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Rolls-Royce Holdings plc

Rolls-Royce 2025 Half Year Results Transcript

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Participants:

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Jeremy Bragg*Head of Investor Relations, Rolls-Royce Holdings plc*

Good morning, everyone. I'm Jeremy Bragg, Head of Investor Relations. And I'm joined today by our CEO, Tufan and our CFO, Helen. So welcome to our 2025 Results. Before we begin, I'm required to show you the safe harbour statement on Slide 2.

So in today's presentation, we're going to cover our first half results in detail and our guidance for the full year. So after the presentation, we will take questions from the room and if there's time from our online audience. For those of you in the room, there are microphones in the seat in front of you, you need to press and hold to the button before you speak.

Before I hand over to Tufan, we'd like to show you a short video that highlights the strong progress we've made over the half. So thank you.

(Video playing)

Tufan Erginbilgic*Chief Executive Officer, Rolls-Royce Holdings plc*

Good morning. We continue to transform Rolls-Royce into a high-performing competitive, resilient, and growing business.

We are creating a sustainably distinctive business in terms of safety, operational effectiveness, customer service, advantaged technologies and products, and a distinctive performance culture.

We continue to expand the earnings and cash potential of Rolls-Royce despite the challenges of supply chain and tariffs.

Our first half results have been strong with significantly improved financial performance across the group. This has been driven by our transformation programme and builds on what we have delivered over the past two years.

We made strong operational and strategic progress in the first half of 2025. This includes achieving key time on wing improvements, delivering strong aftermarket performance and contractual margin improvements in Civil Aerospace, capturing data centre growth in Power Systems with improved profitability, strong order intake in Defence plus the selection of Rolls-Royce's SMR as the preferred provider of the UK's small module reactors.

Our strong first half results gives us confidence to raise our guidance for 2025. It also builds further confidence in midterm targets for 2028 that we set in February.

These midterm targets are significantly underpinned by our strategic initiatives and the actions we have taken. As the first half shows, execution of our strategic initiatives continues to deliver strong results.

We are continuing to invest for growth across the group in a focused and disciplined way. Investments have increased every year since 2022 and will grow again this year.

We are also growing shareholder returns. Today, we announced an interim dividend of 4.5p, our GBP 1 billion share buyback is progressing to plan with GBP 500 million of share buyback as of today.

We have achieved a lot over the past two and a half years, and there is still more to do. We continue to see strong growth to the midterm and beyond.

Despite an uncertain environment, our financial performance has improved significantly in the first half 2025 driven by our transformation programme.

Operating profit of GBP 1.7 billion was 50% higher than last year, driven by the following items. In Civil Aerospace, we delivered strong aftermarket profit with higher volumes and margins across LTSA and time and materials.

In large engines, our aftermarket revenue grew by 28% in the first half with even higher growth in aftermarket operating profit as a result of improved margins in both LTSA and time and materials.

Contractual margin improvements were higher than last year, driven by onerous contract renegotiations and the achievement of key time on wing milestones on the XWB-84.

Spare engine profit was also higher reflecting improved margins and mix.

In Defence, transport OE and aftermarket profit improved. And in Power Systems, we continue to capture growth in the data centre market with improved margins. Plus, governmental performance was also strong.

Our performance continues to be impacted by industry-wide supply chain constraints, which understate the true impact of our transformation. The actions that we have taken have driven an improvement in the supply chain, particularly in the availability of finished parts, with a 15% increase in parts delivered to us in the period. This has supported a higher number of shop visits and reduced turnaround times, particularly for the Trent XWB-84 and Trent 700. Both have fallen significantly.

Despite an improvement in the availability of parts, we have continued to see product cost inflation as a result of supply chain challenges.

We have been quick to react to the tariffs where we have fully mitigated the drag impact across the group as we transform Rolls-Royce into a more proactive agile business. All of this resulted in a group operating margin of 19.1%, 4.9 percentage points higher than last year.

Civil Aerospace's operating margin rose by 7.1 percentage points to 24.9%. Defence operating margin was 15.4%, similar to last year's. And in Power Systems operating margin rose 5.6 percentage points to 15.3%.

Turning now to free cash flow for the group, which was GBP 1.6 billion, 37% higher than last year. Strong free cash flow was largely driven by strong operating profit and continued LTSA balance growth. The growth was supported by higher engine flying hours and an improved EFH rate, partly offset by higher number of shop visits.

The actions we are taking to improve our large engine LTSA contracts, the six levers of improvement that we have often talked about are driving higher LTSA margins and stronger cash flows.

Return on capital rose by 3.1 percentage points to around 17%, driven primarily by operating profit. That shows distinctive value creation by Rolls-Royce and provides us with a competitive advantage.

Our strong first half results were driven by the continued execution of strategic initiatives. I will talk to three key initiatives that have driven significant profit and cash growth, which we first showed you in February.

In widebody, our installed fleet has grown at 10% per year since 2022 versus 5% for the market as we have captured more than 50% of the deliveries. We continue to expect installed fleet growth of 7% to 9% per year to the midterm, driven by rising aircraft deliveries as we continue to capture market share. This is underpinned by our large order backlog of more than 2,000 engines.

The first graph shows the multibillion cash benefits of renegotiating OE and aftermarket contracts in Civil Aerospace. We made great progress in the first half of 2025. The contracts that we renegotiated in the first half alone will benefit cash flows by GBP 1.4 billion over their contract life.

As shown on the graph, only 30% of these OE and aftermarket cash benefits will be realised by 2028, with the remainder being delivered progressively over time. We have now renegotiated all of our OE contracts, which means that our business aviation OE deliveries are now profitable. We remain on track for the Trent XWB installed engine deliveries to be breakeven or positive by the midterm.

We also made strong progress with onerous aftermarket contracts in the first half, which supported gross contractual margin improvements of GBP 402 million. We continue to find win-win solutions for our customers. We have now completed the renegotiation of all our significant onerous airline contracts and expect to largely conclude the remainder this year and 2026.

