousands of shares)	2018	2017
PSP	18,484	13,597
RSP	2,692	5,052
SAYE	5,388	8,372
ESOS	2,675	3,484
At 31 December	29,239	30,505

PSP

Number of awards (thousands of shares)	2018	2017
At 1 January	13,597	9,998
Awards granted	11,918	8,405
Effect of rights issue	—	853
Awards forfeited or cancelled	(6,274)	(5,487)
Exercised	(757)	(143)
Expired	—	(29)
At 31 December	18,484	13,597

Weighted average share price at date of exercise	£1.220	£1.390
Weighted average remaining contractual life of PSP awards outstanding	1.8 years	1.7 years
Number of PSP awards exercisable at 31 December (thousands)	34	26

Awards granted in the year under the PSP scheme were mainly granted in May 2018 with an average fair value of £1.218 (2017 awards: £1.319). There is no exercise price for these awards. Fair values are calculated using the Black-Scholes option pricing model. The weighted average inputs into the model were as follows:

	2018	2017
Weighted average share price	£1.218	£1.381
Expected life	3.0 years	2.9 years
Expected employee cancellation rate	5.0%	3.1%
Risk free rate	n/a	0.3%

The expected lives used in the models have been adjusted, based on management's best estimate, for the effects of non-transferability and behavioural considerations. The expected employee cancellation rates are based on assessments of historic rates of voluntary cancellations of contracts by employees. Dividend yields were nil or were not relevant to the valuation model where participants of the vested awards receive the benefit of dividend equivalent payments.

RSP

Number of awards (thousands of shares)	2018	2017
At 1 January	5,052	3,618
Awards granted	372	3,200
Effect of rights issue	–	524
Awards forfeited or cancelled	(687)	(455)
Exercised	(2,041)	(1,823)
Expired	(4)	(12)
At 31 December	2,692	5,052
Weighted average share price at date of exercise	£1.059	£1.240
Weighted average remaining contractual life of RSP awards outstanding	1.1 years	1.5 years
Number of RSP awards exercisable at 31 December (thousands)	153	4

Awards granted in the year under the RSP scheme were granted in May and September 2018 with an average fair value of £1.240 (2017 awards: £1.375) to specific senior management. Fair values are calculated using the Black-Scholes option pricing model and equate to the market price on the date of grant.

28. Business divestments

The completion of the divestment of the Group's AvComm and Wireless test and measurement businesses, part of the Communications and Connectivity Sector, was announced on 16 March 2018, for an all-cash consideration of US\$455m (subject to certain post-completion adjustments and expenses). In the Group consolidated financial statements for the year to 31 December 2017, the assets and liabilities of these businesses were classified as held for sale and were measured on a non-recurring basis at fair value.

In addition, the Group disposed of the trade and assets of its Opera electromagnetic simulation software business on 25 May 2018. The disposal of the trade and assets of the Lightning Test and Consultancy business was completed on 14 November 2018. Both businesses were formerly within the Communications and Connectivity Sector.

The profit on these divestments has been excluded from underlying operating profit as disclosed in note 4 and analysed below.

£m	AvComm and Wireless	Opera and Lightning Test	Total
Gross consideration	324.2	9.7	333.9
Net assets at date of divestment	(117.3)	(2.1)	(119.4)
Expenses of sale	(11.9)	(0.5)	(12.4)
Foreign exchange adjustments	23.4	–	23.4
Net profit on divestments completed during the year	218.4	7.1	225.5
Net profit relating to divestments completed in prior years			1.5
Net profit on divestments before tax			227.0
Tax charge on net profit on divestments			(11.7)
Net profit on divestments after tax			215.3

The net cash impact of the divestments during the year is as follows:

£m	AvComm and Wireless	Opera and Lightning Test	Total
Cash consideration	325.6	9.7	335.3
Expenses of sale	(11.1)	(0.2)	(11.3)
Net cash impact of divestments in current year	314.5	9.5	324.0
Net cash relating to divestments completed in prior years			0.7
			324.7

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The net assets at the date of divestment were as follows:

£m	AvComm and Wireless at 16.3.2018	Opera and Lightning Test at 25.5.2018 and 14.11.2018	Total
Intangible assets	86.4	2.7	89.1
Property, plant and equipment	18.5	0.2	18.7
Investment property	0.6	—	0.6
Inventories	18.8	—	18.8
Trade and other receivables	39.8	0.3	40.1
Cash and cash equivalents	0.7	—	0.7
Borrowings (finance lease)	(0.3)	—	(0.3)
Trade and other payables	(24.7)	—	(24.7)
Contract liabilities	(9.6)	(1.1)	(10.7)
Current tax liabilities	(5.0)	—	(5.0)
Provisions	(0.7)	—	(0.7)
Deferred tax liabilities	(7.2)	—	(7.2)
Net assets	117.3	2.1	119.4

The net assets of the divested businesses at 31 December 2017 were as follows:

£m	AvComm and Wireless	Opera and Lightning Test	Total
Intangible assets	88.1	1.3	89.4
Property, plant and equipment	18.3	0.3	18.6
Investment property	0.6	—	0.6
Deferred tax assets	3.8	—	3.8
Inventories	20.3	—	20.3
Trade and other receivables	40.6	0.9	41.5
Borrowings	(0.3)	—	(0.3)
Trade and other payables	(23.8)	(0.1)	(23.9)
Contract liabilities	(13.4)	(0.9)	(14.3)
Provisions	(1.0)	—	(1.0)
Deferred tax liabilities	(10.6)	—	(10.6)
Net assets	122.6	1.5	124.1

As noted above and in note 18, the net assets of the AvComm and Wireless test and measurement businesses were presented as assets and liabilities held for sale at 31 December 2017.

29. Operating lease arrangements

At the balance sheet date, the Group had outstanding commitments for minimum lease payments due under non-cancellable operating leases as follows:

£m	2018	2017
Within one year	24.1	28.3
Between one and two years	19.5	24.7
Between two and three years	15.8	17.5
Between three and four years	11.3	16.0
Between four and five years	9.5	13.7
After five years	58.3	66.9
	138.5	167.1

Operating lease commitments include £10.0m (2017: £17.6m) related to onerous leases which have been provided for at the balance sheet date.

Operating lease payments during the year totalled £25.0m (2017: £35.7m) including rental costs of £1.2m (2017: £8.6m) relating to operational aircraft used in the Group's service businesses; the remainder primarily relates to the rental of office and operating facilities.

30. Contingent liabilities

The Group makes provisions when it is probable there will be a cash outflow to settle liabilities and it can be reliably estimated. Contingent liabilities are potential future cash outflows which are less certain or cannot be measured reliably. The disclosure below is intended to highlight potential risks that are not provided for in the Balance Sheet.

At 31 December 2018, the Company and the Group had contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the ordinary course of business. Where it is expected that a material liability will arise in respect of these matters, appropriate provision is made within the Group Financial Statements.

The Company and various of its subsidiaries are, from time to time, parties to various legal proceedings and claims and management do not anticipate that the outcome of these, either individually or in aggregate, will have a material adverse effect upon the Group's financial position.

