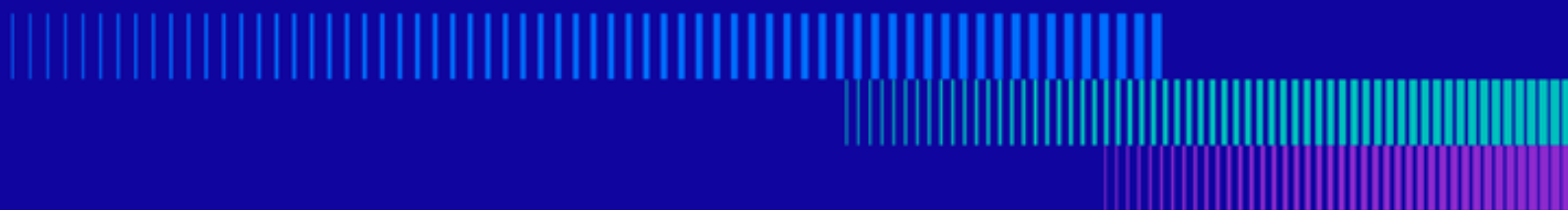




TRANSCRIPT

FULL YEAR
RESULTS 2024



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Jeremy Bragg

Head of investor Relations, Rolls-Royce Holdings plc

I'm Jeremy Bragg, Head of Investor Relations, and I'm joined today by our CEO, Tufan, and our CFO, Helen.

So before we begin today's presentation, I'm required to show you the Safe Harbor Statement on slide two.

So the full materials can be downloaded from our website. And in today's presentation, we are going to cover financial and strategic progress over the past two years; the 2024 results in detail; our guidance for 2025; and our upgraded mid-term targets.

So, after the presentation, there will be time for questions from the room and if there's time from our online audience. So, for those of you in the room, there's microphones in the seat in front of you and you need to press and hold the button before you speak.

So, before I hand over to Tufan, we'd like to show you a short video that highlights some of the progress that we've made this year. Thank you.

(Video Playing)

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Good morning. We are transforming Rolls-Royce into a high-performing, competitive, resilient, and growing business.

We are expanding the earnings and cash potential, alongside delivering significantly improved performance. This is about creating a sustainably distinctive business in terms of safety, operational effectiveness, customer service with advantaged technologies and products, combined with a distinctive performance culture.

These all mean we are taking Rolls-Royce to a place that it has never been before, which opens up further potential for future profitable growth. We have made progress, but we are not done yet.

Today is an important day for Rolls-Royce. 2024 represents another year of strong financial and strategic delivery, building on the progress made last year. We achieved this despite a supply chain environment that remains challenging.

Based on our 2025 guidance, we now expect to reach our CMD targets for profit and cash two years earlier than expected. We have materially increased the potential of the business and delivered at pace. We are upgrading our mid-term guidance based on a 2028 timeframe. We are confident that our actions, investments and how we run the company already significantly underpin future performance improvements.

We now have a strong balance sheet with an investment grade rating from all three agencies. In addition to reinstating the dividend, we are also announcing a GBP 1 billion share buyback, Rolls-Royce's first in a decade, to be completed this year. It is further evidence of our commitment to grow shareholder returns.

Our strategic progress is a result of what we choose to do and how we are running the business. Together, they both enable current and future delivery and develop a sustainable platform to continue to build on. We are operating as one Rolls-Royce, embedding a distinctive performance culture, with a winning mindset where everybody knows their role and how they contribute to strategic delivery.

Our agenda for today, and Jeremy talked about it, is as follows: First, I will briefly talk to the drivers of the step change in performance over the last two years. Laying out some specific examples of our actions set us up, how our actions set us up for continued future delivery. I will then share our guidance for 2025, our upgraded mid-term targets and the key drivers that underpin our mid-term targets.

Helen will then talk to our 2024 results, our mid-term cash outlook and how we are making Rolls-Royce more resilient and our capital framework. I will then finish by talking about the drivers of growth beyond the mid-term.

Let us first look at our delivery over the past two years and the foundations that we have built. Our financial performance has improved significantly over the last two years. This has been achieved despite a supply chain that remains challenging, which understates the true impact of our transformation. Group operating profit has risen by almost 4x from GBP 650 million in 2022 to GBP 2.5 billion last year. Our operating margin has increased from 5.1% to 13.8% last year. All three divisions contributed. Let me give you a brief summary of the key drivers of this performance improvement.

In Civil Aerospace, operating profit has increased by more than 10x from around GBP 140 million in 2022 to GBP 1.5 billion last year with a margin of 16.6%. This has been driven by four factors.

First, stronger LTSA [Long-Term Service Agreement] profitability with a higher profit per shop visit, alongside increased shop visit volumes. Higher LTSA margins have been driven by commercial optimisation, including renegotiating contracts, time on wing initiatives and lower shop visit costs.

Second, time and material profit tripled reflecting improved LLP [Life Limited Parts] margins with almost 60% of LTSA contracts now unbundled.

Third, business aviation profit has more than doubled over the past three years with higher OE [Original Equipment] and aftermarket margins and profit.

And fourth, widebody spare engine profit has improved significantly reflecting commercial optimisation actions.

In Defence, operating profit has increased by 50% over the past two years with a margin of 14.2%. The largest driver was improved aftermarket performance in combat and transport. Submarine profit has also grown significantly.

Power Systems' operating profit has doubled since 2022 with a significantly improved margin of 13.1%. The main driver of higher profit is power generation, where we fix the business model to capture profitable growth. As a result of our actions, we now earn a double-digit operating margin in power generation, including data centres.

Free cash flow has risen by almost 5x to GBP 2.4 billion in 2024 with improved cash generation across all divisions. This was largely driven by higher operating profit and supported by continued LTSA balance growth.

Over the past two years, we have captured more than 50% of total widebody deliveries. This means our market share of the widebody installed base has risen from 32% in 2022 to 36% last year. This helped to drive large engine flying hours to 103% of 2019's level. We have driven a higher normalised EFH rate.

We are also investing more into the business with net investments rising by around GBP 500 million since 2022 which will drive profitable growth to the mid-term and beyond. In

addition, we are seeing working capital benefits as we drive down inventory and receivable days.

Return on capital has risen from 4.9% in 2022 to 13.8% last year, representing significant value creation.

To demonstrate how we improved some of the key drivers for profit and cash, I will now focus on three initiatives that have delivered significant performance improvements over the last two years. These initiatives will also drive stronger performance to the mid-term and beyond.

The first graph shows, we have created a multi-billion cash improvement from renegotiating OE and aftermarket contracts in Civil Aerospace. Over the last two years, we have renegotiated almost all our OE contracts. As a result, business aviation OE engines have turned profitable.

By the end of 2024, we also successfully renegotiated a significant portion of our onerous aftermarket contracts and expect to largely conclude remainder in 2025 and 2026. Only around 30% of these OE and aftermarket cash benefits will be realized by 2028, with the remainder being delivered progressively over time. You can see it on the first graph.

The second graph shows we are driving higher contract margins and therefore higher LTSA margins over time.

Our “contract margin” is the average LTSA margin across all signed contracts, even if the engines are not delivered yet. This is a leading indicator for the LTSA margin that we will book in our income statement in the future.

Our contract margin is improving by 17 percentage points between 2022 and 2028 due to new and renegotiated contracts that are coming in at higher margins and better terms, as well as the operational improvements that we are making. This will drive around a 20 percentage point improvement in the LTSA margins in the income statement over the period. We have already made strong progress in improving both contract and LTSA margins as you can see from the chart.

As our contract margin is a leading indicator for our LTSA margin, in time two lines will converge. Furthermore, our actions will drive further enhancements to both of these margins as we renegotiate more contracts, execute our plans and release contingencies, and as we deliver new operational improvements. These will shift both of the lines up further.

Finally, in power generation, we have restructured our business model and are now delivering a double-digit operating margin. Power generation's margin has increased by more than 10x over the last two years, resulting in a competitive and significantly improved business model. This improvement was driven by reducing overhead and

product costs, driving better pricing and improved mix as we focused on selling higher power engines and eliminating lower power ones.

At our CMD, we set out a target of delivering GBP 400 million to GBP 500 million of efficiency and simplification benefits across the group to make us more competitively advantage, resilient and fit for the future. This target included annualized benefits of GBP 200 million by reducing layers, removing duplication and deriving synergies across the group to enable simpler, more agile ways of working.

