Costain Group PLC

("Costain" or "the Group" or "the Company")

Results for the year ended 31 December 2018

Costain, the smart infrastructure solutions company, announces another strong performance with an increase in underlying[1] operating profit, a record order book and an 8% increase in the total dividend for 2018.

	2018	2017 Restated*
Revenue		
- including share of JVs and associates	**£1,489.3m**	**£1,728.9m**
- reported	**£1,463.7m**	**£1,684.0m**
Operating profit		
- underlying[1]	**£52.5m**	**£49.1m**
- reported	**£43.1m**	**£47.2m**
Profit before tax		
- underlying[1]	**£49.7m**	**£43.8m**
- reported	**£40.2m**	**£41.8m**
Basic earnings per share		
- underlying[1]	**38.2p**	**32.9p**
- reported	**30.9p**	**31.1p**
Net cash balance[2]	**£118.8m**	**£177.7m**
Dividend per share	**15.15p**	**14.0p**

* 2017 has been restated in accordance with common practice to reflect the decision to change the accounting treatment of Research & Development Expenditure Credits ('RDEC'), which is a reclassification between operating profit and taxation. The 2017 reported basic earnings per share of 31.1p remains unchanged as a result of the restatement.

1. Before other items; amortisation of acquired intangible assets, employment related deferred consideration, an exceptional one-off pension charge of £8.6 million in respect of the equalisation of Guaranteed Minimum Pensions ('GMP') impacting UK companies with defined benefit pension schemes and a £2.6 million credit (2017: £2.5 million credit) for the reassessment of the accounting treatment of RDEC
2. Net cash balance is cash and cash equivalents less interest-bearing loans and borrowings

Highlights

- **Another strong performance**
  - Underlying operating profit[1] up 7% to £52.5 million (2017: £49.1 million*), representing a further increase in Group margin
  - Revenue, including share of joint ventures and associates, of £1,489.3 million (2017: £1,728.9 million) reflecting a lower level of capital project activity in the year
  - Net cash balance[2] of £118.8 million (2017: £177.7 million) with an average month-end net cash balance of £77.1 million (2017: £96.7 million)
- **Record order book due to differentiated strategic positioning**
  - Record higher-quality order book of £4.2 billion (2017: £3.9 billion), with over 90% repeat business
  - Continuing differentiation into the UK's leading smart infrastructure solutions company
  - Focus on long-term client relationships and integrated technology-enabled services
- **Positive outlook**
  - Proactive alignment with rapidly-changing market and increasing complexity of client demands
  - Continued involvement in major regulatory-driven procurement processes across our target markets
  - Robust and enhanced balance sheet enabling participation in longer-term and larger strategic contract relationships
  - Confidence reflected in recommended final dividend of 10.0 pence per share (2017: 9.25 pence), increasing the total dividend for the year by 8% to 15.15 pence per share (2017: 14.0 pence)

Dr Paul Golby CBE, chair, commented:

"This has been another strong performance for Costain, with further growth in underlying profit at enhanced margins. We also finished the year with a record higher-quality order book of £4.2 billion.

"This success has been driven by providing smart infrastructure solutions that expertly integrate consultancy, complex delivery, technology and asset optimisation services. Costain is at the forefront of the rapidly-evolving UK infrastructure market, working with our clients on a long-term, strategic basis to deliver their progressively larger and more complex investment programmes. This increasingly differentiated strategic positioning underpins our ambition for continued growth."

"We announced today that Andrew Wyllie CBE, after fourteen years as chief executive of the Company, is retiring in order to pursue a non-executive career and that Alex Vaughan, currently managing director of the Group's natural resources division, will be appointed as CEO with effect from the conclusion of the Company's AGM on 7 May 2019. On behalf of everyone at Costain, I would like to thank Andrew for everything that he has done for the business and to wish him and his family well for the future. We are delighted that Alex will be taking over. He has played a major role in the development of the Group and the implementation of its strategy, and has the expertise and ambition to deliver the future growth of the business.

"As a result of the strong performance across the business and future opportunities, I am pleased to announce the Board's recommendation of a final dividend of 10.0 pence per share, representing an 8% increase in total dividend for the year. With a clear purpose, strategy and record order book, I look forward to reporting on future progress."

Enquiries:

Costain **Tel: 01628 842 444**
Andrew Wyllie CBE, Chief Executive
Tony Bickerstaff, Chief Financial Officer
Carolyn Rich, Investor Relations Director
Sara Lipscombe, Group Communications Director

Instinctif Partners **Tel: 020 7457 2020**
Mark Garraway
James Gray

There will be a presentation to analysts today at 11.00am at Instinctif Partners, 65 Gresham Street, London, EC2V 7NQ. To register your attendance please contact christine.galloway@instinctif.com

The Costain 2018 results film is available at www.costain.com

Notes to Editors

Costain helps to improve lives with smart infrastructure solutions across the UK's energy, water and transportation infrastructures. We help to safeguard the security, increase the capacity, improve customer service and drive efficiency in our clients' infrastructure programmes. Our strategy is to become the UK's leading smart infrastructure solutions company through our focus on blue chip clients whose major spending plans are underpinned by strategic national needs, regulatory commitments or essential maintenance requirements. We offer a broad range of innovative services across the whole life cycle of our clients' assets by integrating complex delivery, consultancy, technology and asset optimisation services. Our culture and values underpin everything we do.

For more information visit www.costain.com

CHAIR'S STATEMENT

I am pleased to report that Costain has delivered another strong performance in the year, with continued growth in underlying profit, enhanced margins, and a record order book.

The Group has made significant progress on its transformation, developing a strong and increasingly differentiated position in a rapidly-evolving market environment by providing smart infrastructure solutions that expertly integrate consultancy, complex delivery, technology and asset optimisation services.

This is strategically positioning Costain at the forefront of the technology revolution underway across infrastructure and underpins our ambition for further growth.

Dividend

The Board recognises the importance of regular dividends to shareholders and, as announced in August, has reviewed its dividend policy following the Group's continued strong performance. Reflecting the historical and expected future pay-out ratio, going forward the Group will target dividend cover of around 2.5 times underlying earnings. The Board is committed to growing the dividend in line with earnings over the medium term.

Our strong performance and confidence in the Group's future opportunities have resulted in the Board recommending a final dividend of 10.0 pence per share (2017: 9.25 pence) which, if approved, will be paid on 17 May 2019 to shareholders on the register as at the close of business on 12 April 2019. This represents an increase of 8% in the total dividend for the year to 15.15 pence per share (2017: 14.0 pence).

Governance

At Costain we have a Board committed to the highest standards of governance. Our Annual Report will set out and explain the processes we have in place to deliver long-term success while also ensuring that the Company complies with all applicable laws and regulations and meets the requirements of our stakeholders.

We measure the Board's effectiveness by holding an externally facilitated evaluation every three years, the most recent of which was in 2017, which found the Board to be well-functioning and effective. An internal evaluation was held during the year which reiterated that conclusion and monitored progress on actions to help ensure the speed of transformation and organisational development is maintained.

We welcome the changes to the Corporate Governance Code, which came into effect for reporting periods starting 1 January 2019 and as appropriate we are adapting to practices required by the code and will report on these in due course.

Board and people

We announced today that Andrew Wyllie CBE, after fourteen years as chief executive of the Company, is retiring in order to pursue a non-executive career. He recently took up the presidency of the Institution of Civil Engineers and is a non-executive director of Yorkshire Water Services. Alex Vaughan, currently managing director of the Group's natural resources division, will be appointed as CEO with effect from the conclusion of the Company's AGM on 7 May 2019.

I would like to thank Andrew for everything that he has done for the business and to wish him and his family well for the future. Andrew can feel extremely proud of what he has achieved at Costain. He leaves the Group in good health, the result of the growth strategy which he and his colleagues have been implementing for the last fourteen years. We are delighted that Alex will be taking over. He has played a major role in the development of the Group and the implementation of its strategy and has the expertise and ambition to deliver the future growth of the business.

As previously announced, and as part of our planned Board succession, James Morley retired as a non-executive director of the Company, and as senior independent director, on 8 May 2018 after the conclusion of the Group's Annual General Meeting (AGM). Jane Lodge was appointed to act as the Company's senior independent director with effect from the conclusion of the 2018 AGM. I would once again like to thank James for more than 10 years of dedicated service to Costain, during which time he has made a significant contribution, and wish him well for the future.

The success of any company is down to the quality of its leadership and the depth of talented and skilled people throughout the organisation. On behalf of the Board, I would also like to thank all of our people for their commitment, dedication and hard work. The strong results we have achieved over several years and the positive outlook for the future would not be possible without them.

Corporate citizenship

Driven by our values, we take seriously our wider corporate responsibility and the role the business plays in society. This corporate perspective is also integral to the development of long-term relationships with our blue-chip clients who increasingly place a demonstrable commitment to corporate responsibility high on their selection criteria for preferred suppliers.

Outlook

This has been a year of continued progress at Costain. The business has delivered another set of strong results with further growth in underlying profit at enhanced margins. We also ended the year with a record higher-quality order book of £4.2 billion.

This success has been driven by providing smart infrastructure solutions which expertly integrate consultancy, complex delivery, technology and asset optimisation services. Costain is at the forefront of the rapidly-evolving UK infrastructure market, working with its clients on a long-term, strategic basis to deliver their progressively larger and more complex investment programmes. This increasingly differentiated strategic positioning underpins our ambition for continued growth.

With a clear purpose, strategy and record order book, I look forward to reporting on future progress.

Dr Paul Golby CBE
Chair

CHIEF EXECUTIVE'S REVIEW

I am pleased to report that we have delivered another strong performance and continued to progress as a business.

We are fulfilling our purpose by improving millions of people's lives across the UK through the deployment of technology-based engineering solutions to address urgent national infrastructure needs in transportation, water and energy.

Our strong trading performance is the consequence of the implementation of our focused and ambitious strategy, our enhanced market differentiation and robust financial management.

We are operating in a dynamic and rapidly changing market environment influenced by major demographic, economic, social and technology trends which are creating a wide array of exciting new business opportunities for the Group.

Another strong trading performance

Results

The 'Costain Way' business management system ensures the rigorous application of policies and procedures across the Group, governing a robust approach to opportunity assessment, continual monitoring of contract and operational performance and effective financial management.

The planned further improvement in operating margins ensured that underlying operating profit increased 7% to £52.5 million (2017: £49.1 million). The reported operating profit was £43.1 million (2017: £47.2 million).

The term 'underlying' throughout this document excludes the following items: amortisation of acquired intangible assets, employment related deferred consideration on acquisitions, an exceptional one-off pension charge of £8.6 million in respect of the equalisation of Guaranteed Minimum Pensions impacting UK companies with defined benefit pension schemes and a £2.6 million credit (2017: £2.5 million credit) for the reassessment of the accounting treatment of Research & Development Expenditure Credits ('RDEC').