The second graph shows we are driving higher contract margins and therefore higher LTSA margins over time. To remind you from February, our contract margin, the top line on the chart, 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 will be booked in our income statement in the future, this is the second line in the chart.

In the first half of 2025, we have driven around 1 percentage point further improvement to both contract and LTSA margins compared to what we set out in February. Improved contract and LTSA margins are both driven by time on wing improvements on Trent XWB-84 and lower shop visit costs. In addition, higher contract margin also reflects the benefits of new LTSA contracts, which are coming in with better terms.

Shop visit costs continued to improve during the first half. For the Trent XWB-84, shop visit costs remain on track to fall by 50% between 2019 and the midterm.

We are also making good progress with time on wing. We hit the significant milestones on the Trent XWB-84 in the first half of 2025, which supported contractual margin improvements and will drive higher LTSA margins going forwards. The upgraded Trent 1000 HPT blade was certified in June which will more than double the time on wing on these engines.

Our Trent XWB-84EP engine deliveries also commence with Delta Airlines in the first half. These engines offer more than 1% improvement in fuel burn and improved durability.

In February, we set a target of improving the time on wing of our in-production engines by more than 80% by the end of 2027. As a result of the progress we made to date, more than half of the targeted improvement is now delivered or secured. Most of the cash benefits from our time on wing improvements will come after 2026 and will support cash flow growth to the midterm and beyond.

The third graph shows operating profit and margins in Power Generation, where we have restructured our business model to profitably capture strong data centre growth. As a result, since 2022, Power Generation's operating margin has increased by 11x. Demand for our backup power generators for data centres remains very strong and we now expect revenue growth of around 20% per year to the midterm in the Power Generation segment. This was previously if you remember, 15% to 17%.

Power Generation has now become one of the most profitable segments within the Power Systems. This is making our financial delivery more evenly balanced through the year, which you can see in our first half results. All these initiatives are driving stronger performance to the midterm and beyond.

We have made significant strategic progress across our four pillars. I already covered some of the key strategic initiatives. Let me talk about the rest very briefly. First, portfolio choices and partnerships.

In March, CEZ Group made a strategic investment into Rolls-Royce SMR, alongside a commitment to buy up to six SMRs, CEZ is an experienced operator of the existing nuclear fleet in the Czech Republic with a strong established supply chain.

In May, we announced that Rolls-Royce and Turkish Technic will establish a new MRO centre in Istanbul. This will be operated by the end of 2027 and will eventually support up to 200 shop visits per year.

In Power Systems, as well as developing our next generation engine we are also simply upgrading our military engines with higher power density to capture growing demand. Our governmental business is also well positioned to capture strong market growth and increased European defence spending. As a result, we now expect higher governmental revenue growth of 12% to 14% per year to the midterm. Previously again, this was 5% to 7%.

In July, we completed the disposal of our Naval Propulsors business to Fairbanks Morse, and we expect to close the disposal of the Naval Handling business at a later date.

Second, strategic initiatives.

Our Pearl business jet engines hit important milestones in the first half. The Gulfstream G800, powered by our Pearl 700 engine was certified in April, ahead of the aircraft's entering into service later this year. In addition, our Pearl 10X engine for the forthcoming Falcon 10X aircraft has completed flight testing, and we are on track to complete all major engine certification tests.

In Defence, we signed two key aftermarket services contracts worth over GBP 1.5 billion in total with the UK MoD and US DoD. These contracts cover the continued maintenance of EJ200 engines for the Eurofighter Typhoon and AE 2100 engines for a variety of aircraft, notably the C130J Hercules.

Third, efficiency and simplification. We have a TCC/GM ratio of 0.35. This is a best-in-class ratio, which represents a competitive advantage for Rolls-Royce amongst its peers.

We have now delivered more than GBP 400 million of efficiency and simplification benefits since the start of 2022, and we remain on track to deliver more than GBP 500 million by the end of this year.

Since the start of 2022, we delivered over GBP 850 million of gross procurement savings and remain on track to deliver more than GBP 1 billion by the end of this year.

Our efficiency and simplification targets are supported by zero-based budgeting and our GBS strategy where efficiencies are scaling up. We have opened a new GBS centre in Poland and are expanding our centre in India.

Fourth, lower carbon and digitally enabled businesses. In June, Rolls-Royce SMR was selected as the preferred bidder to build three SMR units in the UK. We expect to enter a 2-stage contract with GBN in the fourth quarter of this year.

Stage 1 will cover the site-specific design activity and the preparations for the site build, leading up to the final investment decision. Stage 2 will see us deliver three Rolls-Royce SMR

units to go on grid by mid-2030s. The UK's decision also paves the way for further export orders, with our next opportunity being in Sweden where we expect a decision soon.

As Rolls-Royce SMR activities ramp up in the UK and in the Czech Republic, these projects will start to generate revenues and profit from late 2025. Cash flows will be positive on a project basis throughout. We expect the Rolls-Royce SMR business will be profitable and free cash flow positive by 2030.

We have unique capabilities in nuclear leading and highly differentiated position in a growing market. Therefore, we expect the value of this business to grow significantly from now.

In Power Systems, we won major new battery storage orders including the Ignitis group in Lithuania. These orders support strong revenue growth and our ambition to achieve the breakeven in the near term.

We are increasingly adopting AI across the group. Rolls-Royce is testing its generative AI platform for a variety of use cases including accelerating new product introductions and creating a more efficient MRO process. Work is underway in providing greater transparency across the supply chain through digital, data, and AI. We are deploying AI capabilities in cybersecurity and improving the IT support services.

With that, let me pass it to Helen, who will tell you in more detail our first half results.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Thank you, Tufan. Good morning, everyone.

Before I get into the detail, let me start by saying how pleased I am at their progress.

It's real evidence of our transformation. The results, they are strong, double-digit growth across revenue, profit, and cash flow with balance sheet resilience continuing to be built. Every division is delivering, and we're rewarding our shareholders with growing distributions.

