Capita plc

2019 Half-year results

Presentation

and Q & A transcript

Capita plc

2019 Half-year results

CEO Jon Lewis

SLIDE 2

Good morning everyone. I would like to offer a warm welcome to the people here in the room. And also, to everyone watching via the webcast. Thank you for your interest in Capita.

SLIDE 3

Before we begin, I'd like to draw your attention to the legal text on the screen. And on page three of your pack.

SLIDE 4

Over the last 18 months we have undertaken significant work to re-engineer Capita:

- We are improving the operational and financial performance of some legacy contracts
- Investing in the systems and processes necessary to better run our business model
- Strengthening relationships with key public and private sector clients, and
- Investing in propositions and our growth function.

We are not taking a short-term view, but addressing structural and strategic issues, many long in the making, to ensure we create a platform for long-term, sustainable growth. We want to create a better-quality business.

We are now beginning to see tangible reward for this effort. In our improving status with clients, and the first signs of organic growth in some parts of the business.

So, the headline is: our transformation is on track. Our guidance for 2019 remains unchanged. And we are reiterating our 2020 targets.

SLIDE 5

Before I hand over to Patrick for a detailed run through of first half financial performance, a quick reminder of our transformation plan, which is underpinned by three imperatives: to simplify, to strengthen and to succeed. Our plan is transforming Capita into a more consistent and predictable business, and one that will generate sustainable free cash flow.

To deliver growth, we are focusing our business on those markets with attractive margins and strong, long-term structural growth trends as we evolve towards a more focused consulting, digitally enabled services and software business.

Independent research estimates the UK market for such services will grow at mid-single to low-double digit rates over the next three years. And it is not as if we are starting from scratch.

TechMarketView, a leading research firm, recently ranked Capita as the leading supplier of Software, IT and Business Process Services in the UK.

SLIDE 6

This slide – as we showed you in March - gives you a clear insight into the progress of our transformation. We are executing against six key transformation workstreams, listed here, with a starting position on the left, and a definition of success on the right.

The light blue dots are progress made to March 2019. The dark blue dots are the progress we expect to make this year. Whilst there have been some puts and takes, I want to emphasise again that overall we are where we expected to be at this stage of our transformation.

In a moment, I will talk about some of the initiatives we are undertaking to pivot to growth.

But before I do that, over to you, Patrick.

CFO Patrick Butcher

Good morning, I am delighted to be with you again today. This is my second results presentation for Capita and I have now been with the Group for a little over 6 months. My first impressions around the reach of what we do have been confirmed. As has the scale and ambition of our Transformation.

As Jon will discuss later, we are making good progress across a wide range of areas, and by the end of the year, with new management and information systems, and the benefit of stabilised and embedded governance, the business will become more predictable and understandable.

SLIDE 8: Financial overview

This slide contains the key financial metrics for the Group. As a reminder, to provide a clearer picture of the Group's performance, we report our results on an adjusted basis. There are fewer adjustments this year and I expect this simplification to continue. However, this year sees the implementation of IFRS16 which has a material impact on our results. To aid comparison with last year, we will be discussing the results before the impact of this change.

Turning to the results themselves, overall, they were in line with our expectations. Revenue is down, mainly reflecting losses in structurally challenged markets in 2018, but excluding those, revenue has stabilised. The lower revenue impacts operating profit, but at the profit before tax level, after the benefit of lower interest charges, profit is pretty stable.

I will cover cashflow and debt movements in more detail later on.

But first a word on revenue.

SLIDE 9: Revenue

I spoke at the full year about changes in some of our markets. Most notably in Local Government and parts of our Life and Pensions business.

These charts show the breakdown that was explained at the full year between those markets in structural change or run-off and the rest of Capita. The chart on the left shows the order book. It is important to remember that around 40% of our revenue does not flow through the Order Book, examples of this include purely Transactional Revenue such as recruitment and some IT sales as well as revenue earned from framework contracts which do not contain volume guarantees, such as the DWP PIP contract.

