Market Medals

COMPANY ANALYSIS · DATA AS OF 2026-10-02

COMPANY ANALYSIS · INDUSTRIAL MANUFACTURING

Rolls-Royce

Rolls-Royce Holdings plc

Price to earnings **41×**	Sales growth, last year **+19%**	Sales growth, 3 years **+14% a year**	Operating margin **18%**
Net debt to equity **net cash**	Dividend yield **0.7%**	Earnings growth the price needs **17% a year for 5 years**	Growth on the current path **14% a year (operating profit)**

Widebody engine turnaround: more flying, better service deals · established

Backup power for data centres · scaling

Defence: submarines, bomber engines and new fighter programmes · established

Airlines that buy its engines for long-haul jets usually sign up for decades of maintenance, paying for every hour those engines spend in the air.

Where we land

Three years of sales growing 14% a year show a company that has moved from repair to expansion, led by the engines it makes for big long-haul jets. Rolls-Royce earns most of its engine money from service contracts paid by the hour, so the more airlines fly those aircraft, the more it collects. We award it gold, our highest mark.

One figure needs a warning. Return on equity measures profit against the money shareholders have in the business, and Rolls-Royce shows 106%. A number that high most likely says less about extraordinary profitability than about how thin that shareholder base is. The healthier signs are the steadier ones: margins well above their usual range, net cash, and profits in every recent half-year. The gold is for the business, not a claim that the shares are cheap. They are priced above every large peer, and the price asks for more growth than the current trend delivers.

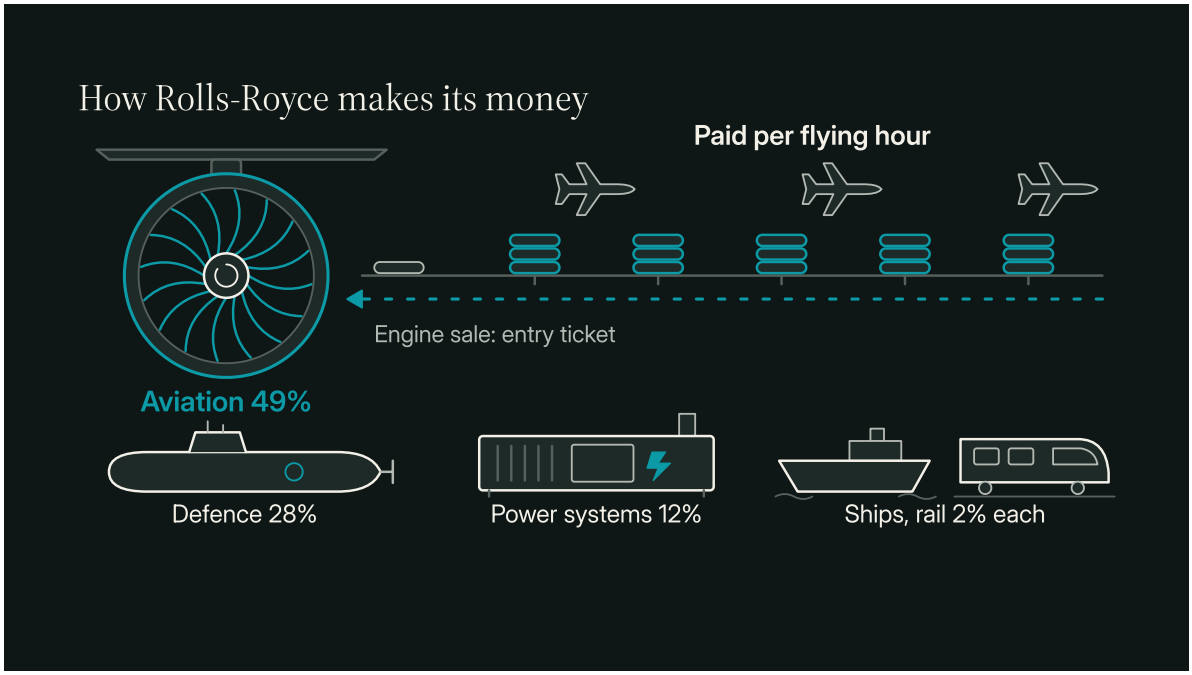


What the business is

Rolls-Royce is mainly a maker and servicer of aircraft engines, with a substantial defence arm and a power-generation business alongside. Aviation equipment brings in 49% of revenue, most of it from the large engines on long-haul passenger jets. Defence manufacturing, which includes submarine reactors and military engines, is next at 28%. Power generation and support products, built around the mtu engines and generator sets, accounts for 12%. Ship-related work and rail equipment are about 2% each.

