



ROLLS-ROYCE plc ANNUAL REPORT 1987

Rolls-Royce is one of the three major aero engine manufacturers in the western world able to produce a wide range of powerplants up to the highest thrusts for civil and military applications.

Founded in 1906, the Company's first aero engines flew in 1915, during World War I. Today, its products are in operation with more than 280 airlines, 110 armed forces and 700 executive and corporate operators. Over 185 industrial customers use its aero engine derivatives for power generation and gas and oil pumping, while the warships of 25 navies are also powered by Rolls-Royce gas turbines. In addition, Rolls-Royce and Associates, a subsidiary company, is responsible for the design, supply and support of nuclear steam raising plant for the Royal Navy's nuclear-powered submarine fleet.

In all, over 1,200 customers operate more than 27,000 Rolls-Royce gas turbines. The Group employs 42,000 people worldwide, of whom over 90 per cent work in the United Kingdom. The Parent Company, Rolls-Royce plc, is organised into three main business groups — Civil, Military and Industrial and Marine — supported by Corporate Engineering and Supply Groups.

COMPANY NUMBER

1005147

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GROUP FINANCIAL HIGHLIGHTS

for the year ended December 31, 1987

	1987 £m	1986 £m
Turnover	2,059	1,802
Operating profit	347	273
Research and development (net)	(187)	(132)
Profit before interest	160	141
Profit before taxation	156	120
Profit attributable to the shareholders	134	120
Shareholders' funds	855	507
Earnings per ordinary share—nil distribution basis	20.1p	18.9p
Dividends per ordinary share	5.25p	—
Average number of ordinary shares in issue	738m	635m
Average number of employees	42,000	41,900

FINANCIAL CALENDAR

Qualifying date for final dividend	April 29, 1988
Annual General Meeting	May 24, 1988
Payment of final dividend	June 6, 1988
Press advertisement of 1988 Interim Results	September 16, 1988
Qualifying date for interim dividend	October 21, 1988
Payment of interim dividend	December 5, 1988
Financial year end	December 31, 1988
Press advertisement of 1988 Preliminary Results	March 1989
1988 Annual Report published	April 1989

CHAIRMAN'S STATEMENT

In the year under review, we achieved a record turnover of £2,059 million, up 14.3 per cent on the 1986 figure. Whilst the civil aero sector produced most of the growth, military aero business also contributed, but industrial and marine activity declined, reflecting the somewhat depressed state of the market for gas turbines in those applications.

Operating profit increased from £273 million in 1986 to £347 million in 1987, a rise of 27 per cent; the margin on sales increased from 15.1 per cent to 16.9 per cent. Civil business showed a further improvement in profitability despite the very competitive environment and the significant weakening of the US dollar during the second half of 1987. In this latter respect, our hedging policy against foreign currency exposure helped considerably to cushion the adverse effects.

After charging net research and development expenditure of £187 million (1986 £132 million) and net interest payable of £4 million (1986 £21 million), profit on ordinary activities before taxation amounted to £156 million, an increase of 30 per cent over 1986. The increase of 42 per cent in the net charge for research and development (R&D) was the result of higher than anticipated costs on the V2500 and RB211-524 development programmes and the absence of launch aid on our civil engine programmes; in 1986 launch aid on the V2500, amounting to £27 million, was credited against R&D expenditure. The variable incidence of launch aid, coupled with our practice of charging R&D expenditure in the year in which it is incurred, puts considerable pressure on annual pre-tax profit performance. Nevertheless, expenditure on R&D is an essential investment for our future competitiveness and must remain a high priority.

New business has continued to be won at a steady rate, as a result of which the value of outstanding orders at the end of 1987 amounted to £2.8 billion. This represents a slight deterioration over the 1986 year-end figure, which was influenced by the large British Airways order for Boeing 747-400s placed in August 1986.

In March 1987, the RB211-524G (previously designated the -524D4D) was offered by Boeing for their B767 family of aircraft; in August British Airways became our first customer for the B767 by placing an order for 11 aircraft with -524H engines, a higher thrust version of the -524G.

1987 also saw the granting of certificates of airworthiness for applications of the Tay engine in the Gulfstream IV in April and in the Fokker 100 in November. Further thrust growth versions of the Tay are under consideration, both for re-engining and new aircraft applications.

Our large-fan civil engines continue to demonstrate the high standards of reliability which our customers have come to expect of us and which we intend to maintain. The RB211-535E4 has followed in the footsteps of its predecessor, the -535C, in its low engine removal rate, but equally remarkable was the recent completion by an RB211-22B engine in a TWA TriStar of 20,000 hours of service since new without removal from the wing—the equivalent of 10 million miles!

The collaborative V2500 engine for the Airbus A320 is now proceeding to programme despite some well-publicised technical problems in the second half of 1987. These have been overcome and engine certification is on target for June 1988, with entry into commercial service in the Spring of 1989. The decision by Lufthansa to opt for the competitor engine instead of the V2500 was a disappointment... but does not affect our resolve, together with our International Aero Engines partners, to press forward with the completion of the engine which we are convinced will be a very attractive one.

The Company's military programmes continued at much the same level as in 1986. Despite cuts in the United States defence budget, the AV8B (Pegasus) and T-45 (Adour) programmes have been little affected in 1988. We are hopeful of seeing more rapid progress by the four European nations in agreeing to the full launch of the European Fighter programme with the EJ200 engine. This programme is crucial to the long-term future of our military engine business.

The Company received the Queen's Award for Technological Achievement in April 1987 for its work on the wide-chord fan. This technology is the result of many years of patient engineering and manufacturing research and development, and gives significant performance improvements to our large-fan engines.

We enter 1988 with a sound balance sheet, with net cash funds of £137 million, and with bank facilities of £250 million (£150 million committed) arranged in March 1987 in the form of a Multi-Option Facility. However, the US-based competition remains strong, aided by the weak dollar, and new business will only be won with excellent products backed up by impeccable customer service. I am confident that we have both these attributes.

1987 was a year of particular significance since it saw the Company's successful return to the private sector after over 16 years of public ownership.

Whilst the flotation was a great success in that it attracted over 2,000,000 shareholders, the administrative task of the receiving banks and the registrar in handling the paperwork was enormous and resulted in an unacceptable number of documentation errors.

This was compounded by two other problems, neither of our own making; firstly the restriction imposed on the size of our overseas shareholding by the Government and secondly the Government's decision not to provide an instalment agreement under which an interim shareholders' register could have been established before the shares became fully paid. As a result, since the establishment of the register, the directors have had to enforce sales of excess foreign shareholdings in accordance with the Company's Articles of Association.

We regret the inconvenience which many shareholders suffered as a result of these problems, but at the same time extend a warm welcome to the many investors on our register. These include many employees and pensioners, from whom an excellent response was received to the various schemes in which they were able to participate; over 96 per cent of eligible employees were allotted shares at the time of the original offer, and in addition over 15,400 employees (41 per cent of those eligible) became members of the Sharesave Scheme.

As ever, our performance depends upon the loyalty and integrity of our workforce to whom I express my thanks on behalf of the Board. In particular, I would like to record our thanks to Mr F. T. Salt, a member of the Board, who retired on September 30, 1987, after 16 years of service to the Company.

The award of a Knighthood to our Managing Director, Ralph Robins, in the New Year's Honours List gave great pleasure to his colleagues, many of whom, like him, have spent all of their working lives with the Company and take great pride in its performance.

Prospects

The size of our order book, together with our wide range of engines and attractive market opportunities, gives confidence for continued progress in 1988 and a series of initiatives is under way to improve further the competitiveness of our products.

Francis Tombs

Sir Francis Tombs
March 24, 1988



GROUP FIVE YEAR REVIEW

for the years ended December 31

PROFIT AND LOSS ACCOUNT

	1987	1986	1985	1984	1983
	£m	£m	£m	£m	£m
Turnover	<u>2,059</u>	<u>1,802</u>	<u>1,601</u>	<u>1,409</u>	<u>1,331</u>
Operating profit	347	273	211	162	74
Research and development (net)	(187)	(132)	(100)	(101)	(131)
Share of losses in related companies	—	—	(1)	—	(2)
Net interest payable and similar charges	<u>(4)</u>	<u>(21)</u>	<u>(29)</u>	<u>(35)</u>	<u>(56)</u>
Profit (loss) before taxation	156	120	81	26	(115)
Taxation	<u>(21)</u>	<u>1</u>	<u>(3)</u>	<u>(6)</u>	<u>(6)</u>
Profit (loss) after taxation	135	121	78	20	(121)
Attributable to minority interests	(1)	(1)	(1)	(1)	(1)
Net restructuring costs	—	—	—	—	(74)
Profit (loss) attributable to the shareholders	134	120	77	19	(196)
Dividends	<u>(42)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
Retained profit for the year	<u>92</u>	<u>120</u>	<u>77</u>	<u>19</u>	<u>(196)</u>
Earnings per ordinary share	20.1p	18.9p	12.1p	3.0p	(19.2)p
Nil distribution basis	18.2p				
Net basis	5.25p				
Dividends per ordinary share					

BALANCE SHEET

	438	405	383	382	393
Fixed assets	<u>1,106</u>	<u>940</u>	<u>838</u>	<u>800</u>	<u>756</u>
Current assets	1,544	1,345	1,221	1,182	1,149
	<u>(685)</u>	<u>(833)</u>	<u>(828)</u>	<u>(867)</u>	<u>(855)</u>
Liabilities and provisions	859	512	393	315	294
	<u>160</u>	<u>127</u>	<u>127</u>	<u>308</u>	<u>508</u>
Share capital	695	380	262	(198)	(219)
Reserves	855	507	389	310	289
Shareholders' funds	4	5	4	5	5
Minority interests in subsidiaries	<u>859</u>	<u>512</u>	<u>393</u>	<u>315</u>	<u>294</u>

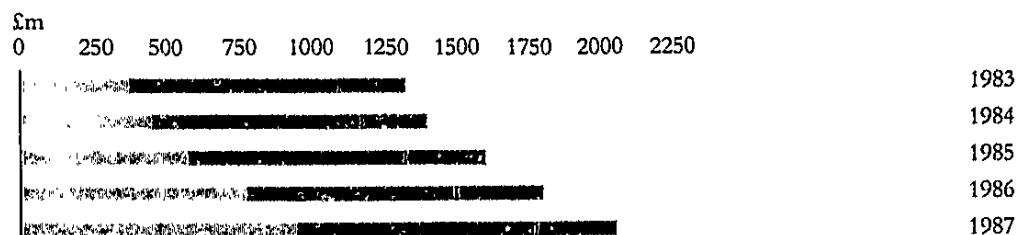
OTHER FINANCIAL INFORMATION

Research and development (gross)	294	255	234	227	262
Funds generated from operations	191	206	93	60	(108)

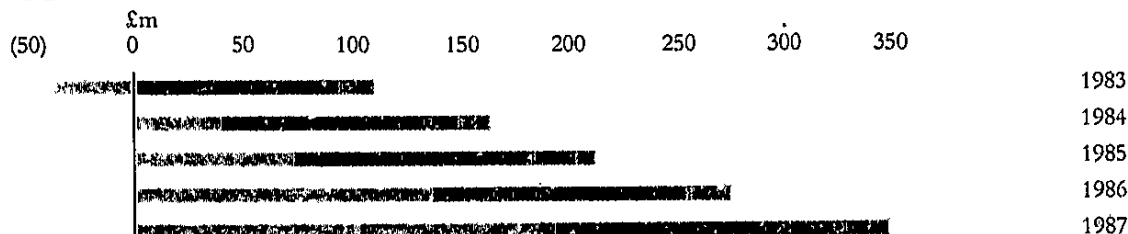
Prior years' earnings per share have been adjusted for the share consolidation and sub-division on April 27, 1987.