While the chart on the right shows annual revenues, where, excluding the structurally challenged markets, revenue is expected to stabilise in 2019 before returning to growth in 2020. As Jon will explain later the investment we are making in building the capacity and capability of our growth function and propositions for our clients is central to driving this growth.

SLIDE 10: Revenue change

So far this year there are three main factors that have influenced our revenues.

1. Contracts that we have lost totalling £138m, which you can see on the second bar. These fell into two main categories.

    - The contract came to an end and we chose not to rebid because the contract was either not consistent with our Corporate Purpose or was not consistent with our Business Strategy; or
    - The contract was terminated early

2. The next bar shows the £27m impact of changes to some of our clients' customer volumes (mainly Telecommunication companies) and the impact where for a number of reasons clients have varied scope mainly in local government.

3. Finally, there have been a number of contract wins in IT and Networks and Government Services, totalling £51m, which is already double the total for the whole of 2018.

SLIDE 11: Divisional revenue

This slide presents a different perspective on revenue and shows the impact of the change by division.

The slight reduction in Software revenue is as a result of an unusually large licence deal in the first half of 2018. Project revenues in Government Services have been strong. However, reductions are expected in the second half as the local government contract terminations discussed earlier start to take effect. Specialist Services revenue also reflects the reductions in Life and Pensions mentioned earlier.

SLIDE 12: PBT

For this slide which shows the change in Profit Before Tax, I am using the divisional breakdown. The first impact shown on the slide is a one-off profit related to the termination of the Marsh contract in 2018.

The reduction in revenue has had an impact in the relevant divisions. However, cost reductions which have realised £38m in the first half across the business are starting to have a real impact, in some divisions, Software, Customer Management and Specialist Services.

Profit in all divisions and in particular in Central Functions has also been affected by the investment of around £23m in professionalising our corporate functions, the costs of Cyber and GDPR and investment across most divisions in addressing service delivery challenges. In addition, we have invested £5m in building sales capacity and capability that will be critical to future revenue growth.

SLIDE 13: Divisional

This slide provides a breakdown of financial results by division. I will not spend much time on this slide, which highlights the wide spread of profitability and margins between divisions. Jon will provide more colour on a division by division basis later in the presentation.

SLIDE 14: Free cash flow

This slide is still more complex than I would like, because a clear presentation of free cashflow is essential to an understanding of our business.

The working capital outflow is reduced as the investment of £146m to normalise period end cash management rolls off.

I have combined the movement in Deferred Income, Accrued Income and Receivables as movements between these categories are influenced by timing differences. The slight increase in outflow reflects the net impact of advanced billing in the Software and IT and Networks divisions, offset by a lower deferred income release on Local and Central Government contracts.

The movement in Trade payables is a result of further investment in improving supplier payment terms and payment differences at period end.

As expected, capital investment is higher and is discussed on the next slide.

SLIDE 15: Capex slide

Net capital expenditure so far this year has been £64m. The major items of investment included:

- Continued progress in upgrading of our financial systems, to improve financial reporting, processes and controls.
- The investment in software to drive new propositions and enhance existing products can be seen coming through these numbers. We are very focussed on driving business cases to increase this investment and deliver revenue growth.

Looking forward, we still expect to invest around £500m between 2018 and 2020.

SLIDE 16: FCF to ND

This slide shows all cashflows that are not included in free cashflow. These include known and expected commitments, such as the £48m investment in business restructuring, and the second of three significant payments under the Pension Deficit Recovery Plan. In the period we used some of our surplus cash to repay a £100m Term loan.

SLIDE 17: Net debt chart

This is a new slide, which shows Net Debt on a 7-day rolling average. It illustrates two major changes. The first is the reduction in Net Debt following the Rights Issue and two business disposals which have significantly strengthened our Balance Sheet. The second is the reduction in period end volatility which was a feature of the cash management activities that we no longer undertake. This is calculated by comparing the Net Debt at the beginning and end of the relevant month, June or December. It is highlighted by the arrows for example £307m in December 17, compared to £59m in June 19. I have looked at the chart going further back and volatility was even higher. I think that this chart marks a step forward in our transparent disclosure agenda.

