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1 October 2020

ROLLS-ROYCE HOLDINGS PLC

PROPOSED RECAPITALISATION PACKAGE TO INCREASE RESILIENCE, STRENGTHEN BALANCE SHEET AND SUPPORT LONG-TERM STRATEGY

RIGHTS ISSUE TO RAISE APPROXIMATELY Â£2 BILLION AND INTENTION TO COMMENCE A BOND OFFERING TO RAISE AT LEAST Â£1 BILLION

COMMITMENTS AGREED FOR NEW Â£1 BILLION TWO YEAR TERM LOAN FACILITY; SUPPORT IN PRINCIPLE FROM UK EXPORT FINANCE FOR EXTENSION OF EXISTING 80% GUARANTEE TO BACK POTENTIAL LOAN INCREASE OF UP TO Â£1 BILLION

Rolls-Royce Holdings plc ("Rolls-Royce" or the "Group" or the "Company") today announces its intention to raise gross proceeds of approximately Â£2bn by way of a fully underwritten 10 for 3 Rights Issue. In conjunction with the Rights Issue, the Company intends to commence, in the near future, a Bond Offering to raise gross proceeds of at least Â£1bn. The Company has also agreed commitments for a new two year term loan facility of Â£1bn and received an indication of support in principle from UK Export Finance for an extension of its 80% guarantee to support a potential increase of the Company's existing Â£2bn five year term loan of up to Â£1bn.

Summary

Â· Proposed fully underwritten 10 for 3 Rights Issue of up to 6,436,651,043 New Ordinary Shares at 32 pence per New Ordinary Share to raise gross proceeds of approximately Â£2bn.

  Â· Rights Issue Price represents a 41.4% discount to the theoretical ex-rights price per Existing Ordinary Share by reference to the Closing Price of 130 pence per Existing Ordinary Share on 30 September 2020.

  Â· The Rights Issue is subject to approval by Shareholders at a General Meeting expected to be held on 27 October 2020.

Â· Intention to commence Bond Offering to raise gross proceeds of at least Â£1bn, denominated in US dollars, euros and/or pounds sterling, currently expected to be completed by settlement of the Rights Issue subject to market conditions.

- Â· Commitments agreed for a new two year term loan facility of Â£1bn, conditional upon the Rights Issue completing, the cancellation of the Â£1.9bn Liquidity Facility and execution of a facility agreement.
- Â· In addition, UK Export Finance has indicated that it would, in principle, support an extension of its 80% guarantee of our existing Â£2bn five year term loan to support a loan amount increase of up to Â£1bn. This is subject to completion of the Rights Issue, agreement of terms with lenders and approval of those terms by UK Export Finance and HM Treasury, and there is therefore no guarantee that this increase will take place.
- Â· Having considered a number of different scenarios, and in particular a "reasonable worst case" scenario, we have determined that it is in the best interests of Shareholders to pursue the Rights Issue and Bond Offering now in order to:
  - Â· Improve our liquidity headroom
  - Â· Reduce our level of balance sheet leverage
  - Â· Support disciplined execution and investment to ensure we maximise value from our existing capabilities and pursue disposals in a manner that delivers value, as we position the Group to benefit from new technologies focused on sustainable power.
- Â· These steps will provide the Group with improved financial resilience and a more appropriate balance sheet structure in order to weather macro-economic risks before we return to strong cash generation, expected in 2022.
- Â· Longer-term prospects remain strong. In Civil Aerospace, we do not expect a similar level of investment as we move forward, given the majority of the development of our current programmes is complete. We expect our relatively young installed base of engines will provide strong, annuity-style cash flows over the long term, reflecting the long in-service lives of our products and our services-oriented business model. We see good growth opportunities in both Defence and Power Systems. Over the longer-term, our capabilities leave us well positioned to capitalise on the transition to sustainable, low-carbon power.

Warren East, Chief Executive, said *"The sudden and material effect of the COVID-19 pandemic has had a significant impact on the commercial aviation industry, resulting in a sharp deterioration in the financial performance of our Civil Aerospace business and, to a lesser extent, our Power Systems business. We are undertaking decisive and transformative action to fundamentally restructure our operations, materially reduce our cost base and improve our financial position. The capital raise announced today improves our resilience to navigate the current uncertain operating environment. By raising additional capital now, we will improve our liquidity headroom and reduce our level of balance sheet leverage, while supporting disciplined execution and investment to ensure we maximise value from our existing capabilities. The strength of our people, brand and global footprint, together with our innovation and technology will support us as we emerge from the COVID-19 pandemic and implement our longer-term strategy, playing a crucial role in the world's transition towards a net-zero carbon economy."*

Background to the proposed recapitalisation

We delivered strong progress in 2019 and started 2020 with real momentum. The sudden and material effect of the COVID-19 pandemic, however, had a significant impact on the commercial aviation industry, resulting in a sharp deterioration in the financial performance of our Civil Aerospace business and, to a lesser extent, in our Power Systems business.

In our initial response to the COVID-19 outbreak, we rapidly implemented a number of proactive safety measures, in line with local and national guidelines, designed to ensure the safety and wellbeing of our people. We also implemented a set of measures to conserve cash from March 2020, which generated total pre-tax cash savings of approximately Â£350m in the first half of 2020 and are expected to generate approximately Â£1bn in pre-tax cash savings in the full year ending 31 December 2020. Alongside this we took early actions to bolster our liquidity position, securing Â£4.2bn of additional funding.

On 20 May 2020, we also announced a major restructuring of the Group to adjust to the new level of anticipated demand from customers in Civil Aerospace as a result of the impact of the COVID-19 pandemic. This restructuring, the largest in the Group's history, is intended to deliver a total annual pre-tax cash saving of at least Â£1.3bn by the end of 2022. We expect the restructuring programme to result in a proposed reduction in headcount of at least 9,000 roles. We have continued to make further good progress on this plan, with approximately 4,800 people having left the business by the end of August, with at least 5,000 expected by the year-end.

We believe this restructuring programme, alongside an anticipated recovery in our end markets, will help us restore financial performance. Our intent remains to return the Group to positive cash flow during the second half of 2021. We are targeting reaching at least Â£750 million FCF (excluding disposals) as early as 2022 and we believe the longer-term prospects remain strong, with further growth in cash flow and returns expected thereafter.

The pathway to strong cash flow, however, remains dependent on the timing and shape of recovery from COVID-19, notably with regards to long-haul air travel. There is significant uncertainty about the precise pace of this recovery and the possibility of delays remains a risk. The Board considers it prudent to prioritise resilience and flexibility, and is therefore pursuing the Rights Issue and Bond Offering.

Trading update

There has been no material change in our outlook for the Group since the 2020 Half Year Results Announcement published on 27 August 2020. As expected, revenue and underlying operating profit for the first eight months of the year were materially below the prior year, significantly affected by the COVID-19 pandemic and related one-off charges taken in the first half of 2020. Consistent with the trends in the first half, our Civil Aerospace and ITP Aero businesses continued to see the largest impact from COVID-19; performance in our Defence business remained resilient; and our Power Systems business experienced disruption in some end markets.

The Group continued to experience free cash outflows in July and August, albeit at a reduced level compared to the first half of 2020 and modestly better than our expectations. This reflected the ongoing management actions to control costs, large engine flying hours slightly ahead of our "base case" forecast and some cash flow timing benefits. We continue to expect a free cash outflow of approximately Â£4bn in the full year ending 31 December 2020, although uncertainties remain around the timing and shape of the recovery in large engine flying hours and the timing of large engine deliveries.