The structure of the engine business matters more than its size. An airline that buys a Rolls-Royce engine usually signs a long-term service contract and pays by the flying hour. The engine is the entry ticket; the decades of maintenance income that follow are where the money is made. That is why the company's fortunes track how much long-haul aircraft fly, not just how many engines it sells in a year.

The business keeps 28% of each sale after the direct cost of making the product, its gross margin, and 18% after the costs of running the company, its operating margin. The gross figure stands out. Over five years it has had a middle value of 22% and typically moved only about 3 points either side, so the current level is outside the band the company has lived in, not a good year within it.



Why now

Airlines are flying long-haul jets harder, and that flows straight into per-hour service income. The company has also been repricing older service contracts that used to earn too little, and cutting its own costs. More flying, better deals and a leaner cost base are together driving the expansion.

August brought the evidence together. Half-year results were followed by share buybacks and a higher dividend, and Moody's, one of the agencies that grades how safely a company can carry debt, improved its outlook on the company. On the quality of the business, Rolls-Royce now sits among the strongest companies we rate. The market has noticed: the business case is strong, and the price already reflects much of it.

The case for

The first argument is pace. Sales rose 18.6% on the year, faster than the three-year rate. Analysts have only raised their forecasts recently, with five upgrades and no downgrades in the past 45 days, and expect earnings to rise about 16% next year. Few companies in the market grow this quickly, though its lead has narrowed a touch over the past year rather than widened.

The second is the margin step-up. Gross margin has reached 28.4%, a large jump for a business that had been so steady, and it fits the story of repriced service contracts and lower costs. The company was profitable in every one of its last ten half-years, and it holds more cash than debt, so the improvement is not being bought with borrowing. On our measures, the quality of the business sits near the top of the market and has edged up over the year.

The third is how management is using the gains. Coverage called the late-July results stunning and the outlook improving. A company that hands back cash and wins a better credit view in

the same season is confident its earnings are durable.

Where the growth could come from

The large-jet engine business drives results now, and it is still accelerating. Service income on a big installed fleet is both high-margin and recurring. The threat to that margin comes from customers: complaints about engine durability and support, like those from United, are the clearest sign of strain. Success would show as flying hours on large engines continuing to rise in the next results, while repair turnaround times and airline complaints fall.

Backup power for data centres is the fastest-growing second engine. Large data centres need big diesel and gas generator sets for backup and on-site power, and the Power Systems business, sold under the mtu name, supplies them. The company does not break out how much of power generation comes from data centres. Its value is that it does not depend on airline traffic or fuel prices, and strong demand could lift margins in a business that used to earn poor returns. Rising Power Systems orders and margins, with data-centre orders named in results, would confirm it.

Defence is the steady base, and it is already contributing. Higher Western defence budgets are feeding work on nuclear submarine reactors, military engines and new combat aircraft, including a push for a role on India's AMCA fighter programme. Long government contracts make this revenue visible and comparatively low-risk, and new fighter programmes could extend the growth well into the next decade. A confirmed engine role on the AMCA or another new fighter, plus a growing order backlog, would show it working.

Small modular nuclear reactors, built in a factory rather than one-off on site, are an option on the future, not yet a source of earnings. Rolls-Royce SMR is moving from design to real orders, with a reactor supply contract won in Sweden in June alongside Britain's own nuclear plans. Its revenue is not separated out and is most likely very small today, but it makes the company less of a single bet on airlines than it was. Repeat orders could make it a large business line; delays or cost overruns would mainly dent confidence rather than current profits. A firm UK build order moving forward, and more European contracts beyond Sweden, are the signs to look for.

The longest-dated option is a return to engines for single-aisle jets, the short-haul aircraft that make up the biggest segment of air travel. Rolls-Royce has no revenue from these engines today but wants a place on the next generation of such planes. Winning one would multiply the fleet that pays it service income, after years of heavy investment. The signal would be Airbus or Boeing choosing Rolls-Royce, or signing a development partnership, for a new single-aisle aircraft.