The nature of much of the contracting work done by the Group means that there are reasonably frequent contractual issues, variations and renegotiations that arise in the ordinary course of business, whose resolution is uncertain and could materially impact the Group's future reported earnings. In particular, on fixed price and fixed fee development contracts, costs incurred and anticipated can significantly exceed amounts estimated as a result of material enhancements to the specifications originally agreed under the contracts. Also, there are onerous contract terms and challenging delivery schedules on air-to-air refuelling development contracts. The Group may take account of the advice of experts as required in making judgements on contractual issues and whether the outcome of negotiations will result in an appropriate recovery of costs. Judgement is therefore required as regards the estimated costs to complete, the outcome of negotiations with customers and the amounts recoverable under these contracts. The amount recoverable may be subject to direct damages due to the customer and damages or penalties they incur from their own end users. In the case where the Group is undertaking development activity at its own cost, including production and service readiness, and has given performance undertakings to prospective customers, then a liability for losses consequent upon the failure to meet such undertakings could exist.

The Group is subject to corporate and other tax rules in the jurisdictions where it conducts its business operations. Changes in tax rates, tax reliefs and tax laws, changes in practice or interpretation of the law by the relevant tax authorities, increasing challenges by relevant tax authorities on transfer pricing and other matters, or any failure to manage tax risks adequately could result in increased charges, financial loss, penalties and reputational damage, which may materially adversely affect the Group's financial condition and results of operations.

In addition, tax enforcement has become a higher priority for many tax authorities in jurisdictions in which the Group operates, which has led to an increase in tax audits, enquiries and challenges, or the testing through litigation of the boundaries of the correct interpretation of legislation. Tax authorities may also actively pursue additional taxes based on retroactive changes to tax laws and the Group may have disagreements with tax authorities which could result in a material restatement to the tax position. For example, the availability of certain interest deductions on one of the Group's internal financing arrangements, principally as a result of various US acquisitions, has been under challenge for some time. Over the life of this internal financing arrangement, the aggregate tax value of the interest deductions amounted to approximately £130m. If decided adversely to the Group, this could lead to increased tax liabilities in excess of those provided in the Group's Balance Sheet, and result in a substantial tax payment becoming due. That payment may also result in an additional interest charge from the relevant authority. The Group is actively involved in attempting to resolve this matter ahead of a Tribunal hearing, which is scheduled for autumn 2019.

The European Commission (EC) has opened an investigation into the UK's controlled foreign company (CFC) rules. The CFC rules levy a charge on foreign entities controlled by the UK that are subject to a lower rate of tax, however there is currently an exemption available for 75% of this charge if the activities being undertaken by the CFC relate to financing. The EC is investigating whether this exemption is in breach of EU State Aid rules, but it is too early to assess what the conclusions of this investigation might be. If there is an adverse final determination on the UK's CFC legislation, the Group estimates that its maximum exposure on this matter is approximately £60m.

31. Related party transactions

During the year, £0.4m (2017: £0.4m) of goods were purchased from and £nil (2017: £nil) of goods were sold to joint ventures and associates. There were no other material transactions between Group entities and related parties during the current or previous year. Group policy is for all transactions with related parties to be made on an arm's length basis and no guarantees have been given to, or received from, related parties.

Details of the compensation of key management personnel can be found in note 5.

The Directors of Cobham plc had no material transactions with the Company during the year, other than as a result of service agreements. Details of Directors' remuneration are disclosed in the Directors' Remuneration Report on pages 71 to 80.

32. Events after the balance sheet date

On 19 February 2019, Cobham announced that it had reached an agreement with Boeing on damages assertions relating to the KC-46 Tanker programme. As detailed on page 7 and in note 3, an additional non-underlying charge of £160.0m has been included in these financial statements as this agreement represents an adjusting event occurring after the balance sheet date.

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33. Subsidiaries and other related undertakings

The Group operates through a number of subsidiary undertakings and a full listing of these as at 31 December 2018 is provided below. The Group owns 100% of the share capital of all subsidiaries with the exception of TEAM SA (98.7% owned).

The Group also has interests in a small number of joint ventures and one associated undertaking which are included in the list below. The joint ventures and associates all have share capital consisting solely of ordinary shares, which are indirectly held, and the country of incorporation or registration is also their principal place of operation. No further disclosures are provided concerning the assets and results of the joint ventures or associated undertaking on the basis of materiality.

Name of undertaking	Address of registered office or equivalent
Aedion Investments Unit Trust	26 New Street, St Helier, Jersey JE2 3RA
Aeroflex Holding Corp.	Wilmington, USA
Aeroflex Incorporated	Wilmington, USA
Aeroflex Test Solutions Limited	Wimborne, England
AFI Flight Inspection GmbH	Hermann-Blenk-Straße 8a, 38108 Braunschweig, Germany
AFI Flight Inspection Holding GmbH	Hermann-Blenk-Straße 8a, 38108 Braunschweig, Germany
Air Précision SAS	5 avenue Denis Papin, BP 36, 92353 Le Plessis Robinson, France
Asia Pacific Airlines (Papua New Guinea) Pty Limited	Blake Dawson, 4th Floor, Mogoru Motor Building, Champion Parade, Port Moresby, National Capital District, Papua New Guinea
Asia Pacific Airlines Pty Limited	Adelaide, Australia
Atlantic Microwave Corporation	Wilmington, USA
Avenue 64 Limited	Wimborne, England
Aviation Défense Service SA (45% joint venture) ¹	Zone Aéroportuaire Nîmes Arles Camargue, 30800 Saint Gilles, France
A-xell Wireless AB	Torhamngatan 30F, 164 40 Kista, Sweden
Axell Wireless Asia Pte Limited	21 Media Circle, Infinite Studios, #06-04 & #05-01, Singapore 138562, Singapore
Axell Wireless Israel Limited	6 Bareket St., Petah-Tikva 49002, Israel, P.O.Box: 2506 4912501, Israel
Axell Wireless Limited	Wimborne, England
Axell Wireless, Inc.	Wilmington, USA
Carleton Life Support Systems, Inc	Wilmington, USA
Carleton Technologies, Inc	Wilmington, USA
Chelton Antennas SA	7 chemin de Vaubessard, 91410 Dourdan, France
Chelton Avionics, Inc	Wilmington, USA
Chelton Limited	Wimborne, England
Chelton Telecom and Microwave SAS	31 avenue de la Baltique, 91140 Villebon sur Yvette, France
Chelton, Inc	Corporation Service Company d/b/a CSC-Lawyers Inco, 211 E. 7th Street, Suite 620, Austin, TX 78701, USA
Cob Finance LLC	Wilmington, USA
Cobham Advanced Electronic Solutions Mexico, S.A. de C.V.	Baker & McKenzie Abogados, S.C., Pedregal 24, Lomas Virreyes, 11040 Ciudad de México, D.F., Mexico
Cobham Advanced Electronic Solutions, Inc.	Wilmington, USA
Cobham AES Holdings Inc.	Wilmington, USA
Cobham Aviation Services Australia Pty Ltd (formerly Jet Systems Pty Limited)	Adelaide, Australia
Cobham Aviation Services Engineering Pty Limited	Adelaide, Australia
Cobham Aviation Services International Limited	Wimborne, England
Cobham Colorado Springs Inc. (formerly Aeroflex Colorado Springs, Inc.)	Wilmington, USA
Cobham CTS Limited	Wimborne, England
Cobham Defence Communications Limited	Wimborne, England
Cobham Defense Products, Inc.	Wilmington, USA
Cobham Exeter Inc (formerly Continental Microwave and Tool Co, Inc.)	Corporation Service Company, 84 State Street, Boston, MA 02109, USA
Cobham Fleet Support Pty Ltd (formerly Fleet Support Pty Limited)	Adelaide, Australia
Cobham Flight Inspection Limited	Wimborne, England
Cobham Gaisler AB	Kungsgatan 12, SE-411, 19 Göteborg, Sweden
Cobham Glyndale Pty Limited (formerly Glyndale Pty Limited)	Adelaide, Australia
Cobham Ground Handling Pty Ltd (formerly National Jet Systems Ground Handling Pty Limited)	Adelaide, Australia