Prospectus

A prospectus in relation to the Rights Issue (the "Prospectus") is expected to be published at www.rolls-royce.com/investors later today. The preceding summary should be read in conjunction with the full text of the following announcement, together with the Prospectus. Unless the context otherwise requires, words and expressions defined in the Prospectus shall have the same meanings in this announcement.

Indicative summary timetable of principal events

Record Date for entitlements under the Rights Issue	Close of business on 23 October 2020
Deadline for proxy appointments for General Meeting	11.00 a.m. on 25 October 2020
General Meeting	11.00 a.m. on 27 October 2020

Despatch of Provisional Allotment Letters (to Qualifying Non-CREST Shareholders only)	27 October 2020
Existing Ordinary Shares marked "ex-rights" by the London Stock Exchange	8:00 a.m. on 28 October 2020
Admission of, and dealings in, Nil Paid Rights commence on the London Stock Exchange	8:00 a.m. on 28 October 2020
Latest time and date for acceptance, payment in full and registration of renunciation of Provisional Allotment Letters	11:00 a.m. on 11 November 2020
Announcement of the results of the Rights Issue through a Regulatory Information Service	By 8:00 a.m. on 12 November 2020
Dealings in New Ordinary Shares, fully paid, commence on the London Stock Exchange	8:00 a.m. on 12 November 2020

The Rights Issue is fully underwritten with BNP Paribas, Citigroup, Goldman Sachs, HSBC, Jefferies and Morgan Stanley acting as Joint Global Coordinators and CrÃ©dit Agricole CIB, Santander, SMBC Nikko and SociÃ©tÃ© GÃ©nÃ©rale acting as Co-lead Managers. Goldman Sachs and Greenhill are acting as financial advisers to the Company. Jefferies and Morgan Stanley are acting as joint sponsors to the Company.

This announcement has been determined to contain inside information.

LEI: 213800EC7997ZBLZJH69

A conference call will be held at 08:30 (BST) today and details of how to join can be accessed at www.rolls-royce.com/investors, along with materials relating to the call.

For further information, please contact:

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About Rolls-Royce Holdings plc

1. Rolls-Royce pioneers cutting-edge technologies that deliver clean, safe and competitive solutions to meet our planet's vital power needs.
2. Rolls-Royce has customers in more than 150 countries, comprising more than 400 airlines and leasing customers, 160 armed forces, 70 navies, and more than 5,000 power and nuclear customers.
3. Annual underlying revenue was Â£15.45 billion in 2019, around half of which came from the provision of aftermarket services.
4. In 2019, Rolls-Royce invested Â£1.46 billion on research and development. We also support a global network of 29 University Technology Centres, which position Rolls-Royce engineers at the forefront of scientific research.

IMPORTANT NOTICES

This announcement has been issued by and is the sole responsibility of the Company. The information contained in this announcement is for background purposes only and does not purport to be full or complete. No reliance may or should be placed by any person for any purpose whatsoever on the information contained in this announcement or on its accuracy or completeness. The information in this announcement is subject to change without notice.

This announcement is not a prospectus (or a prospectus equivalent document) but an advertisement. Neither this announcement nor anything contained in it shall form the basis of, or be relied upon in conjunction with, any offer or commitment whatsoever in any jurisdiction. Investors should not acquire any Nil Paid Rights, Fully Paid Rights, New Ordinary Shares or any Bonds except on the basis of the information contained in the Prospectus or offering memorandum, as applicable.

A copy of the Prospectus will, following publication, be available on the Company's website, www.rolls-royce.com/investors. Neither the content of the Company's website nor any website accessible by hyperlinks on the Company's website is incorporated in, or forms part of, this announcement. The Prospectus will provide further details of the New Ordinary Shares, the Nil Paid Rights and the Fully Paid Rights being offered pursuant to the Rights Issue or an offering memorandum will be available to qualifying institutional investors following
commencement of the Bond Offering.

This announcement does not contain or constitute an offer for sale or the solicitation of an offer to purchase or subscribe for securities in the United States or any other state or jurisdiction in which such release, publication or distribution would be unlawful. The Nil Paid Rights, the Fully Paid Rights, the New Ordinary Shares and the Bonds have not been and will not be registered under the US Securities Act of 1933, as amended (the "Securities Act") or under any securities laws of any state or other jurisdiction of the United States and may not be offered, sold, pledged, taken up, exercised, resold, renounced, transferred or delivered, directly or indirectly, in or into the United States except pursuant to an applicable exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and in compliance with any applicable securities laws of any state or other jurisdiction of the United States or other jurisdiction. There will be no public offer of the Nil Paid Rights, the Fully Paid Rights, the New Ordinary Shares or any of the Bonds in the United States. Subject to certain limited exceptions, Provisional Allotment Letters have not been, and will not be, sent to, and Nil Paid Rights have not been, and will not be, credited to the CREST account of, any Qualifying Shareholder with a registered address in or that is located in the United States. None of the New Ordinary Shares, the Nil Paid Rights, the Fully Paid Rights or the Provisional Allotment Letters, this announcement or any other document connected with the Rights Issue or the Bond Offering has been or will be approved or disapproved by the United States Securities and Exchange Commission or by the securities commissions of any state or other jurisdiction of the United States or any other regulatory authority, nor have any of the foregoing authorities passed upon or endorsed the merits of the offering of the New Ordinary Shares, the Nil Paid Rights, the Fully Paid Rights or any of the Bonds, or the accuracy or adequacy of the Provisional Allotment Letters, this announcement or any other document connected with the Rights Issue or the Bond Offering. Any representation to the contrary is a criminal offence in the United States.

This announcement is for information purposes only and is not intended to and does not constitute or form part of any offer or invitation to purchase or subscribe for, or any solicitation to purchase or subscribe for, Nil Paid Rights, Fully Paid Rights, New Ordinary Shares or any of the Bonds or to take up any entitlements to Nil Paid Rights in any jurisdiction. No offer or invitation to purchase or subscribe for, or any solicitation to purchase or subscribe for, Nil Paid Rights, Fully Paid Rights, New Ordinary Shares or any of the Bonds or to take up any entitlements to Nil Paid Rights will be made in any jurisdiction in which such an offer or solicitation is unlawful.

The information contained in this announcement, the Prospectus and the Provisional Allotment Letters is not for release, publication or distribution to persons in the United States, New Zealand, United Arab Emirates, South Africa or any other jurisdiction where the extension or availability of the Rights Issue or the Bond Offering (and any other transaction contemplated thereby) would breach any applicable law or regulation, and, subject to certain exceptions, should not be distributed, forwarded to or transmitted in or into any jurisdiction, where to do so might constitute a violation of local securities laws or regulations.

The distribution of this announcement, the Prospectus, the Provisional Allotment Letter and the offering or transfer of Nil Paid Rights, Fully Paid Rights or New Ordinary Shares into jurisdictions other than the United Kingdom may be restricted by law, and, therefore, persons into whose possession this announcement, the Prospectus, the Provisional Allotment Letter and/or any accompanying documents comes should inform themselves about and observe any such restrictions. Any failure to comply with any such restrictions may constitute a violation of the securities laws of such jurisdiction. In particular, subject to certain exceptions, this announcement, the Prospectus (once published) and the Provisional Allotment Letters (once printed) should not be distributed, forwarded to or transmitted in or into the United States, New Zealand, United Arab Emirates South Africa or any other jurisdiction where the extension or availability of the Rights Issue or the Bond Offering (and any other transaction contemplated thereby) would breach any applicable law or regulation. Recipients of this announcement should conduct their own investigation, evaluation and analysis of the business, data and property described in this announcement and/or if and when published the Prospectus to be published by the Company in connection with the Rights Issue.