SLIDE 18: Gearing slide

This slide further highlights the scale and impact of the de-gearing of the balance sheet that took place in 2018. Total liquidity remains around £1bn including cash of £377m and the RCF of £600m. This liquidity provides the business with the financial resources it needs to support the ongoing transformational change and investment.

SLIDE 19: IFRS16

As I said earlier, the impact of IFRS16 will be significant. An increase in Assets and Liabilities of 568 and £644m respectively. Lease rentals are replaced by Depreciation and Finance Charges, improving operating profits and margins, BUT, because of the mix of lease lengths there is a reduction in profit before tax.

SLIDE 20: Guidance

The Group is in the second year of a major transformation. The successful delivery of this programme of change and in particular the revenue growth cost savings initiatives is critical to the future performance of the Group.

Net finance costs are expected to decrease to around £40m.

Profit before tax is expected to be within the range of £265m-295m

As usual the key variables in the range are the delivery of the cost savings and the timing and impact of contract wins and revenue growth as well as contract, restructurings or terminations. The cost reduction plan is weighted to the second half of the year.

We expect our Net Debt to EBITDA ratio to remain within our target range of 1 to 2 times. However, as a result of the Pension Deficit contributions and accelerated investment and restructuring it will remain in the top half of the range, for this year.

All these exclude the impact of IFRS16, however the expected impact of the changes are shown in an Appendix.

Thank you for your time and attention and I look forward to your questions, but I will now hand you back to Jon.

CEO Jon Lewis

Thank you, Patrick.

I am pleased with the progress we are making to transform Capita.

We continue to recruit the right talent, as evidenced by the executive hires we have announced today, have put in place a more effective operating model and procedures, and, by the end of this year, will have the appropriate management information systems in place. We continue to transform at pace.

SLIDE 22: Responsible Business

As we talked about at the full year results, at the start of the year we launched Capita's first pan-organisational operating model. This is the foundation for us to act as 'One Capita' and enables us to deliver more consistently and live our purpose: 'to create better outcomes'.

I am pleased with the organisation's adoption of our operating model, which is bringing much needed clarity to how we run the business and facilitating much more collaboration across Capita, particularly on client propositions.

A good example of this would be the work our consulting organization is doing with the Data Communications Company to propose a solution to better predict power demand for a utilities supplier. We still have work to do in driving the cultural change required at Capita, but we are pleased with the progress being made.

Our purpose speaks to our responsible business strategy, an area where we have made encouraging progress in changing key stakeholder perceptions of Capita.

For instance:

- Capita is the only LSE-listed company to include two non-executive employees on its board of directors. We've done this for multiple reasons, but primarily to help bring our 63,000 colleagues with us on our multi-year transformation.

- We have produced our first ever 'supplier charter', outlining how we operate and work together with our 35,000 suppliers, laying out the core principles by which the company does business and what Capita expects from its suppliers in return.

- Capita is also committed to meeting the Government prompt payment code, ensuring full compliance on payment terms for our micro and SME suppliers in particular. In aggregate, Capita has met the requirements of the code for the last 12 months and was recently recognised by No 11 and the Federation of Small Business for being an "exemplar" in this regard.

- We have made a further scheduled payment to reduce our pension deficit in line with a commitment we made to reduce our actuarial pension deficit as a matter of priority, and

- We are seeking accreditation from the Fair Tax Mark this year.

These, and the other tenets of our responsible business strategy will be published in our first responsible business report later this quarter.

SLIDE 23: People

Capita's most important asset is our people, and I want to take this opportunity to thank our colleagues, many of whom are listening in this morning, for their hard work and commitment to our transformation journey.

At a business-to-business-to-customer (or B2B2C) services company, we are only as good as the ability of our colleagues to consistently delight our clients' customers.

For this reason, it is vital we invest to bring our people with us on our transformation journey.