Revenue, including the Group's share of joint ventures and associates, for the year was £1,489.3 million (2017: £1,728.9 million) reflecting a lower level of capital project activity in the year, in line with our strategic change in mix of activities.

Underlying profit before tax increased to £49.7 million (2017: £43.8 million) and underlying basic earnings per share increased to 38.2p pence (2017: 32.9 pence). Reported profit before tax was £40.2 million (2017: £41.8 million) and reported earnings per share were 30.9 pence (2017: 31.1 pence).

Our divisional target blended underlying operating profit margin range remains 4%-5%, and we expect to be operating towards the upper end of that range within the next three years. In 2019 we are targeting further increase in profit with an enhanced margin on a lower revenue profile, reflecting our changing mix in activities and the timing of major regulatory-driven investment programmes, with anticipated revenue growth in 2020.

Although we have two core operating and reporting divisions within our business (Infrastructure and Natural Resources) we have continued to implement our 'One Costain' philosophy which enables us to focus our resources on identifying and securing the most attractive business opportunities across the markets in which we operate. Further detail on our reporting divisions' performance is set out in the operational review.

Record order book

The Group ended the year with a record higher-quality order book of £4.2 billion, reflecting our differentiation and strong market positions. We secured over £1.8 billion of new contract awards and extensions to existing contracts during the year. The order book, which contains over 90% target cost, cost reimbursable contracts continues to evolve to reflect our strategic positioning in a rapidly-changing market environment.

In the second half of the year, the Group notably secured a leading place on a six-year framework contract for Highways England to deliver its Regional Investment Programme. One of the key reasons for our success was our ability to meet Highways England's required outcomes through the application of technology-led solutions; digital modelling, improved productivity through our smart delivery platform and data analytics for customer insights.

Technology contracts won in the year evidence the growing importance of technology integration in our markets reflecting the changing nature of the requirements and spending profile of our clients.

As a consequence of our focus on developing long-term strategic relationships with blue-chip clients, over 90% of the order book comprises repeat business. In addition, the Group has an increased preferred bidder position of c £600 million (2017: £400 million).

As at 31 December 2018, the Group had secured c £0.9 billion of revenue for 2019 (31 December 2017: over £1.1 billion secured for 2018).

The order book provides good medium and long-term visibility and underpins our confidence in the Group's future performance.

Strong balance sheet and robust financial management

A strong balance sheet is paramount to the success of the Group. Evidence of financial strength and robust financial management are prerequisites for qualification with our major clients who are consolidating their supply chains and placing larger long-term contracts to undertake multi-billion pound, multi-year investment programmes.

Costain finished the year with a positive net cash balance of £118.8 million, in line with expectations (31 December 2017: £177.7 million), with the reduction from last year's exceptionally high level due to the timing of receipts in that period. Throughout the year the Group had a positive net cash position with an average month-end net cash balance of £77.1 million (2017: £96.7 million). The period-end and month-end balances have reduced due to a lower level of revenue and therefore cashflow receipts and payments during the year. Going forward average month-end and period-end net cash balances are anticipated to trend closer to each other.

In December 2017, the Group successfully increased and extended its total banking debt facilities to £191.0 million, which now have a maturity date of June 2022. The Group maintains a regular, constructive dialogue with its banking syndicate who remain highly supportive of the business and its significant opportunities. In addition, the Group has in place committed and uncommitted bonding facilities of £320.0 million.

The Board believes that the Group's balance sheet, banking and bonding facilities align the composition and structure of the Group's funding with its prevailing strategic, operational and investment priorities.

Dynamic and rapidly changing market environment

We are entering a new era for Costain, an era defined by the start of the Fourth Industrial Revolution.

The Fourth Industrial Revolution is now having a global impact and is characterised by a fusion of technology breakthroughs that are blurring the lines between the physical, digital and biological spheres. These breakthroughs are occurring in a number of fields including artificial intelligence, robotics, nanotechnology, quantum computing and biotechnology.

These developments are creating a range of new possibilities, and consequently we are now seeing a stream of new policy announcements, product developments and service enhancements.

In highways for example, we have recently seen the introduction of a UK ban on the sale of petrol and diesel cars from 2040, accelerated in Scotland to 2032. In the year, we saw the introduction of the UK's first "Electric Streets" scheme, banning the use of petrol and diesel vehicles on nine roads in the City of London. During the year BMW also launched the trial of its ReachNow "mobility as a service" offering in Seattle to compete with Uber and Lyft. The foremost vehicle manufacturers have launched various new electric models in the last year.

All of these developments are having a profound impact on transport infrastructure, and the associated market participants, and are stimulating a fundamental re-think about how national infrastructure is provided. We are therefore seeing a rapid change in the spending patterns of our clients, with the deployment of emerging technology being core to their next generation of infrastructure solutions.

We are strategically positioning Costain at the forefront of this revolution, transforming the business into a leading smart infrastructure solutions company. This differentiation is allowing us to seize the wide array of exciting opportunities being created for our business. Our considerable expertise across the integration of technology, consultancy, asset optimisation and complex delivery services places Costain well in this rapidly-evolving market.

During the year, we have benefited from the start of a new generation of smart infrastructure contract awards including delivering the first phase of the A2/M2 Connected Corridor and participating in the Midlands Future Mobility testbed programme.

To meet this ever-greater urgency and complexity in delivering the UK's infrastructure needs, our major clients are also consolidating their supply chains by investing in increasingly long-term, collaborative multi-billion-pound programmes and service enhancements, underpinned by redefined legislative and regulatory imperatives.

Costain is therefore actively involved in a number of major, regulatory driven procurement processes including the c £25 billion Highways England's Road Period 2 (2020-2025), the AMP7 (2020-2025) programme in the water sector with an expected Totex of c £50 billion, the RIIO-1 £60 billion (2013-2023) period in the energy sector and the record £47 billion Control Period 6 (2019-2024) for Network Rail.

These changing client trends are why we are also continuing to invest in our skills, services and capabilities, both organically and by targeted acquisition.

We have continued to develop the strength and experience of our outstanding team with some 1,300 of our people working in consultancy or technology roles, representing over one third of our total headcount. We now have over 600 chartered professionals across a wide range of disciplines and also sponsor 25 PhD students who are undertaking leading-edge and targeted research at renowned universities including Cambridge, Imperial College and Edinburgh.

In line with society's rapidly changing attitude toward equality, diversity and inclusion, I am delighted to advise that for the first time in Costain's history, more than half of our graduate intake in the year was female. We have also made significant progress at the senior level with one third of our Executive Board being female. We were delighted to receive for the first time in the year, The Times newspapers' Top 50 Employers for Women award.

To further support the development of our technology capability, we are relocating to an enlarged technology centre in Somerset, where some 150 dedicated staff will develop cutting edge technology solutions for application across all our operations in water, transportation and energy.

While there remains uncertainty about the precise terms of Brexit, we have considered the impact on our business as part of our risk management process. We believe that because of our long-term regulated contract relationships with our clients, and over 90% cost reimbursable contracts in our order book, our business model will remain resilient under the range of most likely scenarios.

This dynamic and rapidly changing market environment is creating a huge and exciting opportunity for Costain, and with a focused strategy, outstanding team and strong balance sheet, we are well-placed to capitalise on the opportunities.

Operational review

Under our 'One Costain' operating model, the Group has two core operating and reporting divisions within the business: Infrastructure and Natural Resources.

Infrastructure

The division, which operates in the highways, rail and nuclear markets, delivered revenue (including joint ventures and associates) of £1,093.6 million (2017: £1,379.7 million) and underlying operating profit of £46.0 million (2017: £52.4 million). The margin in the year has increased to 4.2% from 3.8%, in line with the Group's strategic target range of 4%-5%. The revenue and profit reduction results from a lower level of lower-margin large capital project activity compared to the prior year. In 2019 we are targeting an increase in profit and margin on a lower revenue reflecting our strategic change in mix of activities and the timing of major regulatory investment programmes.

The division has an increased forward order book of £3.4 billion (2017: £3.0 billion).

Highways

Our highways clients are increasingly seeking technology solutions to reduce congestion and improve the safety of the road network. This year we successfully brought two new smart motorways online on the M1 and the M60. We have also started work on the M1 J13-16, our largest smart motorway to date, as well as securing a new contract to deliver the M6 J21a-26. We are providing the signalling and sensing technologies which allow smart motorways to operate, as well as providing project and programme management for overall scheme delivery.

The Government and vehicle manufacturers are increasing their investment in connected and autonomous vehicles (CAV). Costain has secured a market leading position in CAV infrastructure by successfully delivering the first phase of the A2/M2 Connected Corridor and through our role on Midlands Future Mobility, the UK's largest CAV testbed. As CAV uptake grows over the next decade, we will continue to deliver improvements to capacity, journey time and road safety using technology, that were previously only possible through delivery of physical infrastructure.

We are delivering integrated maintenance and network management services to highways infrastructure owners including Highways England and East Sussex County Council. We are continually increasing the efficiency and effectiveness of our operations in this area through the application of digital technology, such as the East Sussex Digital Network Management Hub, ultimately reducing disruption and improving communication with communities and those using the road network.

Our track record of successfully delivering capital investment projects on nationally critical networks has continued in the year with the opening of the refurbished Brynglas tunnels and the remodelled junction 28 on the M4 for the Welsh Government. We are also delivering the technically complex A465 Heads of the Valleys scheme, due to be completed in 2020, and continue to make progress with our client to resolve the effect of significant additional scope and the associated cost and schedule impact.

We are making good progress on Highways England's major A14 upgrade contract, which is expected to deliver a significant increase in capacity on this major transport corridor. This track record of strong performance helped us to secure first place on Highways England's Regional Delivery Partnership, where we will deliver improvements to the Strategic Road Network in the north and east regions to the value of c £1.5 billion over the life of the partnership.

Our ability to manage the impact of major infrastructure investment on communities and the environment continues to be valued by our clients, and this year we have successfully brought the A19 Testos Improvement and the M4 Corridor around Newport through the statutory planning process. The expertise of our people and the value placed on this by our clients is reflected in our growing advisory client base including TfL, local and combined authorities, sub-national transport bodies and central government.

With confirmation in the Autumn 2018 Budget that there will be c £25 billion of investment in roads for the period from 2020-2025, we are well positioned to continue growing and excelling in this market.

Rail

The rail sector in the UK is changing rapidly. Network Rail is introducing new digital technologies to increase the capacity and performance of the network and we are well positioned to take a key role in the delivery of this new generation of schemes by capitalising on our knowledge of the railway and of rail systems.

This year we have substantially completed the £1.0 billion upgrade of London Bridge Station, a flagship project for Network Rail that not only enhances capacity at one of Britain's busiest transport hubs but also transforms the customer experience at the station with over seventy new shops, cafes and leisure facilities.