This announcement does not constitute a recommendation concerning any investor's options with respect to the Rights Issue or the Bond Offering. The price and value of securities can go down as well as up. Past performance is not a guide to future performance. The contents of this announcement are not to be construed as legal, business, financial or tax advice. Each shareholder or prospective investor should consult his, her or its own legal adviser, business adviser, financial adviser or tax adviser for legal, financial, business or tax advice.

NOTICE TO ALL INVESTORS

BNP Paribas ("BNP Paribas"), Citigroup Global Markets Limited ("Citigroup"), Goldman Sachs International (â€œGoldman Sachsâ€), HSBC Bank plc ("HSBC"), Jefferies International Limited ("Jefferies"), Morgan Stanley & Co. International plc (â€œMorgan Stanleyâ€), CrÃ©dit Agricole Corporate and Investment Bank ("CrÃ©dit Agricole CIB"), Banco Santander, S.A. ("Santander"), SMBC Nikko Capital Markets Limited ("SMBC Nikko") and SociÃ©tÃ© GÃ©nÃ©rale ("SociÃ©tÃ© GÃ©nÃ©rale", and, together with Goldman Sachs, Morgan Stanley, BNP Paribas, Citigroup, HSBC, Jefferies, CrÃ©dit Agricole CIB, Santander and SMBC Nikko, the "Banks") are authorised in the United Kingdom by the Financial Conduct Authority and regulated by the Financial Conduct Authority and, in the case of BNP Paribas, lead supervised by the European Central Bank ("**ECB**") and the *AutoritÃ© de ContrÃ´le Prudentiel et de RÃ©solution* ("**ACPR**") (and its London Branch is authorised by the ECB, the ACPR and the Prudential Regulation Authority and subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority). Each of the Banks is acting exclusively for Rolls-Royce Holdings plc in relation to the Rights Issue and no other person in connection with the Rights Issue and will not be responsible to anyone other than Rolls-Royce Holdings plc for providing the protections afforded to their respective clients nor for providing advice to any person in relation to the Rights Issue or any matters referred to in this announcement.Goldman Sachs is acting as Financial Adviser to the Company and no other person in connection with this announcement and will not be responsible to anyone other than the Company for providing the protections afforded to clients of Goldman Sachs nor for providing advice to any person in relation to any matters referred to in this announcement.

None of the Banks, nor any of their respective subsidiaries, branches or affiliates, nor any of their respective directors, officers or employees owes or accepts any duty, liability or responsibility whatsoever (whether direct or indirect, whether in contract, in tort, under statute or otherwise) to any person who is not a client of the Banks in connection with the Rights Issue, this announcement, any statement contained herein, or otherwise.

No representation or warranty, express or implied, is or will be made as to, or in relation to, and no responsibility or liability is or will be accepted by the Banks, nor any of their respective subsidiaries, branches, affiliates or agents as to, or in relation to, the accuracy or completeness of this announcement or any other information made available to or publicly available to any interested party or its advisers, whether written, oral or in a visual or electronic form, and howsoever transmitted or made available, and any liability therefore is expressly disclaimed.

In connection with the Rights Issue, the Banks and any of their respective affiliates, may in accordance with applicable legal and regulatory provisions, engage in transactions in relation to the Nil Paid Rights, the Fully Paid Rights, the New Ordinary Shares and/or related instruments for their own account provided that the Banks and their respective affiliates may not engage in short selling for the purpose of hedging their commitments under the Underwriting Agreement (subject to certain exceptions in the Underwriting Agreement). Accordingly, references in the Prospectus to the Nil Paid Rights, Fully Paid Rights or New Ordinary Shares being issued, offered, subscribed, acquired, placed or otherwise dealt in should be read as including any issue or offer to, or subscription, acquisition, placing or dealing by, the Banks and any of their affiliates acting in such capacity.

The Banks and their respective affiliates may enter into financing arrangements with investors in connection with which the Banks and any of their affiliates may from time to time acquire, hold or dispose of New Ordinary Shares. In addition, the Banks may also co-ordinate a sell-down in the event that any underwriting crystallises as a result of the

Rights Issue. The Banks and their respective affiliates do not intend to disclose the extent of any such investment or transactions otherwise than in accordance with any legal or regulatory obligations to do so.

In the event that the Banks acquire New Shares that are not taken up by Qualifying Shareholders, the Banks and their respective affiliates may co-ordinate disposals of such shares in accordance with applicable law and regulation. The Banks and their respective affiliates do not propose to make any public disclosure in relation to such transactions.

Greenhill & Co. International LLP ("Greenhill") is authorised by the Financial Conduct Authority and regulated by the Financial Conduct Authority and is acting exclusively as financial adviser to the Company and no one else in connection with the matters described in this announcement and will not be responsible to anyone other than the Company for providing the protections afforded to clients of Greenhill nor for providing advice in connection with the matters referred to herein. Neither Greenhill nor any of its subsidiaries, branches or affiliates, nor any of its directors, officers or employees owes or accepts any duty, liability or responsibility whatsoever (whether direct or indirect, whether in contract, in tort, under statute or otherwise) to any person who is not a client of Greenhill in connection with the Rights Issue, this announcement, any statement contained herein, or otherwise.

INFORMATION TO DISTRIBUTORS

Solely for the purposes of the product governance requirements contained within: (a) EU Directive 2014/65/EU on markets in financial instruments, as amended ("MiFID II"); (b) Articles 9 and 10 of Commission Delegated Directive (EU) 2017/593 supplementing MiFID II; and (c) local implementing measures (together, the "MiFID II Product Governance Requirements"), and disclaiming all and any liability, whether arising in tort, contract or otherwise, which any "manufacturer" (for the purposes of the MiFID II Product Governance Requirements) may otherwise have with respect thereto, the Nil Paid Rights, the Fully Paid Rights and the New Ordinary Shares have been subject to a product approval process, which has determined that they each are: (i) compatible with an end target market of retail investors and investors who meet the criteria of professional clients and eligible counterparties, each as defined in MiFID II; and (ii) eligible for distribution through all distribution channels as are permitted by MiFID II (the "Target Market Assessment").

Notwithstanding the Target Market Assessment, Distributors should note that: the price of the Nil Paid Rights, the Fully Paid Rights and/or the New Ordinary Shares may decline and investors could lose all or part of their investment; the Nil Paid Rights, the Fully Paid Rights and the New Ordinary Shares offer no guaranteed income and no capital protection; and an investment in the Nil Paid Rights, the Fully Paid Rights and/or the New Ordinary Shares is compatible only with investors who do not need a guaranteed income or capital protection, who (either alone or in conjunction with an appropriate financial or other adviser) are capable of evaluating the merits and risks of such an investment and who have sufficient resources to be able to bear any losses that may result therefrom. The Target Market Assessment is without prejudice to the requirements of any contractual, legal or regulatory selling restrictions in relation to the offer. Furthermore, it is noted that, notwithstanding the Target Market Assessment, the Banks will only procure investors who meet the criteria of professional clients and eligible counterparties. For the avoidance of doubt, the Target Market Assessment does not constitute: (a) an assessment of suitability or appropriateness for the purposes of MiFID II; or (b) a recommendation to any investor or group of investors to invest in, or purchase, or take any other action whatsoever with respect to the Nil Paid Rights, the Fully Paid Rights and/or the New Ordinary Shares. Each distributor is responsible for undertaking its own target market assessment in respect of the Nil Paid Rights, the Fully Paid Rights and/or the New Ordinary Shares and determining appropriate distribution channels.