We have already delivered efficiency and simplification benefits of more than GBP 350 million, and by the end of this year, we expect to deliver benefits of more than GBP 500 million two years earlier than planned.

At our CMD, we also set out plans to deliver around GBP 1 billion of gross procurement savings over the five years to 2027 to help offset the impact of inflation. We have already delivered more than half of this. By the end of this year, we expect to deliver more than GBP 1 billion of gross procurement savings despite a supply chain environment that remains challenging. Significantly improving our cost base means that our commercial improvements, and therefore gross margin increases, flow directly to our bottom line.

We are also implementing a new global business service strategy which will improve performance further, better efficiency, effectiveness and experience, with a new centre opening in Poland and an expansion of our centre in India. The benefits of this will progressively scale up.

We are also rolling out zero-based budgeting across the group, following successful pilots in Civil Aerospace. These pilots demonstrated savings of 10% to 15% in third-party costs in identified areas. The benefits of all of these initiatives can be seen in our total cash-to-gross margin ratio. This has improved from 0.8 in 2022 to 0.47 last year. If you remember, this ratio in 2019 was actually 0.9. This is a best-in-class ratio providing us with a sustainable competitive advantage.

Hopefully, this gives you an insight into not only how we delivered profit and cash improvements so far, but also how these initiatives will drive improved financial outcomes into the future.

Our strategic plan is based around four pillars. We have made significant progress across each of these. I already covered some of our key strategic initiatives and efficiency and simplification. Let me talk about the rest briefly.

First, portfolio choices and partnerships. As mentioned, we increased net investment by around GBP 500 million over the last three years, focusing on the most profitable projects across the group. In Civil Aerospace, we successfully tested UltraFan in 2023, and we are further improving the design, progressing the development for both narrow and widebody aircraft.

We have invested to grow capacity in Derby, Dahlewitz, and Singapore, which will allow us to increase deliveries of new engines, and by the end of this year, have the capacity to deliver a 50% increase in shop visits as compared to 2023 to support rising aftermarket volumes.

In Power Systems, we successfully tested our next generation engine. This differentiated technology will improve our access to market segments and will enter service in 2028. We announced the disposals of non-core activities of our portfolio, including our direct air capture assets, the naval propulsors and handling business in Defence, and the lower power off-highway engine range in Power Systems. We also made the decision to shut down our electric advanced air mobility activities alongside our electrolyser and fuel cell activities.

Next, strategic initiatives. In Civil Aerospace, one of our most important strategic initiatives is time on wing. At the CMD, we set out our target of delivering a 40% increase in time on wing across our modern engines by the end of 2027. We now believe we can achieve double this time on wing improvement within the same period, i.e., by the end of 2027. We will have already delivered a significant improvement by the end of this year.

Our increased time on wing target is driven by new initiatives. For example, on the Trent XWB-84, we use a combination of a compressor blade modification through the engine in conjunction with improved analysis of millions of hours operating data to systematically raise the cyclic limit of critical parts. As a result, we now expect shot visits to peak in 2026 before falling in the mid-term to below our previous CMD target for 2027.

On Trent 1000, we are in the final stages of the certification of our new HPT [High-Pressure Turbine] blade that will more than double the time on wing of this engine. Flight testing was successfully completed. We have switched over OE production to the new blade already and are aiming for certification in 2Q. We expect to be able to introduce the new HPT blade to all engines across the fleet over the next two years, meaning that it will deliver a near term benefit. We are also on track to complete further improvements to Trent 1000 and Trent 7000 by the end of this year that will add another 30% to time on wing.

On the Trent XWB-97, we are doubling the life of the engine in non-benign environments and increasing it by 50% in benign environments. The first phase of improvements, new coatings for the turbine blade and seal segment, has been certified and is performing well. The next phase of improvements is underway and on track to be delivered by the end of 2027.

Finally, lower carbon and digitally enabled business. Rolls-Royce has unique nuclear capabilities, including SMRs, which I will talk to later.

In Power Systems, we delivered 500 HVO-powered generators to the data centre sector. Our battery storage system business, which will become profitable in the near term, is

growing quickly. We expect to deliver contracts with a total of 2,000 MW over the next two years.

We are capturing the benefits of becoming a more digitally enabled business. We are investing to upgrade our sales and operating planning system and upgrading our engineering mainframe. We are pioneering new tools and techniques in Civil Aerospace, including the use of machine learning and advanced imaging technologies to inspect turbine blades. This results in a faster, more consistent process that extends the time on wing of critical engine components.

Turning now to our guidance for 2025. As you have heard, we delivered a lot over the past three years and laid strong foundations for the group. Our actions and initiatives set us up for another year of strong delivery this year. Our 2025 guidance will see us delivering our operating profit and free cash flow CMD commitments two years earlier than planned.

We expect underlying operating profit of GBP 2.7 million to GBP 2.9 billion, with a year-on-year improvement in operating profit in all core divisions. We expect free cash flow of GBP 2.7 million to GBP 2.9 billion, primarily driven by higher operating profit alongside continued LTSA balance growth. In 2025, we expect a GBP 150 million to GBP 200 million impact from the supply chain to free cash flow, similar to that faced last year. Helen will take you through this in detail.

We are also upgrading our mid-term targets based on a 2028 timeframe. These upgraded targets reflect the strong improvement in performance over the past three years and the potential that we see from the business. A significant portion of the performance improvements to the mid-term are underpinned by the investments and actions that we have already taken. I shared some of them with you earlier. These mid-term targets are a milestone, not a destination. As you will hear later, I am confident and excited about our growth prospects beyond the mid-term.

We target an operating profit of GBP 3.6 billion to GBP 3.9 billion in the mid-term, an improvement of GBP 1.1 billion to GBP 1.4 billion compared to 2024. I will talk to you about the drivers of this improvement shortly. Our mid-term operating margin target is 15% to 17%. This compares to an operating margin of 13.8% in 2024 as we transform Rolls-Royce into a truly competitive company. Our mid-term target for free cash flow is GBP 4.2 billion to \$4.5 billion. This compares to GBP 2.4 billion delivered last year.

Stronger free cash flow is mainly driven by operating profit and continued LTSA balance growth. I would like to highlight one important point here. Our strategic initiatives and actions aim at driving higher LTSA margins and LTSA balance growth. We intentionally do that. Let me explain.

Given our starting point of a young and growing fleet, and the fact that we have a significant time on wing improvement opportunity, you should normally expect continued LTSA balance growth for the foreseeable future. Additionally, our commercial

optimisation and cost efficiency actions further drive LTSA balance growth. I would like to touch on some of the cash drivers, and Helen will talk about cash in detail.

We are capturing more than 50% of new widebody deliveries, which means our installed fleet will grow at 7% to 9% compared to 3% to 5% for the market. These are per-year targets, by the way. We are driving higher normalised EFH rate through commercial optimisation, with a growing cash benefit from contract renegotiations and as new contracts scale up.

Our time on wing initiatives mean that shop visits will peak in 2026 before falling to the 1,250 to 1,350 range in the mid-term. Finally, we expect to deliver an 18% to 21% return on capital in the mid-term, highlighting the economic value creation potential of the business. I believe this will be one of the leading returns in the industry.

I will now talk about the key drivers behind our mid-term operating profit and margins. As I said, Helen will talk about the cash.

These mid-term targets are already significantly underpinned by the actions that we have taken. We expect a continued improvement in operating profit in all three core divisions. The largest improvement will come from civil aerospace, where we target an 18% to 20% margin in the mid-term. We see the potential for this business to deliver a higher than 20% margin beyond the mid-term.

Higher operating profit in civil will be driven by four factors. Firstly, a further improvement in aftermarket performance with an increase in LTSA margins driven by the six levers. As mentioned, the benefits to LTSA margins and cash flows from new contracts will scale up with a further benefit as we negotiate more new and renewing contracts.

I discussed time on wing earlier, which will also be a key contributor to LTSA margin improvements. We now expect to increase the time on wing of our in-production engines by more than 80% by the end of 2027. This will drive a reduction in shop visits in the mid-term.

We are also driving down shop visit costs. By the mid-term, Trent XWB-84 shop visit costs will halve versus 2020-2019, with more than a 35% reduction already achieved by the end of last year. And all of our in-production engines will see a shop visit cost reduction during the time frame.