Name of undertaking	Address of registered office or equivalent
Cobham Helicopters Cyprus Limited (formerly FBH Cyprus Limited)	12 Kennedy Avenue, Kennedy Business Centre, 2nd Floor, Office 203, P.C. 1087, Nicosia, Cyprus
Cobham Holdings Inc.	Wilmington, USA
Cobham India Private Limited	4th Floor, Statesman House, Barakhamba Road, New Delhi – 110001, India
Cobham Leasing Limited	Wimborne, England
Cobham Long Island Inc. (formerly Aeroflex Plainview, Inc.)	Wilmington, USA
Cobham Management Services Inc.	Wilmington, USA
Cobham Microelectronic Solutions Inc. (formerly Aeroflex Microelectronic Solutions, Inc.)	CSC-Lawyers Incorporating Service (Company), 601 Abbot Road, East Lansing, MI 48823, USA
Cobham Mission Equipment Inc.	Wilmington, USA
Cobham NAS Pty Ltd (formerly National Air Support Pty Limited)	Adelaide, Australia
Cobham NAS Services Pty Limited (formerly NAS Services Pty Limited)	Adelaide, Australia
Cobham New Jersey Inc. (formerly Aeroflex Control Components, Inc.)	CSC-Lawyers Incorporating Service (Company), 601 Abbot Road, East Lansing, MI 48823, USA
Cobham NIAP Pty Ltd (formerly National Investments Asia Pacific Pty Limited)	Adelaide, Australia
Cobham NJOS Pty Limited (formerly National Jet Operations Services Pty Limited)	Adelaide, Australia
Cobham RAD Europe Limited (formerly Aeroflex RAD Europe Limited)	Wimborne, England
Cobham RAD Inc. (formerly Aeroflex RAD, Inc.)	Corporation Service Company, 80 State Street, Albany, New York 12207-2543, USA
Cobham SAR Services Pty Limited	Adelaide, Australia
Cobham Slip Rings Naples Inc.	Wilmington, USA
Cobham Trivec-Avant Inc (formerly Trivec-Avant Corporation)	CSC Lawyers Incorporating Service, 2710 Gateway Oaks Drive, Suite 150N, Sacramento, CA 95833, USA
Comant Industries, Incorporated	CSC Lawyers Incorporating Service, 2710 Gateway Oaks Drive, Suite 150N, Sacramento, CA 95833, USA
FB Heliservices Kenya Limited	PO Box 764, 00606, Nairobi, Kenya
FB Heliservices Limited	Wimborne, England
FB Leasing Limited	Wimborne, England
FBS Limited	Wimborne, England
Flight Refuelling Limited ²	Wimborne, England
FR Aviation Group Limited ²	Wimborne, England
FR Aviation Limited	Wimborne, England
FR Aviation Services Limited	Wimborne, England
FR Investments Inc.	Wilmington, USA
Groupelement Troyen d'Electronique	rue Catherine et William Booth, 10000 Troyes, France
Hyper-Technologies SAS	28 rue des Dames, 78340 Les Clayes sous Bois, France
IFR Finance Inc.	10200 West York Street, Wichita, KS 67215-8999, USA
IFR Finance Limited Partnership ³	Wimborne, England
IFR Systems, Inc.	Wilmington, USA
Label SAS	10 allée de Montréal, 74108 Annemasse, France
Lock Financing Limited	12 Merrion Square, Dublin 2, Ireland
Lockman Electronic Holdings Limited ²	Wimborne, England
Lockman Financing S.à r.l	20 rue des Peupliers, L-2328, Luxembourg
Lockman Investments Limited ²	Wimborne, England
Lockman Properties Limited ²	Wimborne, England
Lockwash Investments LLC	Wilmington, USA
Lockwash US Limited	Wimborne, England
Manlock Investments Limited ²	Wimborne, England
Mastsystem International Oy	Muovilaaksontie 8, 82110 Heinävaara, Joensuu, Finland
Micro-Mesh SARL	35 rue de Monthéry, BP 20191, 94563 Rungis, France
NAT Seattle Inc.	Wilmington, USA
National Jet Express Pty Limited	Adelaide, Australia
National Jet Systems Pty Limited	Adelaide, Australia
Northrop Grumman Cobham Intercoms LLC (50% joint venture)	CT Corporation System, 1209 Orange Street, Wilmington, DE 19801, USA
Omnipless Manufacturing (Pty) Limited	Westlake Drive, Westlake Business Park, Westlake 7945, South Africa
Philtech Co., Ltd (associate owned 30%)	Sujeong-gu, Seongnam-si, Gyeonggi-do, South Korea

Notes to the Group Financial Statements

continued

Name of undertaking	Address of registered office or equivalent
Precision Aviation Industries SARL	5 avenue Denis Papin, BP 36, 92353 Le Plessis Robinson, France
Sargent Fletcher Inc.	Wilmington, USA
Satori Air Services Inc	4105 Cousens Street, Saint-Laurent, Quebec H4S 1V6, Canada
Sea Tel, Inc	CSC Lawyers Incorporating Service, 2710 Gateway Oaks Drive, Suite 150N, Sacramento, CA 95833, USA
Sivers Lab AB	Torhamnsgratan 30F, 164 40 Kista, Sweden
Société de Marquage et Signalisation SAS	174-178 Quai de Jemmapes, 75010 Paris, France
Surveillance Australia Pty Limited	Adelaide, Australia
TEAM SA	35 rue de Montlhéry, BP 20191, 94563 Rungis, France
Thrane & Thrane A/S	Lundtoftegårdsvej 93 D, DK-2800 Kongens Lyngby, Denmark
Thrane & Thrane Inc.	CT Corporation System, 4701 Cox Road, Suite 285, Glen Allen, VA 23060, USA
Thrane & Thrane Norge A/S	Cort Adelers gate 16, 0254 Oslo, Norway

Dormant entities

Aeroflex Bloomingdale, Inc.	Corporation Service Company, 80 State Street, Albany, New York 12207-2543, USA
Chelton Aviation Corporation	Corporation Service Company d/b/a CSC-Lawyers Inco, 211 E. 7th Street, Suite 620, Austin, TX 78701, USA
Chelton Satcom, Inc.	Wilmington, USA
Cobham Aviation SDN BHD	Level 8 Symphony House, Block D13 Pusat Dagangan Dana 1, Jalan PJU 1A/46, 47301 Petaling Jaya, Selangor, Malaysia
Cobham Communications and Connectivity Limited	Wimborne, England
Cobham Group Limited ⁴	Wimborne, England
Cobham Helicopter Services Trinidad Ltd	5-7 Sweet Briar Road, St Clair, Port of Spain, Trinidad & Tobago
Cobham Heliservices Curacao N.V. (formerly FB Heliservices Curacao N.V.)	Kaya W.F.G. (Jombi), Mensing 36, Curacao
Cobham Mission Systems Limited	Wimborne, England
Cobham NJRS Pty Ltd (formerly National Jet Regional Services Pty Limited)	Adelaide, Australia
Cobham Whiteley Limited	Wimborne, England
Credowan Limited	Wimborne, England
CTS Patents Limited ⁴	Wimborne, England
European Antennas Limited	Wimborne, England
Falcon Special Air Services SDN BHD	Level 8 Symphony House, Block D13 Pusat Dagangan Dana 1, Jalan PJU 1A/46, 47301 Petaling Jaya, Selangor, Malaysia
Grenedere Limited	Wimborne, England
Lockman Finance Limited	Wimborne, England
Lockman Financing Limited	Wimborne, England
ML Aviation Limited	Wimborne, England
Racal Antennas Limited	Wimborne, England
Strabor (Aircraft) Limited ²	Wimborne, England
Strabor Investments Limited	Wimborne, England
W.E.S. (Manufacturing) Limited	Wimborne, England
W.E.S. Investments Limited	Wimborne, England