A reminder of the group highlights. Group revenues grew by 13% to GBP 9.1 billion with good end market growth, especially across Civil and Power Systems. Group operating profit grew by 50% to GBP 1.7 billion, driven by our strategic initiatives including commercial optimisation and cost efficiency benefits.

Operating margin grew by 4.9 percentage points to 19.1% and free cash flow, it grew by over GBP 400 million to GBP 1.6 billion. Cash delivery was driven by higher operating profit and continued LTSA balance growth.

Strong cash flow in the period meant that we closed the half year with a net cash position of over GBP 1 billion. That's around GBP 2 billion higher than a year ago. Return on capital, it rose to 16.9% for the rolling 12 months, representing significant value creation. And these results have enabled us to declare an interim dividend of 4.5p per share, following through on our capital frame commitments and rewarding our shareholders.

So, a strong set of results across all key financial metrics with every part of the organisation delivering. Results that demonstrate we are making continued strategic, operational, and financial progress, a real team effort.

Now the detail by division, starting with Civil Aerospace. Civil delivered the largest year-on-year improvement in profit and margin, with the impact of our strategic initiatives being very evident.

Operating profit grew to GBP 1.2 billion an increase of 63% compared to last year. Operating margin grew to 24.9%, an increase of 7.1 percentage points compared to last year. Revenues grew to GBP 4.8 billion, an increase of 17% driven by higher shop visits and commercial optimisation.

OE deliveries of 237 were broadly flat year-on-year. Of these, 122 were large engines of which 23 were spares as we continue to increase our operational flexibility and support our customers. Business aviation deliveries of 115 were almost all Pearl engines.

Shop visits, they grew to 696 an increase of 12% year-on-year. Of these, 217 were large engine refurbishments. That compares to 195 last year. The increase in shop visits was supported by stronger MRO performance as we expand capacity, strengthen processes, and leverage AI tools across the network. It was also supported by improvements in parts availability across the supply chain, driven by our interventions, which I will come back to in a moment.

Now operating profit in more detail. Three key factors drove that 63% increase.

First, stronger large engine aftermarket profits. LTSA aftermarket profit grew as a result of a higher average LTSA margin and a higher number of shop visits alongside higher time and material profits.

Second, increased spare engine profits. Similar year-on-year volumes were delivered with improved margins and mix. And third, net contractual margin improvements. They were GBP 288 million. That compares to GBP 223 million in the first half of 2024. The GBP 228 million

comprised a net benefit of GBP 181 million in onerous contracts and GBP 107 million from catch-ups.

You've heard how we have made significant progress renegotiating onerous aftermarket contracts, finding win-win solutions with our customers, allowing us to release onerous contract provisions in the period.

We also achieved key time on wing milestones on the XWB-84, which resulted in a contract catch-up benefit. These two factors contributed to a gross benefit of GBP 402 million in the period. This was partially offset by an additional charge of GBP 114 million which was taken across both onerous and catch ups due to ongoing product cost inflation associated with supply chain challenges.

It's worth pausing for a few moments on Aerospace supply chain. When we spoke to you in February, we shared that we expected the supply chain to remain challenging during 2025 and '26. That is still our view. The industry continues to see product cost inflation, and we have our procurement savings programme to help us mitigate the impact of it.

We continue to manage the supply chain very tightly. Dedicated teams across the organisation and teams we have embedded in our suppliers are driving meaningful improvement.

Indeed, the number of critical suppliers on our watch list has fallen from around 15 to 10 and just heard how MRO turnaround times are improving. So, despite the continuing challenges our actions are having an impact.

Now turning to cash. Civil delivered a trading cash flow of GBP 1.1 billion compared to GBP 1 billion in the prior period. Cash delivery was driven by operating profit and continued net LTSA balance growth, supported by large engine flying hours, which grew to 109% of 2019 levels, and a higher normalised engine flying hour rate.

In summary, a very strong delivery from Civil on profit, margin, and cash.

As we look to the second half for Civil, we expect a lower operating profit and cash flow compared to the first half due to a lower contribution from contractual margin improvements, an increased number of OE deliveries, and higher MRO investment-related costs. And in addition for cash, the impact of higher shop visits, notably Trent 1000 refurb.

Defence, where we continued to make good strategic progress. Key milestones included, the first engine delivery for the MQ-25 development programme, that's the US Navy's first autonomous refueler, and we also started development testing for the MV-75 or FLRAA engine, that's the US Black Hawk helicopter replacement.

Order intake for the period stood at GBP 4 billion with a book-to-bill ratio of 1.8x. And importantly, new orders came with improved profitability. Order backlog was GBP 18.8 billion, a record level and equivalent to around four years of revenue, order cover for the remainder of the year, stands close to 100%.

Now turning to the financials. You may recall that the first half of 2024 included a one-off benefit in submarines. So masking the underlying progress we are making. Revenues, they stood at GBP 2.2 billion, broadly flat year-on-year. Excluding the one-off, revenue growth was 10%, driven by double-digit growth across transport OE and aftermarket.

Operating profit stood at GBP 342 million and operating margin at 15.4%, both broadly flat year-on-year. This reflected improved performance in transport across both OE and aftermarket, again, offset by the absence of the one-off benefits in submarines and continued supply chain constraints, notably in the naval business.

Cash flow in Defence stood at GBP 327 million. Delivery was driven by operating profit alongside tight working capital management.

In summary, a good delivery from our Defence team, which continues to position us well for future growth.

Power Systems, a very strong performance in the period as we continue to capture profitable growth in data centres and governmental.

Operating profit grew to GBP 313 million, an 89% increase year-on-year. And operating margin grew to 15.3%, a 5.6 percentage point increase year-on-year.