The 1983 to 1986 accounts have been restated in respect of overseas taxation for 1984 and earlier years.

Turnover

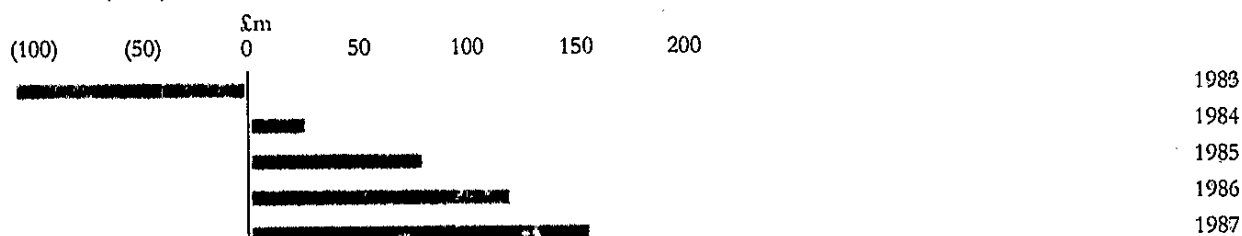


Operating profit (loss)

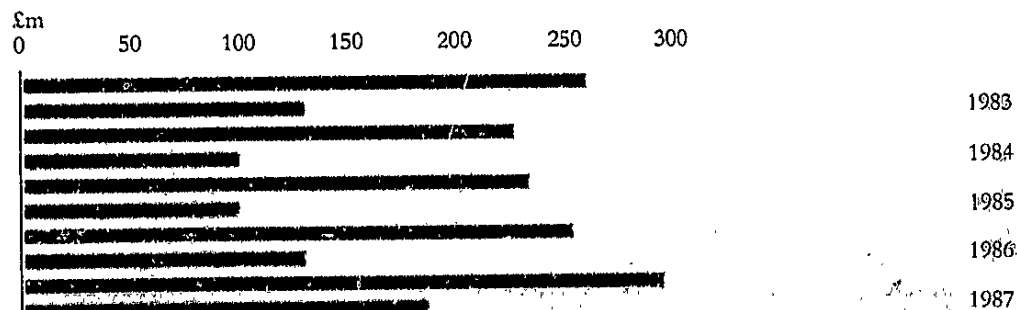


CIVIL AERO MILITARY AERO INDUSTRIAL AND MARINE OTHER ACTIVITIES

Profit (loss) before taxation



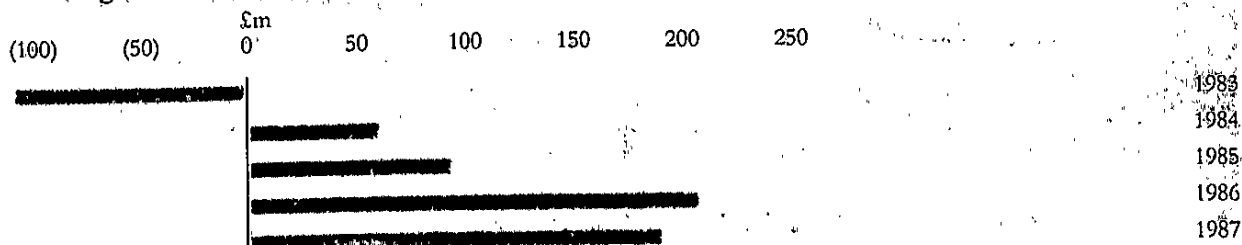
Research and development



GROSS

NET

Funds generated from operations



NET FUNDS OUTFLOW

NET FUNDS INFLOW

BOARD OF DIRECTORS

as at March 24, 1988

CHAIRMAN

Sir Francis Tombs, BSc (Econ), F Eng*

MANAGING DIRECTOR

Sir Ralph Robins, BSc (Eng), C Eng

EXECUTIVE DIRECTORS

J. O. Keir, C Eng, DIRECTOR, SUPPLY

S. C. Miller, BSc (Eng), F Eng, DIRECTOR, CORPORATE ENGINEERING

J. A. Rigg, CBE, FCA, DIRECTOR, FINANCE*

J. D. Wragg, BSc (Eng), C Eng, DIRECTOR, MILITARY ENGINES

NON-EXECUTIVE DIRECTORS

Sir Arnold Hall, FRS, MA, F Eng

Air Chief Marshal Sir Douglas Lowe, GCB, DFC, AFC, CRAeS

H. G. Mourgue, FCA*

Sir Robin Nicholson, FRS, F Eng

Sir Philip Shelbourne*

SECRETARY

A. Warrington, BSc (Econ)

*MEMBER OF THE AUDIT COMMITTEE



The Board of Rolls-Royce plc; (left to right): Front row: Sir Philip Shelbourne, Sir Francis Tombs, Sir Ralph Robins, Sir Arnold Hall. Middle row: Air Chief Marshal Sir Douglas Lowe, H. G. Mourgue, Sir Robin Nicholson. Back row: A. Warrington (Secretary), J. A. Rigg, J. D. Wragg, S. C. Miller, J. O. Keir.

REPORT OF THE DIRECTORS

The directors present their report together with the audited accounts for the year ended December 31, 1987.

Principal activities

The Company's principal business is the design, development, manufacture, sale and support of gas turbine engines and ancillary equipment for aircraft and for industrial and marine applications. Its subsidiary companies include Rolls-Royce and Associates Limited which designs, develops, procures and supports nuclear steam raising plant for naval purposes. Other subsidiary companies are mainly involved in the manufacture of aerospace and related products and in providing sales and service support of the Company's products overseas.

Results for the year

Profit before taxation was £156m (1986 £120m) and, subject to approval of the recommended final dividend, the retained profit for the year of £92m has been added to reserves. The directors recommend the payment of a final dividend of 3.5p per share which, with the interim dividend of 1.75p per share paid on December 7, 1987, will make a total dividend of 5.25p per share for the year. The final dividend, if approved, will be paid on June 6, 1988 to shareholders registered on April 29, 1988.

A review of the year's operations, research and development activities and future prospects is contained in the Chairman's Statement and in the Review of Activities.

Subsidiary and related companies

During the year the Company increased its holding of shares in its subsidiary company, Rolls-Royce and Associates Limited, and also acquired a 50 per cent interest in a newly formed Australian company, Turbine Components Australia Pty. Limited.

Employment

The number of Group employees at the end of the year was 41,600 (1986 42,000).

The Company's policy continues to be to provide, wherever possible, employment opportunities for disabled people, to care for employees who become disabled and to make the best possible use of their skills and potential. It operates an equal opportunity policy.

In 1987 industrial accidents remained at a level well below the average for similar UK manufacturing companies. Rolls-Royce has a continuing programme to assess potential health hazards; this is supported where necessary by environmental measurement. Workforce involvement in health and safety issues is encouraged through safety representatives and the Safety Committee structure.

Cost-effective training has high priority. During 1987 the Company was engaged in many education and training initiatives and the current total of full-time trainees is 1,400, including 220 people in two-year YTS programmes. Over 12,000 employees attended further education and training programmes and 500 school, college and university leavers joined Rolls-Royce as trainees. Schools liaison activity was increased, aimed at improving the Company's recruitment position ahead of the anticipated decline in the number of school leavers over the next few years.

Across the Company there exist various forms of communication, each adapted to the particular needs of individual sites. The Company continues its commitment to consultation with employees and their trade union representatives on a comprehensive range of topics related to its overall business objectives. Joint meetings of management and employee representatives are held regularly at every site to discuss problems and opportunities. In 1987 Rolls-Royce again held a central forum, attended by the most senior members of management and representatives of Staff and Works unions from all sites.

REPORT OF THE DIRECTORS

Directors

The directors listed on page 6 were in office throughout 1987.

Mr F. T. Salt resigned from the Board on September 30, 1987, having reached retirement age for executive directors, and Sir Arnold Hall will retire at the Annual General Meeting on May 24, 1988.

Dr G. R. Higginson (age 58) has been appointed to the Board with effect from April 1, 1988. He is Vice-Chancellor of the University of Southampton.

The beneficial, including family, interests in the share capital of the Company of the persons who were directors on December 31, 1987 were as follows:

	Beneficial holdings of ordinary shares	Options under the Rolls-Royce Executive Share Option Scheme
Sir Francis Tombs	21,811	146,300
Sir Arnold Hall	4,750	—
Mr J. O. Keir	1,510	79,200
Sir Douglas Lowe	4,000	—
Mr S. C. Miller	1,518	95,100
Mr H. G. Mourgue	4,750	—
Sir Robin Nicholson	4,750	—
Mr J. A. Rigg	6,045	136,500
Sir Ralph Robins	6,041	253,600
Sir Philip Shelbourne	4,750	—
Mr J. D. Wragg	1,521	146,300

Except for a purchase of 15,000 shares by Sir Francis Tombs in December 1987, all the beneficial holdings were in respect of shares purchased in May 1987. The options were granted in June 1987. There has been no change in the interests set out above between December 31, 1987 and March 24, 1988.

The Board is not aware of any contract of significance in relation to the Company or its subsidiaries in which a director has, or has had, a material interest.

The directors retiring by rotation at the Annual General Meeting, in accordance with Article 79 of the Company's Articles of Association, are Mr S. C. Miller, Mr H. G. Mourgue, Sir Robin Nicholson and Sir Philip Shelbourne who, being eligible, offer themselves for re-election. Dr G. R. Higginson retires in accordance with Article 84 and, being eligible, offers himself for re-election.

Mr S. C. Miller (age 53), appointed Director, Corporate Engineering in 1985, has a service agreement terminable by the Company upon not less than 24 months' notice. He joined the Company in 1954.