Full registered office addresses are:

Wimborne, England	Brook Road, Wimborne, Dorset BH21 2BJ, England.
Wilmington, USA	Corporation Service Company, 2711 Centerville Road, Suite 400, Wilmington, DE 19808, USA.
Adelaide, Australia	National Drive, Adelaide Airport SA 5950, Australia.

- The 45% investment in Aviation Défense Service SA is treated as a joint venture because the governance structure means that the Group has joint control with its partner.
- Shares in Flight Refuelling Limited, FR Aviation Group Limited, Lockman Electronic Holdings Limited, Lockman Properties Limited, Manlock Investments Limited, Strabor (Aircraft) Limited and Lockman Investments Limited are held directly by, or on behalf of, Cobham plc. Shares in all other entities listed are held by or on behalf of one of these subsidiaries.
- Advantage has been taken of the exemption conferred by regulation 7 of the Partnership Accounts Regulations 2008 from the requirements to prepare and publish audited accounts for IFR Finance Limited Partnership.
- Dissolved subsequent to 31 December 2018.

Parent Company Balance Sheet

As at 31 December 2018

£m	Note	2018	2017
Assets			
Non-current assets			
Investments in Group undertakings	6	3,231.3	1,013.5
Other investments	7	39.5	6.1
Property, plant and equipment	8	0.8	–
Derivative financial instruments	13	28.8	33.1
Other receivables	9	18.3	18.7
		3,318.7	1,071.4
Current assets			
Derivative financial instruments	13	12.4	15.6
Trade and other receivables	9	326.2	2,474.3
Cash and cash equivalents		81.4	409.1
		420.0	2,899.0
Liabilities			
Current liabilities			
Borrowings	10	(258.7)	–
Trade and other payables	11	(685.1)	(511.4)
Provisions	12	(6.2)	(6.3)
Derivative financial instruments	13	(10.9)	(18.5)
		(960.9)	(536.2)
Non-current liabilities			
Borrowings	10	(327.1)	(835.1)
Derivative financial instruments	13	(27.7)	(29.7)
Retirement benefit obligations	14	(18.1)	(25.8)
		(372.9)	(890.6)
Net assets			
		2,404.9	2,543.6
Equity			
Share capital	15	61.7	61.7
Share premium		1,257.9	1,257.9
Other reserves		18.4	17.2
Retained earnings		1,066.9	1,206.8
Total equity		2,404.9	2,543.6

Profit for the financial year

In accordance with the concession granted under Section 408 of the Companies Act 2006, the Income Statement of Cobham plc has not been separately presented in these financial statements. The Company's result for the year ended 31 December 2018 was a loss of £180.9m (2017: profit of £203.8m).

The financial statements on pages 151 to 161 were approved by a duly appointed and authorised committee of the Board on 7 March 2019 and signed on its behalf by:



David Lockwood
Directors



David Mellors

Parent Company Statement of Changes in Equity

For the year ended 31 December 2018

£m	Share capital	Share premium	Other reserves		Retained earnings	Total equity
			Hedge reserve	Share based payment reserve		
At 31 December 2017	61.7	1,257.9	0.3	16.9	1,206.8	2,543.6
Change in accounting policy – IFRS 9 (note 1)	–	–	–	–	39.0	39.0
At 1 January 2018	61.7	1,257.9	0.3	16.9	1,245.8	2,582.6
Loss for the year	–	–	–	–	(180.9)	(180.9)
Other comprehensive expense						
Items that will not be reclassified subsequently to profit or loss	–	–	–	–	(2.0)	(2.0)
Items that may subsequently be reclassified to profit or loss	–	–	(0.6)	–	–	(0.6)
Total comprehensive expense for the year	–	–	(0.6)	–	(182.9)	(183.5)
Share based payments	–	–	–	5.8	–	5.8
Transfer of share based payment reserve	–	–	–	(4.0)	4.0	–
At 31 December 2018	61.7	1,257.9	(0.3)	18.7	1,066.9	2,404.9
At 1 January 2017	44.6	778.3	(0.8)	14.3	997.1	1,833.5
Profit for the year	–	–	–	–	203.8	203.8
Other comprehensive income						
Items that will not be reclassified subsequently to profit or loss	–	–	–	–	2.5	2.5
Items that may subsequently be reclassified to profit or loss	–	–	1.1	–	–	1.1
Total comprehensive income for the year	–	–	1.1	–	206.3	207.4
Issue of shares, net of costs	17.1	479.6	–	–	–	496.7
Proceeds on allocation of treasury shares	–	–	–	–	0.5	0.5
Share based payments	–	–	–	5.5	–	5.5
Transfer of share based payment reserve	–	–	–	(2.9)	2.9	–
At 31 December 2017	61.7	1,257.9	0.3	16.9	1,206.8	2,543.6

The share based payment reserve includes the cost of awards granted to employees of the Company and Group as assessed under IFRS 2. Where awards which gave rise to charges under IFRS 2 have vested or been exercised, the appropriate proportion of the reserve is transferred to retained earnings.

Distributable reserves at 31 December 2018 amounted to £1,008.6m (2017: £1,180.1m).

Notes to the Parent Company Financial Statements

1. Parent Company accounting policies

These financial statements are the financial statements for Cobham plc, the parent company of the Cobham plc Group, which operates as a group holding company.

Accounting convention

The financial statements have been prepared in accordance with Financial Reporting Standard 101, Reduced Disclosure Framework (FRS 101).

The financial statements have been prepared on the going concern basis, under the historical cost convention as modified to include the revaluation of derivative financial assets and liabilities measured at fair value through profit or loss and in accordance with the Companies Act 2006.

The Company has taken advantage of the following disclosure exemptions under FRS 101:

- A cash flow statement and related notes (IAS 7, Statement of Cash Flows and paragraph 10(d) of IAS 1, Presentation of Financial Statements);
- Comparative period reconciliations of the number of shares outstanding (Paragraph 38 of IAS 1, Presentation of Financial Statements in respect of paragraph 79(a)(iv) of IAS 1);
- Capital management disclosures required by paragraphs 134 to 136 of IAS 1;
- The requirements of paragraphs 30 and 31 of IAS 8, Accounting Policies, Changes in Accounting Estimates and Errors concerning the effects of new but not yet effective IFRS;
- Details of compensation of key management personnel required by paragraph 17 of IAS 24, Related Party Disclosures; and
- The requirements in IAS 24 to disclose related party transactions entered into between two or more members of a group.