We have launched our HR Vision 2020 which, pan-Capita, defines for the first time such things as career paths, training opportunities through the newly formed Capita Academy, and Capita's first ever employee performance and succession management system in order that colleagues have clearly defined objectives and clear oversight of performance against them.

These actions are a tangible demonstration of our focus on, and investment in, people at Capita, something that is core to attracting, developing and retaining the right talent, and analogous to what you would expect in any digitally enabled services firm.

And as you can see, our people are choosing to stay for longer.

And the rating employees are ascribing to us as a desirable place to work is trending upward - our Glassdoor rating is at a 4 year high.

We are already seeing a positive economic return from these actions.

For instance, through greater employee engagement in our Customer Management business, we have increased retention and reduced associated costs of recruitment and training by £5m in the last year.

We have also continued to recruit significant talent into the business and at multiple organizational levels.

The executive committee continues to evolve as we build a team to deliver both the near-term operational improvements, and long-term, sustainable growth.

Andy Start joins us this week as our new head of Government Services, and Chantal Free and Aimie Chapple join us in October to head up our People Solutions and Customer Management Divisions respectively. You will find short bios for each of them in the Appendix of the slide pack, but in summary, these proven executives bring the skills to deliver our strategy.

We remain very focused on increasing diversity and inclusion, and for the second year in a row, have submitted improved gender diversity statistics to the Hampton-Alexander review.

SLIDE 24: Managing contracts

I have spoken previously about three significant contracts that presented Capita with operational, reputational and financial challenges in 2017 and 2018.

We are continuing to make encouraging progress here and have made improvements against delivery of their key performance indicators.

For example, in the first half of 2019, we delivered a successful advertising campaign that resulted in the highest level of basic training starts of regular soldiers since we started the Army Recruitment contract in 2012.

In June, Richard Baynham from the National Audit Office said: “It is clear that the higher level [of engagement] of last summer has been translated into action, intent and delivery.”

The second contract is Primary Care Support England, better known as PCSE, for NHS England.

Our operational performance on PCSE is now stable and delivering on the vast majority of its KPIs.

Our new digital solutions for ophthalmic payments and Performer Lists were successfully tested last month, and we will roll these out in the second half of this year. These will enable us to materially improve the end-user experience and significantly reduce the cost of service on this contract in 2020.

We have delivered on the digital transformation of our contract with Mobilcom-Debitel. We are meeting all our key performance indicators and our focus is now on driving further efficiencies to reduce the cost to serve, through amongst other things, the adoption of automation technology.

As a result of these operational improvements, we continue to plan to generate an aggregate profit on these contracts in 2020, including reaching break even on the PCSE and mobilcom-debitel contracts by the end of that year.

SLIDE 25: Recent successes

We will continue to update you on our progress with those contracts.

Our ability to deliver on contracts today is helped by our improved governance and controls: as we are being much more selective and disciplined with the scopes of work we bid on in the first place..

And there is the professionalising of our project management function, including the use of our programme management tool, *Evolve*.

Today, by far the majority of our contracts are being executed on time, on budget and to specification.

For instance:

- Capita has implemented and now operates central London's Ultra Low Emission Zone (ULEZ) system. This was a complex implementation, with highly sophisticated technology, that went live with no operational start up issues.

- We had several successful go-lives for our ControlWorks Emergency Control Room solution with several major police forces in the UK and 6 police forces in the United States are now live on 911eye.

- We set up the help desk to support Key Stage 1 and 2 on our Standards and Testing Agency (STA) contract, and the digital solution underpinning the delivery of this contract is due to go live in the second half of this year.

- Capita achieved the best service delivery, highest quality scores and lowest complaints ever on its contract with O2 in H1 2019. And we have been working with O2 since January to develop a new model for premium Customer Service and are investing in a multi-channel messaging platform, which will replace the current O2 webchat service during Q4.

And by being there with our clients, delivering strong service performance day after day, of itself creates new opportunities which historically we didn't focus sufficiently on. The growth of our business with Transport for London in the last year is a case in point.

SLIDE 26: Cost competitiveness - Operational excellence

Operation excellence is one of the key transformation workstreams by which we will continuously improve our competitiveness.