Our work on High Speed 2 has continued to grow throughout the year. We are progressing well with the enabling works contract covering the southern section of the scheme and completing the design work on our two main civils contracts on the southern sections of the route.

Crossrail, which will be known as the Elizabeth Line, is one of Europe's largest and most complex infrastructure projects and our remaining contracts on the scheme are being completed in accordance with supplemental agreements reached with the client. Our Crossrail Anglia contract for Network Rail, which involved readying their existing network east of London for the new Crossrail fleet, has now been completed.

For London Underground, discussions are well advanced to finalise the account for the completed Bond Street station upgrade and the Bakerloo Line link to the Elizabeth Line at Paddington is nearing completion.

In Scotland, we have made excellent progress on the electrification of the routes between Stirling, Dunblane and Alloa, which will enable faster and more environmentally friendly trains to be introduced.

Fatal incidents at unguarded railway crossings continue to be a source of concern for Network Rail, who have commissioned Costain to develop and introduce a new technology that will alert pedestrians to the presence of an approaching train. The Project Meerkat technology has been under development throughout 2018 and in future years we expect to be installing innovative sensor and alarm systems up and down the railway network in the UK.

Nuclear

Costain's Nuclear team is at the heart of a number of nationally strategic programmes in nuclear new-build and generation; delivering energy security for the UK, decommissioning; dealing with the UK's nuclear legacy and defence; supporting the security of our nation.

Our programme management contract for AWE continues to exceed performance expectations, allowing us to secure opportunities to support AWE on other projects. The recent annual Infrastructure Projects Authority review of the AWE project recognised the outstanding collaborative relationship between the Costain, client and contractors team.

Our expertise in the development of technology to solve client problems has been recognised, with our Concrete Contamination profiling system being highly commended at the recent NDA Supply Chain Awards and a trial of its use on the Sellafield site being awarded the prestigious Sellafield CEO's Award. This technology has the potential to significantly reduce the cost of the concrete decommissioning and waste storage programme for the UK. Another technology being developed to treat liquid radioactive waste is undergoing testing under contract with the MOD.

Our contract with EDF Energy to provide consulting and project controls services across EDF's portfolio continues to grow (from 40 to 60 staff in 2018) and we are supporting the development of a Programme Management Office to plan for the eventual shutdown and decommissioning of all EDF reactors in the UK.

At Hinkley Point C we have substantially completed the Marine Aggregate Jetty and have completed the logistics facilities, our final activities for EDF NNB. The contract was affected by scope increase and weather delays, and we are working with EDF to resolve the impact of the associated cost implications on the contract final account.

Our Sellafield decommissioning framework contract continues to perform in line with expectations and provides access to significant future revenue streams in support of the legacy clean-up mission.

Natural Resources

The Natural Resources division, which operates in the water, power and oil and gas markets, made further significant progress during the period. Revenue (including share of joint ventures and associates) was £390.3 million (2017: £343.9 million), with an underlying operating profit of £14.1 million (2017: £5.0 million).

The significant improvement in the performance reflects growth in the division's water and power activities. We have delivered an improved underlying operating profit margin of 3.6% (2017: 1.5%) and in 2019 we are aiming to be operating within our target margin range of 4%-5% for the division, on higher revenue.

The division has a forward order book of £0.8 billion (2017: £0.9 billion).

Water

We are now in year four of the AMP6 five-year programmes for Thames Water, Severn Trent Water and Southern Water. We are supporting these clients to improve water quality standards, enhance supply resilience, meet anticipated demographic shifts and address their Totex (capital and operational costs) efficiency challenges. These programmes are performing well, and we are using our full range of integrated capabilities to deliver improved customer service, innovative solutions, and achieve significant total whole life expenditure efficiency savings. Our AMP6 contract with Thames Water includes an element of incentivisation, aligned to the client's objectives, through the life of the contract and finalised at the end of the programme.

The Thames Tideway project, on which we are in joint venture to deliver the east section, continues to progress well and will form an integral part of the modernisation of London's Victorian sewerage system and significantly improve water quality in the River Thames, providing capacity to cope with the growing demands of the city well into the 22nd century. The tunnelling elements of the contract commence later this year with overall completion scheduled for 2024.

This year we completed the Shieldhall Tunnel for Scottish Water in Glasgow, one of the largest infrastructure investments in Scotland. The scheme is now operating successfully, improving water quality and resilience of supply through reduced flooding in the city's wastewater network.

Tender activity for targeted AMP7 advisory, asset delivery programmes and capital maintenance programmes has continued through the year, with several clients seeking contracts with early engagement from the supply chain to help develop robust business plans ahead of AMP7 formally commencing in 2020.

Power

Ensuring that the UK has a secure and resilient energy mix is another area of national need in which we are playing a key role.

The contract for the upgrade of National Grid's Peterborough and Huntingdon compressor stations, where we are designing the solution and managing the delivery, is progressing well. This programme of work is part of National Grid's Emissions Reduction Project to ensure that both compressor stations comply with the Industrial Emissions Directive and Pollution Prevention and Control regulations. The project will also enhance system resilience and reduce overall risk on the National Transmission System by replacing ageing assets with modern, efficient equipment.

We continue to provide project services to deliver the replacement of the Humber Estuary crossing for National Grid. The River Humber pipeline is a strategically important asset, connecting the gas import facility at Easington on the Yorkshire coast and providing 70–100 million cubic metres of natural gas per day to the national network.

We also continue to secure and provide a range of asset management, programme management, training, commercial, engineering and other advisory services for key strategic contracts with National Grid, Cadent, BAE Systems, Wales & West Utilities and SSE.

Oil and Gas

Work has completed on the Hydrochloric Acid Dosing Plant and Condensate Mercury Removal System for Total's Edradour-Glenlivet facility and the Stella field development programme for Ithaca.

We continue to provide ongoing support services to Total and Phillips 66 at their Immingham refineries, as well as programme development and design services to key energy operators both on and off-shore in the UK.

In the period we have continued to secure new contracts for our gas process technology service offering and a number of strategic development consultancy services. This includes the appointment by Infrastrata PLC for the FEED design on their Islandmagee gas storage facility in Northern Ireland, which will significantly increase the UK's gas storage capacity.

Although the market remains subdued, there has been a noticeable increase in new business opportunities as clients restructure their operations and investment projects to accommodate prevailing market conditions. We believe that oil and gas will remain an important part of the UK's energy requirements in the medium term, thus providing good future opportunities for Costain.

Alcaidesa

Alcaidesa is a non-core activity in Spain in which Costain owns operating assets of two golf courses with an associated consented parcel of land and a 624-berth marina concession, adjacent to Gibraltar.

Revenue in the year was £5.4 million (2017: £5.3 million). There has been an improvement in the trading returns from the operations and some early improvement in market conditions in Spain and we continue to review options for this non-core asset. The operating loss in the year was £0.7 million (2017: £1.4 million loss).

Costain Cares

The management of Safety, Health and Environment is a core value at Costain. Through the dedicated and diligent efforts of the whole team, the Group's Accident Frequency Rate (AFR) in the year was 0.03, which is our best-ever performance and places us at the leading edge of our industry peer group. We have now launched our Wellbeing Safety Environment Strategy (WiiSE) and objectives for 2019. This strategy aims to further raise the bar in terms of our health and safety performance.

During the year, the Company was fined for a safety incident which occurred in 2015 while undertaking work on a waste water treatment plant. A full investigation was held following the incident and the lessons learnt implemented across the Group.

Our clients place great emphasis on the good citizen credentials of their strategic supply chain partners. Given the profile of their businesses and the nature of the activities we undertake, how we deliver our services is as important to them as what we do. Increasingly, clients insist that their tier-one providers share their corporate and social responsibility values and failure to do this would mean a failure to pre-qualify for future work.

Throughout the year we continued to prioritise the health and wellbeing of the Costain team. Initiatives include recognising and supporting improved mental health, encouraging flexible working and fundamentally re-evaluating traditional working practices.

We are firmly committed to gender equality in the workplace. Across our business we are confident that men and women are paid equally for doing equivalent roles. Our gender pay gap has reduced to 24.25% but still reflects fewer women in senior leadership positions. We continue to work hard to address this and are confident of making further progress in the gender balance of the Group to reduce our gender pay gap. For more information please download the report from our website www.costain.com.

The Costain Charitable Foundation is the focus of the range of charitable and community work we undertake, both individually and as a Group. I am pleased to report that we raised nearly £200,000 for charitable causes in 2018.

Well-positioned for the future

This has been a year of further progress at Costain. The business has delivered another strong result with growth in underlying profit and an improved margin performance, as well as ending the year with a record higher-quality order book of £4.2 billion.

Costain is entering a new era, with the Group winning a growing number of technology-enabled contract awards, evidencing the changing nature of our clients' requirements. Our expertise across the integration of technology, consultancy, asset optimisation and complex delivery services positions us at the forefront of the rapidly-evolving UK infrastructure market, working with our clients on a long-term, strategic basis to deliver their increasingly large and complex investment programmes.

It has been a great privilege for me to be chief executive of Costain for the last fourteen years. Much has been achieved over that time as a result of the combined efforts of an outstanding team and I would like to thank my colleagues for their support and commitment. With a clear strategy, strong balance sheet and a record order book, the business is in an excellent position to deliver further growth in the future.

Andrew Wyllie CBE
Chief Executive

CHIEF FINANCIAL OFFICER'S REVIEW

This review brings together the key financial metrics of the Group and sets out the matters of financial significance.

Overview

In 2018, the Group had another year of strong financial performance with an increase in underlying operating profit and earnings per share. This performance reflects the effective implementation of the Group's focused strategy which has delivered strong financial results over several years.

Revenue, including share of joint ventures and associates, was £1,489.3 million for the year to 31 December 2018 (2017: £1,728.9 million). Reported revenue, excluding share of joint ventures and associates, was £1,463.7 million for the year to 31 December 2018 (2017: £1,684.0 million). The reduction in revenue results from a lower level of capital project activity in line with our strategic change in mix of activities.

The Group generated a 7% increase in underlying operating profit to £52.5 million (2017: £49.1 million). The increased profit reflects the Group's focus on long-term repeat orders with blue-chip clients and an increased margin from the changing mix of activities across the Group.

Reported operating profit for the year was £43.1 million (2017: £47.2 million), with the reduction from last year due to the impact of a one-off pension charge for the equalisation of guaranteed minimum pensions detailed later in this report.

Underlying profit before tax for the year was £49.7 million (2017: £43.8 million). Underlying basic earnings per share amounted to 38.2 pence (2017: 32.9 pence).

Reported profit before tax for the year was £40.2 million (2017: £41.8 million). Reported basic earnings per share were 30.9 pence (2017: 31.1 pence).