The case against

The strongest objection is the price. Rolls-Royce trades at 41 times earnings, meaning buyers pay 41 times the profit attributable to each share. GE Aerospace trades at 37 times, Safran at 35, RTX at 33 and Airbus at 25. Safran is the hardest comparison: similar growth and similar quality at a lower price. Measured by what investors pay for its earnings, sales and assets, Rolls-Royce sits near the expensive end of the market, and it has become more expensive over the past six and twelve months. When a company is this fully valued, good results tend to be already in the price, and disappointments are punished harder.

The second objection is strain among its customers. Brent crude, the international oil benchmark, is at $114 a barrel after rising 62% in three months, and fuel is among an airline's largest costs. If airlines respond by cutting long-haul flying, per-hour service income falls with it. Separately, United's chief executive has publicly criticised Rolls-Royce for lack of engine support, a reminder that the repricing which helps margins can sour relationships with customers who have long memories.

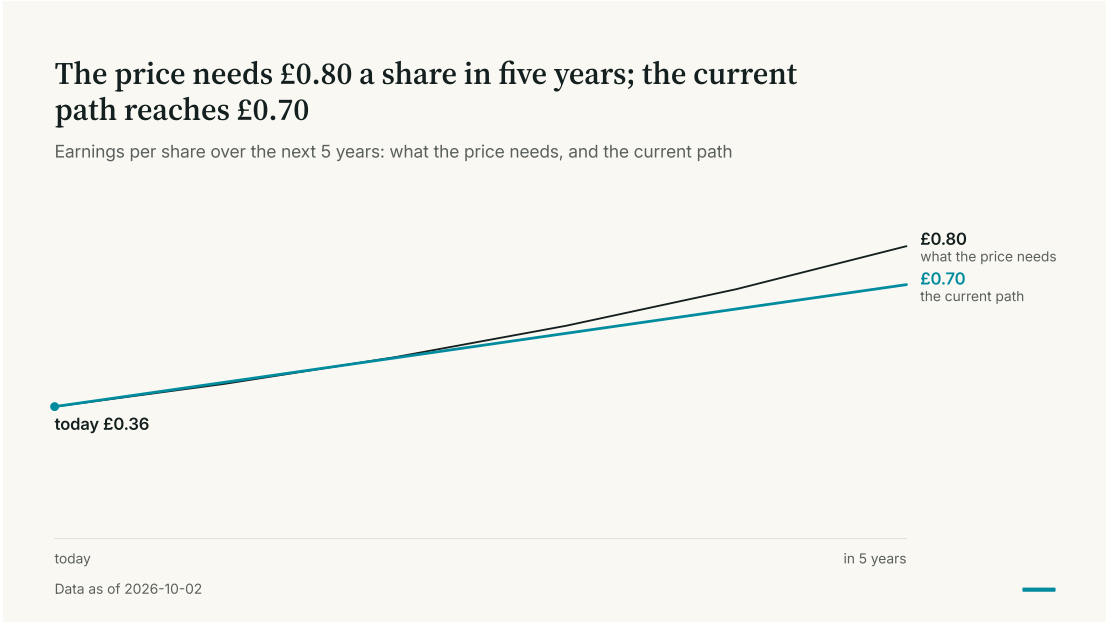
Borrowing costs are a further headwind. The US 10-year government yield, a benchmark for long-term borrowing costs, has risen to 5.29%, euro-area yields are climbing too, and both the Federal Reserve and the European Central Bank have recently raised rates. Higher yields on safe bonds tend to weigh hardest on shares priced for growth years ahead. The share price gives a mixed signal: it has bounced strongly over the past three months, but less briskly than a year ago, which looks more like a recovery than a breakout.

What the price assumes

Suppose the shares stood still for five years and then traded at 18.4 times earnings, the middle value of every profitable listed company we cover. To get there, earnings would need to compound at about 17% a year, reaching 0.80 a share in five years.

The present trend falls a little short. Extending the recent path of operating profit forward arrives at about 0.70 a share, 87% of what the price requires, or roughly 14% earnings growth a year. That is a very good rate, but not quite enough to carry today's valuation without the shares stalling.

