

Capita plc

Pre-close trading update

Intention to sell the majority of Capita Asset Services

Capita plc (“Capita”) is today issuing a pre-close trading update for 2016. In addition, following a group-wide business review, we are announcing the Board’s decision to dispose of the majority of the Capita Asset Services division (“CAS businesses”) and a small number of other businesses which no longer fit Capita’s core business strategy. These actions will consolidate Capita’s position as the UK’s leading provider of customer and business process management services, while underpinning the Company’s balance sheet.

Capita Chief Executive, Andy Parker, said “We are committed to delivering good returns to shareholders, supported by a strong capital structure and a clear growth strategy. In recent months, we have reviewed our management structure, operating model, business portfolio and our leverage to ensure we are in the strongest position to support future profitable growth.

“In November, we announced changes to our management and business structure and today we are announcing our intention to sell the majority of our Capita Asset Services division and a small number of other businesses. We have also commenced a programme of cost reduction and investments to position the Company strongly for renewed future growth. Together, these actions will create a leaner Capita, focused on its core strengths and with a much stronger balance sheet.

“I am confident that the markets Capita addresses offer long-term structural growth. We are however currently facing some near-term headwinds, which continue to make 2016 a challenging year and will affect trading performance in the first half of 2017. Our long-term contracts provide us with good revenue visibility across the year and the structural and cost reduction actions we are taking now will support progress in the second half of 2017 and into 2018. We therefore currently expect a similar trading performance to 2016 in the full-year 2017.

“Our new divisions are now fully aligned to the markets in which they operate and the divisional sales teams are working seamlessly with the central major sales team to better address these markets and fuel greater organic growth in 2018 and beyond.

“The decisive steps we have recently taken and those we are announcing today make us a more resilient business, committed to generating organic growth, maintaining and then growing our dividend and delivering sustained value for shareholders.”

A simpler business, with a clear strategy and a continued focus on organic growth

We remain focused on providing the expertise and capability to deliver technology-enabled outsourced solutions and professional services that make processes smarter, organisations more efficient and customer experiences better.

Our three core objectives are:

- *the development of market-leading proprietary solutions that make use of the latest technical innovations and draw on our existing IT, digital and software operations to create value for our clients

*a continued focus both on the UK market and a gradual extension of our presence across selected growth markets overseas

*and, through the above, the delivery of earnings per share growth, strong cash flow and return on capital, by generating profitable organic growth and investing in incremental small to medium sized acquisitions, where they support our core strategy and meet our strict returns criteria.

To ensure Capita is best positioned to deliver on this strategy, we recently announced a wide-ranging restructure to simplify our business model and provide greater management strength and depth across all of Capita's operations.

Reorganising our 11 divisions into six market-facing divisions (five post the CAS disposal) will reduce complexity and increase oversight, providing better accountability with a more streamlined management structure, reporting directly to the Chief Executive. The divisions' sales teams have been aligned with the central major sales team to strengthen our sales efforts, enhance our sales propositions, and better penetrate our markets. The new divisional structure will be in place from the start of January 2017.

Business review and proposed disposals

The Board additionally undertook a review of all of Capita's businesses with the objective of further simplifying the Company and increasing our focus on our core strengths.

For each business, the Board's review considered the growth potential, future market challenges, capital requirements and, above all, their fit within Capita's core business strategy. The business review identified and concluded that several businesses are no longer core to the future strategic direction of Capita, and consequently we now intend to dispose of the following assets:

*a group of businesses within the Capita Asset Services division which deliver shareholder, fund, debt and banking solutions and trust and corporate services, and operate in a regulated environment. The UK retail banking and mortgage services business process management operations, which currently sit within this division, remain core to Capita's strategy and will be transferred to the new Private Sector Partnerships division

*a small number of other trading businesses which are not integral to supporting our technology-enabled outsourced solutions.

There is strategic and financial logic for the proposed sale of the identified Capita Asset Services businesses and the other assets. The Board also believes these businesses will prosper under different ownership and has therefore commenced a process of divestment.

The identified CAS businesses are expected to contribute approximately EBITDA of £70m and operating profit of £60m in 2016. The other trading businesses and assets in aggregate are expected to contribute operating profit of up to £10m in 2016.

A stronger balance sheet

In line with Capita's strategy to maintain a sustainable balance sheet with a prudent level of financial gearing, the potential proceeds generated from these disposals will be used to reduce gearing and strengthen the balance sheet.

Capita's net debt to annualised EBITDA ratio at end June 2016 was 2.5 times. Whilst net debt at the end of December 2016 is expected to be similar to net debt at the end of June 2016, with lower earnings this year, net debt to EBITDA is expected to be in the region of 2.9 times at year-end.