The results of the Group's operating divisions are considered in the operational review section and are shown in the segmental analysis in the financial statements.

Other items

To aid understanding of the underlying performance of the Group, throughout the annual report underlying operating profit and underlying profit before tax have been used. These measures exclude 'other items' which are considered to be one-off and unusual in nature or related to the accounting treatment of acquisitions. These include amortisation of acquired intangible assets, deferred consideration treated as an employment expense, an exceptional one-off pension charge in respect of the recent High Court ruling on the equalisation of Guaranteed Minimum Pensions ('GMP') and a reassessment of the accounting treatment of Research & Development Expenditure Credits ('RDEC'). These 'other items' are shown in a separate column in the consolidated income statement.

Net finance expense

Net finance expense amounted to £3.2 million (2017: £5.7 million). The interest payable on bank overdrafts, loans and other similar charges was £3.1 million (2017: £4.2 million) and the interest income from bank deposits and other loans and receivables amounted to £0.4 million (2017: £0.4 million). In addition, the net finance expense includes the interest cost on the net liabilities of the pension scheme of £0.4 million (2017: £1.8 million) and £0.1 million (2017: £0.1 million) unwind of discount on deferred consideration.

Tax

The Group's effective rate of tax was 18.4% of the profit before tax (2017: 22.0% restated). The accounting treatment of research and development expenditure credits has been changed to include the credits as grant income in operating profit for 2018 and restated for 2017, previously these were included as a deduction from the tax expense. Changes to estimates of prior year research and development expenditure credits have been disclosed in operating profit as 'other items', giving rise to a credit of £2.6 million (2017: £2.5 million restated).

Dividend

The Board has recommended a final dividend for the year of 10.0 pence per share (2017: 9.25 pence per share) to bring the total for the year to 15.15 pence per share (2017: 14.0 pence per share).

In accordance with the pension deficit recovery plan agreed with the Trustee of The Costain Pension Scheme (CPS), the Group will make an additional cash contribution to the pension scheme to match the total deficit contribution to the total amount of dividends paid to shareholders.

Shareholders' equity

Shareholders' equity increased in the year to £182.3 million (2017: £154.0 million). The movements are detailed in the consolidated statements of comprehensive income and expense and changes in equity in the financial statements. The increase in the year includes a positive movement following the re-measurement of the Group's legacy pension scheme defined benefit obligations to reflect current market-based assumptions.

New accounting standard – IFRS15

The new accounting standard, IFRS15 revenue recognition, is applicable to Costain's financial statements in 2018. Full details of the impact of the standard are included in a note to the 2018 financial statements. In summary, the main impact arises from a change on one of the Group's long-term frameworks which has separate performance obligations within it and under IFRS15 must be accounted for as separate contracts rather than one long-term framework contract. Application of IFRS15, which has no impact on the Group's cash flow, has reduced the net assets of the Group by £4.6 million on 1 January 2018 (£2.7 million as at 31 December 2018). As the framework completes, which is anticipated to be by 2020, it is forecast that this amount will be generated and therefore reverse this impact on net assets.

New accounting standard – IFRS9

The new accounting standard, IFRS9 financial instruments, which is applicable to the financial statements in 2018, did not have any quantitative impact on the financial results.

New accounting standard - IFRS16

The new accounting standard, IFRS16 leases, will be applicable to the financial statements in 2019. Full details of the impact of the new standard are included in a note to the 2018 financial statements.

Pensions

As at 31 December 2018, the Group's pension scheme deficit in accordance with IAS19, was £4.2 million (2017: £23.9 million). The scheme deficit position has reduced significantly in the year due to returns on assets greater than assumed, a fall in liabilities arising from favourable experience over the period since the last triennial valuation, an update to more recent mortality tables and company contributions.

The table below sets out the key details of the pension scheme deficit calculation:

	2018 £m	**2017 £m**
Present value of defined benefit obligations	(752.7)	(803.4)
Fair value of scheme assets	748.5	779.5
Recognised liability for defined benefit obligations	(4.2)	(23.9)
Principal actuarial assumptions (expressed as weighted averages)	**%**	**%**
Discount rate	2.80	2.50
Future pension increases	3.00	2.90
Inflation assumption	3.20	3.10

In accordance with the pension regulations, a triennial actuarial review of the Costain defined benefit pension scheme was carried out as at 31 March 2016. In February 2017, an updated deficit recovery plan was agreed with the scheme Trustee resulting in cash contributions of £10.0 million for the 12 months to 31 March 2017 and then £9.6 million per annum (increasing annually with inflation) until the deficit is cleared, which would be in 2031 on the basis of the assumptions made in the valuation and agreed recovery plan.

In addition, as previously implemented, the Group will continue to make an additional contribution so that the total deficit contributions match the total dividend amount paid by the Company each year. Any additional payments in this regard would have the effect of reducing the recovery period in the agreed plan.

The next triennial actuarial review will be carried out as at 31 March 2019 and a revised recovery plan agreed accordingly.

Guaranteed Minimum Pension ("GMP") Equalisation

On 26 October 2018, the High Court issued a judgement involving Lloyds Banking Group defined benefit pension schemes. The judgement concluded that the schemes should be amended to equalise pension benefits for men and women in relation to GMP benefits. The judgement has implications for the majority of defined benefit schemes with liabilities before 1997, including the Costain Pension Scheme. In conjunction with Costain's actuarial advisors the best estimate of the effect of GMP equalisation to the Group is an increase of £8.6 million on the reported pension liabilities. This increase in liabilities represents a past service cost and has been recorded as a pre-tax exceptional expense on our income statement, shown within "other items".

Contract estimates

A significant proportion of the Group's activities are undertaken via long-term contracts. The majority of these contracts are not fixed price in nature and are based on arrangements which allow for change which is expected during the contract term through the award of compensation events. Management uses detailed contract valuations and cost forecasts when formulating its estimate of costs and revenues and its assessments of the expected outcome of each long-term contractual obligation. This includes, amongst other things, consideration of the number of compensation events on the contract, changes in the design and construction requirements, and whether these all relate to the current obligation or create a new obligation, the impact of any third-party factors and progress to date on agreements with the client. Consideration is made on the extent to which events have impacted on the cost and programme to complete the contract and the associated level of estimation uncertainty and appropriate accounting treatment. In reviewing the contract estimates attention is also made to past performance on contracts and the success or otherwise of resolving any contractual matters.

Project Bank Accounts

Several of the Group's contracts operate an arrangement with the client and suppliers, known as project bank accounts, whereby monies on the contract are paid into a separate bank account covered by a trust deed and distributed to the Group and all suppliers, that join the trust deed, from that account. This is not a financing arrangement but is a form of payment administration, requested by the client, to provide transparency and security of payments to suppliers. The Group does not operate any supplier financing arrangements.

Cash flow and borrowings

The Group has a positive cash balance of £189.3 million as at 31 December 2018 (2017: £248.7 million) including cash held by joint operations of £84.5 million (2017: £87.8 million). The Group had borrowings of £70.5 million (2017: £71.0 million).

The decrease in the reported net cash balance is due to the reversal of the exceptional level of contract receipts in 2017, which were generated due to favourable timing at the year-end. Throughout the year the Group had a positive net cash position with an average month-end net cash balance of £77.1 million (2017: £96.7 million). The Group cash position is impacted by significant levels of work in progress on its large contracts and the period-end and month-end balances have reduced due to a lower level of revenue and therefore cashflow receipts and payments during the year.

Order Book

During the year, the Group secured several new contracts and extensions and the Group's order book was increased to £4.2 billion (31 December 2017: £3.9 billion).

The Group's order book is made up of an estimate of the value remaining on secured contracts, framework arrangements, service delivery arrangements and purchase orders. Several of the Group's contracts have an early contractor involvement ('ECI') phase which involves planning activities and preparation pre-construction, in this case the Group's order book also includes the estimated value of the associated construction activities.

Contract bonding and banking facilities

The Group has in place banking and bonding facilities from banks and surety bond providers to meet the current and projected usage requirements. In December 2017, the Group increased its banking facilities to £191.0 million and extended the maturity date to 25 June 2022 with its relationship banks. These facilities are made up of a £131.0 million revolving credit facility and a £60.0 million term loan.

In addition, the Group has in place committed and uncommitted bonding facilities of £320.0 million. Utilisation of the total bonding facilities on the 31 December 2018 was £102.7 million (31 December 2017: £108.0 million).

Capital allocation

A key element in the successful implementation of the Group's strategy is the efficient allocation of capital. The Board regularly reviews the appropriate allocation with regard to ensuring that the Group can effectively exploit available organic and acquisition opportunities, deliver on its ongoing obligations, including making regular returns to shareholders, and address the Group's legacy pension contribution commitments. In addition, maintaining a strong and flexible balance sheet is a key requirement from clients for the pursuit of large long-term contracts. Typically, the Group will maintain a net cash balance, while being prepared to take on modest leverage if circumstances warrant. The Board believes that its approach to the optimal deployment of capital generates value for all stakeholders on an efficient and equitable basis.

Treasury

The Group’s treasury and funding activities are undertaken by a centralised treasury function. Its primary activities are to manage the Group’s liquidity, funding and financial risk, principally arising from movements in interest rates and foreign currency exchange rates.

The Group’s policy is to ensure that adequate liquidity and financial resources are available to support the Group’s growth, while managing these risks and not to engage in speculative transactions. Group Treasury operates as a service centre within clearly defined objectives and controls and is subject to periodic review by internal audit.

Liquidity risk

The Group finances its operations primarily by a mixture of working capital, funds from shareholders, retained profits and borrowings. The directors regularly monitor cash usage and forecast usage to ensure that projected financing needs are supported by adequate cash reserves or bank facilities.

Foreign currency exposure

Translation exposure: the results of the Group’s overseas activities, mainly non-core activities in Spain, are translated into sterling at rates approximating to the foreign exchange rates ruling at the dates of the transactions. The balance sheets of overseas subsidiaries and investments are translated at foreign exchange rates ruling at the balance sheet date. The Group holds a currency hedge against the assets held in its Spanish subsidiary.

Transaction exposure: the Group has transactional currency exposures arising from overseas supply purchases for business in the UK and from subsidiaries’ commercial activities overseas. Where appropriate, the Group requires its subsidiaries to use forward currency contracts to minimise any currency exposure unless a natural hedge exists elsewhere within the Group.

Interest rate risks and exposure

The Group enters into financial instruments, where necessary, to finance its operations. Various financial instruments (for example, trade receivables and trade payables) arise directly from the Group’s operations. The main exposure to interest rate fluctuations within the Group’s operations arises from surplus cash, which is generally deposited with the Group’s relationship banks, and bank borrowings against which the Group holds the appropriate interest rate hedging arrangements.