Order intake was GBP 2.9 billion, with a book-to-bill ratio of 1.4x, a 32% increase year-on-year. Order cover for the remainder of the year is 100% and with growing order coverage for both 2026 and '27. Demand remains particularly strong in Power Generation which saw an order intake growth of 68%, primarily driven by data centres, where orders grew by 85% year-on-year.

Revenues, they grew to GBP 2 billion, an increase of 20%. Power gen and governmental revenues grew by 26% and 19%, respectively. Data centre revenue growth was 45%.

Operating profit growth of 89% was driven by three factors: first, a standout performance in power generation, notably data centres, where we are capturing profitable growth with a stronger mix in the high-power density sector and all at higher margins following the restructuring of this business.

Second, strong performance in governmental with higher volumes and commercial optimisation benefits, and where we are well positioned to capture growing European defence spending.

And third, good momentum in battery energy storage systems with improving profitability and where we remain on track to break even in the near term.

Cash flow, it increased to GBP 425 million driven by higher operating profit and tight working capital management as well as some timing benefits from early customer receipts.

Simply put, a very strong performance from the whole of the Power Systems team.

Looking to the second half, although we still expect Power Systems profit and cash to be seasonably balanced to the second half that weighting won't be as pronounced as in the past. This is due to the significant growth we have driven in power generation, which is now one of Power Systems most profitable businesses and one which has less seasonality. We also expect some reversal of the early customer receipts that came in the first half.

Before turning to group cash flow, the eagle eyes amongst stream may have noticed that we are no longer reporting a New Markets division. As you know last year, we wind down the electrical advanced air mobility business and this year, with the CEZ Group now a strategic partner in Rolls-Royce SMR, in which we remain the majority shareholder, the equity accounted results of Rolls-Royce SMR now sit within all other businesses.

The funds flow. We delivered GBP 1.6 billion of free cash flow in the first half, more than GBP 400 million higher than last year. The principal driver of this increased free cash flow was operating profit, which grew by almost GBP 600 million.

Other factors included the civil net LTSA balance. It was broadly similar to last year, standing at GBP 472 million. Growth was driven by higher engine flying hours alongside an improved engine flying hour rate, offset by a higher number of shop visits.

Net investments, they were similar to last year, with investment spend in the period standing at more than GBP 400 million. We continue to make purposeful strategic investments that drive growth to the midterm and beyond. This includes investments in time on wing and UltraFan in Civil. And in Power Systems, investments in additional capacity in the US, our next-generation engine for the growing data centre market and in significant upgrades to our military engines.

Working capital. It was broadly neutral in the period. This compares to a build of more than GBP 200 million last year. We continue to drive sustainable improvements in working capital management, and we are making good progress.

Compared to the same period last year, inventory days improved by 14 and days sales outstanding by 4. A strong performance given a tight supply chain and while we supported revenue growth.

Then provisions. They were an outflow of nearly GBP 300 million, around GBP 200 million higher than the same period last year. They included outflows as we continue to successfully renegotiate and trade through our onerous contracts.

Over hedge costs, they were GBP 116 million slightly higher than last year and in line with expectations. Net interest, it was slightly positive compared to a small outflow last year. And finally, cash tax costs they increased to GBP 259 million. Tufan will talk to the full year guidance, but let me give you some additional colour on the cash flow.

Large engine flying hours are expected to be within the guided range of 110% to 115% of 2019 levels. The net LTSA balance growth for the full year is expected to be at the low end of the GBP 0.8 billion to GBP 1.2 billion range, in line with what we previously shared. This means we expect a lower growth in the second half of the year as shop visits, including Trent 1000, refurb increases. Net investments, we expect them to be in the second half of the year.

Over hedge costs for the year will be GBP 148 million. Net interest payments will be broadly neutral for the year, and cash tax is expected to be around GBP 200 million higher year-on-year.

Capital frame and progress against our priorities. First, the balance sheet, which we continue to strengthen. We remain in a modest net cash position. GBP 1.1 billion at the half year, which provides us with flexibility and enhanced resilience, which are even more important in an uncertain macro environment. The credit rating agencies have continued to recognise our progress with further upgrades in the first half and all still hold us on a positive outlook. Gross debt, as previously shared, we will reduce it further by repaying from available cash, the \$1 billion bond, which matures in October.

Then distributions. In June, we paid our first dividend since 2019. Today we're announcing an interim dividend of 4.5p per share in respect of the half year 2025. Representing a distribution to shareholders of approximately GBP 380 million. As a reminder, we target an annual payout ratio of 30% to 40% of underlying profit after tax.

And as of today, we are halfway through our GBP 1 billion share buyback. The remainder of which will be executed across the balance of the year. Taken together, the full year buyback along with the 2024 full year and 2025 interim dividends represents a total cash distribution to shareholders of GBP 1.9 billion to be paid this year. Competitive and evidence of our commitment to growing shareholder returns. And all of this was delivered while we continue to strategically invest in the business to support growth to the midterm and beyond.

To close, a strong first half result across all divisions and against all key metrics. This strategy is delivering. We are performing as we transform.

We know there is more to do, and we also know there is more to come. The teams have done a great job, a huge thanks to everyone.

And with that, let me pass you back to Tufan.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Thanks, Helen. Turning to our guidance now.

Strong first half delivery gives us confidence to raise our 2025 guidance.

We now expect underlying operating profit of GBP 3.1 billion to GBP 3.2 billion with a year-on-year improvement in all core divisions. Compared to an operating profit of GBP 1.7 billion in the first half, we expect slightly lower delivery in the second half of 2025, notably in Civil Aerospace. Here, we expect a lower contribution from contractual margin improvements, an increased number of OE deliveries and higher MRO expansion investment-related costs.

We now expect free cash flow of GBP 3 billion to GBP 3.1 billion. Stronger free cash flow will be primarily driven by higher operating profit alongside continued LTSA balance growth.

We expect a slightly lower free cash flow in the second half compared to the first half. This reflects the lower operating profit in the second half of the year, more large engine refurbs, with a significant step-up in Trent 1000 refurbs, alongside higher net investment.