FORWARD-LOOKING STATEMENTS

This announcement may contain projections and other forward-looking statements. The words "believe", "expect", "anticipate", "intend" and "plan" and similar expressions identify forward-looking statements. All statements other than statements of historical facts included in this announcement, including, without limitation, those regarding the Company's financial position, potential business strategy, potential plans and potential objectives, are forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the Company's actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such forward-looking statements are based on numerous assumptions regarding the Company's present and future business strategies and the environment in which the Company will operate in the future. Further, certain forward-looking statements are based upon assumptions of future events which may not prove to be accurate.

None of the Company, its officers, advisers or any other person gives any representation, assurance or guarantee that the occurrence of the events expressed or implied in any forward-looking statements in this announcement will actually occur, in part or in whole.

The forward-looking statements in this announcement speak only as at the date of this announcement. To the extent required by applicable law or regulation (including as may be required by the Companies Act, the Prospectus Regulation Rules, the Listing Rules, MAR, the Disclosure Guidance and Transparency Rules and FSMA), the Company will update or revise the information in this announcement. Otherwise, the Company assumes no obligation to update or provide any additional information in relation to such forward-looking statements. Additionally, statements of the intentions or beliefs of the board of directors of the Company reflect the present intentions and beliefs of the board of directors of the Company as at the date of this announcement and may be subject to change as the composition of the board of directors of the Company alters, or as circumstances require.

Nothing in this announcement is intended as a profit forecast or estimate for any period and no statement in this announcement should be interpreted to mean that earnings or earnings per share or dividend per share for the Company for the current or future financial years would necessarily match or exceed the historical published earnings or earnings per share or dividend per share for the Company.

BACKGROUND TO AND REASONS FOR THE RIGHTS ISSUE

Context

We are a leading global power technology company, with a portfolio spanning our Civil Aerospace (which contributed 51% of the underlying revenue generated by the Group's businesses in 2019), Power Systems (22%), Defence (20%) and ITP Aero (6%) businesses. The breadth of our business activities provides the Group with access to a wide range of growth opportunities. This, together with our large installed base of engines and the significant performance improvement we expect to deliver in the Civil Aerospace business over the coming years, will drive enhanced value for our stakeholders.

The period prior to the COVID-19 pandemic

Between 2015 and 2019 we delivered substantially improved financial performance, while simultaneously investing heavily in new civil aerospace engine programmes and addressing the in-service issues on the Trent 1000 programme. During this period:

Â· widebody engine deliveries increased by 66%;
Â· EFHs for the Group's engines increased by 43%;
Â· the Civil Aerospace business's installed large engine fleet increased by 29% to 5,000 engines;
Â· the Power Systems business's operating profit margins improved by two percentage points and its underlying revenue compound annual growth rate was 10%; and
Â· FCF increased to Â£873m (from Â£179m), despite incurring Â£405m of in-service cash costs relating to the Trent 1000 programme in 2019 affecting FCF.

Additionally, we worked to improve the strength of our balance sheet during this period, raising around Â£1bn through the disposals of Commercial Marine and L'Orange. Together with the higher FCF generation outlined above, the Group's net debt position improved from Â£111m in 2015 to a net cash position of Â£1.4bn (both excluding lease liabilities) as at 31 December 2019.

Our results published for the year ended 31 December 2019 continued to demonstrate good progress in a number of areas, including:

Â· strong progress in growing underlying operating profit (with growth of 25% year-on-year to Â£808m) and FCF with growth of 54% year-on-year;
Â· a record number of widebody engines delivered in 2019;
Â· a 14% reduction in OE unit losses;
Â· a 64% market share of new widebody engine orders;
Â· a 5% organic increase year-on-year in business aviation OE sales;
Â· a record order intake in our Defence business, amounting to 1.6x underlying revenue for 2019;

Â· an improvement in underlying operating margin of our Power Systems business of nearly one percentage point (10.1% in 2019 compared to 9.2% in 2018);

Â· the fixes to address the Trent 1000 durability issues. We have since brought the number of customer aircraft on the ground as a result of these issues down to zero as at 30 June 2020; and

Â· significant progress on our previous restructuring programme, including the simplification of processes and delivery of a more agile working culture, which resulted in run-rate savings of Â£269m as at 31 December 2019.

We believe that, prior to the COVID-19 pandemic, we were on track to deliver on our 2020 target of Â£1bn of FCF with continued growth towards our medium-term ambition of exceeding Â£1 of FCF per Ordinary Share (which translated into at least Â£1.9bn of FCF).

Further progress was still being pursued to increase cost competitiveness and improve consistency of operational and financial performance. We believe we were well positioned to deliver materially stronger shareholder returns over time and, in parallel, to invest in new technologies to address a range of market opportunities in each of our businesses.

The impact of the COVID-19 pandemic

The COVID-19 pandemic has resulted in wide-ranging measures being implemented across the world in an attempt to contain the spread of the virus. This has had a significant effect on the Group. The commercial aerospace sector in which our Civil Aerospace and ITP Aero businesses operate has been particularly affected:

Â· much of the global airline fleet has been temporarily grounded, resulting in a fall in global airline demand (as measured by revenue passenger kilometres ("RPKs")) by 94%, 91%, 87% and 80% in April, May, June and July 2020 respectively compared to the same period in 2019 (according to IATA); and

Â· airlines have delayed or cancelled planned deliveries and orders for new aircraft, with Airbus and Boeing responding with significant reductions in production rates of the widebody aircraft for which we supply engines.

Our Civil Aerospace business derives the majority of its cash flow from payments based on the number of hours that our engines are powering our customers' aircraft. In 2019, our large engine fleet generated approximately Â£4.0bn of gross cash inflow. In addition, approximately Â£2.7bn of gross cash inflow was derived from the delivery of widebody engines. As a result of the COVID-19 pandemic, large engine deliveries and flying hours were both down approximately 50% in the first half of 2020. We saw a 37% reduction year-on-year in underlying revenue in our Civil Aerospace business in the six-month period ended 30 June 2020, with an underlying operating loss of Â£1.8bn. However, business jets and regional aircraft flying hours proved to be more resilient.

Reflecting the changed market outlook, we expect lower US dollar receipts over the next seven years and, as a result, we took the decision to reduce the size of our hedge book by $10.3bn. This resulted in a Â£1.46bn underlying finance charge in the first half of 2020. Additionally, as net purchasers of US dollars in this period, we were unable to utilise our hedge book over the six-month period to 30 June 2020.

The commercial aerospace activities of our ITP Aero business, which accounted for approximately 77% of its underlying revenues in 2019, have experienced a similar deterioration in end market demand.

Our Defence business has remained resilient. It experienced no material operational or financial disruption. Underlying revenue in the six-month period ended 30 June 2020 increased by 4% year-on-year with operating profit increasing by 19% on an organic basis and an order intake to underlying revenue ratio of 0.8x in that period.

Our Power Systems business has experienced varying levels of COVID-19-related disruption and utilisation, with our customers in industrial markets most affected by lower activity levels. Naval and governmental end market demand has remained robust. As a result, we saw an 11% reduction in underlying revenue with an underlying operating profit down by 79% and a 27% reduction year-on-year in orders in the six-month period ended 30 June 2020.