Anthony Bickerstaff
Chief Financial Officer
6 March 2019

PRINCIPAL RISKS AND UNCERTAINTIES

The table below sets out the principal risks faced by the Company, the link to the Company's strategic priorities, movement in the risk score, examples of relevant controls and mitigating factors and risk appetite.

Principal Risk	Description and impact	Controls and key mitigations	Change in the year
1 Failure to prevent a major accident/hazard	Failure to prevent a major accident or incident for which Costain is held primarily accountable resulting in personal or environmental harm, operational loss, regulatory, legal or financial penalties and/or reputational loss.	Safety, Health and Environment (SHE)management policies and procedures. SHE Strategy & Plans. The Costain Behavioural Safety (CBS) programme.	Activity in 2018 forms part of our three-year SHE strategy which is now reaching its conclusion. The trailing indicators that the strategy targeted – Reportable Injuries, Lost Time Injuries and Environmental Incidents have all fallen in the year. The overall rate of each has fallen to around half the 2016 figure in line with our "Halving Harm" ambition.
2 Failure to deliver the business strategy	The delivery of the future strategy involves growth in several business areas. Specifically, transforming our integrated service offering of consultancy, technology, complex delivery and asset optimisation which is fundamental to our future success. Failure to manage this risk could result in unsuccessful transformation, new opportunities being missed and/or loss of stakeholder confidence.	Board annual approval of plans, setting the strategic direction and confirming strategic choices that are embedded in targets across the business. Technology & consultancy strategy and business plan Implementation. Strengthening of our leadership team to deliver in growth areas including monthly reporting to the Executive Board on the progress of the key hires.	Appointment of capability leads. Rigorous review of M&A targets which could have cross-sector benefit. A number of key hires in 2018. Appointment of and upskilling of key account directors. A review of the top 30 roles to ensure we have the right people to deliver the business plan.
3 Failure to maintain a strong balance sheet	Failure to maintain a strong balance sheet may limit our ability to grow due to failure to win work, inability to maintain competitive scale or failure to maintain adequate working capital.	Treasury function experienced in the management and oversight of investments. Bank and surety bonding facilities maintained to deliver finance requirements. Robust monitoring and management of amounts receivable.	Level of bank and bonding facilities maintained. Strengthening of processes and monitoring of key controls.
4 Failure to identify and secure new work	Costain's business strategy depends on winning work in both current, changing and diversified markets to maintain, grow and diversify a profitable future business which delivers stakeholder value. Failure to adequately manage this risk may mean that we fail to win work from current clients and/or new clients, resulting in an inability to demonstrate our diversified capability and failure to meet our profit targets.	Focus on key, blue-chip clients and understanding their needs including appointment of key account directors. Delivery of consultancy and technology services via strategic acquisitions. Continuing to develop and maintain strong relationships with customers and strategic partners.	Appointing and upskilling of key account directors. In addition, we have allocated a greater proportion of our work winning expenditure to technology and consultancy opportunities and will continue to do so in 2019.
5 Failure to attract and transform the skills, capabilities and competence of our resources	The attraction, retention and succession of the right people with the right skills in the right role at the right time, underpins the achievement of the Costain business strategy. Failure to manage this risk may result in an inability to grow the business as planned and impact short term performance.	A defined people strategy based on culture, Equality Inclusion and Diversity (EDI), wellbeing, training and development, reward and recognition. Comprehensive and planned approach to address the consultancy, technology and advisory resource requirements. Strategic succession planning which targets the right competencies.	In 2018 we have continued to drive a positive HR strategy through the attraction, development and retention of our key capabilities. Overall engagement across the business is strong (79%) measured through our people survey.
6 Failure to manage projects effectively	Costain has a strong reputation for project delivery, with over 90% repeat orders. Failure to maintain discipline in managing our projects could result in, for example, disputes, design faults and rectification works, failure of our supply chain, refusal of insurance claims for loss and/or increased compensation events which may not be fully reimbursable.	Risk assessment prior to contract commitments. Tender work winning gate controls with appropriate delegated authorities and Executive Investment Panel sign-off for appropriate opportunities. Robust financial management and weekly leading indicator reporting.	Improved joint venture governance. Strategic key hires to manage risks associated with specialist projects. Implementation of commercial deep dive reviews on key projects.

Principal Risk	Description and impact	Controls and key mitigations	Change in the year
7 Failure to manage the legacy defined benefit pension scheme	Failure to manage the legacy defined benefit pension scheme so that the liabilities are within a range appropriate to its capital base could result in Costain being exposed to additional liabilities.	Funding arrangement agreed with Trustees after each triennial valuation (next valuation in 2019). Regular reviews of the pension scheme funding position undertaken. Investment performance is monitored, and the Company provides input into the scheme's investment strategy.	Favourable market movements have reduced the scheme deficit by more than the agreed recovery plan. The scheme assets were changed in September 2018 to increase the level of liability hedging with the goal of reducing the level of future volatility.
8 Failure to ensure that our technology is robust, our systems are secure and our data protected.	Effectiveness, availability, security and integrity of our systems and data are essential for our operations. Failure to manage technology and data risks could result in loss of confidential or personal data, regulatory fines, breach of contract and/or cyber attack.	Information security strategy that integrates information systems, personnel and physical aspects to prevent, detect and investigate information security threats and incidents. Engaging with key technology partners and suppliers to ensure potentially vulnerable systems are identified. Annual penetration tests and 24-hour threat monitoring by an external security company.	Move of key business systems into the Microsoft Cloud. Mitigating the risk of cyber breaches through deployment of an additional layer of password security (multi-factor-authentication). 2019 risk mitigation, prioritises activities to focus resources on cyber protection measures.
9 Failure to anticipate and respond to changes in client circumstances	Failure to anticipate and respond to changing client circumstances, particularly where we have new clients, due to different market, regulatory or political conditions and/or change of client leadership may result in a reduction of work won and impact our profitability and cashflow. Failure to understand and respond to the changing marketplace might result in a loss of market share as existing clients move to competitors and future client needs are not met by our service offering. Clients may implement new contract conditions which might adversely impact our business and financial results.	A track record of strong client relationships in target markets. Executive Board members actively engage in discussions with regulatory authorities. Development of effective key account plans and appointment of key account directors.	Appointment of and upskilling of key account directors.

VIABILITY STATEMENT

Prospects and viability

As part of the Group's strategy and ambition to position ourselves at the forefront of the revolution in technology, the Board maintains a sharp focus on assessing the Group's long-term prospects and the company's viability as a business on a three-year basis.

This period is considered appropriate as the Group has reasonable visibility of secured work and pipeline of opportunities and aligns with the period reviewed by the Board in the normal business planning process.

Assessing Costain's prospects

Costain delivers integrated smart solutions to meet urgent infrastructure needs across the UK. The rapidly changing market offers the potential for long-term growth, with an addressable market of £21 billion underpinned by regulation, legislation or strategic national needs.

Costain has all the elements necessary for continued success – valuable brand, long term strategic client relationships, highly skilled and experienced leadership team and financial strength, with a strong balance sheet and positive net cash balance.

The Group seeks to build on these strong foundations, with a clear focus on broadening our integrated technology-led service offering to bring innovative solutions to complex infrastructure challenges.

Costain runs a rigorous annual business planning process, involving divisional and Group management, with Board input and oversight. This produces divisional and Group strategic plans, which in turn generate three-year financial plans that drive the setting of in-year budgets. At the core of this process is the One Costain philosophy and while we operate with two divisions, we focus our resources on identifying and securing the most attractive opportunities across the markets we operate.

This business planning process, combined with the Group's approach to identify, monitoring and managing risk, are a significant contributor to the assessment of the Group's prospects.

Factors in assessing long-term prospects

Group's current position

Responsible business, committed to the highest SHE standards and to operating sustainably, ethically and inclusively

- Focused strategy based on blue chip clients through long term strategic relationships, leading to over 90% repeat business and a record higher quality order book of £4.2 billion
- A strong and robust balance sheet, with banking debt facilities of £191 million to June 2022, together with committed and uncommitted bonding facilities of £320 million
- A rigorous work winning gate process where we seek to actively manage risk of customer selection, opportunity and contract form, adopting the 'One Costain' philosophy
- Strong balance sheet and robust financial management; fundamental to win work, invest and drive sustainable profitable growth
- Broadening our integrated technology-led service offering with 34% of our people in consulting and technology roles

Strategic and business model

- Clear strategy for continued organic growth and targeted acquisition
- A clear strategy to position ourselves at the forefront of the revolution in technology impacting our market, as a smart infrastructure solutions company
- Expertise in technology integration, consultancy, asset optimisation and complex delivery. Attracting industry-leading talent and investing in development
- Clients are consolidating their supply chains and placing larger long-term contracts, we have the financial strength to capitalise on the changing procurement trends

Principal risks related to the Group's business model

The assessment of viability has been made considering the principal risks as detailed in the Annual Report.

Impact of Brexit

The Group has completed a review of the implications of the decision to leave the EU and assessed scenarios around the current uncertainty as we approach the Brexit deadline of 29 March 2019.

While there remains uncertainty about the precise terms of Brexit, we have considered the impact on our business as part of our risk management process. We believe that because of our long-term regulated contract relationships with our clients, and over 90% cost reimbursable contracts in our order book, our business model will remain resilient under the range of most likely scenarios.

Structured strategic and financial planning process

The Group's prospects are assessed through the annual strategic planning process, which involves the creation of three-year divisional business plans which are reviewed in detail by the Executive Board.

To create these plans, each division assesses external factors – market trends, regulatory environment, legislative spend, strategic national needs and our client's business plans, and internal factors – including capability, skills, technology and thought leadership.

This results in a set of objectives and a clear implementation plan, considering known and emerging risks and opportunities over a broader horizon. This includes a three-year financial plan, including detailed financial forecasts, resourcing and skills plan as well as research and development activity to support our customers to address complex infrastructure challenges.

The Board scrutinises and monitors the strategic and financial plans.

Assessing the Group's viability

The assessment of viability has been made considering the principal risks and testing several plausible, but severe and prolonged scenarios. These downside scenarios reflect a combination of risks, including the potential impact of a significant decline in activity resulting from an inability to secure new work, loss of reputation from a major incident and associated fines and the impact on working capital decline arising from a major dispute on contract delivery.

Viability statement

In accordance with provision C.2.2 of the UK Corporate Governance Code, the Directors have assessed the prospects of the Group over a longer period than the 12 months required by the 'Going Concern' provisions.

Based on the results of this analysis, the Board confirms that it has a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the three-year period to 31 December 2021.

Going concern

The Directors consider that the Group and the Company have adequate resources to remain in operation for the foreseeable future and have therefore continued to adopt the going concern basis in preparing the financial statements. The 2016 Code requires the Directors to assess and report on the prospects of the Group over a longer period. The longer-term viability statement is set out above.