In addition, as the consolidated financial statements of Cobham plc include the equivalent disclosures, the following exemptions under FRS 101 have also been taken:

- Share based payment disclosures under paragraphs 45(b) and 46-52 of IFRS 2, Share Based Payment in respect of group settled share based payments; and
- Financial instrument information required by IFRS 7, Financial Instruments: Disclosures and paragraphs 91 to 99 of IFRS 13, Fair Value Measurement.

Management judgement and estimation uncertainty

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

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

Significant judgements in applying accounting policies

There were no significant judgements, apart from those involving estimations, that the Directors made in the process of applying the Group's accounting policies which require separate disclosure in these financial statements.

Assumptions and estimation uncertainties

Management considers that there are a number of assumptions concerning the future and other major sources of estimation uncertainty at the balance sheet date, which have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. Information concerning these assumptions and estimation uncertainties is provided as follows:

- a. Carrying value of investments (note 6)
A review of the carrying value of investments is completed as required to ensure that it is not impaired. This requires an estimate of the expected future cash flows from subsidiary undertakings and also a suitable discount rate in order to calculate the present value of those cash flows.
- b. Valuation of other investments (note 7)
Fair value is determined based on the estimated cash flows expected to be received, discounted to present value.
- c. Pension assets and liabilities (note 14)
Assumptions are made in assessing the costs and present value of the pension assets and liabilities, which include the discount rate, inflation and mortality rates.

Accounting developments

Two new standards have been adopted on 1 January 2018, IFRS 9, Financial Instruments and IFRS 15, Revenue from Contracts with Customers.

IFRS 9, Financial Instruments

Following the adoption of IFRS 9, the accounting policies for financial instruments applied during the year ended 31 December 2017 are, on a practical level, largely unchanged.

As shown in the Parent Company Statement of Changes in Equity, retained earnings at 1 January 2018, and other investments as shown in note 7, have been restated by £39.0m as a result of the transition to this new standard. There was no impact on the income statement or other balance sheet line items and, in accordance with the transitional provisions, comparative figures have not been restated.

The restatement relates to Cobham plc's minority shareholdings in equity investments which were previously accounted for as trade investments and categorised as available for sale under IAS 39. Under IFRS 9, these investments are presented as other financial assets held at fair value, using a present value methodology. The Company has elected to present movements in fair value in other comprehensive income (OCI). Further details are shown in note 7.

Reclassification of other financial assets into the IFRS 9 categories has had no overall impact on the measurement basis applied or the presentation of these items.

Notes to the Parent Company Financial Statements

continued

IFRS 15, Revenue from Contracts with Customers

IFRS 15 introduces a five step model to be applied to all contracts with customers when determining the accounting for revenue. As the Company operates as a group holding company it does not report revenue and hence the adoption of this standard has had no impact on the Company's financial reporting.

A number of other amendments to standards and interpretations of the IFRS Interpretations Committee have been adopted with effect from 1 January 2018. No changes to previously published accounting policies or other adjustments were required on the adoption of these amendments and interpretations.

Principal accounting policies

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

Dividends (note 2)

Dividends payable are recognised as a liability in the period in which they are fully authorised. Dividend income is recognised when the shareholders' right to receive payment has been established.

Retirement benefit obligations (notes 3 and 14)

The Company operates and participates in the Cobham Pension Plan (CPP) and the Cobham Executive Pension Plan (CEPP). The plans are funded defined benefit schemes and assets are held in separate trustee administered funds. The assets and liabilities of the CPP have been allocated to the contributing companies based on the proportional number of members. The Company also operates and contributes to a defined contribution scheme.

For the defined benefit schemes, service costs and costs related to the administration of the schemes are recognised in the income statement. The interest on net assets or liabilities is also included in the income statement. Actuarial remeasurements are recognised in OCI.

Pension scheme assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the scheme liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting net defined benefit asset or liability is presented separately on the Balance Sheet.

For the defined contribution scheme, the amount charged to the income statement in respect of pension costs and other post-retirement benefits are the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are recorded as either accruals or prepayments in the Balance Sheet.

Share based payments (note 5)

For grants made to employees of Cobham plc under the Group's equity share based payment schemes, amounts which reflect the fair value of awards as at the time of grant are charged to the income statement over the vesting period, taking into account management's best estimate of the number of awards expected to vest. The vesting estimate, which includes progress against non-market related performance conditions, is reviewed and updated at each balance sheet date. The fair value of awards made to employees of subsidiary undertakings, net of amounts recovered as management charges, is recognised as a capital contribution and recorded in investments.

Taxation

The tax expense is the sum of current tax and deferred tax. Tax is charged or credited to the income statement except when it relates to items recognised in OCI or directly in equity, in which case the tax is also recognised in OCI or directly in equity respectively.

Current tax is provided at the amounts expected to be paid using rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. It is calculated using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date and that are expected to apply in the period when the asset is realised or the liability is settled. Deferred tax is measured on an undiscounted basis and deferred tax assets are only recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised.

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

Investments in Group undertakings (note 6)

Investments in subsidiary undertakings are stated at cost less any provision for impairment in value and include the fair value at the date of grant of share based payment awards to employees of subsidiary undertakings, net of amounts recovered as management charges.

The carrying amounts of the investments are reviewed at least annually to determine whether there is any indication of impairment.

Where there is an indication of impairment, the recoverable amount is estimated. This is the higher of fair value less costs of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. This is prepared with reference to cash flow forecasts prepared by management and reviewed by the Board which cover a three year period. The growth rates used after this period are based on long term GDP projections of the primary market for each investment.

Other investments (note 7)

Other financial assets such as equity investments not held for trading (the Company's AirTanker investments) are held at fair value, which has been determined based on the estimated cash flows expected to be received, discounted to present value. The estimated cash flows are calculated using an income approach reflecting the cash flows available to the Company after repayment of debt capital and interest, taking into account operating and financing cash flows. The inputs to this calculation are not based on observable market data and hence they fall within level 3 of the IFRS 13 fair value hierarchy. The Company has elected to present subsequent changes in fair value in OCI.

Dividends on these investments are recognised in profit or loss when the Group's right to receive the dividends is established, it is probable that they will be paid and the amount can be measured reliably.

Property, plant and equipment (note 8)

Fixtures and fittings are initially recognised at cost and depreciated on a straight-line basis to their estimated residual values over their estimated useful lives of up to five years.

Provisions (note 12)

A provision is recognised when the Company has a present legal or constructive obligation as a result of a past event and it is probable that settlement will be required of an amount that can be reliably estimated. No provision is recognised where the existence of an obligation is possible but will only be confirmed by uncertain future events.

Share capital (note 15)

Ordinary share capital is classified as equity.

Preference share capital is classified as a liability if it is redeemable on a specific date or at the option of the preference shareholders or if dividend payments are not discretionary.

Financial instruments

The policies disclosed in note 1 to the Group Financial Statements at section 1.6.13 for the recognition, measurement and presentation of financial instruments are applicable to the Parent Company Financial Statements. As noted above, IFRS 9 has been adopted from 1 January 2019.

Amounts receivable from and owed to subsidiaries are recognised at amortised cost using the effective interest method and are reduced by allowances for expected credit losses.

Interest bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs and subsequently held at amortised cost. Interest is accounted for on an accruals basis in the income statement. Premiums payable on settlement or redemption and direct issue costs are capitalised and amortised over the period of the facility.

Foreign currencies

The functional currency of the Company is sterling.

Transactions in currencies other than sterling are translated at the exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in non-functional currencies are retranslated at the exchange rate ruling at the balance sheet date. Non-monetary items (such as investments) that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency (such as some derivative financial instruments) are translated using the exchange rates at the date when the fair value was determined.