We have implemented a number of cost reduction actions to mitigate the effect of the COVID-19 pandemic, which are described below. However, these have not been sufficient to offset the total negative cash impact across the Group. In the six-month period ended 30 June 2020, we therefore reported an underlying operating loss in the period of Â£1.7bn and negative FCF of Â£2.8bn.

Recent trends in EFHs for the Civil Aerospace business have shown some early signs of recovery from their April low points, led by an increase in flight activity in China, Asia Pacific and the Middle East. However, uncertainty remains regarding the overall shape and timing of any recovery.
In our initial response to the COVID-19 outbreak, we rapidly implemented a number of proactive safety measures, in line with local and national guidelines, designed to ensure the safety and wellbeing of our people. At the same time, we are proud to have supported the communities in which we operate in a variety of ways, including forming an alliance of leading companies seeking to use data analytics to provide insights to support government decision making in response to the COVID-19 pandemic.

In relation to our financial position, we implemented a set of measures to conserve cash from March 2020, including:

Â· a reduction of capital expenditure on non-critical programmes by around one third compared to our initial expectations for 2020 and cancellation of capacity expansion projects that are no longer required;
Â· a significant reduction in spend on consulting, professional fees and subcontractors, together with a material reduction in travel expenditure;
Â· a review of R&D and engineering expenditure, which led to expenditure reductions reflecting a re-phasing of certain programmes, such as UltraFan, over a longer period of time; and
Â· an approximately 10% reduction in our global salary costs, largely achieved through temporary pay cuts for senior management, use of government furlough schemes and pay deferrals for staff.

These mitigating actions generated total cash savings of approximately Â£350m in the first half of 2020 and are expected to generate approximately Â£1bn in pre-tax cash savings in the full year ending 31 December 2020. In addition to these cash savings, we also moved quickly to reduce direct purchase volumes, as well as cancelling our final 2019 shareholder payment to preserve an additional Â£137m of cash in 2020. As announced in our 2020 Half Year Results Announcement, no interim shareholder payment was proposed for 2020.

Alongside this, we took early actions to bolster our liquidity position, allowing us time to conduct a more detailed review of the Group's capital structure and funding options. These actions included:

Â· entering into an additional Â£1.9bn Liquidity Facility with a maturity date in October 2021 (which is currently undrawn and will be cancelled on completion of the Rights Issue);

Â· issuing Â£300m of commercial paper through the UK Government's CCFF with a maturity date of 17 March 2021; and

Â· entering into a Â£2bn five year Term Loan Facility, which is supported by an 80% guarantee from UK Export Finance.

On 20 May 2020, we also announced a major restructuring of the Group to adjust to the new level of anticipated demand from customers in certain of our end markets as a result of the impact of the COVID-19 pandemic and to seek to restore our financial performance.

Further actions to enhance our financial resilience and deliver a more appropriate balance sheet to position us for the post-COVID-19 environment
In response to the impact of the COVID-19 pandemic, the Board has conducted a detailed review of the Group's outlook, balance sheet and funding options. As a result of this, we are undertaking decisive and transformative action to fundamentally restructure the Group's operations, materially reduce our cost base by at least Â£1.3bn by the end of 2022 and improve our financial position. We have conducted a detailed review of the Group's capital structure and funding options, considering a number of different scenarios and assessing their potential impact on the Group's financial position. This included consideration of a "reasonable worst case" scenario, further details of which are set out in section 12 (Working Capital) of Part XII (Additional Information) of the Prospectus.

Taking into account, in particular, this "reasonable worst case" scenario, alongside continued global and macro-economic uncertainty, we have determined that it is in the best interests of Shareholders to take the following actions:

Â· to deliver a number of potential disposals (which include the ITP Aero business) to raise gross proceeds of more than Â£2bn, as announced in our 2020 Half Year Results Announcement;

Â· to raise additional capital of approximately Â£2bn through the Rights Issue and at least Â£1bn by way of a Bond Offering; and

Â· to agree commitments for a new term loan facility of Â£1bn, which is subject to conditions including completion of the Rights Issue (and the resulting cancellation of the Liquidity Facility) and agreement and execution of a facility agreement. This new term loan would have a final maturity date falling two years from entry into a facility agreement.

In addition, UK Export Finance has indicated that it would, in principle, support an extension of its 80% guarantee of our existing Â£2bn five year term loan to support an increase in the loan amount of up to Â£1bn. This is subject to completion of the Rights Issue, agreement of terms with lenders and approval of those terms by UK Export Finance and HM Treasury, and there is therefore no guarantee that this increase will take place.

By raising additional capital now, we will improve our liquidity headroom, reduce our level of balance sheet leverage while supporting disciplined execution and investment to ensure we maximise value from our existing capabilities. It will also allow us to deliver disposals in a manner that ensures value for our shareholders as we position the Group for the long term to benefit from new technologies focused on sustainable power. We believe these steps will provide the Group with improved financial resilience and a more appropriate balance sheet structure across 2021 in order to weather the macro-economic risks before we return to strong cash generation, which is expected in 2022.

We are also focused on ensuring we maintain a suitable capital structure for the markets in which we operate and believe that an investment grade credit rating is appropriate for our business. We have an ambition to return to a net cash position in the base case over the next few years and to secure an investment grade credit rating in the medium term.

We believe execution of this strategy will ultimately provide a strong platform to drive a significant improvement in FCF and deliver attractive shareholder returns. If we do not successfully execute the Rights Issue, the Bond Offering or one or more of the targeted disposals in the required timescales or if the impact of the COVID-19 pandemic is more severe than we expect, even in a "reasonable worst case" scenario, we will need to consider whether it is appropriate to pursue certain of the alternative actions outlined in section 12 (Importance of vote) of Part V (Letter from the Chairman of Rolls-Royce Holdings plc) of the Prospectus.

OUR STRENGTHS

We believe that the strengths summarised below, together with key enablers, such as the strength of the Rolls-Royce brand, our people and our global footprint, will play an important role as we emerge from the COVID-19 pandemic and implement our longer-term strategy.

Our products incorporate cutting-edge technologies. We have a track record of developing commercially successful new technologies

Our products incorporate significant intellectual property, capturing cutting-edge technologies that have been developed over decades. In our Civil Aerospace and ITP Aero businesses, commercial aero engines are extremely complex mechanical engineering products, requiring significant expertise in aerodynamic, thermodynamic and materials technologies. Similarly, in our Defence business, we are one of only a handful of companies currently capable of designing, integrating and manufacturing complete military jet engines, mainly for the UK and US governments. In our Power Systems business, we have focused on demanding, high-end applications for reciprocating engines, in areas such as mission critical back-up power where start-up time and reliability are critical. We also have significant expertise in powerplants for nuclear-powered submarine applications. We have a long-established track record of developing commercially successful technology and products, which have enabled us to grow our share in key markets.

We focus on developing integrated power system solutions

We integrate individual enabling technologies into complete systems and power solutions. This provides our customers with the ability to work with a single partner to provide their entire power needs for their chosen application. In our Civil Aerospace and Defence businesses, our capabilities cover end-to-end design, assembly and through-life support of complete gas turbine power solutions. Our Power Systems business is increasingly moving into the provision of complete power generation systems such as power 'gensets' as well as integrated propulsion systems for the rail and marine markets.