Our free cash flow guidance includes a GBP 150 million to GBP 200 million impact from the supply chain as previously guided.

Our transformation plan is delivering strong results as is evident this half. And we feel confident about the remainder of the year.

I will conclude today's presentation with key takeaways.

We shared a lot with you. I actually thought I should give you the key takeaways. I'm sure you will take yours, but hopefully, this is helpful.

We continue to expand the underlying earnings and cash potential of the Rolls-Royce in a challenging environment.

Across the group, all divisions have delivered underlying performance improvement in the first half. Civil Aerospace's strong underlying operating profit and cash flow is driven by continued LTSA margin improvements and continued market share growth.

We have renegotiated all of our significant contracts and achieved major progress in our time on wing programme. These initiatives will both contribute significantly to our profit and cash flow delivery to the midterm and beyond.

In Power Systems, we continue to improve our profitability and now see higher growth potential in power generation, driven by data centres. We also see higher growth in governmental.

In Defence, where we have delivered a year-on-year improvement in underlying performance with a record order book. Our significant programmes will scale up in the late 2020s.

All these, which are driven by our strategic initiatives, continue to improve our operating margin and return on capital. As a result, we see good profit and cash flow growth in our existing businesses, to the midterm and beyond. While we are taking concrete steps to generate further long-term profitable growth in new areas such as narrowbody, SMRs, and AMRs.

Rolls-Royce SMR business will be profitable and free cash flow positive by 2030.

Strong delivery in the first half of the year gives us confidence to raise our guidance for the full year 2025. And also builds further confidence in our midterm targets for 2028. These midterm targets are a milestone, not a destination. I am confident and excited about our growth prospects beyond the midterm.

We are continuing to reward our shareholders with GBP 1.9 billion to be returned to shareholders through 2025, in line with our capital framework, as Helen talked about. This shows our commitment to shareholder distributions. There is a lot we achieved in the first half and still so much more we can deliver.

I'm very proud of all that the Rolls-Royce team has done and look forward to all that we will continue to accomplish together.

Thank you for listening. Now I'm going to open it for your questions.

Nick Cunningham

Analyst, Agency Partners

Thank you, Nick Cunningham from Agency Partners.

Some of your customers, airlines, and lessors have been vocal recently, complaining perhaps that Rolls isn't as nice as now as it has been for most of the last 30 or 40 years. But you negotiated all those key onerous contracts. You just told us that. So does that mean that there's no real practical effect from their grumbling, if you like, the deal is done?

And then linked to that, your narrow-body colleagues have been enjoying an exceptional windfall from the lack of supply of new engines and new aircraft. So it's keeping older ones in the air for longer with more scope on the overhauls and so on. Presumably the same dynamics apply to the large engine market, and so are you seeing that effect in your T&M in particular? And has that helped you with your onerous contract renegotiations?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. There is a lot there. I'm not sure it's two questions, but more than two. But I think let me start.

First of all, I think I don't know some of our customers have been disappointed with Trent 1000 time on wing issues. And we have a big task force dealing with it.

We actually have improved relations with customers. I can categorically tell you, there isn't any contract we renegotiated, actually, relationship didn't improve relative to where it was. I can categorically tell you because every time we were able to find win-win solutions.

So there is some noise because of Trent 1000 time on wing issues now with BoM B upgrading, obviously certification. Frankly, that will go away because by the end of this year, we will have an engine very, very competitive.

Let me tell you this. By the end of this year, actually Trent 1000, depending on how it is operated obviously, different airlines will operate differently, but we expect 4 to 6 years time on wing relative to where we have been, right? That was creating the sort of - we are actually serving our customers better than before. And you can hear it from airframers easily if you are following that.

We are actually improving our customers service, and there is a big focus on it. This was the sort of issue. Now we solve that issue. We have a very, very competitive engine.

So I think that's the way to think about - in renegotiations that was - yes, if somebody is experiencing AOG, it's not a brilliant start to renegotiation, obviously. But we were able to do all the significant renegotiations, and we were all - we have done it in a style that actually relationship improved.

Why is that? Because they now know when we commit something, we honour it. We are that company. We don't commit that easily. But when we commit, you hear some noise because we are not committing some things. I actually tell them when we commit, we will deliver. So until I am sure we will deliver, I'm not committing.

So actually, that's not a bad noise. That's actually good noise because, frankly, this industry doesn't have a great track record on that one. So we don't want to contribute to that. We want to change that.

Your question around sort of whether we are actually - yes, I think when you look at our best, obviously Trent 700, right, if you create parallels with narrow-body. Yes, we are seeing and it is - if you remember, that's one of our six levers.

We kept saying earning - actually flying those things longer. We have a deliberate programme on that, whether with the current customers, obviously if they want to continue with that or with freight conversions or with sort of transfers to other commercial customers. Yes, I think Trent 700, frankly, doing well and we believe our projections suggest it will continue do well.

In fact, in February, if you remember, I said our Trent 700 LTSA balance growth didn't peak yet. I don't know any of you remember that, but that was there.

So your question is it helping our renegotiations? Not really because, frankly, none of our renegotiations are around Trent 700. It is pretty profitable engine. You guys well know that.

So was that - yes, Ben? And then, Ian, I'll come to you.

Benjamin Heelan

Analyst, Bank of America

Thank you, can I ask three? First one, you've given us some outlines on capital allocation. Can you talk a little bit about that in 2026 and 2027? Are there parts of the portfolio, I'm thinking maybe Power Systems that you want to add to, given the balance sheet that you have now, or can we assume that there could be more buybacks down the line? That's the first question.

Second question, you haven't talked today about UltraFan and narrowbody. Can you give us an update there? You made some noise at the air show about this. So just an update there would be great.

And then in terms of the Civil business, you talked and guided historically for margins to be in the 18% to 20% range now in H1, you've already achieved the 19% on an underlying basis, stripping out the catch-ups. Are we not going to grow margins from here? How can we think about that? Thank you.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Thanks, Ben. Three good questions. I'm going to ask Helen to capture the capital allocation.