All exchange differences arising are recognised in the income statement.

Notes to the Parent Company Financial Statements

continued

2. Dividends

No dividends were paid or approved during the year ended 31 December 2018 (2017: £nil).

3. Employees

The monthly average number of employees, including Directors, during the year was 167 (2017: 162). All staff were employed in administrative functions. Costs for these employees were as follows:

£m	2018	2017
Wages and salaries	16.9	13.2
Social security costs	1.7	1.1
Pension costs	7.8	9.4
Share based payments	1.6	1.3
	28.0	25.0

Disclosures in respect of the emoluments of Directors and key management personnel can be found in the Directors' Remuneration Report on pages 71 to 80 and in note 5 to the Group Financial Statements.

4. Audit fees

The audit fee in respect of the Parent Company Financial Statements was £45,000 (2017: £44,000).

5. Share based payments

Employees of Cobham plc participate in equity settled share based payment schemes which are operated by the Group for senior executives and also in the Group's SAYE scheme which is open to all UK employees.

At 31 December, the following awards were outstanding under each scheme:

Number of awards (thousands of shares)	2018	2017
PSP	7,137	3,942
RSP	776	1,082
SAYE	635	818
ESOS	84	84
	8,632	5,926

Options outstanding under the SAYE scheme had a weighted average remaining contractual life of 2.2 years (2017: 3.0 years) and exercise prices which range from £1.10 to £1.78 (2017: £1.10 to £1.78). Options outstanding under the ESOS scheme had a weighted average remaining contractual life of 0.3 years (2017: 1.3 years) and exercise prices which range from £1.36 to £1.72 (2017: £1.36 to £1.72).

Exercises of awards under the SAYE schemes were made at various times throughout the year. The average share price in that period was £1.190 (2017: £1.241).

Further details of these schemes can be found in the Directors' Remuneration Report on pages 71 to 80 and in note 27 to the Group Financial Statements.

6. Investments in Group undertakings

£m	Shares	Share based payments	Total
Cost			
At 1 January 2018	998.3	15.2	1,013.5
Additions	2,490.3	1.3	2,491.6
At 31 December 2018	3,488.6	16.5	3,505.1
Accumulated impairment			
At 1 January 2018	—	—	—
Impairment provision	273.8	—	273.8
At 31 December 2018	273.8	—	273.8
Carrying amount			
At 31 December 2018	3,214.8	16.5	3,231.3
At 31 December 2017	998.3	15.2	1,013.5

During the year, the Company subscribed for additional shares in two of its subsidiary undertakings at a total cost of £2,490.3m. There were no changes to the proportion of shares held and, as a result of one of these internal refinancing transactions, amounts owed by Group undertakings as shown in note 9 were reduced. In addition, share based payment awards were granted to employees of Group undertakings which are recorded at fair value net of recoveries.

In the opinion of the Directors, the value of investments in subsidiary undertakings is not less than the aggregate amount at which they are shown above, after taking account of the impairment charged in the year. This assessment is based on value in use with reference to the discounted cash flow forecasts prepared by management and reviewed by the Board covering a three year period. These cash flows are subject to the same assumptions and dependencies as described in note 10 to the Group Financial Statements.

The impairment charge relates to two direct subsidiaries of the Company, Lockman Investments Limited and Flight Refuelling Limited. This reflects, to a large extent, the impact of cash flows from the KC-46 programme (see note 3 to the Group Financial Statements). This valuation is considered a key estimation uncertainty, as the value of the Company's investments remains sensitive to cash flow projections on the Group's development programmes, specifically the completion and production ramp up in subsidiaries in the Mission Systems and Advanced Electronic Solutions Sectors. A reduction in the future cash flows in these subsidiaries would result in a further impairment.

A list of all subsidiaries is provided in note 33 to the Group Financial Statements. The market capitalisation of the Group as a whole is given in the Group Financial Record on page 162.

7. Other investments

£m	2018
At 1 January 2017 and 31 December 2017	6.1
Change in accounting policy – adoption of IFRS 9	39.0
At 1 January 2018	45.1
Revaluation losses recognised in OCI	(5.6)
At 31 December 2018	39.5

Other investments represent Cobham plc's investments of 13.33% of the issued share capital of AirTanker Holdings Limited and 5.0% of the issued share capital of AirTanker Services Limited in connection with the Voyager (FSTA) project. During the year ended 31 December 2018, dividends of £9.9m (2017: £nil) were received.

8. Property, plant and equipment

£m	Fixtures and fittings
Cost	
At 1 January 2018	0.6
Additions	0.8
Disposals	(0.2)
At 31 December 2018	1.2
Accumulated depreciation	
At 1 January 2018	0.6
Disposals	(0.2)
At 31 December 2018	0.4
Net book amount	
At 31 December 2018	0.8
At 31 December 2017	–

9. Trade and other receivables

Current assets

£m	2018	2017
Amounts owed by Group undertakings	295.4	2,456.1
Corporation tax receivable	10.3	–
Deferred tax assets	7.3	7.4
Prepayments and accrued income	13.2	10.8
	326.2	2,474.3

Amounts owed by Group undertakings are unsecured and repayable on demand. All such balances, excluding trading balances, are interest bearing.

Notes to the Parent Company Financial Statements

continued

The net deferred tax asset can be analysed as follows:

£m	2018	2017
Derivative financial instruments	3.1	1.9
Retirement benefit obligations	3.8	5.3
Share based payments	0.3	0.2
Accelerated capital allowances	0.1	–
	7.3	7.4

Movements in the net deferred tax asset are as follows:

£m	
At 1 January 2018	7.4
Charge to income statement	0.6
Charge to reserves	(0.7)
At 31 December 2018	7.3

Non-current assets

£m	2018	2017
Loan notes	18.3	18.3
Other debtors	–	0.4
	18.3	18.7

Loan notes are due from AirTanker Holdings Limited. They are interest bearing and due for repayment in 2035.

10. Borrowings

Current liabilities

£m	2018	2017
Bank overdrafts	212.2	–
Senior notes	46.5	–
	258.7	–

Bank overdrafts are repayable on demand and accrue interest at floating rates.

Non-current liabilities

£m	2018	2017
Bank loans	152.4	204.3
Senior notes	174.7	630.8
	327.1	835.1

Senior notes of US\$572.8m were repaid on 17 April 2018. Further details of the Company's principal borrowing facilities are disclosed in notes 14 and 19 to the Group Financial Statements.

The loans falling due after more than one year are due for repayment as follows:

£m	2018	2017
Between one and two years	148.8	55.4
Between two and five years	3.6	148.9
	152.4	204.3

Senior notes falling due after more than one year mature as follows:

£m	2018	2017
Between two and five years	64.7	317.3
After five years, maturing in 2024	110.0	313.5
	174.7	630.8

11. Trade and other payables

£m	2018	2017
Trade payables	1.5	2.5
Amounts owed to Group undertakings	666.6	484.5
Corporation tax payable	–	6.5
Other tax and social security	2.8	1.0
Accruals and deferred income	14.2	16.9
	685.1	511.4

Amounts owed to Group undertakings include £87.1m (2017: £86.8m) on which interest is charged at rates of between 0.4% and 9.0% (2017: 0.4% and 9.0%). The remaining amount owed by Group undertakings is interest free. All amounts are unsecured and are repayable on demand.