Our products provide an attractive aftermarket opportunity

Many of our products have significant aftermarket and maintenance requirements during their operating lives, which typically run for decades. We provide complete through-life maintenance and support for our power solutions, including extensive use of "power-by-the-hour" LTSAs, as well as more traditional time and materials business. In 2019, 52% of our underlying revenue was generated from aftermarket services. Accordingly, we believe our substantial installed base provides a large, captive, visible, and long-term revenue and cash flow stream. The Civil Aerospace business installed base is relatively young, with approximately 9,000 small and business aviation engines in service with an average age of 19 years for small civil jets and 13 years for business jets, as well as approximately 5,000 large engines with an average age of less than 9 years. Given an average expected engine life of approximately 40 years for a small or business aviation engine and approximately 25 years for a widebody engine, we expect significant aftermarket revenue and value from this installed base. Similarly, the installed base in our Defence business of approximately 16,000 defence engines is expected to continue to operate for many decades.

We enjoy strong customer relationships

We believe our focus on building complete power solutions provides the basis for strong customer relationships, with the Group acting as a single, trusted power provider for the customer. The LTSA model for through-life support further deepens these relationships. We have built strong, direct customer relationships with major aircraft manufacturers, such as Airbus, Boeing, Gulfstream and Lockheed Martin, and with more than 400 airlines and leasing customers, 160 armed forces, 70 naval forces and more than 5,000 power and nuclear customers. Globally, our largest defence customers are the US Department of Defense and the UK Ministry of Defence. These relationships have allowed the Group to continue winning business during a period of increased macro-economic uncertainty associated with the COVID-19 pandemic.

We have a successful track record of partnerships globally
We have a long track record of working with external partners spanning corporations, governments and universities in order to leverage outside expertise, market access, and capital. The Civil Aerospace business makes extensive use of RRSPs to outsource components or complete engine modules to trusted suppliers, forming closer relationships and aligning the incentives of suppliers to the overall programme ambitions. In our Defence business, we act as a major partner on key European defence collaborations and are an important member of the Team Tempest fighter jet consortium. In our Power Systems business, we have significantly accelerated partnering efforts in recent years, including launching joint ventures for engine assembly in both India and China.

OUR STRATEGY

As explained above, we are undertaking a number of transformative actions in light of the impact of the COVID-19 pandemic and have refined our strategy accordingly.

Our strategy is to:
Â· restore financial performance in order to improve returns and build a more resilient and more appropriate balance sheet;
Â· drive growth and maximise value from our existing capabilities; and
Â· position the Group to benefit from new technologies, with a focus on sustainable power.

We believe that the key end markets for our businesses remain fundamentally attractive. Our Civil Aerospace business benefits from a sizeable and young installed base generating a significant long-term aftermarket annuity stream. The civil aerospace industry is expected to deliver long-term growth, albeit from a lower base, as GDP recovers and an increasing proportion of the world's population travels. The industry has experienced a number of shocks in the past - including the events of 11 September 2001 and the global financial crisis - and it has undergone a process of recovery each time.

While spending on the products manufactured and services provided by our Defence business may come under some pressure in the near term given fiscal spending priorities, we believe that governments will continue to invest in maintaining and upgrading their defence capabilities.
Finally, the range of end markets served by our Power Systems business is expected to experience cyclical recovery, including strong structural growth in mission critical power supply.
We further believe that over the longer term, the end markets in which we operate will see growing demand for cleaner and, more sustainable power, electrification and digitalisation. We will be well-positioned to play a crucial role in the world's transition towards a net-zero carbon economy.
We believe that the strengths described above and the execution of our strategy will allow us to capitalise on this, ultimately driving a significant improvement in FCF and delivering attractive shareholder returns.

Restoring financial performance in order to improve returns and build a more resilient and more appropriate balance sheet
Given the current significant uncertainty, we are today announcing the Rights Issue and the Bond Offering alongside the potential additional term loans described above and the targeted disposals announced as part of our 2020 Half Year Results Announcement on 27 August 2020. We believe these measures will build a more resilient and more appropriate balance sheet and provide additional liquidity headroom to navigate through the COVID-19 recovery. We have launched a major restructuring programme, the largest in the Group's history, that will re-size the cost base and capital requirements of our Civil Aerospace business and increase cost efficiency. We intend to retain a strong set of capabilities and technologies following completion of this programme, allowing us to benefit from the strong fundamentals of our businesses.

We believe this restructuring programme, alongside an anticipated recovery in our end markets, greater discipline in R&D expenditure and the absence of certain one-off cash outflows expected to be incurred this year, will help us restore financial performance and return to FCF of at least Â£750m (excluding disposals) as early as 2022.

In response to the lower-demand environment in the civil aerospace market over the medium term, we are taking decisive actions to:

Â· re-size the manufacturing footprint of the Civil Aerospace business: we are significantly reducing the scale and, therefore, fixed costs of our manufacturing footprint. This includes a proposed reduction of the headcount in the Civil Aerospace business by approximately one third (around 8,000 roles) (subject, where applicable, to consultation) as well as a major manufacturing footprint consolidation. As part of this consolidation we intend to reduce the number of global sites involved in widebody engine assembly and test from three to just one (in Derby) as well as consolidating fan blade, turbine blade and blisk production activities;

Â· optimise our MRO capabilities: we will maintain core in-house capability at a reduced number of locations to reduce our capital intensity, while supporting longer-term growth in maintenance demand primarily through an enlarged external MRO supplier network;

Â· implement a capital-light spare engine strategy: the Group typically commits approximately Â£100m-Â£150m each year of its own capital to spare engines, to support customers who pay for spare engine coverage under the Group's LTSAs. We intend to pursue third-party partnerships to reduce this capital intensity and increase flexibility of spare engine provision; and

Â· reduce central functions: by the end of 2021, it is proposed that central functions headcount will be reduced by approximately 20%-25% (subject, where applicable, to consultation) to match a leaner Group structure.

This programme is intended to deliver larger, permanent savings to replace and expand on the temporary mitigating actions delivered by the Group in 2020. We anticipate a resulting total annual pre-tax cash saving of at least Â£1.3bn to be achieved by the end of 2022. The restructuring is expected to result in cash restructuring costs of approximately Â£800m, phased as approximately Â£400m in 2020, Â£300m in 2021 and Â£100m in 2022.

We expect the restructuring programme to result in a proposed reduction in headcount of at least 9,000 roles (subject, where applicable, to consultation) from a global workforce of 52,000, with around 8,000 of these proposed headcount reductions in our Civil Aerospace business. Headcount reductions of approximately 4,800 had taken place at the end of August, with at least 5,000 expected by the year-end. The scope of this exercise has already been determined, with specific implementation plans formed and subject to consultation currently underway with trade unions. We deeply regret the need to take these difficult decisions and steps, particularly as we consider the impact on employees directly affected by this restructuring. The Group has therefore sought voluntary severance where possible, in order to mitigate the need for compulsory redundancy, as well as putting in place a suite of measures to help employees as they transition out of the Group. There have been more than 2,500 voluntary severance and early retirement agreements in the UK, substantially reducing the need for compulsory redundancies.

In addition, within our Power Systems business, as a response to changes in global demand, the business is working actively to improve its manufacturing fixed cost base; optimising efficiency and balancing its global footprint by moving capacity from Europe and the US to India and China. These initiatives are expected to deliver in excess of Â£50m of annual pre-tax cash savings by the end of 2022 In addition, the Power Systems business is also implementing a series of measures intended to reduce indirect costs through process improvements and headcount reduction.

Driving growth and maximising value from our existing capabilities
In light of the effects of the COVID-19 pandemic, we are implementing a shift in our medium-term strategy, pursuing stronger medium-term growth opportunities. In our Civil Aerospace business, our priority is to drive higher cash returns from our existing installed base while seeking new approaches to reduce the investment requirements for the development of our next generation gas turbine technology. We are also placing a greater relative focus on investment opportunities in our Defence and Power Systems businesses.