The non-executive directors at the date of this report are:

Sir Arnold Hall, (age 72). Appointed 1983, he was Chairman of Hawker Siddeley Group PLC from 1967 to 1986.

Air Chief Marshal Sir Douglas Lowe, (age 66). Appointed 1984, he was Controller—Aircraft and Chief of Defence Procurement with the Ministry of Defence.

Mr H. G. Mourgue, (age 60). Appointed 1985, he is a director of Thames Television PLC and T&N PLC; he was formerly Vice-Chairman of Thorn EMI plc and Chairman of INMOS International plc.

Sir Robin Nicholson, (age 53). Appointed 1986, he is an executive director of Pilkington Brothers plc and had been Chief Scientific Adviser in the Cabinet Office.

Sir Philip Shelbourne, (age 63). Appointed 1986, he is Chairman of Britoil plc and Chairman designate of Henry Ansbacher Holdings PLC.

Fixed assets

Expenditure on fixed assets during the year amounted to £82m (1986 £81m), mainly in respect of gas turbine manufacturing and engineering facilities and supporting computer equipment.

The professional valuation of the Company's land and buildings at December 31, 1985 has been updated to the end of 1987 and suggests a value marginally greater than the figure shown in the accounts.

Share capital

On May 20, 1987 the Company allotted 166,470,588 ordinary shares of 20p each (aggregate nominal value £33,294,118) at £1.70p each and one special rights redeemable preference share of £1 at £1 to a nominee of the Secretary of State for Trade and Industry. The major proportion of the proceeds was used to repay most of the Company's borrowings.

On the same date the Secretary of State sold his holding of 801,470,588 ordinary shares of 20p each, being the total issued and allotted ordinary share capital at that date. He retained the one special share.

Consequently after 16 years of ownership by HM Government, the Company, with its internationally famous trademarks—including the Rolls-Royce name and the distinctive RR symbols—was successfully returned to the private sector. Rolls-Royce Motor Cars Limited, a subsidiary of Vickers PLC, continues, under licence from the Company, to use the name and symbols on certain of its products.

Details of employee share schemes are given in note 23 to the accounts.

At the Annual General Meeting a resolution will be proposed to give the directors authority, for a limited period, to allot shares for cash both by way of rights issues and, in respect of a limited number of ordinary shares (40,073,525 representing 5 per cent of the issued share capital), to people other than existing ordinary shareholders. The directors recommend the resolution to shareholders in order to provide flexibility to finance business opportunities as they arise.

At March 24, 1988 no person had notified the Company of an interest of 5 per cent or more in the issued share capital of the Company.

Close company status

The close company provisions of the Income and Corporation Taxes Act 1970 do not apply to the Company.

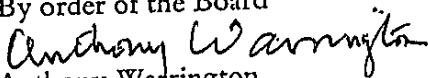
Donations

Charitable donations amounted to £54,600 (1986 £45,300). A political contribution of £50,000 (1986 Nil) was made to the Conservative and Unionist Party.

Auditors

A resolution to re-appoint the auditors, Coopers & Lybrand, and to authorise the directors to approve their remuneration will be proposed at the Annual General Meeting.

By order of the Board


Anthony Warrington

Secretary

March 24, 1988

REVIEW OF ACTIVITIES

Although most of its personnel and facilities are in the United Kingdom, Rolls-Royce co-operates with companies in 16 countries on gas turbine development and manufacture. It has business in many countries and in recent years, more than 70 per cent of turnover has been generated outside the UK. Extensive customer support is provided by a worldwide network of over 250 representatives together with several overseas operating subsidiaries.

Civil Engines

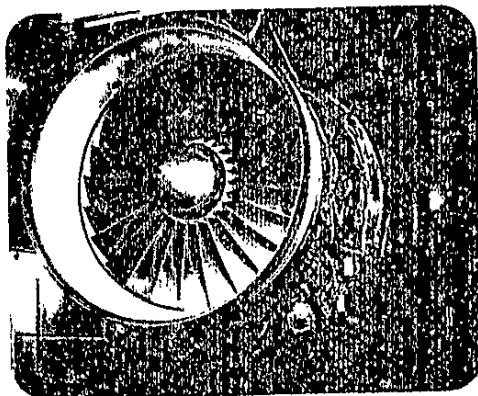
The RB211 family continued to accumulate significant business during 1987, and in July the Australian airline Qantas ordered the 58,000 lb thrust RB211-524G for its long-range Boeing 747-400 airliners. This engine, previously known as the -524D4D, is on schedule for certification in March 1988. It has already been ordered by Cathay Pacific and British Airways.

In August, the RB211 was launched into the widebodied twinjet market when British Airways chose a high-thrust version for 11 Boeing 767-300 airliners. Deliveries of this engine, the RB211-524H rated at 60,600 lb thrust, begin in November 1989. The availability of the RB211 to power Boeing 767s will widen the market for the engine, particularly among airlines which seek a common engine type for their Boeing 747 and 767 fleets.

Orders for the RB211-535 series increased in 1987 and over 75 per cent of the customers for the Boeing 757 airliner have selected Rolls-Royce engines. Since March 1986, the -535E4 has been successful in all 11 engine evaluations by new customers for this airplane. These powerplants have logged over a million hours of operating experience and their reliability is outstanding. Many Boeing 757s are flown intensively — up to 19 hours a day.

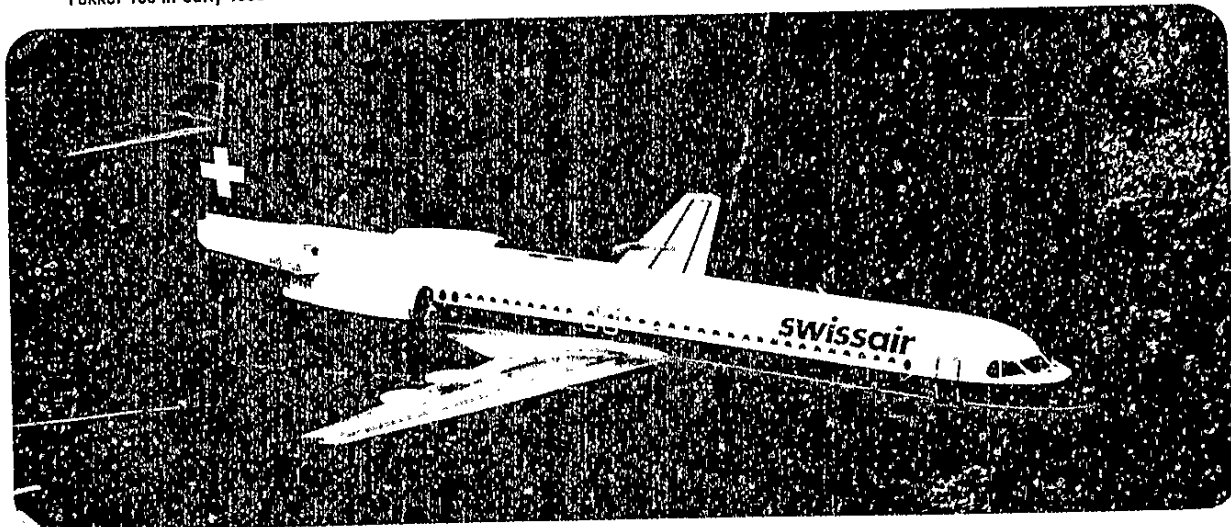
The latest version of the RB211 now planned (the -524L) would provide growth to more than 70,000 lb of thrust. It would then be over 65 per cent more powerful and 20 per cent more fuel efficient than the original RB211 which entered service 16 years ago.

Good progress was made with the new Tay engine. The Gulfstream IV business jet entered service in July and Swissair took delivery of its first Fokker 100 airliner on February 29, 1988. Orders for Tay engines now stand at 580



The new RB211-524G engine will power long-range Boeing 747-400 airliners

Swissair took delivery of the Tay-powered Fokker 100 in early 1988

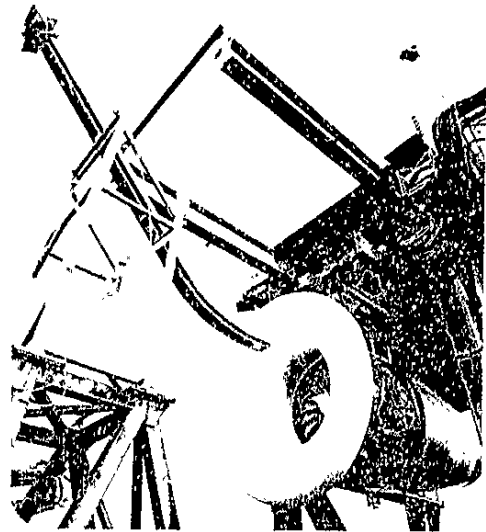


with nearly 200 delivered. Development of the higher-thrust Tay 650 is on schedule for certification in August 1988. Further growth versions are being studied.

The RB211 and Tay engines exemplify the performance improvement and outstanding reliability which can be achieved by Rolls-Royce's derivative approach to engine development — to the direct benefit of the customer by reducing overall cost of ownership.

The development of the five-nation V2500 engine for the Airbus A320 airliner continued during 1987. By the end of the year the programme was moving towards the scheduled certification date of June 1988 with 40 of the 77 tests required by the airworthiness authorities either completed or underway.

Major milestones included the successful first run to certification standard and a 1,000-cycle endurance test, carried out at high operating temperatures and thrusts well above the design take-off thrust of 25,000 lb, and delivery of the first engines to Airbus in February 1988. This advanced engine has been ordered in quantity to power A320 airliners and will enter service in the Spring of 1989.



Rig for ice-ingestion testing of the five-nation V2500 engine

Deliveries of Rolls-Royce powered Boeing 767s will begin in late 1989



REVIEW OF ACTIVITIES

Military Engines

Production of the three-nation Turbo-Union RB199 for Tornado aircraft continued throughout 1987. The latest RB199s in service have turbine blades of single-crystal alloy and advanced digital fuel control units. Performance benefits of the RB199 for agile new fighters were comprehensively displayed during the flight testing of the British Aerospace Experimental Aircraft Programme (EAP) demonstrator.

The four-nation Eurojet company has reached agreement on the design and specification of the EJ200 engine for the proposed new European Fighter Aircraft (EFA). The engine programme and workshare arrangements for development were also agreed between Rolls-Royce and its Eurojet partners.