Secondly, improved widebody OE profitability. By the mid-term, Trent XWB installed engine deliveries will be breakeven or positive, thanks to our commercial optimisation and cost efficiency actions. We also expect higher profitability on spare engines, also reflecting commercial optimisation and mix effect.

Thirdly, a further increase in business aviation performance, with increased volumes as our Pearl engine deliveries ramp up, alongside a continued business improvement with

both OE and aftermarket growing profitably. In business aviation, we expect to grow by double-digit percentages to the mid-term and significantly higher than the market.

And fourthly, these benefits will be partly offset by a reduced contribution from contractual margin improvements. As I mentioned, we expect to finish our renegotiations by 2026.

In Defence, we continue to target a 14% to 16% margin in the mid-term. The performance improvement between now and the mid-term will be mainly driven by self-help. Higher operating profit will be driven by improved OE and aftermarket performance, notably in transport, supported by the commercial optimisation actions we have taken over the past two years. This is partly offset by the divested earnings.

In Power Systems, we now target a 14% to 16% margin in the mid-term. Across Power Systems, more than half of our profit comes from services, notably governmental and marine, but also our gas engines and industrial. This makes our business more robust. We expect strong services growth going forward, which will also support margin improvements to the mid-term.

In Power Generation, we expect revenue growth of 15% to 17% per year, compared to around 10% for the market. This is driven by our differentiated products and systems offering and global account management and our disproportionate weighting to data centres. A good portion of data centre growth to the mid-term is already underpinned by firm orders.

In governmental, we see market growth of 5% to 7% to the mid-term. Our strong programme positions mean that we will grow faster than the market with attractive margins.

And in marine, market growth of 5% to 7%, we expect to grow in line with the market, but at a faster rate than we assumed at CMD. We anticipate significant growth in our lower carbon products, particularly battery storage systems, where we expect very strong growth over the next four years.

Now, I'm going to hand over to Helen.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Thank you, Tufan. Good morning, everyone. I will now take you through our 2024 performance and then for the mid-term, our free cash flow growth and capital frame.

So, let's start with 2024. Strong results. Double digit growth across revenue, profit and cash flow, with the balance sheet continuing to be strengthened. And what's important is that every division is delivering.

Key financial highlights: Group revenues grew by 17% to GBP 17.8 billion, with good end growth across all divisions. Group operating profit grew by over 55% to GBP 2.5 billion, supported by delivery of our strategic initiatives. Operating margin grew by over 3 percentage points to 13.8%.

Free cash flow, it grew by GBP 1.1 billion to GBP 2.4 billion, supported by higher operating profit, continued LTSA growth, and a working capital release, alongside higher net investments.

Strong cash flow generation meant that we closed the year with a net cash position of GBP 0.5 billion, the first time since 2018 that we have been in a net cash position. Return on capital, it rose to 13.8%, driven by improved operating profit and margins. And yes, those strong results have enabled us to declare our first dividend in over five years and to announce a GBP 1 billion share buyback, our first in a decade.

Now to the detail by division. I'll start with Civil Aerospace.

Civil delivered the largest year-on-year improvement in profit and cash; record outcomes. Operating profit grew to GBP 1.5 billion, an increase of 79%. Cash flow grew to GBP 2 billion, more than 3x higher than 2023. Operating margins grew to 16.6%, a 5 percentage point increase year-on-year. And revenues grew to GBP 9 billion, an increase of 24%, with strong growth across both OE and services. Indeed, service revenues grew 28%, driven by higher LTSA shop visits, and the benefit from our commercial optimisation actions.

OE deliveries grew by 16% to 529. Of these, 278 were widebody engines, which included 221 installed engines, giving us a widebody delivery share of more than 60% in 2024. And spare engines were 57, four higher than the prior year, increasing our operational flexibility and our ability to serve our customers.

Business aviation deliveries grew to 251, 174 of which were Pearl engines, where we see strong and growing demand for this leading engine. And total shop visits grew by 7% to just over 1,300. Of these, 430 were large engine refurbishments. That compares to 368 in 2023.

Now, to operating profit in more detail. Four key factors drove that 79% increase. First, higher large engine aftermarket profits. This was primarily driven by our six levers to improve LTSA profits, alongside higher shop visit volumes and increased time and material profit.

Second, stronger business aviation profits across both OE and aftermarket. OE deliveries grew by 28% and were done at higher margins than the prior year. And in aftermarket, shop visits grew by 13%, again, done at higher margins.

Third, cost efficiencies. Our actions supported lower year-on-year indirect costs. This despite continued inflationary pressure.

And fourth, contractual margin improvements. Net contractual margin improvements were a benefit of GBP 235 million. This compares to a charge of GBP 54 million in 2023. The GBP 235 million comprised a benefit of GBP 290 million from catch-ups and a GBP 55 million charge against onerous contracts.

We continued to make good progress across both large engine and business aviation contracts. In large engines, we continued to find win-win solutions with customers. As a result, we released further onerous provisions. We also saw benefits from catch-ups across both large engines and business aviation, driven by our actions on lifecycle costs and commercial improvements.

In total, all of this contributed to a gross benefit of GBP 617 million in the year. However, this benefit was partially offset by additional charges of GBP 382 million, taken across both onerous and catch-ups, largely as a result of prolonged supply chain challenges.

We continue to manage the supply chain very tightly. Let me give you just a few examples of what we are doing.

Procurement and supplier management teams have been integrated. Teams have been upskilled, have better tools and have better processes. In Aerospace, we have secured additional raw material buffer stocks, which we are sharing with suppliers to help them tackle shortages.

We are embedding around 250 people across key suppliers to provide additional skills, capability and to drive stronger integrated planning. Agile teams are stood up. Our Trent 1000 task force is in place. These bring together people from operations, supply chain, engineering, technology, safety and planning. These changes are driving positive impacts.

For example, we increased Trent 1000 supply chain output by around 20% in 2024. We expect the supply chain to remain challenged for the next 12 to 18 months, but it is being managed very tightly.

Let me now turn to cash. Civil delivered more than GBP 2 billion of trading cash flow. That was driven by operating profit, a continued net LTSA balance growth, which I will come back to, and a working capital release. Then investments, which were higher than depreciation and amortization, as we continue to strategically invest in areas such as time on wing, UltraFan, MRO and OE capacity. In summary, a very strong performance from the civil team, delivering higher profit, margins and cash, and all while continuing to invest in the future.

Defence, also a strong performance, reflecting the benefits of strategic initiatives, particularly our commercial optimisation and cost efficiency actions. Order intake, order book, revenue, profit, margins and cash were all at record levels. Operating profit grew to GBP 644 million, an increase of 16% year-on-year. Operating margins grew to 14.2%, a 0.4% increase year-on-year. A strong improvement when you consider the higher mix from the lower margins in submarines.

Order intake was GBP 13.3 billion, with a book-to-bill ratio of 2.9x. This was supported by a first of its kind multi-year submarine contract, worth GBP 9 billion with the Ministry of Defence. Order backlog at the end of the year was GBP 17.4 billion, with an order cover of 90% for 2025. Revenues grew to GBP 4.5 billion, an increase of 13%. This was led by submarines, which reported growth of over 50%, while combat and transport were broadly flat.

As I mentioned at half year results, Defence revenue growth was boosted by a one-off item associated with a submarine contract. Even excluding this, revenue growth was still 7% for the division.

Year-on-year improvement in operating profit was driven by three key factors.

First, strong aftermarket profit led by transport, reflecting a more favourable mix, including more spare parts sales and improved pricing. Second, strong submarines growth, reflecting the ramp-up of programmes such as AUKUS. Third, cost efficiencies, including an increase in customer funded R&D, as we ramp up on projects such as FLRAA, GCAP, B-52 and AUKUS. And these benefits were partially offset by the impact from lower OE volumes, due to supply chain constraints.

Defence's cash flow increased to GBP 591 million. Cash delivery was driven by operating profit and a disciplined approach to working capital. So, a strong year, higher profits, margins and cash, and critical contract wins that underpin long-term growth.

Power Systems. Another set of record results. Significant year-on-year performance improvement was driven by our actions on pricing and costs. And in particular, strong profit growth in Power Gen, where our restructuring of the business has led to double-digit operating margins.