Enhancing value in our Civil Aerospace business: there is significant value embedded in our existing installed base of approximately 5,000 large engines and 9,000 small and business aviation engines. The investment required to develop the programmes within this installed base is largely complete and the Group now has an important opportunity to realise that value. The Group's fleets are among the youngest in their respective markets, providing protection from the risk of premature aircraft retirements and driving higher utilisation than for older fleets. As investment in new product introductions continues to reduce in the coming years, we will focus on driving value through a number of initiatives, including enhanced time-on-wing, enhanced services offerings and improved engineering efficiency.

We are looking at new ways of working in order to deliver more compelling returns for Shareholders. For example, we are actively exploring new forms of industrial partnership on the UltraFan programme to optimise investment returns and risk (which we consider important to our continued investment in the UltraFan programme), in addition to a re-phasing of our investment to adapt to the likely delay in entry into service of new UltraFan-powered aircraft. More broadly, we have explored new and different forms of partnerships and collaborations with industry participants in respect of our wider Civil Aerospace business. We intend to continue exploring these to deliver a new approach to investment.

Significant medium-term opportunities in our Defence business: we have invested significantly in recent years in pursuing growth opportunities in the defence market, including in two major opportunities in the US market, being the B-52 re-engine programme (where we have submitted our proposal) and the future vertical lift programme, which we believe have the potential for over 650 engines and over 4,000 engines respectively, with a combined estimated lifetime value of approximately Â£7bn. We believe we are well positioned in respect of these opportunities, which will be important to the Defence business's future growth.

Delivering growth in our Power Systems business: following the COVID-19 pandemic, many of the end markets of our Power Systems business are expected to recover quickly, with some even seeing accelerated growth opportunities. As a result, we are increasing the proportional allocation of investment to the Power Systems business. Investment will also continue in new technologies such as hybrid systems, as outlined in further detail below. We see key opportunities in:

Â·   the Chinese market, where our strategy has already begun to deliver results, with growth of approximately 40% in underlying revenue from China in our Power Systems business in 2019 and expected further growth of 25% in 2020;

Â·   the mission critical back-up power market, where we expect to deliver significant growth in the medium to long term;

Â· our recently expanded gas portfolio, with strong growth underpinned by a rising focus on carbon emissions;
Â· our Power Systems business aftermarket offering, which has historically been a more reactive, spare parts sales focused business, but has the potential to provide a broader range of services and support; and
Â· our integrated power systems solutions, with our focus shifting towards important developing technologies, including hybrid, hydrogen and electric power solutions.

We expect this revised approach to capital allocation to result in an overall reduction in R&D and capital expenditure from Â£1.9bn in 2019 to approximately Â£1.5bn in 2022. In the medium term, this investment strategy is expected to result in around 20% of capital and engineering expenditure directed towards our Power Systems business (compared to around 14% in 2017 to 2019), with around 20% focused on our Defence business (compared to around 9% in 2017 to 2019).

Positioning to benefit from new technologies, with a focus on sustainable power
We believe that the breadth of our engineering expertise and our established access to a range of end markets mean that we are well positioned to play a crucial role in the world's transition to a net-zero carbon economy. Once we achieve our aim of restoring financial returns and a more appropriate balance sheet, we intend to accelerate this aspect of our strategy to deliver substantial growth by 2025. In line with this strategy, we are building the capability to produce world-class, modular and scalable electric power and propulsion systems.

Due to the space and weight constraints of airborne applications, we are focusing our electrical efforts on smaller, sub-megawatt applications with faster routes to revenue, which will create new, disruptive business opportunities. For example, we have conducted a successful ground test of a hybrid M250 engine for the electric vertical take-off and landing ("EVTOL") market and have developed an all-electric aircraft through the ACCEL programme which is designed to break the world electric air speed record.

Simultaneously, we are working to enhance our megawatt scale capability, with a short-term focus on land and sea applications where markets are already electrifying. Our Power Systems business is already generating revenue in this area, with substantial growth expected by 2025. Through our Power Systems business, we were first-to-market with a hybrid system for the rail sector, are developing the first hybrid system in the yacht market and have developed a proven microgrid product offering. Longer term, we intend to leverage the expertise gained through these megawatt scale land and sea applications, and the domain expertise gained through certifying sub-megawatt scale airborne systems, in order to ready the technologies for the eventual electrification of larger regional aircraft in the 2030s.

For aircraft larger than regional jets, weight constraints pose a significant challenge to electrification. As a result, in addition to the electric power solutions described above, we are using our expertise in aviation to work with governments and industrial partners to explore the development of sustainable aviation fuels. Sustainable fuels offer a viable path to low carbon, long-haul travel and can be used with our existing gas turbine architecture. As the cost of sustainable fuels is expected to be higher than existing kerosene-based fuel, an efficient gas turbine architecture, such as our UltraFan programme, is expected to be critical to our airline customers in the future.

We are also exploring commercial applications for the production of low carbon power through development of small modular reactors ("SMRs"), which leverage our nuclear skills and knowledge from submarine applications. In 2019, we received initial match funding from the UK Government to progress this new type of compact smart nuclear power station. We believe that our expertise puts us in a favourable position in the SMR market.

FINANCIAL OUTLOOK

As outlined above, the COVID-19 pandemic has had, and continues to have, a significant effect on our business. Despite rapid actions to conserve cash, the impact of COVID-19 on EFHs and other aftermarket activity in the Civil Aerospace business, the decision to cease invoice discounting (Â£1.1bn at FY19), and a large working capital outflow due to lower activity levels together means that we anticipate a free cash outflow during 2020 of approximately Â£4bn (with underlying revenue of approximately 25-30% lower than 2019). The majority of this impact occurred in the first half of 2020, with a free cash outflow of Â£2.8bn. A reduced free cash outflow of approximately Â£1bn is expected in the second half of 2020, including as a result of a modest recovery in EFHs expected in the fourth quarter of 2020. In 2021 we expect a significantly reduced free cash outflow relative to 2020, as EFHs continue to recover and savings from our restructuring programme are realised, with positive cash flows targeted during the second half of 2021.

Over the long term we believe that the key markets for our businesses remain fundamentally attractive. In the Civil Aerospace business we expect aftermarket activity to gradually recover, with large engine EFHs reaching 2019 levels by 2024-2025, though remaining below the pre-COVID-19 pandemic trajectory. New widebody engine deliveries are expected to remain lower at around 250 per year in 2020-2022, but still to exceed retirements of 100 to 150 per year during the same period (excluding the one-off impact of retirements in 2020, particularly on older Trent 900 and Trent 500 fleets). In a "reasonable worst case" scenario we expect approximately 130 widebody engine deliveries in 2022. The widebody engine delivery outlook also drives a large portion of the ITP Aero business's expected demand, though we expect some growth in its non-widebody activities in narrowbody and business aviation. In the Power Systems business we anticipate a recovery in most key end markets by 2021, with particularly strong growth in mission critical power generation, and strong regional growth from China. The key markets for our Defence business, the US and UK, are expected to remain resilient.

Supported by this recovery of our end markets, as well as the decisive actions we have taken to significantly restructure the Group's cost base, we are targeting a return to annual FCF of at least Â£750m (excluding disposals) as early as 2022. This expected improvement of approximately Â£4.75bn in FCF performance from 2020 to 2022 (excluding disposals) is expected to be driven by four main factors:

Â· No repetition of one-off working capital outflows: comprising the approximately Â£1.1bn of one-off cessation of invoice-factoring and approximately Â£1bn expected working capital movement driven by lower activity levels described above.