There are three elements to this workstream:

- First, we have a programme of continuously improving our operations, clearly defining and standardising our processes, using lean methodologies to drive productivity and making better use of operational data.
    - And, most importantly, reducing the cost of poor quality and cost to serve.

- Second, we continue to benefit from the 12,000 colleagues we have in our global delivery centres in India, South Africa and Poland, who deliver exceptional service for our clients.

  We expect to add in the region of 800 people to our organizations in India and South Africa this year, including further expansion of our Digital Development Centre, our shared services support for the Functions and contact centre agents.

- Third, we are also focussed on playing a leading role delivering automation, robotics and artificial intelligence-based solutions.

    - In the first half of 2019, we became a regional partner of UI Path, one of the world's largest Robotic Process Automation providers.

    - And we now have more than 100 developers, analysts and programme managers working at our newly established Automation Centre of Excellence in Birmingham, leveraging not just UI Path, but our strategic relationship with Microsoft to deliver this from the cloud.
    - On the back of voluntary attrition, we expect to reduce our headcount by 3% through the use of automation by the end of 2020 and also offer this as a service to our clients through our consulting practice in due course. Automation also allows us to focus colleagues on more value adding activities for our clients.

As a result of these actions and others, we remain on track to deliver £175m in savings by the end of this year.

SLIDE 27: Investing in capabilities

Patrick has talked about some of the investments that we are making to improve Capita's management systems, and modernise and professionalise the way the business is run.

Over the next two slides, I want to give you some colour regarding the increasing proportion of our investments that we are now making into growth.

First, I want to tell you about two new digital products that we will launch in the second half of this year in the human resources sector.

The first product involves the digitalisation of Security Watchdog, our existing UK market-leading pre-employment screening service, with current revenues in the region of £30m per annum. It fulfils an important role for clients, helping them to make appropriate recruitment decisions and preventing illegal working and identity fraud.

We are building on our existing domain expertise, creating a digital version of the process that is both more efficient and comprehensive in the background checks it undertakes on individuals.

Using advanced analytics and integration with open data sources, we are significantly shortening the average screening cycle times from 25 days to 5 days.

We are also working with channel partners such as Workday and SAP to make this digital service available to their customers. Security Watchdog will be the only screening service to be included in the Workday partner marketplace in the UK from the fourth quarter.

We are one of the first in the market to offer a digital screening solution, developed by us in partnership with our established portfolio of blue chip HRO clients.

The second product is a new digital onboarding application, which is a neat fit with the new Security Watchdog offering.

This product is designed to significantly improve the experience of new employees, particularly in the period between accepting a new role and starting it.

We have developed this product for our own use, and alongside existing and new clients in sectors such as retail, hospitality and financial services, to create a digital solution that:

- Engages new employees between offer acceptance and their first start date.
- Enables new starters to be more productive from Day 1.
- Increases retention in those sectors where the highest turnover is in the first few weeks of employment.

Both products will contribute to the growth of our People Solutions division in 2020.

Historically, Capita would have acquired such innovation. These solutions represent two of a growing number of examples of organic, digital innovation at Capita.

SLIDE 28: Reigniting growth

This is an area where we need to make significant progress in 2019 to deliver an acceptable level of revenue growth.

We made real progress in the first half, and believe we have now put in place the foundations for growth:

- First, by pooling existing consulting capabilities in data analytics and digital experience at the group level, and combining these with 20 new partner level hires from global professional services firms, we are using consulting more strategically to create revenue opportunity. Through consulting engagements, we believe this proven model will generate more pull through revenue for the rest of the Divisions.

- Second, by ensuring we have the right competencies across our growth function to change the types of conversation we have with our clients and that we close the right scopes of work. To this end, we are adopting a consultative selling model within our sales function and have delivered sales methodology training to 650 front-line sales executives in the first half.

  The recent expansion of the scope of our contract with Southern Water to provide end-to-end customer services, billing and collections is a great example of working consultatively with a client to create additional value for both parties.