Costain Group PLC

Results for the year ended 31 December 2018

Consolidated income statement

Year ended 31 December		**2018**			2017 (Restated)		
	Notes	**Underlying**	**Other items**	**Total**	Underlying	Other items	Total
		£m	**£m**	**£m**	£m	£m	£m
Continuing operations							
Revenue including share of revenue of joint ventures and associates		**1,489.3**	**-**	**1,489.3**	1,728.9	-	1,728.9
Less: Share of revenue of joint ventures and associates		**(25.6)**	**-**	**(25.6)**	(44.9)	-	(44.9)
Group revenue		**1,463.7**	**-**	**1,463.7**	1,684.0	-	1,684.0
Cost of sales		**(1,373.8)**	**-**	**(1,373.8)**	(1,595.8)	-	(1,595.8)
Gross profit		**89.9**	**-**	**89.9**	88.2	-	88.2
Administrative expenses before other items		**(37.4)**	**-**	**(37.4)**	(39.1)	-	(39.1)
Pension GMP equalisation charge		**-**	**(8.6)**	**(8.6)**	-	-	-
RDEC grant income		**-**	**2.6**	**2.6**	-	2.5	2.5
Amortisation of acquired intangible assets		**-**	**(3.0)**	**(3.0)**	-	(3.2)	(3.2)
Employment related and other deferred consideration		**-**	**(0.4)**	**(0.4)**	-	(1.2)	(1.2)
Administrative expenses		**(37.4)**	**(9.4)**	**(46.8)**	(39.1)	(1.9)	(41.0)
Group operating profit		**52.5**	**(9.4)**	**43.1**	49.1	(1.9)	47.2
Share of results of joint ventures and associates		**0.3**	**-**	**0.3**	0.3	-	0.3
Profit from operations	2	**52.8**	**(9.4)**	**43.4**	49.4	(1.9)	47.5
Finance income	3	**0.4**	**-**	**0.4**	0.4	-	0.4
Finance expense	3	**(3.5)**	**(0.1)**	**(3.6)**	(6.0)	(0.1)	(6.1)
Net finance expense		**(3.1)**	**(0.1)**	**(3.2)**	(5.6)	(0.1)	(5.7)
Profit before tax		**49.7**	**(9.5)**	**40.2**	43.8	(2.0)	41.8
Taxation	4	**(9.1)**	**1.7**	**(7.4)**	(9.3)	0.1	(9.2)
Profit for the year attributable to equity holders of the parent		**40.6**	**(7.8)**	**32.8**	34.5	(1.9)	32.6
Earnings per share							
Basic	5	**38.2p**	**(7.3)p**	**30.9p**	32.9p	(1.8)p	31.1p
Diluted	5	**37.4p**	**(7.2)p**	**30.2p**	32.3p	(1.7)p	30.6p

The impact of business disposals in either year was not material and, therefore, all results are classified as arising from continuing operations.

Consolidated statement of comprehensive income and expense

Year ended 31 December

	2018 £m	2017 (Restated) £m
Profit for the year	**32.8**	32.6
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of foreign operations	**0.2**	0.5
Net investment hedge:		
Effective portion of changes in fair value during year	**0.1**	(0.7)
Net changes in fair value transferred to the income statement	**-**	0.2
Cash flow hedges :		
Effective portion of changes in fair value during year	**(0.1)**	(1.4)
Net changes in fair value transferred to the income statement	**-**	0.3
Total items that may be reclassified subsequently to profit or loss	**0.2**	(1.1)
Items that will not be reclassified to profit or loss:		
Remeasurement of defined benefit obligations	**13.3**	39.2
Tax recognised on remeasurement of defined benefit obligations	**(2.5)**	(7.4)
Total items that will not be reclassified to profit or loss	**10.8**	31.8
Other comprehensive income for the year	**11.0**	30.7
Total comprehensive income for the year attributable to equity holders of the parent	**43.8**	63.3

Consolidated statement of changes in equity

	Share capital	Share premium	Translation reserve	Hedging reserve	Retained earnings	Total equity
	£m	£m	£m	£m	£m	£m
At 1 January 2017	52.1	8.8	2.3	1.9	34.5	99.6
Profit for the year	-	-	-	-	32.6	32.6
Other comprehensive income/(expense)	-	-	-	(1.1)	31.8	30.7
Issue of ordinary shares under employee share option plans	0.6	1.6	-	-	-	2.2
Shares purchased to satisfy employee share schemes	-	-	-	-	(1.4)	(1.4)
Equity-settled share-based payments	-	-	-	-	2.2	2.2
Dividends paid	0.1	1.7	-	-	(13.7)	(11.9)
At 31 December 2017	52.8	12.1	2.3	0.8	86.0	154.0
At 1 January 2018	**52.8**	**12.1**	**2.3**	**0.8**	**86.0**	**154.0**
Adoption of IFRS 15 'Revenue from Contracts with Customers'	**-**	**-**	**-**	**-**	**(4.6)**	**(4.6)**
Restated total equity at the beginning of the financial year	**52.8**	**12.1**	**2.3**	**0.8**	**81.4**	**149.4**
Profit for the year	**-**	**-**	**-**	**-**	**32.8**	**32.8**
Other comprehensive income/(expense)	**-**	**-**	**0.3**	**(0.1)**	**10.8**	**11.0**
Issue of ordinary shares under employee share option plans	**0.5**	**1.6**	**-**	**-**	**(0.3)**	**1.8**
Shares purchased to satisfy employee share schemes	**-**	**-**	**-**	**-**	**(1.3)**	**(1.3)**
Equity-settled share-based payments	**-**	**-**	**-**	**-**	**2.3**	**2.3**
Dividends paid	**0.2**	**1.3**	**-**	**-**	**(15.2)**	**(13.7)**
At 31 December 2018	**53.5**	**15.0**	**2.6**	**0.7**	**110.5**	**182.3**

Consolidated statement of financial position

As at 31 December

	Notes	2018 £m	2017 (Restated) £m
Assets			
Non-current assets			
Intangible assets	7	**58.5**	62.5
Property, plant and equipment		**40.0**	43.0
Investments in equity accounted joint ventures		**0.4**	0.3
Investments in equity accounted associates		**0.5**	0.8
Loans to equity accounted associates		**1.6**	1.6
Other		**3.6**	4.9
Deferred tax		**2.7**	10.1
Total non-current assets		**107.3**	123.2
Current assets			
Inventories		**1.5**	1.4
Trade and other receivables		**276.5**	289.7
Cash and cash equivalents	8	**189.3**	248.7
Total current assets		**467.3**	539.8
Total assets		**574.6**	663.0
Equity			
Share capital		**53.5**	52.8
Share premium		**15.0**	12.1
Foreign currency translation reserve		**2.6**	2.3
Hedging reserve		**0.7**	0.8
Retained earnings		**110.5**	86.0
Total equity attributable to equity holders of the parent		**182.3**	154.0
Liabilities			
Non-current liabilities			
Retirement benefit obligations	9	**4.2**	23.9
Other payables		**0.9**	1.3
Interest bearing loans and borrowings		**60.5**	60.6
Total non-current liabilities		**65.6**	85.8
Current liabilities			
Trade and other payables		**313.2**	402.5
Taxation		**2.6**	9.0
Interest bearing loans and borrowings		**10.0**	10.4
Provisions for other liabilities and charges		**0.9**	1.3
Total current liabilities		**326.7**	423.2
Total liabilities		**392.3**	509.0
Total equity and liabilities		**574.6**	663.0

Consolidated cash flow statement

Year ended 31 December

	Notes	2018 £m	2017 (Restated) £m
Cash flows from operating activities			
Profit for the year		**32.8**	32.6
Adjustments for:			
Share of results of joint ventures and associates		**(0.3)**	(0.3)
Finance income	3	**(0.4)**	(0.4)
Finance expense	3	**3.6**	6.1
Taxation	4	**7.4**	9.2
Depreciation of property, plant and equipment		**3.2**	3.9
Amortisation of intangible assets		**3.4**	3.7
Employment related and other deferred consideration		**0.4**	1.2
Pension GMP equalisation charge		**8.6**	-
Shares purchased to satisfy employee share schemes		**(1.3)**	(1.4)
Share-based payments expense		**2.9**	2.7
Cash from operations before changes in working capital and provisions		**60.3**	57.3
(Increase)/decrease in inventories		**(0.1)**	0.2
Decrease in receivables		**8.6**	11.3
(Decrease)/increase in payables		**(90.9)**	3.4
Movement in provisions and employee benefits		**(15.8)**	(12.4)
Cash (used by)/from operations		**(37.9)**	59.8
Interest received		**0.4**	0.3
Interest paid		**(2.4)**	(3.2)
Taxation paid		**(8.2)**	(5.3)
Net cash (used by)/from operating activities		**(48.1)**	51.6
Cash flows from/(used by) investing activities			
Dividends received from joint ventures and associates		**0.5**	0.1
Additions to property, plant and equipment		**(1.0)**	(1.8)
Additions to intangible assets		**(0.3)**	(0.3)
Proceeds of disposal of property, plant and equipment and intangible assets		**2.1**	0.2
Repayment of loans to joint ventures and associates		**-**	0.1
Acquisition related deferred consideration		**-**	(2.4)
Net cash from/(used) by investing activities		**1.3**	(4.1)
Cash flows from/(used by) financing activities			
Issue of ordinary share capital		**1.8**	2.2
Ordinary dividends paid		**(13.7)**	(11.9)
Drawdown of loans		**30.0**	70.7
Repayment of loans		**(30.5)**	(70.0)
Net cash used by financing activities		**(12.4)**	(9.0)
Net (decrease)/increase in cash, cash equivalents and overdrafts		**(59.2)**	38.5
Cash, cash equivalents and overdrafts at beginning of the year	8	**248.7**	210.2
Effect of foreign exchange rate changes		**(0.2)**	-
Cash, cash equivalents and overdrafts at end of the year	8	**189.3**	248.7

Notes to the financial statements

1 Basis of preparation

Costain Group PLC ("the Company") is a public limited company incorporated in the UK. The consolidated financial statements of the Company for the year ended 31 December 2018 comprise the Group and the Group's interests in associates, joint ventures and joint operations and have been prepared and approved by the directors in accordance with International Financial Reporting Standards as adopted by the EU ('Adopted IFRS') and their related interpretations.

The financial information set out herein (which was authorised for issue by the directors on 6 March 2019) does not constitute the Company's statutory accounts for the years ended 31 December 2018 or 2017 but is derived from those accounts. Statutory accounts for 2017 have been delivered to the Registrar of Companies, and those for 2018 will be delivered in advance of the Company's Annual General Meeting. The Auditors have reported on those accounts; their reports were unqualified and did not include reference to any matters to which the Auditors drew attention by way of emphasis without qualifying their reports and did not contain statements under section 498(2) or (3) of the Companies Act 2006.