Â· Recovery in our Civil Aerospace business: we expect widebody EFHs to decline by approximately 55% in 2020 compared to 2019, recovering to approximately 70% of 2019 levels in 2021 and approximately 90% of 2019 levels by 2022, before returning to GDP-driven growth. This anticipated recovery to approximately 90% of 2019 levels in 2022 is expected to drive more than Â£1.5bn of additional cash receipts (as compared to 2020), with further growth expected thereafter. Additionally, an FCF improvement of over Â£300m is expected to be driven predominantly by improved time and materials revenues and lower widebody OE losses. We also expect an ongoing reduction of Trent 1000 in-service costs of approximately Â£200m to Â£300m. In a "reasonable worst case" scenario, we expect widebody EFHs to recover to approximately 80% of 2019 levels by 2022.

Â· Operating cost reduction: the Group's restructuring is expected to deliver Group-wide pre-tax cash savings of at least Â£1.3bn per annum by the end of 2022 (including remaining savings of approximately Â£100m from the restructuring programme announced in 2018). This will replace and expand the expected Â£1bn of temporary cost saving measures implemented by the Group during 2020. The reorganisation is focused on reducing the fixed cost footprint in the Civil Aerospace business, with a significant reduction in headcount and facility footprint to match the new demand outlook. This lower fixed cost base supports a continued reduction in the average losses on widebody OE engines.

Â· Power Systems business recovery and Defence business resilience: improved performance in the Power Systems business and continued resilience in the Defence business, along with receipts from the ITP Aero business, is expected to drive approximately Â£200m of additional FCF compared to 2020. We expect this improvement in the Power Systems business to be driven by a cyclical recovery in key end markets as well as the Group's continued strategy to boost growth through a focus on power generation systems, aftermarket growth, and market-share gains in China.

The targeted return of FCF of at least Â£750m (excluding disposals) as early as 2022 includes the expected impact of temporary outflows in that year, including approximately Â£300m of foreign exchange cash costs relating to our decision to reduce the size of the Group's hedge book.

Having restored financial performance as early as 2022, we believe that thereafter the Group has an attractive medium-term outlook. We expect our target FCF of at least Â£750m (excluding disposals) described above to continue to grow in the future, as the temporary negative outflows relating to the reduction in the Group's hedge book and ongoing Trent 1000 costs unwind over time. This expected FCF growth after 2022 is expected to lead to continued deleveraging. In addition, our underlying businesses are expected to deliver growth. The Civil Aerospace business is expected to return to a growing installed base and we expect to deliver additional growth in FCF as we improve cash returns from the current installed base. Our Defence business is expected to continue delivering resilient performance, with important growth opportunities over time as major projects are awarded. The Power Systems business is expected to return to 2019 underlying revenue levels by 2022 and to deliver growth in excess of GDP given the tailwinds the business benefits from, including low carbon opportunities over time.

PRINCIPAL TERMS OF THE RIGHTS ISSUE

Overview
We are proposing to raise aggregate gross proceeds of approximately Â£2bn from the Rights Issue.

Pricing
The Rights Issue Price represents a 75.4% discount to the Closing Price of 130 pence per Existing Ordinary Share on 30 September 2020 and a 41.4% discount to the theoretical ex-rights price of 54.6 pence per Existing Ordinary Share based on that same Closing Price.

The Rights Issue Price has been set, following discussions with major Shareholders, at the level which the Board considers necessary to ensure the success of the Rights Issue, taking into account the aggregate proceeds to be raised. The Board believes that the Rights Issue Price, and the discount which it represents, is appropriate.

Dilution

The Rights Issue will result in up to 6,436,651,043 New Ordinary Shares being issued and the number of Ordinary Shares being increased from a total of 1,930,995,313 Ordinary Shares to a total of up to 8,367,646,356 Ordinary Shares, representing an increase of approximately 333%, assuming no Ordinary Shares are issued due to the vesting or exercise of any awards under the Share Plans or otherwise between the Latest Practicable Date and the completion of the Rights Issue.

If a Qualifying Shareholder does not (or is not permitted to) take up any New Ordinary Shares under the Rights Issue, such Shareholder's proportionate ownership and voting interests in the Company will be diluted by approximately 76.92% as a result of the Rights Issue, assuming that no Ordinary Shares are issued due to the vesting or exercise of any awards under the Share Plans or otherwise between the Latest Practicable Date and the completion of the Rights Issue.

Key terms

On and subject to, among other things, the terms and conditions described in Part VII (Terms and Conditions of the Rights Issue) of the Prospectus, up to 6,436,651,043 New Ordinary Shares will be offered by way of rights at the Rights Issue Price of 32 pence per New Ordinary Share to Qualifying Shareholders on the basis of:

10 New Ordinary Shares for every 3 Existing Ordinary Shares

held and registered in their name on the Record Date (and so in proportion for the number of Existing Ordinary Shares then held, subject to fractional entitlements).

Qualifying Non-CREST Shareholders with registered addresses in the United States or in any of the other Excluded Territories will not be sent Provisional Allotment Letters and will not have their CREST stock accounts credited with Nil Paid Rights, except where the Company and the Underwriters are satisfied that such action would not result in the contravention of any registration or other legal or regulatory requirement in such jurisdiction.

Entitlements to New Ordinary Shares under the Rights Issue will be rounded down to the nearest whole number and fractions of New Ordinary Shares will not be provisionally allotted to Qualifying Shareholders. Holdings of Existing Ordinary Shares in certificated and uncertificated form will be treated as separate holdings for the purpose of calculating entitlements under the Rights Issue.

The Rights Issue has been fully underwritten by the Underwriters in accordance with the terms and subject to the conditions of the Underwriting Agreement, details of which are set out in section 9.1 (Underwriting Agreement) of Part XII (Additional Information) of the Prospectus.

The Rights Issue is conditional upon (among other things): (i) the passing of the Ordinary Resolution at the General Meeting without material amendment; (ii) the Underwriting Agreement having become unconditional in all respects (save for the condition relating to Admission of Nil Paid Rights); and (iii) Admission of Nil Paid Rights becoming effective by not later than 8.00 a.m. on 28 October 2020 (or such later date as the Company and the Underwriters may agree).

Application will be made to the FCA for the New Ordinary Shares (nil and fully paid) to be admitted to listing on the premium listing segment of the Official List and to the London Stock Exchange for the New Ordinary Shares (nil and fully paid) to be admitted to trading on its main market for listed securities. It is expected that Admission of Nil Paid Rights will become effective, and that dealings in the New Ordinary Shares, nil paid, on the London Stock Exchange's main market for listed securities will commence, at 8:00 a.m. on 28 October 2020. It is also expected that Admission of the New Ordinary Shares (fully paid) will become effective, and dealings in New Ordinary Shares, fully paid, on the London Stock Exchange's main market for listed securities will commence, at 8:00 a.m. on 12 November 2020.

The New Ordinary Shares will, when issued and fully paid, rank pari passu in all respects with, and will carry the same voting and dividend rights as, the Existing Ordinary Shares.

Overseas Shareholders, including Shareholders resident in the United States, as well as holders of ADRs, should refer to section 7 (Overseas Shareholders) of Part VII (Terms and Conditions of the Rights Issue) of the Prospectus for further information regarding their ability to participate in the Rights Issue.