- Third, by providing better client advocacy through classic account management and industry segment expertise.

- Fourth, we are investing in our CRM systems, to better define and track the pipeline of opportunities we have, allowing us to allocate sales resources more effectively and, ultimately, improve sales accountability.

Through the above, we are identifying client opportunities more proactively and will win a higher percentage of our revenues through non-competitive processes.

Already, this work is paying off…

Our pipeline of opportunities is growing and revenues in our core businesses are pivoting to growth.

And our consulting practice has won several engagements including:

- implementing artificial intelligence to support a German TelCo with better customer retention
- automating processes for a client in the financial services sector, and
- supporting a major retail bank to implement agile working practices.

SLIDE 29: Recent wins

Capita was awarded contracts worth £830m that went into the order book in the half year. Of course, this figure does not include the work we win on framework contracts or transactional work – which is a significant percentage of our revenue.

Our Software division performed particularly well, winning a number of contracts in the emergency services and utilities sectors.

These included contracts for communications with Metropolitan Police, records management for Police Scotland and a new contract with SSE Business Energy to support the delivery of the next generation of smart meters.
Customer Management has extended its contract with Carphone Warehouse for a further 5 years.

And IT & Networks won more work with Transport for London and a new contract with Energia.

Momentum has picked up since the HY…

We have recently announced:

- A £525m contract to modernise and support improvement to the operational effectiveness of the Ministry of Defence’s fire and rescue service, and
- A projected £145m extension of our contracts with the Department for Work and Pensions and the Department of Communities in Northern Ireland to deliver Personal Independence Payment (PIP) assessments.

Both awards are a measure of the confidence and trust government has in Capita’s ability to deliver critical public services.

SLIDE 30: Divisional summary

This slide contains an overview of the broad range of progress we are making in each division.

Over the next 6 slides I will take you through some of the highlights for each division, starting with Software.

SLIDE 31: Software

We are a top 5 software business in the UK, with high margins and good cash flow, a strong platform for growth.

There were a number of important milestones in the half year:

- First, our Software order book increased by 6% and our book-to-bill ratio exceeded 110%, giving us confidence for our ambition for 2020.

  In addition to the wins already mentioned, we won a new contract for a Police force in North Africa and we extended our contract to support UK ambulance radio terminals, communication and mobile data solutions from 2020 for a period of three years.

- Second, we have continued to invest in our Digital Development Centre in Pune, which now employs more than 1,300 people supporting both categories of software development at Capita:
  - that we sell though our classic software licensing model in Capita Software, and
  - the proprietary software platforms we develop for our digitally enabled services.

- Third, we have made encouraging progress in the US.

We continue to expect to grow division revenues from the second half of this year and target at least mid-single digit growth in 2020.

SLIDE 32: People solutions

Last year we brought all of Capita's Human Resources businesses together under a single leadership team for the first time, creating our People Solutions division, which provides services across the employment life cycle.

In the half year:

- We created a new data and analytics platform to support the modernisation of existing and launch of new digital solutions.

- We won several new contracts, including resourcing services for the Home Office, learning services for Network Rail, pensions administration for a leading pensions insurer and screening services for Nestle.

- We increased investment in client service which took priority over actions to reduce costs and impacted margins in the first half.

- The proportion of our clients taking more than one service has doubled, admittedly from a low base, in the last year and there remains significant opportunity to sell more to them.

SLIDE 33: Customer management

Capita is a leading provider of customer engagement services in the UK, Switzerland and Germany, with a strong presence in the telecommunications, retail and utility sectors.

In the half year in addition to the awards already mentioned, we expanded contracts with British Gas and

SLIDE 34: Government services

Government Services remains a key segment for us, with many long-term contracts, strong relationships and cash generation.

Government is no different to the private sector in its need to embrace digital transformation as a means of addressing budgetary pressures and improving how it serves its citizens.

In the half year:

- We have identified 200 opportunities to use automation to improve productivity, from using on-line forms on our Gas Safe Register contract to automating the downloading of files from 82 NHS databases on our PCSE contract.