Operating profit grew to GBP 560 million, a 40% increase year-on-year. Operating margins grew to 13.1%, a 2.7% increase. Order intake grew to GBP 5.1 billion, a 19% increase with a book-to-bill ratio of 1.2x. OE order coverage for 2025 stands at 82%. Demand remains particularly strong in power generation, where we have strong exposure to the fast-growing data centre market, leading to a 42% increase in orders. In governmental, our order intake was also up by a third year-on-year.

Revenues grew to GBP 4.3 billion, an increase of 11%. Power generation and governmental delivered increases of 25% and 17% respectively. Data centre revenue growth was 46%. You will see on the slide that industrial revenues were 20% lower year-on-year. This was largely due to the disposal of the lower power range off-highway business.

Operating profit growth was driven by three factors. Commercial optimisation. We continued to see the benefits from our pricing actions. This was particularly evident in power generation, which also benefited from an improved mix as we focused on larger, higher margin products. Battery energy storage systems, where we continue to see

strong opportunity and where we are on track towards profitability in the near term. And cost efficiencies, where our actions helped mitigate the impact of inflation.

Trading cash flow stood at GBP 452 million. That compares to GBP 461 million in 2023. This slight decrease reflected strong operating profit growth, record levels of investment, for example, in our next generation engine, which will offer best-in-class fuel efficiency and power density. And higher working capital as we support continued business growth. To wrap, a strong outcome for power systems across all key metrics.

Now, let's move to the cash flow. We delivered GBP 2.4 billion of free cash flow, more than GBP 1.1 billion higher than in 2023. The main driver of the year-on-year increase was higher operating profit, which grew by approximately GBP 900 million.

Other factors included:

Investments. We continue to invest for future growth across the group, with a clear focus on investments that are strategically aligned; attractive projects that generate profitable growth to the mid-term and beyond. These include our GBP 1 billion multi-year time on wing programme. Additional capacity in Derby, Dahlewitz, and Singapore to support higher OE and aftermarket volumes, continued investments in Power Systems and Defence. Investments in our engineering mainframe and in our sales and operation planning processes. As a result, net investments were GBP 280 million of an outflow. That is GBP 360 million higher than in 2023.

The net LTSA balance. This was just below the lower-end of the guided range, standing at approximately GBP 700 million at year-end. Around GBP 400 million lower than in 2023. The net LTSA balance was driven by higher engine flying hours and an improved normalised engine flying hour rate. This was partially offset by a higher number of shop visits, including a record number of Trent 1000 refurbishments and the impact of managing through supply chain headwinds.

Then, working capital. As you know, this is one of our key priorities at CMD and we continue to make good progress. We released around GBP 280 million of working capital in the period. That compares to a build of GBP 360 million in 2023, a strong performance given industry-wide supply chain challenges and while we supported revenue growth. We are driving a much stronger working capital culture and discipline across the group.

In the two years since we stood up our working capital programme, inventory days have improved by more than 45 days. Day sale outstanding by 14 and overdue debt has fallen by more than 40%.

Next, provisions. They were an outflow of GBP 170 million. This included outflows as we traded through our onerous contract provisions. They were about GBP 100 million lower than in 2023.

Then, over-hedge costs. As guided, they were around GBP 150 million, more than GBP 200 million lower than in 2023.

Net interest costs. They were broadly neutral, an improvement of GBP 145 million year-on-year, driven by improved cash delivery.

And finally, cash tax costs. They stood at GBP 380 million, GBP 200 million higher than in 2023.

Tufan shared the free cash flow outlook for 2025. Let me give you some additional data to help with your models.

We expect the net LTSA balance growth to be at the lower end of the guided range of GBP 0.8 to GBP 1.2 billion. This reflects continued growth in large engine flying hours to 110% to 115% of 2019 levels, and a higher normalised engine flying hour rate, as well as the impact from higher shop visits which grow to between 1,400 to 1,500, and the continued impact from the supply chain environment.

We expect net interest costs to remain broadly neutral. And then the cash tax costs of unwinding the over-hedge position to be similar at GBP 148 million. And cash tax costs to be around GBP 200 million higher.

Resilience. We have been consistently clear that our key priority is to make our business more resilient. Our results today demonstrate that we are delivering. Operating leverage continues to fall. We continue to strengthen the balance sheet, returns continue to improve.

Tufan shared how our total cash costs to gross margin ratio is now a best-in-class, and there is more we want to do.

The balance sheet is being strengthened. Look at the chart in the middle. We reduced net debt by GBP 2.4 billion in the year. To end 2024 with a net cash position of GBP 500 million. In May, we reduced gross leverage by repaying a EUR 550 million bond. And we cancelled the last remaining undrawn UKEF supported loan.

Our liquidity position also remains strong. Standing at GBP 8.1 billion at year end. And as you've heard, all three credit rating agencies now rate us at investment grade. And all three hold us on a positive outlook.

The chart on the right brings home our improved resilience. We're in 2019 for the first bar. It represents the percentage decline in large engine flying hour receipts. That would have taken the group to a cash flow break even position.

Now look at the right-hand bar, which shows the equivalent percentage in 2024. Across the group, we could have weathered a much steeper decline in engine flying hour receipts—almost twice the level of 2019. Twice the level. And we would still have achieved

cash break even. We are building foundations that are much, much stronger. We are a much more resilient business.

Now moving to the mid-term free cash flow. Which as a reminder, we hold as a 2028 timeframe.

We are driving for sustainable, higher quality cash flow growth as we continue to improve the business model. And benefit from the actions already put in play. We are targeting between GBP 4.2 billion and GBP 4.5 billion of free cash flow. A growth for around GBP 2 billion compared to 2024.

The main elements of this growth are operating profits. Growth of between GBP 1.1 billion and GBP 1.4 billion over the period is key. We achieve that by continuing to strategically and sustainably expand the earnings potential of the business with every division delivering.

LTSA. By the mid-term, we expect the net Civil LTSA balance to grow towards the top end of the GBP 0.8 billion to GBP 1.2 billion range. We will drive LTSA growth through five important factors.

One, continued engine growth and engine flying hours. Driven primarily by air growing installed fleet. As we continue to grow faster than the market. We expect large engine flying hours to grow to between 130% to 140% of 2019 levels by the mid-term.

And business aviation where we hold a material and growing market share. And where the time between shop visits is longer driving LTSA balance growth.

Two, a higher average normalised engine flying hour rate. You have heard how a significant amount of work has been done to improve our LTSA contracts. And how most of the cash benefit is still to come.

Three, time on wing. Which helps extend the time between shop visits. So also supporting LTSA balance growth. We've shared how the opportunity is significant. And how we're going even further than initially planned. And again, most of the benefit is still to come.

As a result, we expect shop visits to peak in 2026. And then fall to around 1,250 to 1,350 by the mid-term.

Four, we expect an advance of the mid-term. The cash drag from the supply chain to be gone.

And five, currency. The consumption of our legacy hedge book means our mid-term guidance assumes a blended forex rate of \$1.31 to the pound compared to \$1.48 in 2024. This will drive a higher sterling equivalent for our dollar-based inflows.

Next, investments. Our approach will continue to be disciplined with spend always prioritising safety and strategic growth. Looking across the period, we expect CapEx and R&D to average above depreciation and amortization.

Working capital. As group revenues continue to grow, this will naturally result in an increase in working capital. Our working capital programme will help mitigate this impact.

As shared at CMD, we had a gross working capital reduction target of around GBP 2 billion by 2027. We have plans to go further.

Taking all of this together, hold that across the period, we expect to release working capital. Then, the cash costs of closing out over hedge positions, which were a drag of GBP 146 million in 2024, will be gone by 2027. And, as our profits grow, cash tax payments will naturally increase.

Whilst we expect cash to grow in all years between now and the mid-term, it is important to note it will not necessarily always be linear. Due, for example, to the timing and mix of shop visits.

Capital frame. Our frame will continue to focus on striking a balance between three clear priorities. A strong balance sheet, a commitment to regular and growing dividends, and a disciplined approach to further investments and to additional shareholder distributions.

First, the balance sheet, which we have worked hard to rebuild. We are now in a modest net cash position, which is not uncommon in our industry, and a sensible place for us to operate from, especially in the near term.

Gross Debt. We will reduce it further, repaying from available cash the USD 1 billion bond, which matures in 2025. These measures, along with strong operational execution and earnings and cash flow growth, should help us achieve a strong investment-grade rating.