The Adour-powered T-45A Goshawk will be used for training US Navy pilots

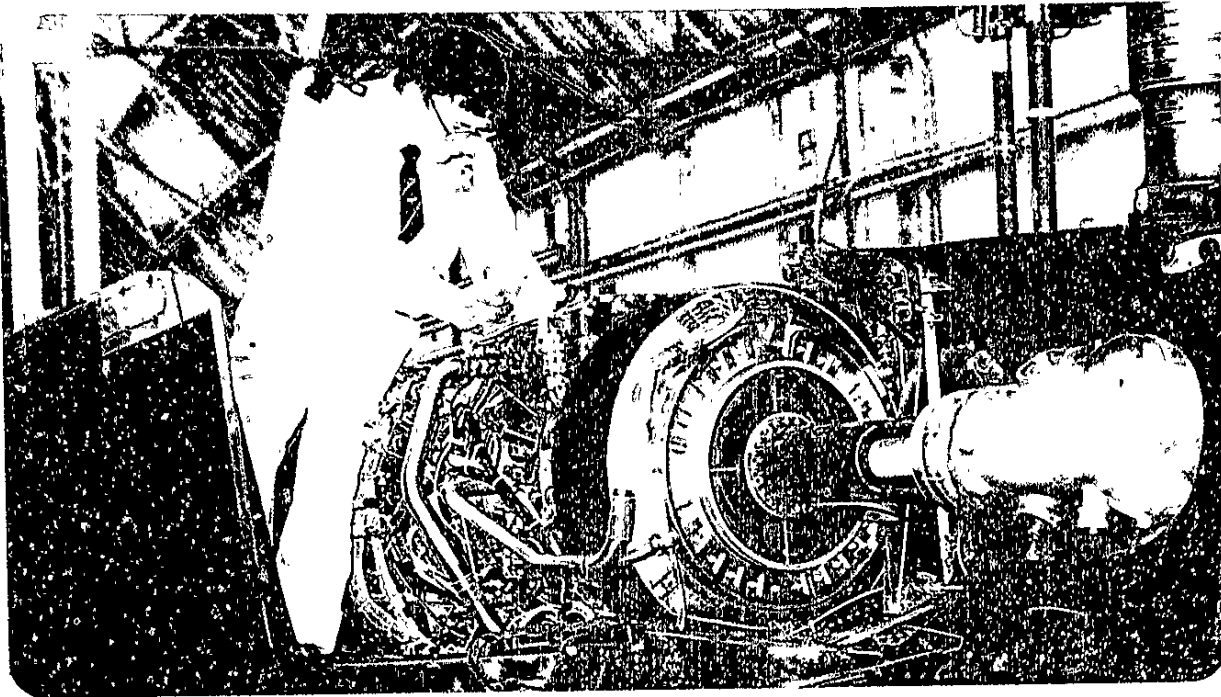
RB199-powered Tornados in the camouflage marking of the Royal Saudi Air Force

During the year 104 Pegasus vectored-thrust engines were delivered for V/STOL Harrier aircraft. The engine has now completed over 600,000 hours in service. In 1987 the United States Marine Corps was joined by the Royal Air Force and the Spanish Navy in procuring the advanced AV-8B Harrier II, powered by the latest production Pegasus. First deliveries of this engine were also made for Royal Navy Sea Harriers.

In July the US Navy placed an initial contract for the Pegasus 11-61 engine which will enhance Harrier V/STOL and combat performance. This thrust-growth engine is being developed for initial production deliveries in 1990.

Production of the Rolls-Royce Turbomeca Adour engine continued in 1987, with the first Adour-powered Hawks being delivered to the Royal Saudi Air Force. The Swiss Government also announced the purchase of 20 Hawks. Adour development is on schedule for the US Navy T-45A Goshawk and other Hawk variants; initial production orders have been placed. Engineering work is in hand to sustain the Adour's competitiveness into the 21st century.



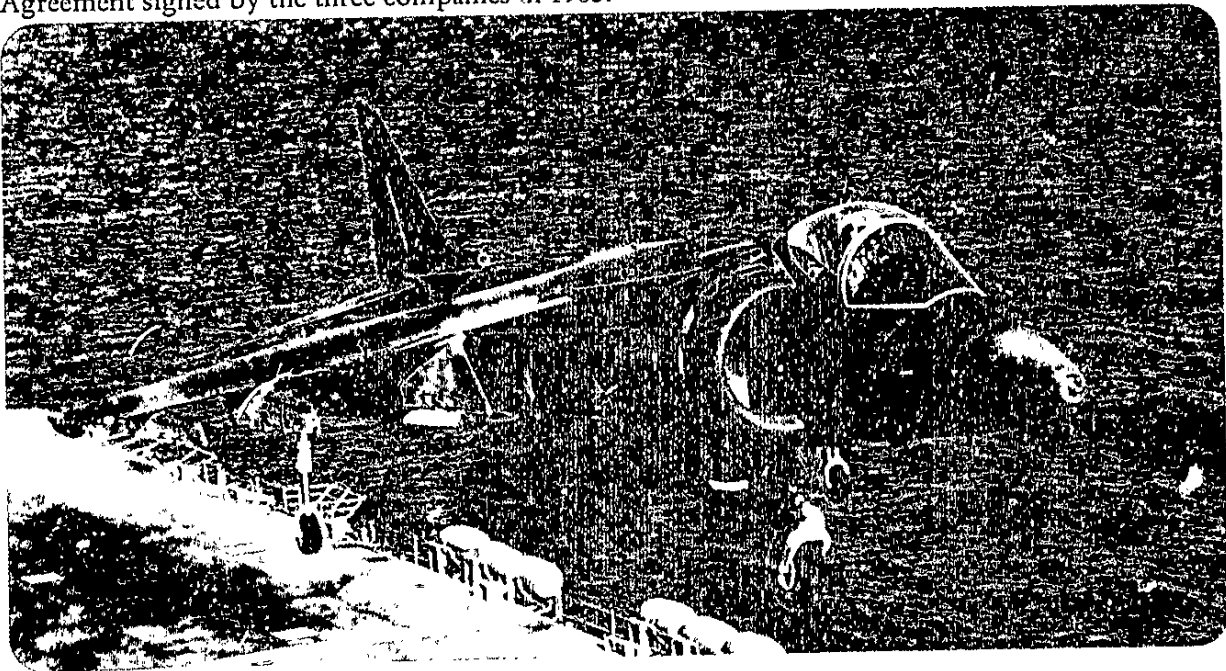


The Rolls-Royce Turbomeca RTM322 turboshaft completed an intensive flight evaluation by the US Navy in a Seahawk helicopter during 1987. Immediate RTM322 marketing activity is focused on the UK Government for its purchase of the EH101 helicopter; Canada, also for the EH101; and the US Army and Navy for Blackhawk and Seahawk.

Installing an RTM322 turboshaft in the Sikorsky S-70 helicopter used for engine flight demonstration

During the year Rolls-Royce joined Turbomeca and MTU to develop the new 1,300 shp MTM390 turboshaft engine for helicopters. It is initially aimed at a new Franco-German anti-tank helicopter and is also suitable for other military and civil applications. Involvement in the MTM390 further develops the European Small Engine Agreement signed by the three companies in 1985.

Pegasus-powered AV-8B in service with the US Marine Corps



REVIEW OF ACTIVITIES

Industrial and Marine

During 1987 the sale of the 100th industrial RB211 was achieved and this engine type also passed one million operating hours since entering service in 1974. It is used in land-based and off-shore installations, mainly by the oil and gas industry.

The SM1C marine Spey, which produces 40 per cent more power than its predecessor, first ran in August and full power was demonstrated on the second day of test running. This engine incorporates technology from the Company's latest aero engines.

Engineering Research and Development

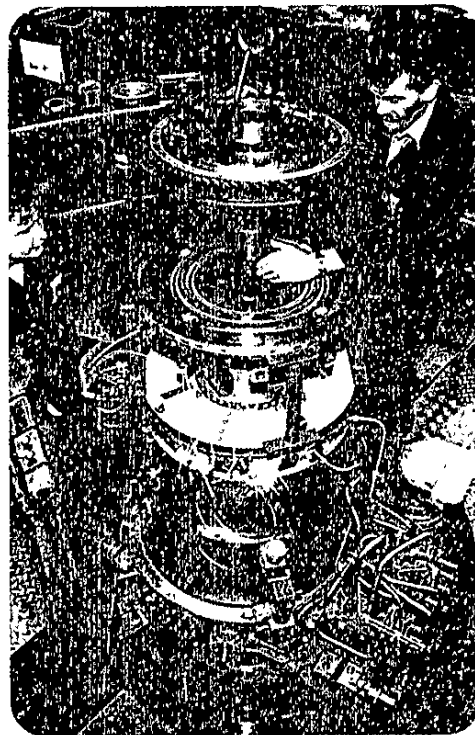
Steady progress was made in research, technology and design programmes to ensure that the Company's products continue to be fully competitive in the future.

This work provides the technical advances for existing engines to be developed to their fullest potential — and for new designs to begin their life based on the latest proven technology.

The first XG40 demonstrator engine was tested successfully early in the year. It is proving the propulsion advances planned for Europe's new fighter aircraft (EFA) before the EJ200 engine is designed in detail. The XG40, a reheated two-shaft turbofan demonstrator in the 20,000 lb thrust class, is jointly funded by Rolls-Royce and the Ministry of Defence. It is aimed at a thrust-to-weight ratio of 10 to 1 and low life-cycle costs. The engine's advanced reheat system was run to its maximum thrust target in mid-1987.

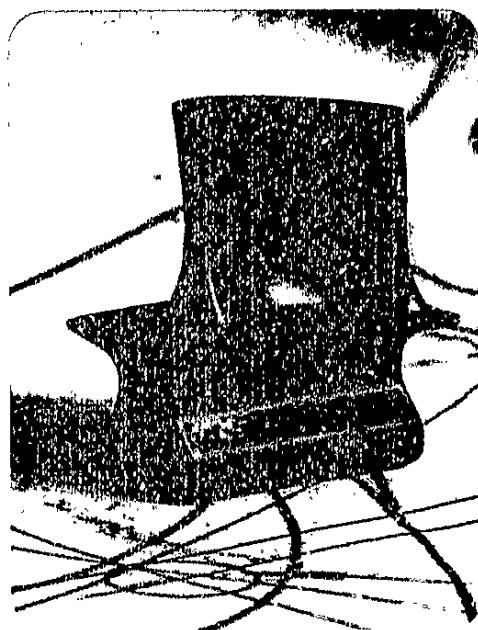
Studies to widen the market for RB211 engines concentrated on the -524L version. With an initial thrust of 65,000 lb and growth to over 70,000 lb, this proposed engine is aimed at the McDonnell Douglas MD11, Airbus A330 and larger versions of the Boeing 767. Preliminary design is nearing completion with certification targeted for 1992; the engine is aimed at availability for airline service in 1993. The -524L has a larger fan than previous RB211s. Its higher-performance core could be retrofitted to earlier RB211-524 engines to further improve their performance.

Work accelerated in 1987 on a programme covering ceramics which can operate at very high temperatures and new high-strength low-density composite materials. These will be needed to provide the performance advances required in engines over the next 20 years and beyond.