- In local government, we have separated our operations into growth services – scalable, repeatable digital solutions such as revenue and benefits collection and planning services - and legacy multi-service contracts that are in structural decline. We are working closely with councils such as Birmingham to agree and manage a smooth transfer of services back to local authority management.

SLIDE 35: IT & Networks

We are a top 10 player in UK IT and network services.

Having brought our IT businesses together last year, we have increased the use of shared service centres and common processes and can provide end-to-end enterprise services to mid-sized third party customers, government and other parts of Capita.

We are now beginning to pivot toward growth, building our sales capability and developing new products.

In the first half:

- We continued to modernise and strengthen our IT infrastructure, by investing in our data centres.

- We began to transform Transport for London's network estate and won additional work with them to deploy cellular infrastructure in the London Underground and to facilitate the delivery of dedicated mobile connectivity for the emergency services.

- We won a new contract with Energia and extended our contracts with the Education Authority Northern Ireland and Liberata.

- We have begun to see the first evidence of improving sales trajectory in our pipeline which has increased significantly (by nearly 50%) since the end of last year.

SLIDE 36: Specialist services

Specialist Services includes:

- Our financial services & regulated operations
- Government & specialist commercial partnerships
- And other stand-alone businesses such as travel, print and property

We are managing these businesses to optimise their value and each business has its own strategy.

In the first half:

- We stepped up our efforts with some of our closed book clients in Life Insurance to seek better long-term solutions for both parties.

- We further developed our partnership with Zurich by bringing all of their UK customer service operations together and taking responsibility for administering their new Life Protection proposition, a market leading set of products and digital services platform.

- We took a number of actions to reduce our costs, limiting the impact of last year’s loss of Prudential and Marsh.

SLIDE 37: Wrap up and thanks

So, to recap…

We continue to transform Capita into a more predictable, lower risk business.

A year and a half into our multi-year transformation plan we remain on course, including the generation of at least £200 million of sustainable free cash flow in 2020 … And double-digit margins.

Thank you.

Patrick and I are happy to take questions.

Q&A

Paul Sullivan:

Thank you very much its Paul Sullivan from Barclays. Just firstly, you seem to have quite a lot of confidence and visibility on the software business and you are sort of given a hard target for second half of the next year. Could you talk about the other parts of the portfolio and how you envisage them performing in the second half? That's the first one. And just tied to that, the order book for the digitally enabled part of the business ex-software looked like they were down year on year so again, what is going on there and is it more phasing than anything else? And then local government, would you help us be splitting out the revenue decline you saw there? Because as it sounds like it did better than expected, but is sounds like it is going to get worse before it gets better, unless it doesn't get better.

Jon Lewis:

So Paul, you are asking a level of detail there we're probably not going to satisfy you on I'm afraid. Clearly we are now, and we did do on the full year results, distinguish between what we call the structurally challenged elements of Capita - local government, local government multi-service contracts, we are not exiting the local government markets I hasten to add, as well as our Life and Pensions business and I think there is a very helpful slide, it was slide 9 I think it is in Patrick's section, which speaks of course to what is happening to revenue overall. If we look at the non-structurally challenged parts of Capita, what you might wish to refer to as core Capita going forward, then clearly revenues have stabilised and on the basis of the order book and what we are forecasting for the second half of the year, we are starting to pivot to growth in some of those businesses. I am not going to get in to detail as to which are and which are not. They are each at different stages in their evolution, but the very fact that revenue decline has stabilised after many years of decline I hasten to add, is encouraging obviously.

Patrick Butcher:

Just picking up one or two perhaps slightly more specific points. You are correct within government services because the revenue grew and we are expecting in some of those local authority contracts to go in second half of the year, the impact of that whilst still sooner than we first thought is now later than we second thought. As we look to revenue for the whole of the year, we are comfortable with where consensus is which roughly means that revenue in the second half will be the same as in the first half. The important point on order book is that about 40% as I mentioned of our revenue doesn't go through the order book, so that isn't the sole measure of how we feel about the future and in fact if you take the DFRP contract alone and had we signed that in June rather than in July then actually the order book would have been flat so the order book itself is heavily influenced by the timing of signing extensions or big contracts so it's a much better thing to look at over a longer time horizon rather to over-react to six month windows.