We have made good progress building balance sheet resilience, and as we continue through transformation, we will remain prudent in our approach to leverage, and we will maintain robust liquidity levels.

Then, distributions. Having strengthened the balance sheet, we are now able to reward our shareholders with a competitive level of returns. As shared at our 2024 half-year results, we are reinstating regular shareholder dividends, and we are pleased to announce that the Board is recommending a cash dividend of 6 pence per share in respect of the full year 2024, representing a pay-out ratio of 30% of underlying profit after tax. The first dividend paid by Rolls-Royce in over five years, and a distribution to shareholders of approximately GBP 500 million.

Going forward, we will pay an interim and a final cash dividend each year, and full-year dividends will be based on a pay-out ratio of between 30% to 40% of underlying profit after tax. We assume an effective tax rate in the mid-20% range.

Over the mid-term, we expect to be broadly in the middle of that 30% to 40% pay-out ratio. A competitive pay-out ratio for our industry, and as our earnings grow, so too will our distributions.

Another important milestone in our transformation, we are announcing a share buyback. It will total GBP 1 billion, will start immediately, and will complete over the remainder of 2025. Taken together with the dividend, this represents a total distribution to shareholders of GBP 1.5 billion, competitive and evidence of our commitment to growing shareholder returns.

Going forward, we will continue to strike a balance of holding a strong and flexible balance sheet as we make active and disciplined capital allocation decisions to drive shareholder value, be they further investments, organic or inorganic, or additional shareholder distributions, all of which will be assessed by strategic fit and how they contribute to growing long-term value.

To close, when we spoke at Capital Markets Day in 2023, I said transformation was not easy, but that it could be done. Our results today clearly demonstrate not only that it can be done, but that we are doing it.

Everyone in Rolls-Royce has worked immensely hard. It's most definitely been busy. We are immensely proud of everything that everyone has done. And we are clear there is more to do and there is more to come.

With that, let me pass you back to Tufan.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay, there is definitely more to do and more to come, and I'm going to go to that. But before I go to that, let me recap. Thanks, Helen.

We covered a lot of ground, so let me recap on the key messages. Our transformation programme has already delivered a step change in financial performance across the group. We have given you insights into what we are doing and how we are achieving this. The strategic actions we have taken and the investments we have made significantly underpin our 2025 guidance and upgraded mid-term targets. In fact, the full benefits of our actions will not be realised in full until beyond the mid-term.

Let me now talk to you about why we are excited about the outlook beyond the mid-term. In civil aerospace, we are uniquely positioned to capitalise on our advantage positions in widebody and business aviation.

As discussed earlier, the benefits of our OE and aftermarket contract renegotiations and commercial optimisation actions on new and renewing contracts are progressively scaling

up, with the full benefits to come beyond mid-term. As contracts with higher margins scale up, we expect to deliver further progress in improving LTSA margin and cash generation.

The same is true for time on wing. We are spending GBP 1 billion on improving the time on wing of our modern engines by the end of 2027. Not only will this investment be concluded by that point, but the cash benefits of our time on wing improvements will ramp up beyond the mid-term.

UltraFan positions us strongly for the next generation of aircraft, either wide or narrowbody. UltraFan is 10% more efficient than the Trent XWB-84, the most efficient engine in the market. It has a geared architecture and is 100% SAF sustainable aviation fuels compatible.

In business aviation, we are strongly positioned on the latest large cabin business jets, including the G700, G800 and the Dassault Falcon 10X. All of these improvements in Civil Aerospace are complemented by widebody and business aviation growing faster than the market. In Defence, the growth will be driven by ramp-up of several major programs. On the B-52, we expect to deliver around 600 engines, with production starting in the late 2020s.

On FLRAA, OE revenues will also start to ramp up in the late 2020s. As a replacement for the Black Hawk helicopter, this looks set to be a very large programme, with potential for significant export sales, in addition to the sales to U.S. Army. Production for GCAP, a next generation combat aircraft, will be ramping up in the mid-30s.

And in submarines, revenues from AUKUS will ramp up by around 50% from today to the late 2020s. This is a CapEx light business model with a very high return on capital. Rolls-Royce looks forward to powering the U.S. Navy's MQ-25, the first autonomous refueller in aviation history. This aircraft will use the AE 3007N engine and expands Rolls-Royce's leadership in unmanned propulsion.

In addition, we anticipate sustained demand for our mature and profitable products in both combat and transport, for example, the EJ200 engine for Eurofighter. Our strong product offering means that we are well-placed to win future contracts. Great examples of this are the SAOC and TACAMO contracts that we announced last year.

In Power Systems, we have differentiated products in power generation, governmental, marine, and industrial end markets. They are all expected to grow. Our position in power generation remains highly attractive with significant long-term growth potential in data centres.

Additional profitable growth will be underpinned by our next generation engine in power systems, the first new engine in over two decades, which will offer significantly improved power density and efficiency. This differentiated product will create commercial opportunities and new market segment access.

We also see exciting opportunities in our lower-carbon products, notably profitable growth from battery storage system business, and for lower-carbon fuel products, for example, hydrogen for our stationary business, methanol for marine, and the increased use of HVO for data centres, mining, and rail.

Our unique nuclear capability also means that we are well-placed to capture growing demand for SMRs. We see a significant market opportunity for micro-reactors in defence, space, and commercial applications.

Finally, we see a significant value creation opportunity in SMRs, which I will talk to now.

We are uniquely placed to win in this large and growing market and create significant value. Let me explain why.

Rolls-Royce SMR is a business with a unique and differentiated product offering and an attractive cash-generative business model. The addressable market for SMRs is large and growing quickly. The International Energy Agency, IEA, currently forecasts that global electricity generation will double by 2050.

Nuclear has a growing role to play from an energy supply security and net zero perspective as other continuous generative assets are phased out. Based on IEA's estimates, we see a credible SMR market of almost 200 gigawatts by 2050, equivalent to around 400 of our 470-megawatt SMRs. We are well-positioned to win in this market.

Rolls-Royce has over 60 years' experience in powering the UK Royal Navy's fleet of nuclear submarines. Our SMRs are based on proven technologies. Our SMRs are fully modularised, reducing deployment time and opening up new locations without customised infrastructure needs, which will reduce cost and speed up our time to market.

Around 80% of our SMRs will be built in factories as opposed to on-site, materially reducing the risks associated with traditional nuclear projects. The larger power output will result in green electricity at a highly competitive cost without the intermittency issues associated with solar and wind. Therefore, they don't require storage or backup systems.

Finally, we are around 18 months ahead of our competitors in the GDA regulatory process in the UK.

Rolls-Royce SMR is already winning and making significant progress. Last year, we signed a new strategic partnership with ČEZ to deploy up to six SMRs in the Czech Republic. We were also down selected in both the UK and Sweden's competitions. Additionally, we have significant interest from many other countries.

Our cash-generative business model is very attractive, with positive OE margins from the very first unit, rising over time driven by economies of scale and the learning curve effect.

Our SMR contracts will also be immediately cash-flow-generative because of customer advance payments, as shown on the chart on the right. More than 80% of the components that make up our SMRs will be delivered by third-party suppliers. This will materially reduce our capital intensity and mitigate risks.

As a result, we expect to generate a strong double-digit return on capital from SMRs. Risks also be tightly controlled. Using tried and tested technology towards R&D reduces risk and increases speed to market.

Our financial risks are shared by our strategic partners and suppliers, each of whom bring key strengths and capabilities to the business. For example, ČEZ, who has experience as a nuclear operator and brings deep supply chain capability. And our initial contracts will have margin protection built into them, using for example “cost plus” contracts.

So, this is a differentiated business and one that we believe has a significantly higher value than its listed or unlisted peers. The value of the business will grow materially from now as we successfully execute and deliver growing revenues, profit and cash flows.

To summarise, we are delivering on our proposition to transform Rolls-Royce into a high-performing, competitive, resilient, and growing business.

We have achieved a lot over the past three years, with significantly improved financial performance across the group, driven by our strategic initiatives, despite the impact of a challenging supply chain environment. We are delivering this at pace. Our 2025 guidance will see us delivering our CMD targets two years earlier than planned.