The latest marine Spey gives 40 per cent more power than the previous version

Research is continuing into the use of ceramic blades which can operate at very high temperatures



Manufacturing

A new manufacturing system unique to Rolls-Royce was installed at Hillington which further enhances the Company's competitiveness in the manufacture of variable compressor vane parts. The system consists of a computer-controlled machining centre for milling and turning linked with automatic loading of parts, tool changing and handling equipment. Two more machining centres will complete a £2.3 million investment in this system. It will be used initially to produce variable guide vanes for the V2500 engine.

A manufacturing cell to machine light-alloy castings entered service at Coventry during the year. New computer-controlled machines have been linked with existing equipment to create a very efficient production system.

Another fully automated manufacturing cell was installed at Bristol to produce moulds for shell investment castings. It forms part of an integrated manufacturing system which will produce nozzle guide vane components for the Company's engines.

Nuclear

During the year Rolls-Royce and Associates commissioned the prototype of the advanced nuclear plant for the next generation of Royal Navy nuclear submarines.

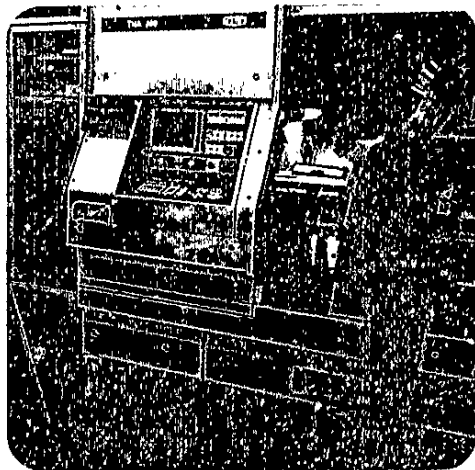
An existing reactor was also decommissioned and converted into a test facility to study loss-of-coolant incidents in pressurised water reactors.

As part of its planned diversification the company won a major CEBG contract to inspect the reactor pressure vessel at the Sizewell B nuclear power station. This contract, gained against tough competition, establishes Rolls-Royce and Associates in the civil nuclear programme.

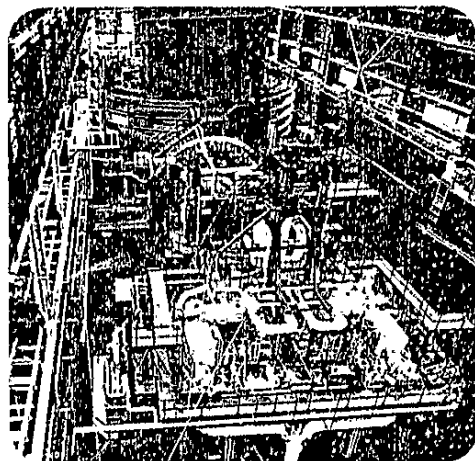
Repair Business

The Company continued to win new repair business during 1987 and consolidated the organisation of its repair and overhaul activities to increase responsiveness to customer needs.

In August, an advanced new facility was installed at East Kilbride to repair nozzle guide vanes. This, together with selected investments throughout the Company's seven repair centres, resulted in faster turn-round times and lower costs. Facilities to support the Tay have now been established at East Kilbride (where the engine was developed) and Montreal, to meet the needs of the growing number of Gulfstream IV operators and airlines who have selected the Fokker 100.

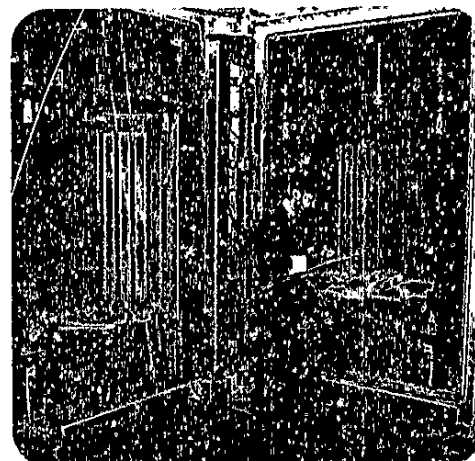


New computer-controlled manufacturing system at Hillington for production of V2500 variable guide vanes



Test facility for Rolls-Royce and Associates' latest design of pressurised water reactor for future Royal Navy nuclear submarines

East Kilbride's advanced new nozzle guide vane repair facility



GROUP PROFIT AND LOSS ACCOUNT

for the year ended December 31, 1987

		1987	1986
	Notes	£m	£m
Turnover	2	2,059	1,802
Cost of sales		(1,528)	(1,369)
		<u>531</u>	<u>433</u>
Gross profit		(89)	(82)
Commercial, marketing and product support costs		(95)	(78)
General and administrative costs	2	<u>347</u>	<u>273</u>
Operating profit		(187)	(132)
Research and development (net)	3	<u>(4)</u>	<u>(21)</u>
Net interest payable	4	156	120
Profit on ordinary activities before taxation	7	<u>(21)</u>	<u>1</u>
Taxation		135	121
Profit on ordinary activities after taxation		<u>(1)</u>	<u>(1)</u>
Attributable to minority interests in subsidiaries		134	120
Profit attributable to the shareholders of Rolls-Royce plc	8	<u>(42)</u>	<u>—</u>
Dividends	27	<u>92</u>	<u>120</u>
Retained profit for the year			
	9		
Earnings per ordinary share		20.1p	18.9p
Nil distribution basis		18.2p	
Net basis			

The notes on pages 19 to 32 form part of these accounts

BALANCE SHEETS

at December 31, 1987

		Group		Company	
	Notes	1987 £m	1986 £m	1987 £m	1986 £m
Fixed assets					
Tangible assets					
Investments:	10	438	405	374	334
Shares in group companies	13	—	—	25	23
Shares in related companies	14	—	—	—	—
		<u>438</u>	<u>405</u>	<u>399</u>	<u>357</u>
Current assets					
Stocks	15	623	604	585	556
Debtors	16	329	315	637	615
Cash at bank and in hand		<u>154</u>	<u>21</u>	<u>130</u>	<u>1</u>
		<u>1,106</u>	<u>940</u>	<u>1,352</u>	<u>1,172</u>
Creditors – amounts falling due within one year					
Bank loans, overdrafts and other borrowings	17	(8)	(171)	—	(128)
Other creditors	18	(443)	(367)	(476)	(425)
Net current assets		<u>655</u>	<u>402</u>	<u>876</u>	<u>619</u>
Total assets less current liabilities		<u>1,093</u>	<u>807</u>	<u>1,275</u>	<u>976</u>
Creditors – amounts falling due after one year					
Bank loans and other borrowings	19	(9)	(79)	(1)	(66)
Other creditors	20	(118)	(103)	(387)	(359)
Provisions for liabilities and charges					
Deferred taxation	21	(1)	(1)	—	—
Other provisions	22	(106)	(112)	(91)	(97)
		<u>859</u>	<u>512</u>	<u>796</u>	<u>454</u>
Capital and reserves					
Called up share capital	23	160	127	160	127
Share premium account	24	241	—	241	—
Revaluation reserve	25	141	145	136	139
Other reserves	26	10	9	9	9
Profit and loss account	27	<u>303</u>	<u>226</u>	<u>250</u>	<u>179</u>
Shareholders' funds		<u>855</u>	<u>507</u>	<u>796</u>	<u>454</u>
Minority interests in subsidiaries		<u>4</u>	<u>5</u>	<u>—</u>	<u>—</u>
		<u>859</u>	<u>512</u>	<u>796</u>	<u>454</u>

Francis Tombs
J. A. Rigg

} Directors

Francis Tombs

March 24, 1988

J. A. Rigg

The notes on pages 19 to 32 form part of these accounts

GROUP STATEMENT OF SOURCE AND APPLICATION OF FUNDS
for the year ended December 31, 1987

	1987 £m	1986 £m
Source of funds		
Profit on ordinary activities before taxation	156	120
Adjustments for items not involving the movement of funds:		
Depreciation of tangible fixed assets	41	56
(Decrease) increase in other provisions for liabilities and charges	(6)	30
	<u>191</u>	<u>206</u>
Funds generated from operations		
Issue of shares for cash, less issue expenses	274	—
Exchange adjustments	(12)	(2)
Disposals of tangible fixed assets	2	3
Increase (decrease) in creditors falling due after one year	15	(15)
	<u>470</u>	<u>192</u>
Application of funds		
Capital expenditure	(82)	(81)
Taxation paid	(6)	—
Dividend paid	(14)	—
Miscellaneous items	(2)	—
	<u>366</u>	<u>111</u>
Changes in net current assets		
Increase (decrease) in current creditors excluding corporate taxation and proposed dividend	33	(14)
(Increase) in stocks, net of progress payments	(19)	(26)
(Increase) in debtors	(14)	(91)
	<u>366</u>	<u>(20)</u>
Changes in net liquid assets and loans		
Represented by:		
Increase (decrease) in cash balances	133	(12)
Decrease (increase) in bank loans, overdrafts and other borrowings:		
Amounts falling due within one year	163	9
Amounts falling due after one year	70	(17)
	<u>366</u>	<u>(20)</u>

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES

Basis of accounting

The accounts have been prepared on the historical cost basis, modified to include the revaluation of land and buildings at December 31, 1985.

Basis of consolidation

The Group accounts include the accounts of the Company and all of its subsidiaries made up to December 31.

The Group's share of the results of related companies up to December 31 is included in the Group accounts on the basis of either audited accounts or, where these are not available, unaudited management accounts.

Any provisions for diminution in value of the Company's investment in subsidiary or related companies are made in the Company's profit and loss account.

As permitted by the Companies Act 1985, a separate profit and loss account for the Company has not been included in these accounts.

Turnover and trading profit

Turnover excludes value added tax and comprises:

- (i) Amounts invoiced to customers in respect of deliveries made, work completed or services rendered during the year.
- (ii) Estimated sales values, where prices have not been agreed with customers.
- (iii) Income from licences and management fees.

Trading profit is taken at the time of sale; in the case of long-term contracts, profit is arrived at by reference to the estimated overall contract profitability.

Foreign currencies

Company accounts

- (i) Transactions in currencies other than sterling are translated at the average achieved exchange rate for the year, taking account of maturing forward exchange contracts.
- (ii) Assets and liabilities in foreign currencies are translated into sterling on the following bases:
 - (a) Intra-group balances at the exchange rates ruling at the year end.
 - (b) Other assets and liabilities at the estimated sterling equivalent, taking account of future forward exchange contracts.
- (iii) Differences on exchange are charged or credited in determining profit on ordinary activities before taxation.