Rob Plant:

Rob Plant from Panmure Gordon. Has the change of government and the focus on Brexit had any impact on activity on your central government businesses generally? Thanks.

Jon Lewis:

To date no. There have been some modest engagement opportunities that we have undertaken for various government departments to help them with their Brexit planning. Clearly there is potential to do more as government furthers its Brexit planning and obviously there have been statements in the last week about the commitment of funds to achieve that. None of that today is coming our way but are we going to actively engage with central government given the degree to which we have improved contract execution and relationships with central government to see what we can do to help them with Brexit planning, well of course we would.

Tom Sykes:

Morning, thank you. Tom Sykes from Deutsche Bank. Few questions please. Firstly, just on the PCSE deal, I think in the second half you get a milestone payment from switching on the ophthalmic admin system or whatever it's termed, but in H2 do you therefore get the milestone payment and a cost saving and so therefore you get a double benefit in H2? And then are there any other milestone payments to think about on that contract please? Just in terms of the second half, you gave that adjusted free cash flow slide where you were about minus 20 million or so when you considered the movement in year on year organic revenue and the movement in deferred income, would you expect that adjusted what was minus 20 million to then be actually a positive number in the second half of this year now? Is that the scale of cash improvement that we're seeing? And maybe, is it possible to give some kind of view on the scale of larger contracts that you're actually bidding on? Some kind of visibility on whether there are other defirmo type contracts, customer management contracts, of reasonable size that you're actually in a competitive process on now that you'd expect a decision on in the next 6 to 12 months please?

Jon Lewis:

So, Tom thanks for the question, I'll do one and three and then Patrick can do two. There is no milestone payment on PCSE in the second half of this year, that's not how that contract is constructed. We will realise the benefits of that contract as and when we deliver the cost savings to the client. We will largely reallocate a significant number of people in that contract to other opportunities we have through 2020 and it will be through the reallocation of that resource that we will realise the cost savings, and they are material, and they are one of the key reasons why we are stating that the contract will turn to profitability at the latest by the back end of 2020.

You might want to do two Patrick.

Patrick Butcher:

So on the cash flow it was as you said a small outflow where we're talking about broadly flat over the year so it will be a small positive in the second half but not significant. What causes that difference; capex is probably going to be slightly higher in the second half and the restructuring, it is not free cash flow but a net debt that restructure will be a little bit higher. Working capital, we are guiding differed income will be somewhere between 100-150, it's quite volatile depending on the exact timing of any further contract restructuring.

Jon Lewis:

Tom, to your third question. I said in our prepared remarks that we are encouraged by the growth in the pipeline, particularly as we have invested in our growth function and that pipeline includes some material large contracts that we are going to be bidding on through to the end of this year and into 2020.

Tom Sykes:

Okay, nothing more you can give us? You are bidding on something, but that's it?

Jon Lewis:

There are large contracts in government around the provision of, for example HR back office services, there are similarly large contracts in government around training. These are in the hundreds of millions not the tens of millions. We have a number of opportunities in the financial services arena for a very large bank, that's probably all I want to say at this stage, given that we are in a competitive process on some of them and we're progressing in a non-competitive dialogue on others.

Tom Sykes:

Would you expect any announcements on them in H2 this year or is that into H1?

Jon Lewis:

I learnt a long time ago never to predict when you can close a contract with Government in particular. I'm afraid I'm not going to change that policy. We bid on Defence Fire and Rescue three and a half years ago and we closed it in July of this year. It just would be inappropriate for me to voice a timing. We are progressing them very actively, we're very engaged. We have a much more professionalised growth function today to engage with clients on those sorts of opportunities but some of these will close when they close.

Thanks very much everyone for your interest in Capita this morning. Thank you.

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