Today we also issued new upgraded mid-term guidance, benefiting from our expanded earnings and cash potential. Our strong delivery over the past two years gives us confidence that we can not only achieve our mid-term targets but also significantly grow beyond the mid-term. This growth is underpinned by our strategic initiatives and the investments that we have been making over the past two years and their continued implementation going forward.

A stronger balance sheet also gives us confidence to reinstate dividends and enhance a GBP 1 billion share buyback for 2025. These all show our commitment to grow shareholder returns. We have made great progress and we see a lot more potential. We are creating a sustainably distinctive business in terms of safety, operational excellence, customer service, advantage products and technologies with a high-performance culture.

I am very proud of the Rolls-Royce team and what we delivered so far. They know their role in delivering our strategic progress and are energized to make a difference.

Thank you for listening.

Now we are going to open it up for your questions.

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

Thanks very much everybody. We will take questions in the room and then if there is time, a few on the webcast.

So, you are quick Charles, do you want to start?

Charles Armitage

Analyst, Citi

Yes, good morning. Charles Armitage.

One clarification and a couple of questions. The first is a clarification. I think you said amongst your key drivers of improvement pretty much in the first three minutes of your comments, there was something about T&M and moving LTSAs to T&M. Is that -- what did that mean?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Yes.

Charles Armitage

Analyst, Citi

The other two questions are, one is the Trent 1000 time on wing improvements. Does that mean you can start regaining share or is it a case of most of the widebody choices have already been made and you will probably be ticking along in the 20% to 30% range?

The third one is GBP 450 million improvements from procurements from 2024 to 2025, GBP 150 million in indirect, that is GBP 600 million, possibly offset by some of the catch-ups maybe, also whether contract provisions, owners contract provisions. Sounds like your '24, your '25 EBIT looks a bit low.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Sorry, are you talking about cost improvements?

Charles Armitage

Analyst, Citi

Yes. What is the offsetting factor on the cost?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Yes, I will come to that. Okay, let's go in the order, I think.

Clarification, what I said is, I think in CMD we talk about that. We have been unbundling LLPs because it gives you more flexibility with commercial optimisation and so on.

So, I said in my speech that 60% of our contracts are now unbundled, that's what I said.

Charles Armitage^ Okay.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Trent 1000, yes, that's what that means. Frankly, we are -- I said it in my speech, we are making good progress. By the end of this year, this is going to be totally competitive engine in terms of time on wing.

And the main issue with Trent 1000, I know this precedes my time definitely, there are lots of noises about this. Reliability of this engine is as good as the next. Our main issue has been time on wing. And we are effectively fixing it for good, and we know it works. I mean, flight test was successful, but it wasn't a surprise, because, Trent 7000, we actually did it.

Now, Trent 7000 is performing, last three years, better than we expected. It is the -- as you know, they are brother, sort of, engines. So we are saying doubling the time, but, actually, Trent 7000, so far, even in an environment like Kuwait, performing brilliantly.

So -- and this BoM B -- we call it BoM B, first improvement will bring in 2Q, once the certification happens, actually, that will double the time on wing. Then, the next improvement by the end of the year will come with 30%.

But the good news is this required flight test, and therefore, Boeing -- working with Boeing and FAA certification, et cetera. The other one is only engine level certification we can quickly implement it. Yes, we are looking to increase the share on 787. Why not? Because this is going to be highly competitive product. That's why we focused -- we focused on that.

Your sort of calculation, I will challenge that a little bit, because you cannot add them up that way, because there are -- we are -- for example, procurement. We are saying those things will offset -- partially offset some of the supply chain increases, number one.

Number two, while we are decreasing indirect costs, as you highlighted, we are growing -- we are increasing other costs, okay? So therefore, you -- these benefits help. Gross margin flows through, but you cannot add them up the way you just did.

So, it is not a catch-up or onerous contract issue, because, as we -- as we talk about in our conversation, we still expect good sort of onerous and catch-up in '25 and '26. We are making great progress after '26, they go -- especially, onerous go down.

Catch-up will definitely not disappear, because, as we continue -- the way you should hold catch-ups is underlying business improvement. Actually, onerous contracts is also underlying business improvement by definition. But therefore, we continue to improve the business, catch-ups will continue to be there.

You raised, actually, first your hand, but Jeremy weren't there, so I let that happen. So, I don't want to be unfair. So --

Chloe Lemarie

Analyst, Jefferies

Thank you. Chloe Lemarie from Jefferies. I actually have two questions. The first one is on the contract margin improvement from 2022 to 2028. Could you maybe break down the 17 points between what you got on pricing versus cost, versus time on wing improvement? And is it fair to assume that the improvement beyond 2028 would be mainly the remainder of the time on wing benefits that you're targeted by 2028?

And the second question is, actually, on the narrowbodies. So, can you detail the key technologies that you'd bring to a potential partner, because we're seeing the two incumbents going very different routes, technology-wise? So how do you think you would fit into that landscape, please?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. Two good questions. I think -- contract, let's talk about that. I'm not going to break it down for you. That's why we talk about six levers, but they all played a role.

So if you ask me, what are the big ones? You -- specifically, you talk about contract margin. So contract margins -- it is very true that new contracts are coming with a much better margin profile than our historical contracts, okay?

Contract margin, even if -- as I said in my speech, even if the engine is not delivered yet, once you sign the contract, it becomes contract margin, if you like. Therefore, even some undelivered engines in that with higher margins. Definitely, the further you go, that mix will change in favour of us, because old contracts will expire, new contracts with higher margins, that will continue, definitely -- that plays a big role.

Renegotiate contracts play a big role. I showed you the cash profile. We are talking about multi-billion sort of numbers there. Those two -- and then, time on wing, probably three big things, like shop visit cost, in this period, XWB went down, but, actually, in the

next period, shop visit reductions will add more than it did in this period, okay? That's how you may -- why you will say supply chain didn't allow us to do some of the things there, okay? Product cost the same. Next period will be better than this period.

So, your point around going forward, I would disagree with your characterization. So, let me tell you how it is going to play out. So, that's why I said, my expectation, those two curves will shift up. Why?

So, first of all, if you actually -- we said we are going to renegotiate more contracts, '25-26, that's not in the numbers, because this is only what we achieved rather than what we may achieve, if you like. So those things -- we are making good progress. That will actually increase that.

Operational improvements will definitely improve that. But also, even if you deliver your plan, so the way you think about our contracts, inherently, you say I'm going to achieve time on wing X, like, I'll -- I will double time on wing on Trent 1000. You put a contingency against that because it's not 100% certainty that you will.

If you effectively execute that, which we have been doing so far, you actually release the contingency. So even executing your plan on time, in budget, will improve those things. Therefore, three things will improve.

Further renegotiations, executing your plans the way you want to execute, and then finding new operational improvements and time on wing going from 40% to 80% is enormous. This is not sort of peanuts.

So, that is -- that's -- If I go to your narrow body, so, I will say this, we are very well-positioned on narrow body. Therefore, everybody is talking to us and we are talking to everybody. So I said it in CMD, we -- our preference is partnership. We don't need partnership for capability, but our preference is that.

So, we will see where that goes. It is early days. But we have -- with UltraFan, great technologies, that's why everybody is talking to us, and great engineering capability in general there. And UltraFan is more efficient engine, as I said, than any other engine available in the market at this point in time.

And the IPs we have on that, on a gear structure, is very favourable. Let me put it that way. So, I think we will see how that story unfold. But we believe we can actually do things in that space.

David, you were third.

David Perry

Analyst, J.P. Morgan

Yes, thank you. I've got one very short question, one slightly longer. The short one is, would it be silly just to assume ongoing share buybacks every year, given the amount of cash you're going to generate?

The longer question, if you bear with me, is, you've told us that the Civil Aero margin in '28 will be 18% to 20%. You've also told us that the bulk of the widebody OE, your biggest engine, is going to be breakeven, which is a lot better than I assume.

Very crudely, the implication of that is LTSA margins are probably still only 30% in 2028, which is a lot lower than the aftermarket margins of your peers. So, would you agree with my crude maths? Apologies if I'm wrong. If you do agree, why are the LTSA margins so low and where could they go to?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. I'm going to ask Helen to answer buyback programme. Let me answer your, sort of, operating margin question. So, I think -- first of all, I didn't say all engines, because we still have -- at that point, we want to sell Trent 1000 and A380 -- sorry, A330neo, obviously. I was only referring to XWBs, which is factually correct.