Whilst the financial information included in this preliminary announcement has been prepared in accordance with International Financial Reporting Standards (IFRS), this announcement does not itself contain sufficient information to fully comply with IFRS.

The directors have acknowledged the guidance in respect of going concern published by the Financial Reporting Council. The directors have considered these requirements, the Group's current order book and future opportunities and its available bonding facilities. Having reviewed the latest projections, including the application of reasonable downside sensitivities, the directors believe that the Group is well-placed to manage its business risks successfully. Accordingly, they continue to adopt the going concern basis in preparing these financial statements.

The accounting policies set out below have been applied consistently by the Group and the Company to each period presented in these financial statements, except for the policy on accounting for research and development expenditure credits (RDEC), which has been changed in the year.

The following standards and interpretations are effective for the year ended 31 December 2018:

- The adoption of IFRS 15 'Revenue from Contracts with Customers' has required an adjustment to brought forward reserves.
- The Group has also adopted IFRS 9 'Financial Instruments' which did not have any quantitative impact on the financial results.

The impact of the adoption of these standards and the new accounting policies is discussed in note 11.

Significant areas of judgment and estimation

The estimates and underlying assumptions used in the preparation of these financial statements are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The most critical accounting policies and significant areas of judgement and estimation arise from the accounting for long-term contracts under IFRS 15 'Revenue from Contracts with Customers', the carrying value of goodwill and acquired intangible assets and the assumptions used in the accounting for defined benefit pension schemes under IAS 19 'Employee benefits'.

Long-term contracts

The majority of the Group's activities are undertaken via long-term contracts and IFRS 15 requires the identification and separation of individual, distinct performance obligations, which are then accounted individually. The most common type of contracts undertaken by the Group with multiple performance obligations are framework contracts. In most cases, the obligations are satisfied over time and estimates are made of the total contract costs and revenues. In many cases, these obligations span more than one financial period. Both cost and revenue forecasts may be affected by a number of uncertainties that depend on the outcome of future events and may need to be revised as events unfold and uncertainties are resolved. Cost forecasts take into account the expectations of work to be undertaken on the contract. Revenue forecasts take into account compensation events, variations and claims and assessments of the impact of pain/gain arrangements to the extent that the amounts the Group expects to recover and incur can be reliably estimated and is highly probable not to reverse based on most likely outcome.

Management bases its estimates of costs and revenues and its assessment of the expected outcome of each long-term contractual obligation on the latest available information, this includes detailed contract valuations, progress on discussions over compensation events, variations and claims with clients and forecasts of the costs to complete and, in certain limited cases, assessments of recoveries from insurers. Revenue is recognised to the extent that amounts forecast from compensation events, variations and claims are agreed or considered highly probable to be agreed. The estimates of the contract position and the profit or loss earned to date are updated regularly and significant changes are highlighted through established internal review procedures. The impact of any change in the accounting estimates both positive and negative is then reflected in the financial statements.

Management believes it is reasonably possible, on the basis of existing knowledge, that outcomes within the next financial year could require material adjustment. Given the pervasive impact of judgements and estimates on revenue, cost of sales and related balance sheet amounts, it is difficult to quantify the impact of taking alternative assessments on each of the judgements above.

Carrying value of goodwill and intangible assets
Reviewing the carrying value of goodwill and intangible assets recognised on acquisition requires estimation, principally, in respect of growth rates and future cash flows of cash generating units, the useful lives of intangible assets and the selection of discount rates used to calculate present values are set out in note 7.

Defined benefit pension schemes
Defined benefit pension schemes require significant estimates in relation to the assumptions for inflation, future pension increases, investment returns and member longevity that underpin the valuation. Each year in selecting the appropriate assumptions, the directors take advice from an independent qualified actuary. The assumptions and resultant sensitivities are set out in note 9.

IFRSs not applied

The following IFRSs having been endorsed, will be applicable as stated below:

IFRS 16 'Leases' was issued in January 2016. It will result in almost all leases being recognised on the balance sheet, as the distinction between operating and financial leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short term and low value leases.

The standard will primarily affect the accounting for the Group's operating leases and hire charges and is mandatory for reporting periods beginning on or after 1 January 2019. The Group is adopting the modified retrospective approach including an exemption for leases with terms ending inside one year of the date of initial application and will not be restating comparative information. The impact of implementing the standard on 1 January 2019, will be an increase in right-to-use assets of approximately £36.1 million and similar increase in liabilities (approximately £14.4 million current liabilities).

Except for IFRS 16, the directors do not currently anticipate that the adoption of any other standard or interpretation that has been issued but is not yet effective will have a material impact on the financial statements of the Group in future periods.

2 Operating segments

The Group has two core business segments: Natural Resources and Infrastructure plus the non-core business Alcaidesa in Spain. The core segments are strategic business units with separate management and have different core customers or offer different services. This information is provided to the Chief Executive who is the chief operating decision maker.

2018	**Natural Resources**	**Infrastructure**	**Alcaidesa**	**Central costs**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Segment revenue					
External revenue	**383.2**	**1,075.1**	**5.4**	**-**	**1,463.7**
Share of revenue of joint ventures and associates	**7.1**	**18.5**	**-**	**-**	**25.6**
Total segment revenue	**390.3**	**1,093.6**	**5.4**	**-**	**1,489.3**

Segment profit/(loss)					
Operating profit/(loss)	**14.1**	**46.0**	**(0.7)**	**(6.9)**	**52.5**
Share of results of joint ventures and associates	**0.3**	**-**	**-**	**-**	**0.3**
Profit/(loss) from operations before other items	**14.4**	**46.0**	**(0.7)**	**(6.9)**	**52.8**
Other items:					
Pension GMP equalisation charge	**-**	**-**	**-**	**(8.6)**	**(8.6)**
RDEC grant income	**-**	**-**	**-**	**2.6**	**2.6**
Amortisation of acquired intangible assets	**(1.4)**	**(1.6)**	**-**	**-**	**(3.0)**
Employment related and other deferred consideration	**(0.4)**	**-**	**-**	**-**	**(0.4)**
Profit/(loss) from operations	**12.6**	**44.4**	**(0.7)**	**(12.9)**	**43.4**
Net finance expense					**(3.2)**
Profit before tax					**40.2**

2017	Natural Resources	Infrastructure	Alcaidesa	Central costs	Total
	£m	£m	£m	£m	£m
Segment revenue					
External revenue	333.5	1,345.2	5.3	-	1,684.0
Share of revenue of joint ventures and associates	10.4	34.5	-	-	44.9
Total segment revenue	343.9	1,379.7	5.3	-	1,728.9
Segment profit/(loss)					
Operating profit/(loss)	5.0	52.4	(1.4)	(6.9)	49.1
Share of results of joint ventures and associates	0.3	-	-	-	0.3
Profit/(loss) from operations before other items	5.3	52.4	(1.4)	(6.9)	49.4
Other items:					
RDEC grant income	-	-	-	2.5	2.5
Amortisation of acquired intangible assets	(1.5)	(1.7)	-	-	(3.2)
Employment related and other deferred consideration	(1.2)	-	-	-	(1.2)
Profit/(loss) from operations	2.6	50.7	(1.4)	(4.4)	47.5
Net finance expense					(5.7)
Profit before tax					41.8

3 Net finance expense

	2018 £m	2017 £m
Interest income from bank deposits	**0.3**	0.2
Interest income on loans to related parties	**0.1**	0.2
Finance income	**0.4**	0.4
Interest payable on bank overdrafts, interest bearing loans, borrowings and other similar charges	**(3.1)**	(4.2)
Unwind of discount on deferred consideration	**(0.1)**	(0.1)
Interest cost on the net liabilities of the defined benefit pension scheme	**(0.4)**	(1.8)
Finance expense	**(3.6)**	(6.1)
Net finance expense	**(3.2)**	(5.7)

Other similar charges includes arrangement and commitment fees payable. Interest income on loans to related parties relates to shareholder loan interest receivable from investments in equity accounted joint ventures and associates.

4 Taxation

	2018 £m	2017 £m
On profit for the year		
UK corporation tax at 19% (2017: 19.25%)	**(6.6)**	(11.0)
Adjustment in respect of prior years	**3.7**	(0.8)
Current tax expense for the year	**(2.9)**	(11.8)
Deferred tax expense for the current year	**(0.8)**	2.5
Adjustment in respect of prior years	**(3.7)**	0.1
Deferred tax (expense)/credit for the year	**(4.5)**	2.6
Tax expense in the consolidated income statement	**(7.4)**	(9.2)

	2018 £m	2017 £m
Tax reconciliation		
Profit before tax	**40.2**	41.8
Taxation at 19% (2017: 19.25%)	**(7.6)**	(8.0)
Share of results of joint ventures and associates	**0.1**	0.1
Amounts qualifying for tax relief and disallowed expenses	**0.1**	(1.3)
Utilisation of previously unrecognised temporary differences	**-**	0.9
Rate adjustment relating to deferred taxation and overseas profits and losses	**-**	(0.2)
Adjustments in respect of prior years	**-**	(0.7)
Tax expense in the consolidated income statement	**(7.4)**	(9.2)

5 Earnings per share

The calculation of earnings per share is based on profit of £32.8 million (2017: £32.6 million) and the number of shares set out below.

	2018 Number (millions)	2017 Number (millions)
Weighted average number of ordinary shares in issue for basic earnings per share calculation	**106.3**	104.7
Dilutive potential ordinary shares arising from employee share schemes	**2.3**	2.0
Weighted average number of ordinary shares in issue for diluted earnings per share calculation	**108.6**	106.7

6 Dividends

	Dividend per share pence	**2018 £m**	2017 £m
Final dividend for the year ended 31 December 2016	8.40	**-**	8.7
Interim dividend for the year ended 31 December 2017	4.75	**-**	5.0
Final dividend for the year ended 31 December 2017	9.25	**9.8**	-
Interim dividend for the year ended 31 December 2018	5.15	**5.4**	-
Amount recognised as distributions to equity holders in the year		**15.2**	13.7
Dividends settled in shares		**(1.5)**	(1.8)
Dividends settled in cash		**13.7**	11.9

7 Intangible assets

	Goodwill £m	Customer relationships £m	Other acquired intangibles £m	Other intangibles £m	Total £m
Cost					
At 1 January 2017	54.1	15.4	9.7	8.1	87.3
Additions	-	-	-	0.3	0.3
At 31 December 2017	54.1	15.4	9.7	8.4	87.6
At 1 January 2018	**54.1**	**15.4**	**9.7**	**8.4**	**87.6**
Additions	**-**	**-**	**-**	**0.3**	**0.3**
Disposals	**-**	**-**	**-**	**(1.0)**	**(1.0)**
At 31 December 2018	**54.1**	**15.4**	**9.7**	**7.7**	**86.9**
Amortisation					
At 1 January 2017	-	7.9	7.3	6.2	21.4
Charge in year	-	2.3	0.9	0.5	3.7
At 31 December 2017	-	10.2	8.2	6.7	25.1
At 1 January 2018	**-**	**10.2**	**8.2**	**6.7**	**25.1**
Charge in year	**-**	**2.3**	**0.7**	**0.4**	**3.4**
Disposals	**-**	**-**	**-**	**(0.1)**	**(0.1)**
At 31 December 2018	**-**	**12.5**	**8.9**	**7.0**	**28.4**
Net book value					
At 31 December 2018	**54.1**	**2.9**	**0.8**	**0.7**	**58.5**
At 31 December 2017	54.1	5.2	1.5	1.7	62.5
At 1 January 2017	54.1	7.5	2.4	1.9	65.9

8 Cash and cash equivalents

Cash and cash equivalents are analysed below, and include the Group's share of cash held by joint operations of £84.5 million (2017: £87.8 million).