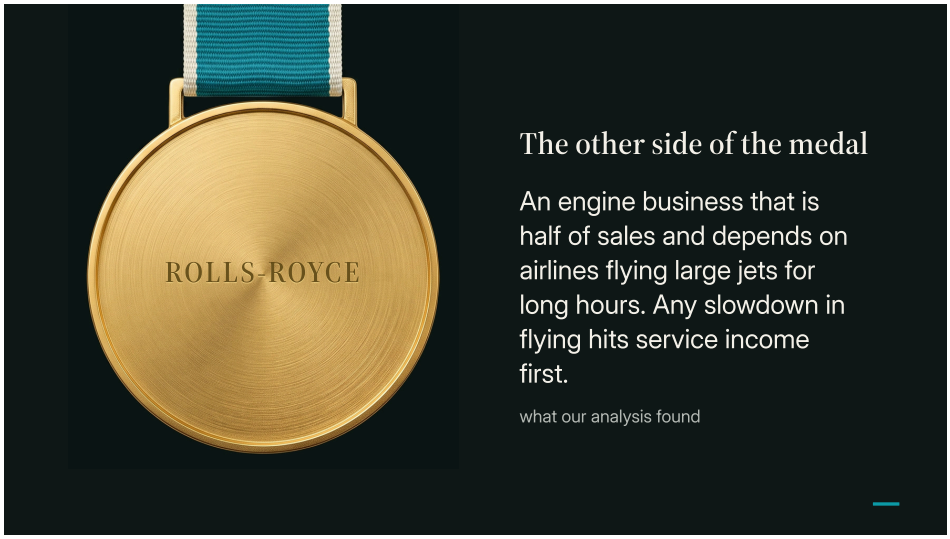
A single smooth growth rate drawn across recent years would mislead, because earnings changed shape partway through as the company moved from repair to growth. The fairer test compares where earnings could plausibly be in five years with where the price needs them to be, and that gap is modest but real. The shares have risen 26% over the past year and 24% over the past six months, which has pushed the price ahead of the trend.

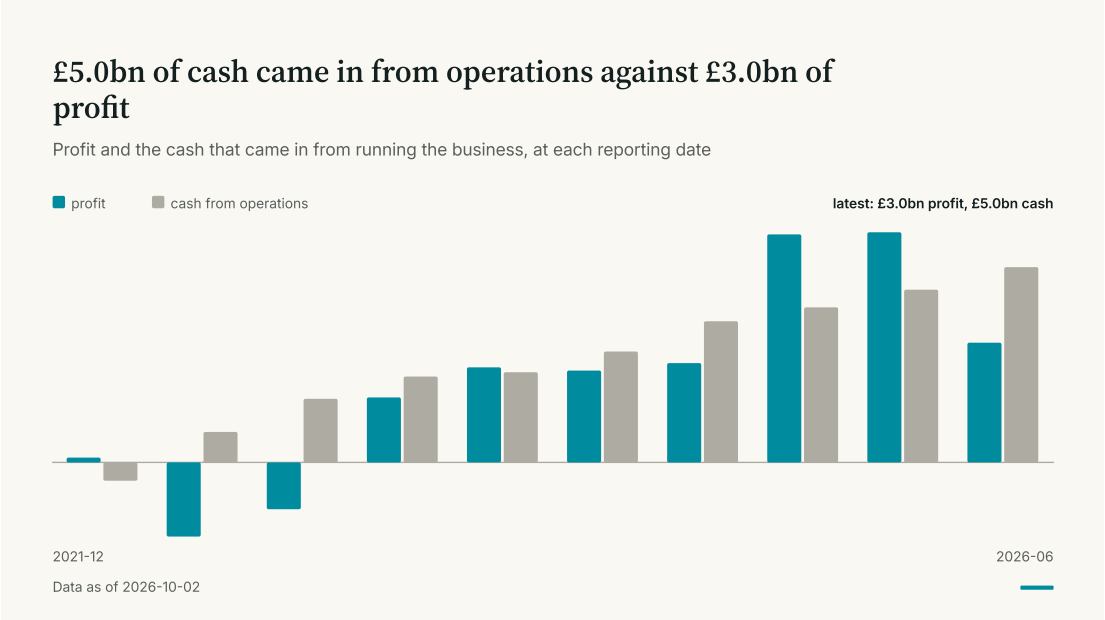


The other side of the medal

The risk that matters most is built into the business that earned the gold. Half of sales depend on airlines flying large jets for long hours, so any slowdown in long-haul flying hits service income first and fastest, before new engine orders or defence work have any effect. The arrangement that turns busy skies into high-margin, recurring income turns quieter skies into a quick shortfall.

The price makes this sharper, leaving little room for a soft patch in flying. With oil where it is, the trigger is easy to picture: airlines trimming long-haul schedules to protect their own margins. The first signs would be flat or falling large-engine flying hours in results, analysts trimming forecasts, or more airlines going public with complaints about support.