Second, I think when you think about, sort of, your calculation, David, especially from today to that point, today, we were very successful with negotiations. Therefore, we were able to book, yes, some of it, as Helen talked about, because of product costs and supply chain challenges partially offset, but we were able to deliver big commercial improvements.

That will not be available by mid-term, because, we will have done that already. So onerous contracts and so on, we will have delivered by that time, frankly.

So I think that is going to be for 20 timeframe that will be negative, definitely, in the equation.

Do you want to answer buyback?

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Thanks, David. So, David, hold it, we have a clear capital frame, and as we've said, going forward, we will be consistent as how we strike that balance between our priorities.

We've been consistently clear we will protect the balance sheet, with a net cash position or modest net cash position. We're comfortable operating from there, particularly in the near term. Not an unusual place, as I said, for the industry.

Then, we'll ensure that shareholder dividends are regular. They will continue to grow in line with their earnings growth. And then, we will continue to assess the options beyond that, be it additional investments, organic, inorganic, or additional distributions, and buybacks are in that toolkit.

But we'll be very disciplined as to how we assess that. We will look at the strategic fit. We will look at what they do for shareholder value and return, and we'll look at the appropriateness of the timing of that. So that's how you should hold that going forward.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

You, go ahead.

Ben Heelan

Bank of America, Analyst

Hey. Morning. Two for me. So firstly, Tufan, time on wing, going from 40% to 80% is obviously a very, very significant improvement. You've been talking about 40%. Come on. Like, how are you getting there? Like, what is -- what is really incremental that is driving that material improvement, because it is significant?

And then, on your 2028 guide, your cash is still significantly ahead of your profit. So when we think about your guidance beyond the mid-term, you've given us some colour. Is that cash going to roll and meet the profitability, or is the profitability going to come up as the cash flow will continue to grind higher, because, at some point, there's going to have to be a realignment there? So, those were the two. Thank you.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

That's great. Normally, I pass to Helen. I'm going to make, on the second one, one big point, because I think -- I think you may want to think about this slightly differently. I'm going to make an offer to you. Then, Helen will, obviously, build on it.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

I don't know what's coming.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

So, full of surprises, life, I guess. But, time on wing, this -- there is the direct answer, which I will come to. Then, there is the, sort of, how does that happen, right? Here is how that happens.

Effectively, that's an insight into how we run the business. I keep saying, we are running the business differently. I'm not sure it resonates yet. But this is part of that. So, Rolls-Royce has been talking about time on wing, I don't know how long. It definitely precedes my time.

But when you actually put, okay, we are not going to talk about it. We have made strategic choices, not very granular strategy. That cascades into 17 strategic programmes. Whole company, if you are working for Rolls-Royce, you are working one of those programmes. So you know your role, right?

By resourcing, time on wing is one of them. You wouldn't be surprised. By resourcing with the right talent, right money, suddenly, you accelerate and more stuff comes out. So I can repeat this. So, this is an insight to you, how we run the company.

There is the direct answer to you. This is mainly -- I actually referred to that in my speech. This is mainly -- other programmes are there we have been talking about it. But, mainly is XWB-84. XWB-84, effectively, what we did there is, it's a conjunction -- combination of two things. We actually do a modification on compressor blade. We are hardening the root of the blade, effectively. That's what we are doing there.

In addition to that, this is millions of hours of operating data with higher fidelity understanding of speed, pressure, and temperature within an engine, with a highly instrumented sort of testing. So normally we do our LLPs, when I say critical parts, some of critical LLPs there, okay?

We do it different than our competition. Our competition goes with long times, a lot longer than we put on LLPs. We go, here is the limit, and only when we understand operational with high fidelity, we sort of raise the limit, right? So, on XWB, we had a great time on wing, mostly driven by HPT blade, right? Our time on wing limitations mostly come from HPT blade. So, think that way.

So -- but the issue was, so HPT blade goes from here to here, more than 4,000 cycle, actually, which is, for the new engines, enormous. We had LLPs cannot go that long. So when you actually take those LLPs up because of the process I talk about, suddenly, you

have enormous, and actually, refurb reduction in this timeframe. We talk about after '26. That's a combination of two things. Effectively, refurb reduction in -84 because of this, because it is refurb, because we are changing many parts. It is refurb. Combination of that and Trent 1000 blade change not required with non-refurbs. So you see both of them go down, and that actually drives total shop visit costs down. I hope -- long answer, but I wanted to sort of give you -- this is not smoke and mirrors sort of thing.

But we may find more opportunities. I just -- therefore, I went through that. But on the cash, obviously, Helen will answer it. But I would like you guys, here's the offer, to think about LTSA balance growth slightly differently, okay, for us.

We have a young growing fleet, and we have big time on wing improvement opportunity. If our starting point was everything is brilliant, time on wing, this 80% is not there, then, I think you may be right, when does it actually end?

But our starting point is -- I'm telling you, almost doubling time on wing, and you are in this industry, right? You will know what that means for the whole modern engines, right? That, plus all our programmes do two things, increase the cut effectively balance -- LTSA balance, and increase our take on it, our margin. That is what is designed for, effectively. Cost efficiencies the six levers, plus everything else we do, renegotiating, all that.

So, effectively, when you guys continue to think -- I think this LTSA balance growth, sort of, temporary, think again, because of our starting position and because of what we do for -- I'll tell you this. Our Trent 700 LTSA balance didn't peak yet after 30 years.

You will say, why, Tufan? I will say, you keep improving it, right? So, now, Helen will answer, but I wanted --

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

I don't know what's left to say?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

But, I want you to think very differently about LTSA balance. That's why I said it. Because some people think, oh, that's not cash. It is. Why am I driving it if it is not? And the important thing is, when I'm driving it, I'm increasing my portion significantly, 20 percentage points. We are not done.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

I think I'm just going to summarise. So, I mean, if you think about cash in 2028, so around GBP 2 billion higher than in 2024. Think of five things behind that. Operating profit

growth, obviously, of over a billion. LTSA gets to the top end of that range because of their actions.

Supply chain, that drag has gone away. Onerous, we heard in 2026, how we've been through most of our onerous contracts. So as you know, when we do that, you get the profit benefit, the cash takes a longer time to come through. And then tax, obviously, we expect to grow.

But that LTSA growth, as you've heard, because of our position in that young and growing widebody fleet, what we're doing around LTSA margins, what we're doing on time on wing, up to 2028, there is some Forex benefit, all of that helps support.

And I think your example of the Trent 700 is a fantastic way to bring that to life, an engine that's been in service for --

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Thirty years.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

30 years?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Exactly.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

And we actually we haven't --

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

1994.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Yes. And we haven't seen that LTSA balance peak yet. So, I think that's just an easy example to bring that to life. But that's how you should hold it going forward. Yes. Thanks.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Yes. Then, I'll go there.

Ian Douglas-Pennant

Analyst, UBS

Thank you. Thirteen years of an (inaudible), I still haven't got used to these microphones. Trent 1000 certification is now expected in Q2 versus Q1 before. Could you help us understand what the -- what the slip there is?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

I mean, it's very simple. Boeing strike two months that delayed around two months.

Ian Douglas-Pennant

Analyst, UBS

Okay. I'll follow-up on that afterwards.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

No. I mean, it is -- because it's a successful test and there isn't anything else yet. So, we said at first half -- 1Q, then, frankly, Boeing strike sort of happened and we couldn't continue with the flight test.

So, we start -- if you remember, I think I said it early August when we were making presentation. We started flight tests yesterday or something, I said, which was true. But then, we had to stop when the strike happened.

Ian Douglas-Pennant

Analyst, UBS

Thank you. Helen, just to follow up on David's question earlier. Do you have a target capsule structure in mind, a certain gearing ratio that you're aiming before? You mentioned something at H1 last year, and then we haven't heard that again.

And then, last question. There was -- there was one slide, Tufan, late in your presentation, where you -- if my read of that chart is correct, you suggest that SMR will be as big or larger than Defence in 2040. Can I just sense check that as a statement?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. So I'll answer that, and your capital frame question, Helen will answer it. But, so, it can be, right? I mean, it can be. If you actually think about it -- the reality is, I always start with big picture. Does that actually make sense, right?

Whether you are a supply security person or net zero person, SMRs will have to play a big role, definitely in Europe, if not, the world, but definitely, in Europe, therefore, quite a few central European countries went there already, as you know, and some of the Scandinavian countries as well.