Let me answer the second and third, and Helen will pick up the first one.

So, I think UltraFan narrowbody is - we are actually making good progress in multiple dimensions. One is, continue to work on the UltraFan demonstrator. We are actually on UltraFan doing two things. We are doing further tests on widebody UltraFan, just to progress that, at the same time working on the demonstrator for narrowbody, which may take two years to build a demonstrator. So that's the current plan. So that's one sort of technology angle, if you like, and product angle.

The other angle is our preference continues to be partnerships. Therefore, we are in active dialogue with almost all the parties, I should say. So that is also progressing well. So that's where we are. I'm actually very optimistic definitely for the next generation of narrowbody and our participation in that given all that.

So if I go to your Civil question, your math is absolutely spot on. So if you adjust for commercial improvements, it is 19%. So here is what I'm going to say. I mean I said it, Helen said it, hopefully, it was clear. We are making underlying performance improvement, right, beyond sort of what we shared with you in February. Otherwise, how would we upgrade the guidance for this year if that's not true. So that's actually factually true. So we are - we were expecting obviously improvement when we gave the midyear guidance and everything. And we are now ahead of that progress, which is great to see, frankly, in that.

But you need to obviously look at a couple of things sort of in that sort of - when you look at, I always say sometimes our competitors, they issue one quarter, I got 30% margin. So you cannot really look at, because our targets are sustainable targets as opposed to touch and go, if you like, right?

So, we just told you that effectively second half we have significant step-up on shop visits. That's not the issue for operating margin, but step-up comes with Trent 1000. And therefore, full year will equalise somewhere lower than 19, because those are the engines where we have the lowest shop visit profitability, if you like. So, they will a little bit dilute that picture.

But big point is underlying performance is improving, and that's very encouraging for me. And as a result, we are ahead of the plan. When you go to midterm targets, we are in an uncertain world, right, an increasingly the uncertain world, tariffs, supply chain challenges, impact of tariffs on world GDP, all that live conversation.

So, if we continue to manage those risks well, given our mindset which I will come back to, yes, we are ahead of the sort of plan but we need to manage those things. So those risks are real.

So, I take your final comment I'm going to make then I'll pass to Helen for capital framework. But - so you guys get surprised sort of what's going on because our mindset change. Every time I talk about it, we are not after a bunch of budget numbers. We are after improving the business every day. And that means improving the underlying performance every day, every year. That excites me, frankly.

Now when you do that, you combine it with your strategic initiatives very granular and embedded in the organisation, i.e. 42,000 people on them. Suddenly, that mindset, combined with that clarity, you go as fast as you can go because we are - we increased the pace and intensity in the company. That's understood by everybody. So that is actually causing these things.

But there are big risks that we need to be thoughtful therefore I'm thinking, Ben, maybe it's too early to talk about midterm targets, but I'll leave you with a thought that we are making great underlying improvement.

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Fantastic. Thanks, Ben.

So, I think two elements to your question. There was one around investments and then one is that tied into capital frame.

So, in relation to investments, maybe just a couple of data points to help you there. So actually, Tufan referenced that since 2022, we've increased our investments in the business every year. And you will see that for 2025 as well. When we took you through in February,

our midterm targets, we shared then that we expected over the midterm net investments on average to be higher than they were at 2024.

So again, you can see the confidence building that we're continuing to invest in this business, not just for the midterm, but beyond the GBP 1 billion on time on wing, a classic example of that, we don't see by any means the full benefit of that beyond the midterm.

You specifically mentioned in power gen, our Power Systems, Ben. Power Systems last year had a record level of capital spend in 2024; 2025, expect to see the same, very strong positions in data centres and governmental. So investment is going in to support that business.

In fact, just in the last three or four weeks, we announced \$100 million investment in the US across two of our sites there, specifically to support that build-out in production for data centres. So purposeful, strategic investments happening. And that is very important, purposeful and strategic investments happening.

In relation to capital frame and buyback, we've always been quite consistent around how we look to strike that balance between ensuring that we protect that balance sheet and then being very thoughtful about how we drive for additional investment, be that organic or inorganic or additional shareholder returns. And we've been clear that buybacks are in our tool kit.

And Tufan spoke about, you know we don't promise and not deliver. We were clear that we have a very clear capital frame, GBP 1.9 billion in cash distribution in our first year of cash distributions in more than five years, I think, is a demonstration that we follow through on our commitments. And actually, that's in an environment where we're also repaying a \$1 billion bond.

So that's how you should hold that going forward. Thank you, Ben.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Thanks. Ian. I see you well. Thanks for sitting there.

Ian Douglas-Pennant

Analyst, UBS

The episode Tufan is referring to is when he didn't take my question. I think it was two years ago now it's still haunting you.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

I thought that was scar zone.

Ian Douglas-Pennant

Analyst, UBS

Thank you very much, it's Ian Douglas-Pennant at UBS.

First on 2028 guidance. I mean it sounds churlish, but why not upgrade the 2028 guidance today? I mean as Ben points out, your Civil margins are already there. They are actually already there in Defence and Power Systems as well. Clearly, your expectations for Power Systems growth have increased since you gave that guidance. I mean why did the 2028 guidance at the same time?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

You have more questions?

Ian Douglas-Pennant

Analyst, UBS

Just one more. And then the outperformance that you've seen this year, to what extent is that market? I mean it seems like what you're seeing in Power Systems seems to - sorry, forgive me if I'm wrong, but it sounds like the majority of that is just faster market growth than expected. Civil, clearly, the situation is better than a lot of you and your competitors expect at the beginning of the year? Or is there still, you know, you're just achieving more internally than you expected?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. Very good.

So let me go in that order. My answer to your question will sound very similar to my answer to Ben's question because they were similar questions. But yes, underlying performance improvement is happening and it is driven by transformation. When we come to your second question, hopefully, I can bring it to life a little bit more.