Group accounts

- (i) Assets and liabilities of overseas subsidiary and related companies are translated into sterling at the exchange rates ruling at the year end.
- (ii) The trading results of overseas subsidiary and related companies are translated at the average exchange rates for the year.
- (iii) On consolidation, differences on exchange arising from the retranslation of the opening net investment in overseas subsidiary and related companies, and from the translation of the profits or losses of those companies at average rate, are taken to reserves.

Research and development

The charge to the profit and loss account consists of total research and development expenditure incurred in the year less costs recoverable on contracts, contributions by Her Majesty's Government (HMG) to shared engineering programmes and any launch aid received from HMG under the provisions of the 1982 Civil Aviation Act.

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES (CONTINUED)

Taxation

Provision is made at the rate for the year for United Kingdom corporation tax, for overseas taxation on profits of overseas subsidiaries and for deferred taxation on all timing differences where a liability is expected to arise in the foreseeable future. Advance corporation tax which is not recoverable in the immediate future by offset against United Kingdom corporation tax liabilities is included in the taxation charge for the year.

Stocks

Stocks are valued at cost of materials, labour and relevant manufacturing overheads, less provisions for obsolete and surplus items and, where necessary, provisions to reduce cost to estimated realisable value. Progress payments received are deducted from stocks up to the limit of the relevant work in progress. Other advance payments and deposits are included in creditors.

Accounting for leases

Assets financed by leasing agreements which give rights approximating to ownership (finance leases) have been capitalised at amounts equal to the original cost of the assets to the lessors and depreciation provided on the basis of Group depreciation policy. The capital elements of future obligations under finance leases are included as liabilities in the balance sheet and the current year's interest element is charged to the profit and loss account. The annual payments under all other lease arrangements, known as operating leases, are charged to the profit and loss account as incurred. Rentals receivable as lessor under operating leases are included in turnover for the year on an accruals basis.

Depreciation

(i) Properties

Depreciation is provided on the valuation of properties adopted at December 31, 1985 and on the original cost of purchases since 1985 and is calculated on the straight line basis over estimated lives advised by the Group's professional valuers. Depreciation is not provided on freehold land. The estimated lives are:

- (a) Freehold buildings—10 to 45 years (average 28 years).
- (b) Leasehold land and buildings—lower of valuers' estimates or period of lease.

(ii) Plant and equipment

In accordance with the requirements of the 1987 revision of Statement of Standard Accounting Practice No. 12, a review of the useful economic lives of the Group's plant and equipment has been completed. This review indicated the need for the following change, implemented with effect from January 1, 1987:

Depreciation is provided on the original cost of plant and equipment and is calculated on the straight line basis over estimated lives in the range 5 to 25 years (1986 5 to 14 years).

Book values of plant and equipment at December 31, 1986, including those for assets which were fully depreciated at that date, have not been restated; these values are being written off over the revised remaining lives of the assets concerned.

The effect of implementing the 1987 revision of Statement of Standard Accounting Practice No. 12 has been to increase profit before taxation by £10m.

2. TURNOVER AND OPERATING PROFIT

	1987				1986			
	United Kingdom		Overseas		United Kingdom		Overseas	
	£m	£m	£m	%	£m	£m	£m	%
Turnover								
Civil Aero	153	800	953	46	130	627	757	42
Military Aero	228	592	820	40	220	520	740	41
Industrial and Marine	44	92	136	7	58	95	153	9
Other activities	<u>118</u>	<u>32</u>	<u>150</u>	<u>7</u>	<u>119</u>	<u>33</u>	<u>152</u>	<u>8</u>
	<u>543</u>	<u>1,516</u>	<u>2,059</u>		<u>527</u>	<u>1,275</u>	<u>1,802</u>	
	<u>26%</u>	<u>74%</u>		<u>100</u>	<u>29%</u>	<u>71%</u>		<u>100</u>

Geographical analysis by market:

North America	733	497
Europe	409	397
Asia	286	291
Australasia	29	44
Africa	21	19
Other countries	<u>38</u>	<u>27</u>
	<u>1,516</u>	<u>1,275</u>

Exports from the United Kingdom:

Direct	1,148	918
Indirect	<u>286</u>	<u>271</u>
	<u>1,434</u>	<u>1,189</u>
Sales by overseas subsidiaries	145	165
Company sales to overseas subsidiaries	<u>(63)</u>	<u>(79)</u>
	<u>1,516</u>	<u>1,275</u>

	1987		1986	
	£m	% on Turnover	£m	% on Turnover
Operating profit				
Civil Aero	194	20	137	18
Military Aero	133	16	118	16
Industrial and Marine	11	8	10	7
Other activities	<u>9</u>	<u>6</u>	<u>8</u>	<u>5</u>
	<u>347</u>	<u>17</u>	<u>273</u>	<u>15</u>

3. NET INTEREST PAYABLE

	1987 £m	1986 £m
Interest payable on:		
Borrowings repayable within five years otherwise than by instalments	7	12
Other loans	2	10
Finance leases	<u>4</u>	<u>5</u>
	<u>13</u>	<u>27</u>
Less interest received	<u>9</u>	<u>6</u>
	<u>4</u>	<u>21</u>

4. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

5. EMOLUMENTS OF DIRECTORS AND SENIOR EMPLOYEES

The emoluments, excluding pension contributions, of directors and senior employees working wholly or mainly in the United Kingdom were:

£	Number	Number
5,001 to 10,000	5	6
50,001 to 55,000	—	1
55,001 to 60,000	—	1
60,001 to 65,000	—	2
70,001 to 75,000	1	—
75,001 to 80,000	2	1
80,001 to 85,000	1	—
85,001 to 90,000	1	—

22

6. EMPLOYEE INFORMATION

	1987 £m	1986 £m
Group employment costs		
Wages and salaries	523	482
Social security costs	40	37
Other pension costs	43	40
	<u>606</u>	<u>559</u>
Average weekly number of Group employees during the year	Number	Number
United Kingdom	38,900	38,800
Overseas	3,100	3,100
	<u>42,000</u>	<u>41,900</u>

7. TAXATION CHARGE (CREDIT)

	1987 £m	1986 £m
United Kingdom – corporation tax at 35%	3	—
– advance corporation tax written off	14	—
– deferred taxation	—	(1)
Overseas – current taxation	4	5
– deferred taxation	—	(5)
	<u>21</u>	<u>(1)</u>

The corporation tax charges for 1987 and 1986 have been reduced by the utilisation of tax losses brought forward.

8. DIVIDENDS – ORDINARY SHARES

	1987 £m	1986 £m
Interim paid 1.75p (1986 nil) per share	14	—
Final proposed 3.5p (1986 nil) per share	28	—
	<u>42</u>	<u>—</u>

9. EARNINGS PER ORDINARY SHARE

Earnings per ordinary share on a nil distribution basis are calculated by dividing the profit attributable to the shareholders of Rolls-Royce plc of £134m (1986 £120m), plus £14m (1986 nil) being the irrecoverable advance corporation tax attributable to dividends paid and proposed, by 738 million (1986 635 million) ordinary shares, being the weighted average number of ordinary shares in issue during the financial year, as adjusted for the share consolidation and sub-division on April 27, 1987 (see note 23).

Earnings per ordinary share on a net basis are calculated as for the nil distribution basis but ignoring the add-back of irrecoverable advance corporation tax.

A fully diluted earnings per ordinary share figure based on outstanding share options is not provided as the effect on the earnings per ordinary share is not material.

NOTES TO THE ACCOUNTS

10. TANGIBLE FIXED ASSETS

	Land & buildings (see note 11) £m	Group Plant & equipment £m	Total £m	Land & buildings (see note 11) £m	Company Plant & equipment £m	Total £m
Cost or valuation:						
At January 1, 1987	201	564	765	179	437	616
Exchange adjustments	(2)	(8)	(10)	—	—	—
Additions at cost	10	72	82	8	62	70
Disposals	—	(12)	(12)	—	(9)	(9)
At December 31, 1987	<u>209</u>	<u>616</u>	<u>825</u>	<u>187</u>	<u>490</u>	<u>677</u>
Depreciation:						
At January 1, 1987	8	352	360	6	276	282
Exchange adjustments	—	(4)	(4)	—	—	—
Provided during year	8	33	41	6	23	29
Disposals	—	(10)	(10)	—	(8)	(8)
At December 31, 1987	<u>16</u>	<u>371</u>	<u>387</u>	<u>12</u>	<u>291</u>	<u>303</u>
Net book value at December 31, 1987	<u>193</u>	<u>245</u>	<u>438</u>	<u>175</u>	<u>199</u>	<u>374</u>
The net book value at December 31, 1987 includes the following amounts in respect of assets held under finance leases	<u>—</u>	<u>45</u>	<u>45</u>	<u>—</u>	<u>199</u>	<u>199</u>
Net book value at December 31, 1986	<u>193</u>	<u>212</u>	<u>405</u>	<u>173</u>	<u>161</u>	<u>334</u>
The net book value at December 31, 1986 includes the following amounts in respect of assets held under finance leases	<u>—</u>	<u>58</u>	<u>58</u>	<u>—</u>	<u>161</u>	<u>161</u>

Group assets held for use in operating leases at December 31:

	1987 £m	1986 £m
Cost or valuation	56	52
Depreciation	(33)	(28)
Net book value	<u>23</u>	<u>24</u>

The original cost of assets fully written off, but still in use and included in the Group figures above, amounts to **£146m** (1986 £150m).

11. LAND AND BUILDINGS

	Freehold	Leaschold		Total
	£m	Long	Short	£m
		£m	£m	
Group				
Valuation at December 31, 1985	177	10	2	189
Cost	18	3	1	22
Exchange adjustments	(2)	—	—	(2)
	193	13	3	209
Depreciation	(14)	(2)	—	(16)
Net book value at December 31, 1987	179	11	3	193
Net book value at December 31, 1986	180	11	2	193
Company				
Valuation at December 31, 1985	164	8	2	174
Cost	12	—	1	13
	176	8	3	187
Depreciation	(12)	—	—	(12)
Net book value at December 31, 1987	164	8	3	175
Net book value at December 31, 1986	163	8	2	173

On an historical cost basis the value of land and buildings would have been as follows:

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Cost	132	124	108	100
Depreciation	(80)	(76)	(69)	(66)
Net book value at December 31	52	48	39	34

12. CAPITAL EXPENDITURE COMMITMENTS

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Contracted but not provided	19	34	16	31
Authorised but not yet contracted	23	26	21	24

NOTES TO THE ACCOUNTS

13. INVESTMENTS IN GROUP COMPANIES

	Company	
	1987	1986
	£m	£m
Shares at cost:		
At January 1	27	26
Additions during year	1	1
At December 31	28	27
Provision for post-acquisition losses:		
At January 1	(4)	(4)
Credit for year	1	—
At December 31	(3)	(4)
Net book value at December 31	25	23

The principal subsidiary companies are listed on pages 34 and 35.