12. Provisions

£m	Legal claims	Other provisions	Total
At 1 January 2018	0.4	5.9	6.3
Additional provisions in the year	–	0.1	0.1
Utilisation of provisions	(0.2)	–	(0.2)
At 31 December 2018	0.2	6.0	6.2

Other provisions of £6.0m (2017: £5.9m) relate to longer term warranties given on divestments completed in 2005, together with provision for dilapidation of leased buildings. All amounts were determined based on the Directors' current estimates of likely outcomes and the timing of any claims remains uncertain.

13. Derivative financial instruments

The Company's activities expose it to the financial risks of changes in foreign currency exchange rates and interest rates. The Company uses foreign exchange contracts and interest rate swap contracts to reduce these exposures and does not use derivative financial instruments for speculative purposes. Other derivative financial instruments may be used from time to time to manage exposures such as inflation risk.

The fair values of derivative financial instruments are as follows, these are financial assets and financial liabilities measured at fair value through profit or loss:

£m	Foreign exchange derivatives	Inflation swap	Total
Non-current assets	28.8	–	28.8
Current assets	12.4	–	12.4
Current liabilities	(10.9)	–	(10.9)
Non-current liabilities	(27.7)	–	(27.7)
At 31 December 2018	2.6	–	2.6

Non-current assets	33.1	–	33.1
Current assets	15.2	0.4	15.6
Current liabilities	(18.1)	(0.4)	(18.5)
Non-current liabilities	(29.7)	–	(29.7)
At 31 December 2017	0.5	–	0.5

The movements in the fair values of derivative financial instruments during the year are as follows:

£m	Interest rate swaps	Foreign exchange derivatives	Total
At 1 January 2017	(1.8)	(7.7)	(9.5)
Gain through income statement – not hedged	–	8.0	8.0
Gain/(loss) reclassified to income statement	0.7	(0.1)	0.6
Ineffectiveness of net investment hedge through income statement	–	0.2	0.2
Gain through OCI – hedged items	1.1	0.1	1.2
At 31 December 2017	–	0.5	0.5
Gain through income statement – not hedged	–	2.7	2.7
Loss reclassified to income statement	–	(0.3)	(0.3)
Ineffectiveness of net investment hedge through income statement	–	0.1	0.1
Loss through OCI – hedged items	–	(0.4)	(0.4)
At 31 December 2018	–	2.6	2.6

Notes to the Parent Company Financial Statements

continued

The majority of foreign exchange derivative financial instruments are not accounted for using hedge accounting and movements in fair values are recorded in the income statement. The Company has a small number of cross-currency swaps which have been designated as hedging instruments, further details can be found in note 22 to the Group Financial Statements. In addition, a small number of specific foreign exchange derivatives were previously designated as cash flow hedging instruments and hedge accounting was applied. These were, however, de-designated as hedging instruments during the year. The fair value of these contracts at 31 December 2017 was £0.1m.

Floating to fixed interest rate swaps were cancelled in the year ended 31 December 2017 following the repayment of the associated floating rate borrowings. These interest rate swaps were previously designated as cash flow hedging instruments and hedge accounting was applied.

The most significant assumptions in valuing the derivatives are the exchange rates for GBP: US\$, GBP: DKK and GBP: EUR.

14. Retirement benefit schemes

Retirement benefit obligations in the Balance Sheet comprise:

£m	2018	2017
Defined benefit scheme assets	399.4	431.4
Defined benefit obligations	(417.5)	(457.2)
	(18.1)	(25.8)

Defined benefit pension schemes

The Company operates and participates in the Cobham Pension Plan (CPP) and the Cobham Executive Pension Plan (CEPP). The plans are funded defined benefit schemes (where benefits are based on employees' length of service and average final salary) and assets are held in separate trustee administered funds. The plans have been closed to new members since 2003 and were closed to future accrual from 1 April 2016.

During the year, there have been two major events affecting the defined benefit schemes:

- The CPP completed its triennial valuation; and
- In October 2018, the English High Court determined that UK defined benefit pension schemes with Guaranteed Minimum Pensions must be equalised between men and women. The impact of this ruling has been estimated at £2.8m and recognised as a past service cost. This has been calculated using the 'C2' method as the Company's current best estimate; the actual method of satisfying the obligations to the members of the pension plans will ultimately need to be agreed by the Company and the trustees of the pension plans.

Details of actuarial valuation processes and risks, assumptions and sensitivities relating to the CPP and CEPP are not significantly different to those disclosed in note 23 to the Group Financial Statements.

The Company expects to contribute £3.1m to its defined benefit pension schemes in 2019 and future years. At 31 December 2018, £0.5m (2016: £0.7m) of contributions were outstanding.

Changes in the fair value of scheme assets are as follows:

£m	2018	2017
At 1 January	431.4	415.7
Interest	10.0	10.9
Actuarial (losses)/gains	(29.4)	18.0
Employer contributions	6.7	8.7
Benefits paid	(19.3)	(21.9)
At 31 December	399.4	431.4

Changes in the present value of the defined benefit obligations are as follows:

£m	2018	2017
At 1 January	457.2	452.5
Past service cost	2.8	–
Interest cost	10.6	11.7
Actuarial (gains)/losses arising from changes in financial assumptions	(26.4)	20.7
Actuarial gains arising from changes in demographic assumptions	(7.4)	(5.8)
Benefits paid	(19.3)	(21.9)
At 31 December	417.5	457.2

The actual return on scheme assets was £19.4m (2017: £28.9m). The weighted average duration of the scheme liabilities is estimated to be 17 years.

The fair value of major categories of scheme assets, and as a percentage of total scheme assets, is as follows:

	2018		2017	
	£m	%	£m	%
Global equities	45.9	11.5%	48.1	11.1%
Liability driven investments	59.9	15.0%	77.9	18.1%
Corporate bonds	37.9	9.5%	42.5	9.9%
Private credit	18.0	4.5%	14.5	3.3%
Insurance contracts	160.2	40.1%	180.8	41.9%
Diversified growth funds	62.7	15.7%	66.5	15.4%
Other assets	14.8	3.7%	1.1	0.3%
	399.4	100.0%	431.4	100.0%

Scheme assets do not include any of the Company's own financial instruments, nor any property occupied by, or other assets used by the Company.

Defined contribution pension schemes

The Company also operates and participates in the Cobham Personal Pension Plan, a defined contribution scheme. The assets of the scheme are held separately from those of the Company in independently administered funds. The pension cost charged represents contributions payable by the Company to the funds and amounted to £1.2m (2017: £0.8m). No contributions were outstanding at the end of 2018 or 2017.

15. Share capital

£m	2018	2017
Allotted, issued and fully paid		
Equity		
2,466,961,115 (2017: 2,466,961,115) 2.5p ordinary shares	61.7	61.7
Non-equity		
19,700 (2017: 19,700) 6% second cumulative preference shares of £1	—	—

Preference shares with a value of £19,700 are classified as borrowings.

Further details of the share capital of Cobham plc can be found in the Directors' Report on page 81 and in note 25 to the Group Financial Statements.

16. Contingent liabilities and commitments

The Company has contingent liabilities in respect of bank and contractual performance guarantees and other matters arising in the ordinary course of business entered into for, or on behalf of, certain Group undertakings.

Further details of contingent liabilities related to the Company, including risks related to uncertain tax positions and the nature of contract risks supported by performance guarantees, can be found in note 30 to the Group Financial Statements.