	2018 £m	2017 £m
Cash and cash equivalents	**189.3**	248.7
Borrowings – current	**(10.0)**	(10.4)
Borrowings – non-current	**(60.5)**	(60.6)
Cash, cash equivalents and overdrafts in the cash flow statement	**118.8**	177.7

9 Pensions

A defined benefit pension scheme is operated in the UK and a number of defined contribution pension schemes are in place in the UK and overseas. Contributions are paid by subsidiary undertakings and, to the defined contribution schemes, by employees. The total pension charge in the income statement was £20.8 million comprising £20.4 million included in operating costs plus £0.4 million included in net finance expense (2017: £12.9 million, comprising £11.1 million in operating costs plus £1.8 million in net finance expense).

Defined benefit scheme

The defined benefit scheme was closed to new members on 31 May 2005 and from 01 April 2006 future benefits were calculated on a Career Average Revalued Earnings basis. The scheme was closed to future accrual of benefits to members on 30 September 2009. A full actuarial valuation of the scheme was carried out as at 31 March 2016 and this was updated to 31 December 2018 by a qualified independent actuary. At 31 December 2018, there were 2,858 retirees and 2,962 deferred members. The weighted average duration of the obligations is 16.6 years.

	2018 £m	2017 £m	2016 £m
Present value of defined benefit obligations	**(752.7)**	(803.4)	(827.5)
Fair value of scheme assets	**748.5**	779.5	754.0
Recognised liability for defined benefit obligations	**(4.2)**	(23.9)	(73.5)

Movements in present value of defined benefit obligations

	2018 £m	2017 £m
At 1 January	**803.4**	827.5
Past service cost – GMP equalisation charge	**8.6**	-
Interest cost	**19.6**	21.9
Remeasurements – demographic assumptions	**(25.9)**	16.8
Remeasurements – financial assumptions	**(20.7)**	6.9
Remeasurements – experience adjustments	**3.9**	(34.5)
Benefits paid	**(36.2)**	(35.2)
At 31 December	**752.7**	803.4

Movements in fair value of scheme assets

	2018 £m	2017 £m
At 1 January	**779.5**	754.0
Interest income	**19.2**	20.1
Remeasurements – return on assets	**(29.4)**	28.4
Contributions by employer	**15.7**	12.5
Administrative expenses	**(0.3)**	(0.3)
Benefits paid	**(36.2)**	(35.2)
At 31 December	**748.5**	779.5

Expense recognised in the income statement

	2018 £m	2017 £m
Administrative expenses paid by the pension scheme	**(0.3)**	(0.3)
Administrative expenses paid directly by the Group	**(1.7)**	(1.9)
GMP equalisation charge	**(8.6)**	-
Interest cost on the net liabilities of the defined benefit pension scheme	**(0.4)**	(1.8)
	(11.0)	(4.0)

The GMP (Guaranteed Minimum Pension) equalisation charge results from a decision on 26 October 2018 when the High Court issued a judgement involving Lloyds Banking Group defined benefit pension schemes. The judgement concluded that the schemes should be amended to equalise pension benefits for men and women in relation to GMP benefits and has implications for the majority of defined benefit schemes with liabilities before 1997. The effect of GMP equalisation, which has been recorded as a past service cost, is an increase of £8.6 million on the reported pension liabilities.

Fair value of scheme assets

	2018 £m	2017 £m
UK equities	**-**	128.5
Overseas equities	**80.7**	104.2
Global equities	**52.4**	-
Multi-asset growth funds	**140.7**	-
Multi-credit fund	**90.8**	90.7
LDI plus collateral	**276.6**	-
Index linked gilts	**-**	319.4
PFI Investments	**51.6**	52.2
Property	**21.2**	22.1
Absolute return fund	**-**	52.8
Cash	**34.5**	9.6
	748.5	779.5

Principal actuarial assumption (expressed as weighted averages)

	2018 %	2017 %
Discount rate	**2.80**	2.50
Future pension increases	**3.00**	2.90
Inflation assumption	**3.20**	3.10

Weighted average life expectancy from age 65 as per mortality tables used to determine benefits at 31 December 2018 and 31 December 2017 is:

	2018		2017	
	Male (years)	**Female (years)**	Male (years)	Female (years)
Currently aged 65	**22.4**	**24.3**	22.8	24.8
Non-retirees currently aged 45	**23.8**	**25.9**	24.5	26.7

The discount rate, inflation and pension increase and mortality assumptions have a significant effect on the amounts reported. Changes in these assumptions would have the following effects on the defined benefit scheme:

	Pension liability £m	**Pension cost £m**
Increase discount rate by 0.25%, decreases pension liability and reduces pension cost by	30.3	0.8
Decrease inflation, pension increases by 0.25%, decreases pension liability and reduces pension cost by	26.3	0.7
Increase life expectancy by one year, increases pension liability and increases pension cost by	27.8	0.8

In accordance with the pension regulations, a triennial actuarial review of the Costain defined benefit pension scheme was carried out as at 31 March 2016. In February 2017, the valuation and an updated deficit recovery plan were agreed with the scheme Trustee resulting in cash contributions of £10.0 million for the 12 months to 31 March 2017 and then £9.6 million per annum (increasing annually with inflation) until the deficit is cleared, which would be in 2031 on the basis of the assumptions made in the valuation and agreed recovery plan.

In addition, as previously implemented, the Group will continue to make an additional contribution so that the total deficit contributions match the total dividend amount paid by the Company each year. Any additional payments in this regard would have the effect of reducing the recovery period in the agreed plan. The Group will also pay the expenses of administration in the next financial year.

Any surplus of deficit contributions to The Costain Pension Scheme would be recoverable by way of a refund, as the Group has the unconditional right to any surplus once all the obligations of the Scheme have been settled. Accordingly, the Group does not expect to have to make provision for these additional contributions arising from this agreement in future accounts.

Defined contribution schemes
Several defined contribution pensions are operated. The total expense relating to these plans was £9.8 million (2017: £8.9 million).

10 Related party transactions
The Group has related party relationships with its major shareholders, subsidiaries, joint ventures and associates and joint operations, in relation to the sales of construction services and materials and the provision of staff and with The Costain Pension Scheme. The total value of these services in 2018 was £255.3 million (2017: £211.0 million) and transactions with The Costain Pension Scheme are included in Note 9.

11 Impact of new accounting standards and change in accounting policy

a) IFRS 9 'Financial Instruments' - impact of adoption
IFRS 9 replaces the provisions of IAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting.

The adoption of IFRS 9 from 1 January 2018 did not result in adjustments to the amounts recognised in the consolidated financial statements. Financial assets are held by the Group predominantly in order to collect the contractual cash flows. There is no material impact of adopting an expected credit loss model for impairment of financial assets. Hedge transactions undertaken by the Group meet the requirements of IFRS 9 and are not impacted by adopting the new standard.

b) IFRS 15 'Revenue from Contracts with Customers' - impact of adoption
The Group has adopted IFRS 15 'Revenue from Contracts with Customers' from 1 January 2018, which resulted in some changes in accounting policies and adjustments to the amounts recognised in the financial statements. In accordance with the transition provisions in IFRS 15, the Group has adopted the modified retrospective approach and has restated the brought forward reserves as at 1 January 2018.

Under IFRS 15, revenue recognition is based on the satisfaction of individual performance obligations and where these obligations are satisfied over time revenue is based on the cost profile of each obligation rather than in line with the total contract costs profile. The main change resulting from adopting IFRS 15 is the separation of individual, distinct performance obligations within framework and multiple revenue stream type contracts. This change results in a reduction in revenue recognised in periods prior to 1 January 2018 and a corresponding decrease in the amounts recoverable on contracts in the statement of financial position of £5.7 million and a decrease in opening retained earnings as at 1 January 2018 of £4.6 million, net of current tax. It will reverse over the remaining periods of the contracts. During the year, the Group recognised additional revenue and operating profit of £2.3 million (£1.9 million net of tax) as a result of adopting IFRS 15.

There is no impact on the commercial activities, lifetime profitability or cash flows of the Group, as a result of the adoption of this accounting standard.

c) Research and development expenditure credits (RDEC)
The Group has changed its accounting policy for research and development expenditure credits for 2018 because these credits have characteristics similar to government grants and it is considered more appropriate to offset the income against the relevant expenditure rather than reflect them in the tax charge.

The Group has changed its process for collating this data during the year and this has enabled collection of more current data rather than the lag previously experienced. This will reduce the size of balancing adjustments in respect of prior period grants included in the current year. As a consequence, as part of the policy change the Group has included the prior year amounts in other items.

In the statement of financial position, grants receivable are now included in other debtors and not as a reduction to tax payable and in the cash flow, in cash from operations not tax paid.

12 Forward-looking statements
The announcement contains certain forward-looking statements. The forward-looking statements are not intended to be guarantees of future performance but are based on current views and assumptions and involve known and unknown risks, uncertainties and other factors that may cause actual results to differ from any future results or developments expressed or implied from the forward-looking statements.

13 Responsibility statements

The responsibility statement set out below has been prepared in connection with (and will be set out in) the Annual Report and Accounts for the year ended 31 December 2018.

“Each of the Directors of the Company confirms that, to the best of his or her knowledge:

- The Group accounts, which have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profits/losses of the Company (and of the Group taken as a whole); and
- The Strategic Report includes a fair review of the development and performance of the business and the position of the Company (and of the Group taken as a whole), together with a description of the principal risks and uncertainties that they face."

The directors of the Company are Paul Golby (Non-Executive Chairman), Andrew Wyllie (Chief Executive), Tony Bickerstaff (Chief Financial Officer), Jane Lodge (Independent Non-Executive Director), Alison Wood (Independent Non-Executive Director), David McManus (Independent Non-Executive Director) and Jacqueline de Rojas (Independent Non-Executive Director).

On behalf of the Board:

PAUL GOLBY
Chairman

ANDREW WYLLIE
Chief Executive

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