14. INVESTMENTS IN RELATED COMPANIES

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Shares at cost	1	1	1	1
Provision for share of post-acquisition losses	(1)	(1)	(1)	(1)
Net book value at December 31	—	—	—	—

The principal related companies are listed on page 36.

15. STOCKS

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Raw materials	73	79	63	69
Work in progress, jigs and tools	425	447	396	416
Finished parts and engines	408	428	400	413
Payments on account	22	9	31	17
	928	963	890	915
Progress payments against stocks	(305)	(359)	(305)	(359)
	623	604	585	556

The replacement cost of stocks is not considered to be materially different from the historical cost value.

16. DEBTORS

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Amounts falling due within one year	247	205	207	161
Trade debtors	—	—	19	21
Amounts owed by:	—	—	32	34
Group companies	32	34	2	13
Related companies	4	16	13	31
Other debtors	15	33	—	—
Prepayments and accrued income	<u>298</u>	<u>288</u>	<u>273</u>	<u>260</u>
Amounts falling due after one year	12	14	6	8
Trade debtors	—	—	339	334
Amounts owed by:	—	—	5	—
Group companies	5	—	14	13
Related companies	14	13	364	355
Prepayments and accrued income	<u>31</u>	<u>27</u>	<u>364</u>	<u>355</u>
Total debtors	<u>329</u>	<u>315</u>	<u>637</u>	<u>615</u>

17. BANK LOANS, OVERDRAFTS AND OTHER BORROWINGS – AMOUNTS FALLING DUE WITHIN ONE YEAR

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Bank loans and overdrafts	4	131	—	128
Other loans	4	40	—	—
	<u>8</u>	<u>171</u>	<u>—</u>	<u>128</u>

18. OTHER CREDITORS – AMOUNTS FALLING DUE WITHIN ONE YEAR

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Trade creditors	180	168	159	151
Amounts owed to Group companies	—	—	20	60
Payments received on account	94	87	92	84
Corporate taxation	18	3	16	—
Other taxation and social security	19	12	18	11
Other creditors	77	70	72	51
Accruals and deferred income	13	10	12	10
Proposed dividend	28	—	28	—
Capital obligations under finance leases	14	17	59	58
	<u>443</u>	<u>367</u>	<u>476</u>	<u>425</u>

Company capital obligations under finance leases include £51m (1986 £46m) owed to a Group company.

NOTES TO THE ACCOUNTS

19. BANK LOANS AND OTHER BORROWINGS – AMOUNTS FALLING DUE AFTER ONE YEAR

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Unsecured				
Bank loans repayable 1989 to 1990 (interest rates 7.2% and 7.9%)	3	71	—	65
Other loans repayable 1989 to 1995 (interest rates nil and 11.5%)	5	7	—	—
Secured				
Loan repayable 1989 to 1994, secured by charges on related buildings (interest rates 8.8% and 10.5%)	1	1	1	1
	<u>9</u>	<u>79</u>	<u>1</u>	<u>66</u>
Repayable by instalments:				
Between one and two years	5	19	—	11
Between two and five years	4	40	1	35
	<u>9</u>	<u>59</u>	<u>1</u>	<u>46</u>
Repayable otherwise than by instalments:				
Between two and five years	—	20	—	20
	<u>9</u>	<u>79</u>	<u>1</u>	<u>66</u>

20. OTHER CREDITORS – AMOUNTS FALLING DUE AFTER ONE YEAR

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Payments received on account	70	37	70	37
Accruals and deferred income	24	29	24	28
Capital obligations under finance leases payable:				
Between one and two years	12	13	58	55
Between two and five years	12	23	151	139
After five years	—	1	84	100
	<u>118</u>	<u>103</u>	<u>387</u>	<u>359</u>

Company capital obligations under finance leases include **£283m** (1986 £276m) owed to a Group company.

21. PROVISIONS FOR LIABILITIES AND CHARGES – DEFERRED TAXATION

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Movements on the provision were:				
At January 1	1	7	—	—
Charge (credit) to profit and loss account	—	(6)	—	—
At December 31	<u>1</u>	<u>1</u>	<u>—</u>	<u>—</u>
Analysis of provision and full potential liability:				
Provision:				
Fixed asset timing differences	<u>1</u>	<u>1</u>	<u>—</u>	<u>—</u>
Full potential liability:				
Fixed asset timing differences	13	8	—	—
Revaluation of land and buildings	27	24	27	24
Advance corporation tax recoverable	(14)	—	(14)	—

There is no present intention to dispose of any land and buildings.

At December 31, 1987 the Company has estimated taxation losses of approximately £600m (1986 £675m), which are available for relief against future trading profits of the Company.

22. OTHER PROVISIONS FOR LIABILITIES AND CHARGES

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Movements on other provisions were:				
At January 1 as previously reported	102	72	87	67
Prior year adjustment (see note 27)	10	10	10	10
As restated	<u>112</u>	<u>82</u>	<u>97</u>	<u>77</u>
Charge to profit and loss account	32	66	28	55
Utilised	(32)	(29)	(28)	(28)
Released	(6)	(7)	(6)	(7)
At December 31	<u>106</u>	<u>112</u>	<u>91</u>	<u>97</u>

Other provisions include principally warranty relating to sales up to the year end and estimated future losses on current contracts.

NOTES TO THE ACCOUNTS

23 SHARE CAPITAL

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Authorised				
1,050,000,000 ordinary shares of 20p each (1986 750,000,000)	210	150	210	150
Special rights redeemable preference share of £1 (1986 nil)	—	—	—	—
Allotted and fully paid				
801,470,588 ordinary shares of 20p each (1986 635,000,000)	160	127	160	127
Special rights redeemable preference share of £1 (1986 nil)	—	—	—	—

On April 27, 1987 the 600,000,000 ordinary shares of 25p each in the Company were consolidated into 150,000,000 ordinary shares of £1 each and then each such ordinary share was sub-divided into five ordinary shares of 20p each. As a result, the authorised share capital of the Company became £150,000,000 divided into 750,000,000 ordinary shares of 20p each. On the same date the authorised share capital was increased from £150,000,000 to £210,000,001 by the creation of 300,000,000 ordinary shares and the special share.

On May 20, 1987, 166,470,588 ordinary shares and the special share were allotted credited as fully paid to a nominee of the Secretary of State for Trade and Industry, who may, subject to the Companies Act 1985, require the Company to redeem the special share at par at any time. The Company was floated on May 20, 1987, when the Secretary of State sold his total holding of 801,470,588 ordinary shares.

The Company has established the following employee share schemes:

- (i) Under the Free and Matching Offer Share Scheme 9,468,221 ordinary shares of the Company were held in trust at December 31, 1987 on behalf of 35,972 employees who were beneficially entitled to the shares under special arrangements made at the time of the Offer for Sale.

- (ii) At December 31, 1987 the following shares were subject to options:

	Date of grant	Number of shares	Option price per 20p share	Normal dates of exercise
Executive Share Option Scheme	1987	2,537,000	205p	1990
Sharesave Scheme	1987	20,117,051	185p	1992-1994

- (a) Under the terms of the Executive Share Option Scheme the Board has granted options to purchase ordinary shares in the Company to 44 directors and senior executives.
- (b) Under the terms of the Sharesave Scheme the Board may grant options to purchase ordinary shares in the Company each year to those employees who enter into an Inland Revenue approved Save As You Earn (SAYE) savings contract for a period of either 5 or 7 years.

24. SHARE PREMIUM ACCOUNT

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Arising during year	250	—	250	—
Share issue expenses	(9)	—	(9)	—
At December 31	241	—	241	—

On May 20, 1987, 166,470,588 ordinary shares were paid up in cash at 170p per share by the Secretary of State for Trade and Industry, resulting in a premium of 150p per share.

25. REVALUATION RESERVE (NON-DISTRIBUTABLE)

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
At January 1	145	147	139	141
Exchange adjustments	(1)	—	—	—
Transfer from profit and loss account of depreciation charge attributable to revaluation surplus	(3)	(2)	(3)	(2)
At December 31	<u>141</u>	<u>145</u>	<u>136</u>	<u>139</u>

26. OTHER RESERVES (NON-DISTRIBUTABLE)

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
At January 1	9	9	9	9
Transfer from profit and loss account	1	—	—	—
At December 31	<u>10</u>	<u>9</u>	<u>9</u>	<u>9</u>

27. PROFIT AND LOSS ACCOUNT

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
At January 1 as previously reported	236	116	189	68
Prior year adjustment (see below)	(10)	(10)	(10)	(10)
As restated	<u>226</u>	<u>106</u>	<u>179</u>	<u>58</u>
Retained profit for the year	92	120	68	119
Exchange adjustments	(17)	(2)	—	—
Transfer to revaluation reserve of depreciation charge attributable to revaluation surplus	3	2	3	2
Transfer to other reserves	(1)	—	—	—
At December 31	<u>303</u>	<u>226</u>	<u>250</u>	<u>179</u>

£110m (1986 £119m) of the Group profit attributable to the shareholders of Rolls-Royce plc has been dealt with in the profit and loss account of the Company.

The prior year adjustment represents a provision in respect of overseas taxation for 1984 and earlier years. This adjustment was included in the Offer for Sale document dated April 28, 1987.

The undistributed profits of overseas subsidiary and related companies may be liable to overseas taxes and/or United Kingdom taxation (after allowing for double tax relief) if declared as dividends.

28. PENSION FUNDING

The pension schemes for employees of the Company and its United Kingdom subsidiaries are of the defined benefits type and are administered by Trustees; the assets of the schemes are invested by them independently of the finances of the Group. The schemes are funded by annual contributions from both the Company and its UK subsidiaries, which are charged against profits for the year, and from members. Based upon actuarial valuations carried out not less than once every three years, the joint contributions provide for benefit entitlements in respect of pensionable service with the Company and its UK subsidiaries. The actuaries have confirmed, following valuations as at March 31, 1985, that the present contribution rates are adequate to meet the benefits provided under the rules of the schemes. If the schemes had been discontinued at the valuation date, the existing assets would have more than covered the accrued benefits of contributing members as well as pensions in payment and other benefits for former contributors.

Pension arrangements for employees of overseas subsidiaries are managed and funded in accordance with local requirements and professional advice.