But - and that's happening. Therefore, we upgraded our guidance. That should signal to you if our previous guidance was in line with midterm then we are ahead of it by definition. That's for sure. So therefore, I'm actually happy with the progress we are making.

But at the same time there are risks out there. And remember, midterm targets we set out only in February, if you remember, which was, I don't know five months ago, you can count. So that is the - I think it is too early, given - frankly, if anything, world got more uncertain than certain.

I think we are a lot more agile, a lot more responsive company. Therefore, we are dealing with it. It may look easy to you guys. But actually, that needs to continue, okay? But world definitely, I'm not sure anybody in the room can tell what tariffs and what economic growth and what supply challenges will be about hitting any business, frankly, going forward. So that's the world you are dealing with, and you need to take that into account.

We manage those risks, because of the company we are becoming, a lot better, therefore, you are sitting, say, what's the problem? So - but we need to continue to manage them.

If we continue to manage them well, yes, given the mindset, I'm not going to repeat again what I said to Ben's question. Given that mindset, given that process in the company, if we can deliver midterm targets earlier, we will because that's how we operate. But you need to actually hold it in that way.

Coming to your point. So, there is a clear transformation impact, okay? I'll come to power gen. But let me start with Civil.

I think look at today's results, one of the big drivers of those results, even if cash impact is not there profit-wise, was time on wing improvement? Remember, one of our strategic initiatives out of '17 is that, right? So that - we allocated GBP 1 billion investment in four years.

This is not like we are talking about UltraFan development. This is not like in 15 years, GBP 1 billion. This is actually four years, right? So you allocate that kind of resource, very rigorous

execution, it is driving that. That's not market. That has nothing to do with the market. Again, that is improving LTSA margins.

Shop visit cost reduction. Think about improving shop visit cost at an inflationary supply chain challenge environment. It is counterintuitive, it is very much counterintuitive.

Shop visits is one of our strategic initiatives. There is the driving of that, right? I'm talking about OE, XWB will be breakeven or positive in midterm, that is counterintuitive. So, I can keep growing much time you got. But the sort of - our market share capture is coming, right?

So Civil Aerospace, we gave you some LTSA margins. And in five months' time I came and said, actually whole pack profitability went up 1 percentage point in five months. Don't think 1%, like it is increasing the whole contract margins, whole LTSA margins of the company.

So, let's talk about power gen. How long have you been following Rolls-Royce? Probably longer than I've been here. Here's the breaking news for you. Data centre volumes were always there. They didn't show up last two years, okay? Suddenly AI was not discovered last two years. Trust me, we can all follow that.

They were there, nobody talking about it because what are you going to say? My biggest business is power gen. I have the biggest volumes. I'm not making money. Normally, results presentations don't go like that, right?

So but - by fixing the business model, we enabled profitably capturing that growth. If we didn't, I said it last year this time probably or whenever it was, zero times one million, it is still zero.

So - but that is big underlying, yes, from now on top of that, so we fixed the business model, right? But if you look at my chart, after fixing it is still going up. Why is it going up?

There are three factors. We are pushing the mix to higher power density. Helen talk about that, in data centres. It is good for customers. It is good for us, but don't make any mistake, it is our initiative.

And then pricing continues to play a role. I think Helen talked about commercial optimisation. Those two like-for-like improving then you have the volume effect, obviously further improving because your fixed cost, we are managing, that's the last thing I'm going to say, you see all that it is coming with improved profitability.

These results are saying to you the following: Civil and Power Systems, profitability, unit base is improving. That's what it is telling you, right? Hopefully, you get that.

So that sort of then the whole - that is big contributor there is the cost initiatives we have, and they continue - GBS initiatives, we didn't yet benefit. I mean I talk about we are scaling up, but really early days. It can be very big. So that's my answer to your question.

Actually, last point, I was talking to Ben sort of before we showed up here. I said the difference between Rolls-Royce are many of our peers. They are talking about market growth. We are talking about transformation benefits plus market growth. If you actually think that way, you may understand our results better.

Jeremy has a question. Okay, Jeremy, I thought we worked this together?

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

Very good.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

I'm kidding. I think digital question.

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

Okay. Quite a few digital questions. So going to turn to those.

So firstly, from David Perry. Congratulations on excellent results.

Three questions. First one on SMR, which was the prior CEO said that this could be a business that generates GBP 3 billion to GBP 4 billion of revenues by the mid-2030s. Is this still the case? And what sort of equity contribution? And by that, he means the equity accounted share of the results. Could we expect by that point? So that's question one.

Question two is on Power Systems, which is, again, on the theme of the midterm targets, which is given that data centres is the highest margin bit and the fastest-growing isn't it mechanical that you will achieve a higher margin than your midterm target range for Power Systems.

And then question three is also on Power Systems, which is why was the cash generation so strong in the first half? Is that something we should expect to continue? Thanks.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

I think the third one, Helen, talk about that, therefore, I'm going to pass to Helen again to capture it.

I think on SMR, so I don't want to sort of comment on who said what. But here is how I see it, David, I think.

We now have tangible to - sort of initiatives. One is with GBN for three units, but actually, hopefully, we are going to run them in a way that actually sort of we will change the nuclear track record on that. And that will actually mean that we can create a lot more than that as fleet solution for UK beyond three. And then CEZ, same timeframe, really, we are going to be up to six SMRs.

So, and both of them, I said it in my speech, both of them has similar commissioning target dates, i.e. mid 2030s, okay, '34, '35. That's the target for both CEZ and frankly, that is, I'm going to actually go beyond any revenue numbers. Yes, given that every unit is sort of GBP 2.5 billion, GBP 3 billion. So you can start to think about revenue numbers in that context.

But I'm going to go further to say today, actually, we told you this business will be free cash flow positive business and the positive profit business by 2030, which is actually before the commissioning because revenues don't come when you sort of commission.