The Company had no capital commitments at 31 December 2018 (2017: £nil).

17. Related party transactions

During the year, the Company entered into transactions, in the ordinary course of business, with related parties that are part of the Cobham plc Group or investees of the Group. The Company has taken advantage of the exemption under paragraph 8(k) of FRS 101 from disclosing related party transactions with its wholly owned subsidiary undertakings. The only transactions with non-wholly owned subsidiaries relate to the receipt of management and brand charges totalling £1.3m (2017: £1.4m) from TEAM SA which is 98.7% owned within the Cobham Group. No amounts were outstanding at the current or prior year end.

There were no material transactions with the Directors, their close family members or other connected parties to be reported during the year, other than arising from Directors' service agreements. Details of Directors' remuneration are disclosed in the Directors' Remuneration Report on pages 71 to 80.

Group Financial Record

£m	2014	2015	2016	2017 (restated for IFRS 15)	2018
Revenue	1,851.7	2,072.0	1,943.9	2,091.6	1,863.3
Underlying operating profit	286.7	332.2	225.0	213.1	196.1
Underlying profit before taxation	257.0	280.4	175.2	175.9	155.2
Underlying earnings attributable to owners of the parent	204.8	220.1	135.5	138.4	119.4
Profit/(loss) before taxation	24.3	(39.8)	(847.9)	69.7	71.0
Taxation	4.7	2.1	52.8	14.4	2.7
Profit/(loss) after taxation for the year	29.0	(37.7)	(795.1)	84.1	73.7
Working capital	374.2	424.8	409.3	217.1	231.2
Net cash/(debt)	(1,222.7)	(1,206.8)	(1,028.2)	(383.5)	10.3
Retirement benefit obligations	(102.0)	(56.7)	(87.0)	(63.2)	(46.6)
Net assets	1,112.3	909.7	489.9	1,032.4	1,191.7
Operating cash flow	207.9	234.6	181.8	217.6	123.4
Operating cash conversion	73%	71%	81%	102%	63%
Free cash flow	114.4	105.5	50.7	140.6	62.6
Net cash/(debt): EBITDA (for covenant purposes)	2.6	2.9	3.0	1.3	n/a
Average number of employees	10,941	12,527	10,898	10,736	10,359
pence					
Dividend paid per ordinary share	7.33	7.96	7.76	—	—
Earnings per ordinary share – underlying	13.7	14.3	7.8	6.2	5.0
Earnings per ordinary share – basic	1.9	(2.4)	(45.9)	3.7	3.1
Earnings per ordinary share – diluted	1.9	(2.4)	(45.9)	3.7	3.1
£m					
Market capitalisation as at 31 December	3,934	3,440	2,920	3,116	2,411

In the table above, figures for 2017 have been restated, where appropriate, for the impact of IFRS 15 as described in note 2 to the Group Financial Statements. Information for prior periods is presented in accordance with accounting standards in force at that time.

Other Information — Shareholder Information

Analysis of shareholders

Analysis of ordinary shareholders on the register at 31 December 2018:

Size of holding (number of ordinary shares held)	Number of registered holders	Percentage of registered holders	Number of ordinary shares held	Percentage of ordinary shares
Up to 1,000	1,204	27.72%	552,061	0.02%
1,001-10,000	2,130	49.03%	7,784,248	0.32%
10,001-50,000	630	14.50%	12,725,857	0.52%
50,001-250,000	156	3.59%	18,225,105	0.74%
250,001-1,000,000	91	2.09%	53,441,263	2.17%
1,000,001 and above	133	3.06%	2,374,232,581	96.24%
Total	4,344	100.00%	2,466,961,115	100.00%

Source: Equiniti Group plc

At 31 December 2018, there were 4,344 ordinary shareholders on the register, compared with 4,611 at 31 December 2017. The total includes 75,951,724 shares held in treasury.

Registrars

Enquiries concerning shareholdings or dividends should, in the first instance, be addressed to the Company's registrars, Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA (telephone: 0371 384 2163* or +44 (0) 121 415 7047 if calling from outside the UK). Shareholders should promptly notify the registrars of any change of address or other particulars.

The registrars provide a range of shareholders' services online. The portfolio service provides access to information on investments including balance movements, indicative share prices and information on dividends and also enables address and mandate details to be amended online. For further information and practical help on transferring shares or updating your details, please visit www.shareview.co.uk. The share dealing service enables shares to be sold by UK shareholders by telephone, post or over the internet. For telephone sales please call 0345 603 7037 between 8:00am and 4:30pm, Monday to Friday. For postal sales, please send your completed documentation to the address above. For internet sales, please visit www.shareview.co.uk/dealing.

Individual Savings Accounts (ISAs)

The registrars also offer an ISA for Cobham shareholders. Further information may be obtained by visiting www.shareview.co.uk, or telephone 0345 300 0430 (or +44 (0) 121 415 0105 if calling from outside the UK).

You should bear in mind that investments, both their value and the income they provide, can go down as well as up and you might not get back what you originally invested.

ShareGift

Do you have a small shareholding which is uneconomical to sell? You may want to consider donating it to ShareGift (registered charity no. 1052686), a charity that specialises in the donation of small, unwanted shareholdings to good causes. You can find out more by visiting www.sharegift.org or calling +44 (0) 20 7930 3737.

Shareholder security

Shareholders are advised to be wary of any unsolicited advice, offers to buy shares, or offers of free reports about the Company. Details of any share dealing facilities that the Company endorses will be included in Company mailings or on our website. If you receive any unsolicited advice, make sure you get the correct name of the person and organisation and check that they are appropriately authorised by the FCA by visiting www.fca.org.uk. You can also call the FCA Consumer Helpline on 0800 111 6768 (or +44 (0) 20 7066 1000 if calling from outside the UK).

* Lines are open Monday to Friday 8:30am to 5:30pm; excluding Public Holidays in England and Wales.

Financial calendar

AGM	25 April 2019
Interim results	1 August 2019

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Cautionary statements

This publication contains 'forward looking statements' with respect to the financial condition, results of operations and business of the Cobham Group and to certain of Cobham's objectives with respect to these items.

Forward looking statements are sometimes but not always identified by the use of a date in the future or such words as 'anticipates', 'aims', 'due', 'could', 'may', 'should', 'expects', 'believes', 'intends', 'plans', 'targets', 'goal', or 'estimates' (or the negative thereof). By their very nature forward looking statements are inherently unpredictable, speculative and involve risk and uncertainty because they relate to events and depend on circumstances that may or will occur in the future.

There are various factors that could cause actual results and developments to differ materially from those expressed or implied by these forward looking statements. These factors include, but are not limited to, changes in economies, political situations and markets in which the Group operates; changes in government priorities due to programme reviews or revisions to strategic objectives; changes in regulatory or competition frameworks in which the Group operates; the impact of legal or other proceedings against or which affect the Group; changes to or delays in programmes in which the Group is involved; the completion of acquisitions and divestitures and changes in commodity prices, inflation or exchange rates.

All written or verbal forward looking statements, made in this publication or made subsequently, which are attributable to Cobham or any other member of the Group or persons acting on their behalf, are expressly qualified in their entirety by the factors referred to above. Neither Cobham nor any other person intends to update these forward looking statements.

No statement in this publication is intended as a profit forecast or should be interpreted to mean that underlying operating profit for the current or future financial years would necessarily be above a minimum level, or match or exceed the historical published operating profits or set a minimum level of operating profit.

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Find out more online

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