NOTES TO THE ACCOUNTS

29. OPERATING LEASES

Annual commitments under operating leases are as follows:

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Leases of land and buildings which expire:				
Within one year	1	1	—	—
Between one and two years	1	1	—	1
Between two and five years	2	1	1	—
After five years	3	3	2	2
Other leases which expire:				
Within one year	2	2	1	1
Between one and two years	—	—	—	—
Between two and five years	1	1	—	1
After five years	2	2	1	—

30. CONTINGENT LIABILITIES

	Group		Company	
	1987	1986	1987	1986
	£m	£m	£m	£m
Guarantees, customs bonds, recourse on supplier credit arrangements subject to ECGD insurance cover, counter-trade obligations and minor miscellaneous items	4	6	4	5
Guarantees under sales financing arrangements with customers, after taking into account the estimated realisable value of any underlying security	1	—	1	—
Together with other companies involved in a collaborative agreement, the Company has provided a joint and several guarantee to a customer. The Company's share, after taking into account the estimated realisable value of the underlying security and recourse amongst the collaborating companies in accordance with the terms of relevant agreements	3	3	3	3
Guarantees in respect of financial obligations of subsidiaries	—	—	95	103

In the opinion of the directors, no significant losses are likely to arise in respect of the above.

Contingent liabilities exist in respect of certain arrangements to secure engine deliveries and under performance and reliability guarantees, entered into in the ordinary course of business. In the opinion of the directors, any claims under such arrangements and guarantees, after allowing for provisions already made, will not be significant in relation to the Group's future activities.

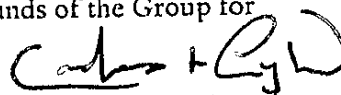
REPORT OF THE AUDITORS

To the members of Rolls-Royce plc

We have audited the accounts on pages 16 to 32 in accordance with approved Auditing Standards.

In our opinion the accounts give a true and fair view of the state of affairs of the Company and the Group at December 31, 1987 and of the profit and source and application of funds of the Group for the year then ended and comply with the Companies Act 1985.

London
March 24, 1988


Coopers & Lybrand
Chartered Accountants

ANALYSIS OF ORDINARY SHAREHOLDERS at December 31, 1987

	Number of holdings	% of total holdings	% of total shares
By size of holding:			
1-400	867,839	93.82	18.40
401-600	20,899	2.26	1.34
601-1,000	14,565	1.58	1.39
1,001-5,000	17,474	1.89	3.95
5,001-10,000	2,189	0.24	1.77
10,001-50,000	1,026	0.11	3.05
50,001-100,000	292	0.03	2.74
100,001-500,000	468	0.05	12.14
500,001 and over	218	0.02	55.22
	<u>924,970</u>	<u>100.00</u>	<u>100.00</u>
By category of holding:			
Individuals (including joint accounts)	921,820	99.66	25.66
Banks (including clients' accounts)	775	0.08	4.24
Nominee companies	1,633	0.18	43.56
Insurance companies	94	0.01	6.20
Pension funds	67	0.01	2.45
Other corporate bodies	581	0.06	17.89
	<u>924,970</u>	<u>100.00</u>	<u>100.00</u>

PRINCIPAL SUBSIDIARY COMPANIES at December 31, 1987

	Class of capital	Issued share capital Percentage held by Rolls-Royce plc	Percentage of total equity held by Rolls-Royce plc
REGISTERED IN ENGLAND:			
Deeside Titanium Limited <i>Production of titanium granules</i>	Ordinary	82½	82½
Rolls-Royce and Associates Limited <i>Design, development, procurement and support of nuclear steam raising plant for naval purposes</i>	A Shares B Shares	38 } 100 }	53
Rolls-Royce (China) Limited <i>Commercial information and liaison</i>	Ordinary	100	100
Rolls-Royce (Far East) Limited <i>Commercial information and marketing and service support</i>	Ordinary	100	100
Rolls-Royce (France) Limited <i>Commercial information and marketing support</i>	Ordinary	100	100
Rolls-Royce India Limited <i>Commercial information and marketing and service support</i>	Ordinary	100	100
Rolls-Royce Leasing Limited <i>Leasing of aero and industrial gas turbine engines</i>	Ordinary	100	100
Rolls-Royce MatEval Limited <i>Design and manufacture of ultrasonic inspection systems</i>	Ordinary	100	100
Rolls-Royce Plant Leasing Limited <i>Leasing of plant and equipment</i>	Ordinary	100	100
Sawley Packaging Company Limited <i>Packaging</i>	Ordinary	100	100
Sensotect Limited <i>Development of intelligent sensors</i>	Ordinary	100	100
Sinfin Freight Forwarding Limited <i>Freight forwarding</i>	Ordinary	100	100

Except where otherwise indicated by their name the above companies operate principally in the country of their registration.

		Issued share capital		Percentage of
		Class of	Percentage	total equity
		capital	held by	held by
			Rolls-Royce plc	Rolls-Royce plc
INCORPORATED OVERSEAS:				
Australia	– Rolls-Royce of Australia Pty. Limited <i>Marketing and support services</i>	Ordinary	100	100
Brazil	– Motores Rolls-Royce Limitada <i>Repair and overhaul; component manufacture</i>	Quota	100	100
Canada	– Rolls-Royce Industries Canada Inc <i>Intermediate holding company</i>	Common	100	100
	– Bristol Aerospace Limited <i>Repair and overhaul; assembly of rocket motors and manufacture of components and propellants</i>	Common	100	100*
	– Rolls-Royce (Canada) Limited <i>Sales, service and overhaul of aero engines; manufacture of industrial gas turbines</i>	Common Preferred	100 100 }	100*
Guernsey	– Nightingale Insurance Limited <i>Insurance underwriting</i>	Ordinary	100	100
USA	– Rolls-Royce Holdings Inc <i>Intermediate holding company</i>	Common	100	100
	– Rolls-Royce Inc <i>Marketing and product support; component manufacture; engineering research</i>	Common	100	100**
	– Rolls-Royce Capital Inc <i>Financing company</i>	Common	100	100**
	– Rolls-Royce Credit Corporation <i>Financing company</i>	Common	100	100**
Saudi Arabia	– Rolls-Royce Industrial Turbines (Saudi Arabia) Limited <i>Operation and maintenance of electrical generating plant</i>	Ordinary	51	51

The interests in companies marked * are held by Rolls-Royce Industries Canada Inc
The interests in companies marked ** are held by Rolls-Royce Holdings Inc

The above companies operate principally in the country of their incorporation.

PRINCIPAL RELATED COMPANIES

at December 31, 1987

		Issued share capital*	Percentage held by Rolls-Royce plc	Percentage of total equity held by Rolls-Royce plc
	Class of capital	£		
REGISTERED IN ENGLAND:				
Cooper Rolls Limited (England) <i>Sales of mechanical drive units</i>	Ordinary	1,000	50	50**
Rolls-Royce Turbomeca Limited (England and France) <i>Management of collaboration for Adour, RTM 322 and other engines</i>	A Shares	50	100	50
	B Shares	50		
Turbo-Union Limited (England, Germany and Italy) <i>Management of collaboration for RB199 engine</i>	Ordinary	992	40	40
	A Shares	16	37½	
INCORPORATED OVERSEAS:				
Australia:		A\$		
Turbine Components Australia Pty. Limited (Australia) <i>Manufacture of investment castings</i>	A Shares	250,001	100	50
	B Shares	250,001	—	
Canada:		Can\$		
Cooper, Rolls Corporation (Canada) <i>Sales and marketing of mechanical drive units</i>	Common	20,000	50	50†
Germany:		DM		
Eurojet Turbo GmbH (England, Germany, Italy and Spain) <i>Management of collaboration for EJ200 engine</i>	Ordinary	100,000	33	33
USA:		US\$		
Cooper Rolls Inc (Europe and North America) <i>Sales and marketing of mechanical drive units</i>	Common	200,000	50	50
Switzerland:		S Fr		
IAE International Aero Engines AG (England, Germany, Italy, Japan and USA) <i>Management of collaboration for V2500 engine</i>	A shares	300,000	100	30
	B shares	300,000	—	
	C shares	199,000	—	
	D shares	121,000	—	
	E shares	80,000	—	

* At date of latest available audited accounts

**The interest is held through Cooper Rolls Inc

† The interest is held by Rolls-Royce Industries Canada Inc

The countries of principal operations are stated in brackets after each company's name.

NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the Annual General Meeting of Rolls-Royce plc will be held at the National Exhibition Centre, Birmingham, West Midlands on Tuesday May 24, 1988 at 11.30 am to transact the following business:

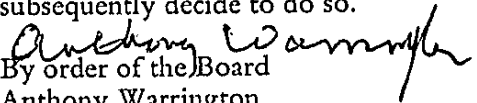
1. To receive the Report of the Directors and the audited accounts for the year ended December 31, 1987, and to declare a dividend.
2. To re-elect Mr S. C. Miller as a director.
3. To re-elect Mr H. G. Mourgue as a director.
4. To re-elect Sir Robin Nicholson as a director.
5. To re-elect Sir Philip Shelbourne as a director.
6. To re-elect Dr G. R. Higginson as a director.
7. To re-appoint Coopers & Lybrand as auditors and to authorise the directors to determine their remuneration.
8. To consider and, if thought fit, to pass the following Resolution which will be proposed as a Special Resolution:

THAT the directors be empowered, pursuant to Section 95 of the Companies Act 1985, to allot equity securities (as defined in Section 94 of that Act) wholly for cash as if Section 89 (1) of that Act did not apply to any such allotment, provided that this power shall be limited to:

- (i) the allotment of equity securities in connection with an offer by way of rights in favour of the holders of ordinary shares where the equity securities respectively attributable to the interests of all holders of ordinary shares are proportionate (as nearly as maybe) to the respective numbers of ordinary shares held by them, provided that the directors may make such arrangements as they consider necessary or expedient in relation to fractional entitlements, or as a result of legal or practical problems arising under the laws of any territory or the requirements of any regulatory body or stock exchange; and
- (ii) the allotment of equity securities (otherwise than pursuant to sub-paragraph (i) above) up to an aggregate nominal amount equal to £8,014,705.

and shall expire on the earlier of August 23, 1989 and the conclusion of the next Annual General Meeting of the Company after the date on which this Resolution is passed, save that the Company may before such expiry make an offer or agreement which would or might require equity securities to be allotted after such expiry and the directors may allot equity securities in pursuance of such an offer or agreement notwithstanding that the power conferred hereby has expired.

A member entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and, on a poll, vote instead of him or her. A proxy need not be a member of the Company. Appointment of a proxy will not preclude a member from attending and voting at the meeting should he/she subsequently decide to do so.


By order of the Board
Anthony Warrington
Secretary
65 Buckingham Gate
London SW1E 6AT
April 23, 1988

NOTES:

- (1) To be effective, forms of proxy must be lodged with the Registrar not less than 48 hours before the time fixed for holding the meeting. The address of the Registrar is given on the inside front cover of this Report.
- (2) The following will be available for inspection during normal business hours at the Company's registered office from the date of this notice until the date of the meeting and at the place of the meeting from 10.30 am until its conclusion:
 - (i) The register of directors' interests in shares of the Company.
 - (ii) Copies of the directors' contracts of service.