Equity accounting, we own more than 50%. And obviously we continue to be a very big player on this one. So we should benefit from that. I said it in my speech, frankly. I expect, given we can be - given where things are I think if we are not market leaders in SMRs globally, I think we did something wrong because we are the leading company right now. So that's the potential you may want to think about in this business. That's definitely the potential I think about.

On your Power Systems margin, yes. It is one of the most profitable - by the way, governmental is profitable because of the service angle of governmental, David. So you need to think that way. It is not only power generation, but it is one of the profitable businesses definitely.

And yes, do I actually expect - I mean it's Ben's question, Ian's question, you guys get sort of similar questions, it's sort of different angles, but similar questions. Yes, we just - what did we tell you today on Power Systems? We said two things in my takeaways. We are improving the margins. I talk about when I answered Ian's question, how we are doing that. And we now see higher growth. That's what we said to you today. And we also upgraded the guidance. Yes. Therefore, we see an upside.

But talking about op margins for midterm with all the uncertainties in the world, I really find it at this point, too early to talk about it.

So again, I'm going to go back to my mindset question, David, probably when you raised that question, you didn't know my answer. So I think if we can achieve it earlier, we will, obviously.

Do you want to pick up?

Helen McCabe

Chief Financial Officer, Rolls-Royce Holdings plc

Fantastic. So thanks, David. We miss you here today.

So in relation to your question, so we have this period seen a more even cash distribution in Power Systems. In the past, the cash delivery was very second H2 weighted. We're seeing that more even distribution.

We still always expect it to be more weighted towards the second half, but it won't be as pronounced and in this period, that's because of two primary reasons. Tufan spoken at length around how we're driving growth in power generation. That has got a much more consistent growth and delivery pattern during the year.

So governmental, which used to be the one which actually brought in the seasonality is much more muted because we're seeing that power generation business be a much more substantial part of the portfolio.

Its delivery is more ratable. You heard how we've improved the margins in that business by 11x compared to 2022. So more substantial and ratable delivery from power generation, particularly data centres, and then in the first half of this year, we also did have some benefits from early receipts of customer advances. So we are seeing a little bit of a timing impact between H1 and H2.

But I think going forward, we should expect to see a slightly different balance in relation to profit and cash flow between H1 and H2 in Power Systems because we have that much more substantial power generation business in the portfolio now.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Jeremy, more questions from you?

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

Yes. This is from Ross Law of Morgan Stanley.

So first question is, congratulations on the achievements on the time on wing programme.

Could you update us on how much of the GBP 1 billion has been spent and how much is still to go? And then the second question is could you elaborate on the product cost inflation that you've seen as a result of the supply chain? Is it in a particular area? And what's causing it? And how should we hold that versus your comments about parts availability getting better?

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. Very good. So I think, Ross, thanks for the questions.

So time on wing sort of programme, we are actually making great progress. Remember that GBP 1 billion was between '23, '27 period and we are obviously, I'm not going to talk about how much of it we spend, how much of it we didn't spend yet. But we are making good progress in that.

So what I am going to tell you what is, what we have done, what is left to do and that may give you a sense of how much we spend, how much we didn't spend, but that's the time period. So actually, that GBP 1 billion will stop after '27 with all the implication of that.

Time on wing, the big elements of that when we started, there are small elements, by the way, but I'm only focusing on the big ones. Definitely Trent 1000, what we call two upgrades, BoM B and BoM C and we obviously did BoM B, which is more than doubling time on wing. By the end of this year, we will do BoM C. It is already product, is already on test. By the way, it is going well.

So once we do BoM C, so Trent 1000 time on wing programme in a way is finished, and that will create by the end of this year, highly competitive engine. You need to think about time

on wing sort of depending on how the operator sort of uses these engines and aircraft, four to six years type of time on wing, which is actually competitive, okay. And so that's going to be done by the end of this year.

XWB-84, we hit milestones therefore, we actually secured that and we are looking that sort of not completely done, some to go, but we are making great progress there.

The remaining big one that we continue to invest, is this 97 in non-benign environments, we are going to double the time on wing and in benign environments, we are going to increase time on wing by 50%. That is progressing, but that won't be completed before 2027. And so we will continue to invest in that.

By the way, this engine is a very good engine in benign environments. In fact, orders, actually airlines, especially hub airlines love it because of the distance and capacity and so on. But we - that is how I would articulate our - where we are on time on wing.

I think on product cost, effectively, it is in aerospace because that's where the supply chain - in Power Systems, frankly, because supply chain is more stable, and there is a hint there for you and for us, frankly. When supply chain stabilises, you can actually improve procurement initiatives a lot more, right? We are actually almost fully mitigating, almost, in Power Systems, any product cost, i.e. inflationary effects.

So therefore, this is exclusively aerospace. Obviously, aerospace includes defence as well because it is the same supply chain when I say aerospace.

But how does it work with 15% parts improvement? It's actually different things. Our initiatives make sure that 15% is improving. But at the same time given constrained environment, some suppliers are able to increase their prices.

We are obviously - that doesn't - if you are thinking, is it hitting your underlying numbers? Are they going to get worse? No. We are not that company anymore. We are obviously reflecting that in our prices. So that is how I would like you to think about.

Jeremy Bragg

Head of Investor Relations, Rolls-Royce Holdings plc

I suggest we take one more in the room if there is one and then we close.

Tufan Erginbilgic

Chief Executive Officer, Rolls-Royce Holdings plc

Okay. In that case, I'm going to close. Thanks for coming here, and thanks for listening to us if you are on the digital.

So I think we believe we are making great progress in the company. And we are actually what is interesting for me, interesting in a positive sense for me is actually, our execution is getting better.

We are hitting operational milestones. We are making great strategic progress that drives underlying performance. Because today's financials are today's financials. I worry about tomorrow's financials. And as long as you continue to improve the business underlying performance, tomorrow's financials will be secured. And that's the journey we are in. And that's how we run the business, frankly.

So thanks for listening. Have a great day.