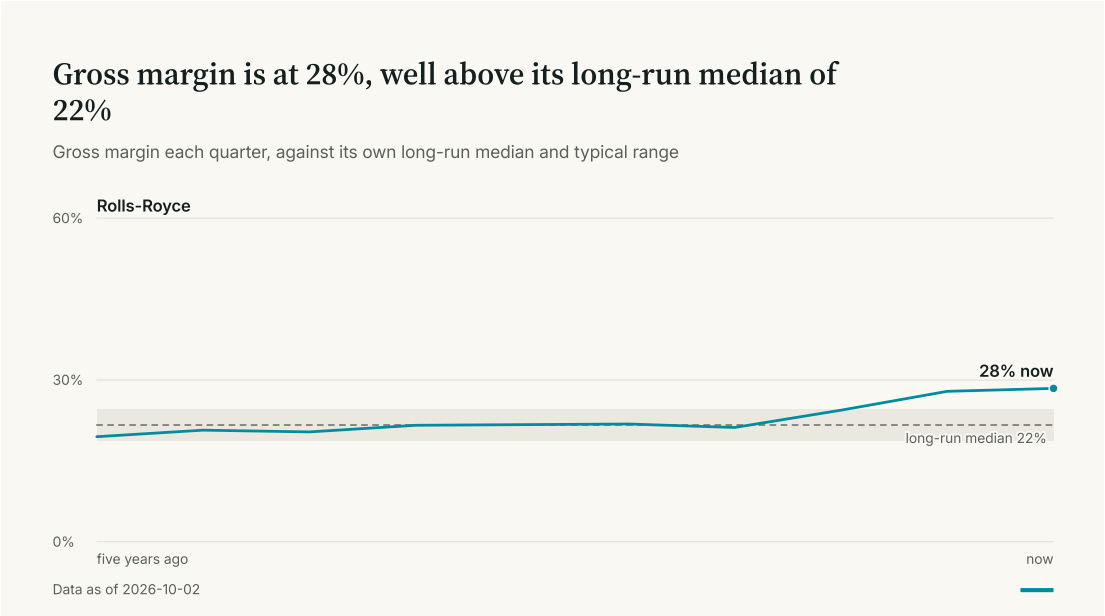




What to watch

The next results are the test. Flying hours on large engines need to keep rising and repair turnaround times to keep falling, because that combination has to deliver the 16% rise in earnings per share analysts expect next year. If both move the right way, the margin step-up looks durable rather than a fortunate peak.

Our reading would be wrong if gross margin slid back toward its recent norm of about 22%, or if analysts began cutting estimates after a long run of upgrades. The likeliest route to either is oil at $114 a barrel squeezing the airlines behind half of Rolls-Royce's revenue.



The numbers

Gross margin	**28.4%**

Operating margin	**18.4%**
Net margin	**13.1%**
Return on equity	**106.5%**
Sales growth, year on year	**18.6%**
Sales growth, 3-year compound	**14.5%**
Price to earnings	**40.7x**
Enterprise value to operating profit	**28.1x**
Profitable results, last five years	**10 of 10 half-yearly results**

The same industry, for comparison

GE Aerospace	**35% gross margin, 37x earnings, profitable at 20 of 20 quarterly results**
RTX Corporation	**20% gross margin, 33x earnings, profitable at 20 of 20 quarterly results**
Airbus SE	**16% gross margin, 25x earnings, profitable at 20 of 20 quarterly results**
Rolls-Royce Holdings plc (this company)	**28% gross margin, 41x earnings, profitable at 10 of 10 half-yearly results**
Safran SA	**14% gross margin, 35x earnings, profitable at 10 of 10 half-yearly results**
Boeing Company	**5% gross margin, 88x earnings, profitable at 4 of 20 quarterly results**
Howmet Aerospace Inc.	**33% gross margin, 49x earnings, profitable at 20 of 20 quarterly results**
Honeywell International Inc.	**38% gross margin, 8x earnings, profitable at 20 of 20 quarterly results**

DISCLOSURES

Market Medals publishes research and model portfolios for information. This is not personal investment advice and not a recommendation to buy, sell or hold any security. Conflicts of interest: the people behind Market Medals may hold shares, or manage funds that hold shares, in companies covered in this report. Data as of 2026-10-02.