So I think that big picture is true. I mean, I come from energy industry. I can tell you this. You don't want to go to net zero with solar and wind, because it will be -- with the energy storage technology in the world available, that will be a disaster solution for any country, goes there with solar and wind if -- with the current technology, unless you put a gas-powered backup system, which will be a lot more expensive than SMR, right?

So, when I say SMR, big picture, it makes sense. It is a competitive electricity. If you take into account, you are going to do like gas with CCS, then SMR will be cheaper. Electricity cost, I'm talking about. Or solar and wind with a backup system, again, SMR will be cheaper.

So, therefore, big picture, it makes sense. Comparatively, it makes sense. Therefore, it can grow quickly. Absolutely, Ian. So, I'm not going to speculate, sort of -- because, those numbers -- the point of that chart, there is lots of underpinning. They are not as robust numbers as our mid-term targets, by the way. So there is a qualification there in that sense. But, over to you.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Fantastic. So, thanks for the question, Ian. And you do have a good memory as I've come to expect from you. So, net cash, as I said, we're comfortable working from that net cash position, particularly in the near term.

We're back to investment-grade rating. We would like to actually get to a strong investment-grade rating. So if you think about what that equates to, it would be commensurate with a leverage of up to 1 and 1.5. So, we could go up to that point.

But we would obviously be very deliberate if we did that. It would need to be for the right opportunity, which we would assess against our very strict criteria around strategic fit and how it drives shareholder value. And I think just worth saying, in case it's at the back of your mind, we don't have any intent of leveraging up for buybacks.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Thanks, Helen. Yes.

Nick Cunningham

Analyst, Agency Partners

Thanks very much. Nick Cunningham from Agency Partners. It's a little bit of a detailed one, and then, perhaps, a very general one. The supply chain charges that you saw going, GBP 382 million in Civil, I just wondered what exactly those are. Are they your best guess at the impact on the cost to complete on the existing contract portfolio, and therefore, do they not recur, or are they a sort of in-year cost? So that's the first question.

And the second, much more general one, the cash flow, both in the year you just reported and looking forward, it's very pleasing, particularly because I didn't actually believe my own forecasts, but they were roughly there. That does have the effect of making cash pile up very rapidly and in very substantial quantities. So that really obviously opens up those strategic opportunities.

In the broadest sense -- because obviously you don't want to open too much, but in the broadest sense, where do those opportunities lie in sort of general -- within your existing segments or in nuclear, or whatever? Anything you can say would be interesting. Thank you.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

So, Helen, do you want to pick up both of them, and I may add sort of where I see in the big picture opportunities bit?

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Fantastic. So -- thanks, Nick. So as you see, charge in the supply chain is just under 400. That reflects our best estimate based on supply chain situation at the minute. The way that long-term contract accounting works, if you've got onerous contracts, then that impact that you see, you actually take it all in year. So that's how you should think about that.

In relation to what's driving that, I mean, it's very consistent with what we spoke about in the past, you know, particularly part supply availability, casting, forging. As we said, we expect the supply chain to remain a challenge for the next 12 to 18 months, but that's how you should hold it. That's our best view at the minute.

In relation to cash flow, and you said that pile up, I think it gets back to some of the questions earlier. We've got a clear capital frame as to how you will think about decisions about what we do with cash balances, and how we strike that balance between the strong balance sheet you've heard, how we want to get to strong investment-grade rating.

We've got a clear dividend policy. We've started at 30%. We expect to be in the middle of that range going forward. Not only is that an increase, but as our earnings grow, if you're doing a payout ratio, the dividend will also grow as a result of that.

And then, we've got clear guide rails as to how we will assess opportunities. Organic/inorganic, which I think Tufan wants to speak about, or additional distributions, which could include share buybacks. But, it's a good place to be operating from. Yes.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

So I think -- I mean, Helen said it -- a couple of things. First of all, that -- it's great to hear we are forecasting the same way. But I think that forecast already includes what we want to invest in anyway, okay?

So therefore, I'm going to take your question, like, where are the big opportunities, rather than where do you want to invest, because we are already investing. We increase the net investment, therefore.

Frankly, we are in a privileged situation. I think a part of it where we operate, a part of it, the opportunities we created for ourselves, frankly. And there is the growth potential, obviously, in Civil Aerospace, where we are highly differentiated and that can be narrowbody, widebody, and -- but UltraFan investments, for example, in our forecast, obviously, right? You should think that way.

So, time on wing, GBP 1 billion will expire by that time, as we talk about. SMR -- at this point, SMR will not actually require big investment. It will grow. Only think what Helen said is -- and power systems -- one point I'm going to make, just to point out.

Power System, capital, and Research and Development right now highest in their history, 100 plus years. That should tell you how we think about it. There is a growth potential. Let's invest, but -- there's a mess with proper returns, right? So there is lots of rigor. There is lots of challenge, but there is never hold back.

That's why -- I'm not talking about in '28. Today, their CapEx and R&Ds is the highest on record for Power Systems. Why? Because there is so much data centre-driven growth opportunity that -- and some governmental, frankly, that we want to actually benefit from.

So, we have -- only thing I'm going to talk about -- because we are already investing, only thing I can talk about where the sort of -- it can come from any of our businesses,

because, if we had low return business, low margin business, frankly, we are already getting out of them. So therefore, that opportunity, organic or inorganic, may come from many places, and we will evaluate the way Helen talk about.

Jeremy, do we have digital question or do you have a question?

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

Not my question. So there's a couple of questions here. Maybe we could finish on these, and one is, what do you consider the impact of potential tariffs to be in the U.S.? And the second one, which I think you'll like, Tufan, is, when do you expect the decision on SMRs from the U.K. government?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

I always like that. And so, I think -- I think tariffs first. We have done lots of work, as you can expect. Frankly, I will say this. All the tariffs already announced, there is limited impact for us.

And what else may come, obviously, I'm not going to speculate here. But I'm going to say the following. Our mindset and the processes we are putting in place, some of it being very proactive to mitigate the impacts.

And because we want to run a company. That's part of -- I talk about distinctive performance culture. This is actually one of the principles there. How do you create response capability? Mindset and capability, because mindset is important. So, that's my tariff answer.

I think that's GBN questions. I mean, it has been delayed, obviously. But we expect in 2Q -- probably towards the end of 2Q, GBN to come and select technologies, and so on. But here is the good news. So, again, this should give you an insight how we run the business.

We, actually -- we didn't want to, sort of, bet on one thing for the whole business, therefore, we went out there, work with other countries and develop options, so that we can actually unlock SMR potential. And ČEZ deal is highly strategic deal, effectively, does that.

So therefore, we are not sitting here and saying, wow, we got 800 people. We don't know what to do with it. No. They are actually, as we speak, working with ČEZ on the first site already, because ČEZ already identified the first site. In fact, ČEZ CEO is actually coming here early March to meet with me, et cetera.

So, my big point is, yes, that process is very important for us. I argue, very important for U.K., because I said it publicly and privately. These new technologies come in. Offshore

wind, I was in energy industry when that came. Frankly, U.K. didn't move fast enough and lost the first mover advantage, and therefore lost the opportunity to develop wind supply chain in the U.K. It was developed elsewhere and it will never come back.

Right now, we have a leading SMR in the U.K. This is a perfect opportunity to create U.K. supply chain in the U.K. with the first mover advantage, because, frankly, our nuclear capability is unique in the world.

I may have said it before. I don't know how it resonates with you. There is -- let me spell it. There is no other private company in the world with our nuclear capabilities. I actually tell the nuclear team, if we are not market leader in SMRs and micro-reactors, we made a mistake in going after that, because we should be natural leaders in that space given our unique capability.

So that's my GBN answer. Always long answer for GBN.

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

Thank you.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Any other questions? I think -- I think we are going to close.

Thanks for coming. Thanks for great questions, as usual. We are making progress. Hopefully, you agree with that. We actually expanded the earnings and cash potential of the business.

But more importantly, our future mid-term targets already underpinned to a great extent by the actions we have taken, for example, 80% time on wing. We know that, otherwise, we wouldn't share with you other 40%, right? So, there is no technology risk there, for example. So that's what I mean. So, I think that's what we are on to. And we talk about beyond mid-term because we are excited about it.

Thanks again. Have a great day.