Post successful completion of the sale of the CAS businesses, the Board would expect the Group's leverage to be around the bottom end of our 2.0 to 2.5 long term net debt to EBITDA target range. We expect to continue to invest in incremental small and medium sized acquisitions where they support our core strategy and meet our strict returns criteria, but the rate of investment will be lower in 2017 and 2018 than in previous years, as we continue to focus on maintaining a lower level of leverage.

The sale of the identified CAS businesses is anticipated to complete during the second half of 2017, subject to a number of regulatory clearances. At this stage, there is no certainty that any of the proposed disposals will ultimately be completed.

Trading update

Major new sales: Capita recently announced its first transformational contract in Europe, having been selected as strategic partner to deliver customer services for mobilcom-debitel, with a seven-year contract expected to be valued at €230m (£197m). This marks the successful introduction by Capita of a new longer-term outsourced customer management operating model into Continental Europe. The partnership, key to supporting mobilcom-debitel's digital lifestyle strategy and continued growth, is due to commence on 1 March 2017. Mobilcom-debitel is one of Germany's largest mobile and internet services and telecoms products providers, with a growing customer base.

Capita has announced £1.2bn major contract wins and extensions in 2016 to date and, following recent decisions, the bid pipeline currently stands at £3.8bn (July 2016: £5.1bn). Within our sphere of interest, the number of major contracts coming to market this year has been slightly lower than usual and some contract decisions have been delayed, resulting in a lower than expected contribution from new major contracts in 2016. As the long-term drivers for outsourcing remaining compelling, we anticipate that the customer and business process management markets will become more active again. The potential for growth in these markets in the UK and Europe continues to be strong.

Divisional trading: Since Capita last updated the market in September trading has remained challenging across some of our divisional businesses. Specifically, performance in our IT Enterprise Services division has weakened further. We have made extensive management and structural changes across this division and expect to make progress on improving its performance over the course of 2017. Additionally, as a result of some clients' own cost saving measures, we have recently experienced lower volumes of discretionary spend in a number of the Company's other trading businesses.

Cost actions and investment: To address these current trading challenges, we are taking actions to reduce the cost base across the Company. We expect restructuring costs of around £50m to be charged to the profit and loss account in 2016, the cash spend against which will be around a quarter incurred this year and three-quarters in 2017. We expect a commensurate benefit from these actions to be realised over the course of 2017 and 2018 and to be ongoing thereafter.

Some of the benefit of these actions will be re-invested in capability and initiatives to support the future growth of our business. Specifically, we have started two additional programmes that will drive longer term sustainable efficiencies and strengthen Capita's competitive position. The first programme is to move some of our IT applications support offshore to our operation in India. The second programme is an investment in a proprietary robotic solution to achieve scale automation across some of our operations and, more significantly, to deliver benefits to new clients. We expect the benefits of these two programmes to flow through into 2018.

Outlook and dividend

2016 and 2017 outlook: As a result of the trading challenges outlined above, Capita expects revenue to be around £4.8bn and underlying profit before tax to be at least £515m, excluding the cost of restructuring, for the full-year to December 2016. We expect interest to be around £66m in 2016. Our outlook for 2016 and 2017 excludes the potential impact from actions in relation to the planned disposal of the CAS businesses and the other assets outlined above.

The headwinds we have faced in the second half of 2016 will affect trading performance in the first half of 2017. Our long-term contracts provide us with good revenue visibility across the year and the structural and cost reduction actions we are taking now will support progress in the second half of 2017 and into 2018. We therefore currently expect a similar trading performance to 2016 in the full-year 2017. Our average cost of debt in 2017 will continue to rise as a result of the rolling off of our interest rate swaps.

We remain confident that the markets Capita addresses offer long-term structural growth. Our new divisions are now fully aligned to the markets in which they operate and the divisional sales teams are working seamlessly with the central major sales team to better address these markets and fuel greater organic growth in 2018 and beyond.

The successful conclusion of the potential disposal of the CAS businesses and the other assets, alongside Capita's new simplified organisational and management structure, will position Capita robustly to continue funding its business strategy and growth aspirations in the short and long term.

Dividend: The Board expects to recommend a final dividend for 2016 of 20.6p which, together with the interim dividend of 11.1p, makes a total dividend of 31.7p, unchanged on 2015. The Board expects to maintain the dividend in 2017, rebuild dividend cover in the medium term and return to steady dividend growth more reflective of the organic growth of the Company thereafter.

Future updates and Capital Markets Day: At the full-year, we will update investors more fully on the progress of cost reductions, the benefits of the new divisional structure and the prospects for profitable growth. We intend to hold a capital markets day for investors in mid-2017 to ensure a fuller understanding of each of our new divisions and showcase the unique properties of the Company, including its long-term partnerships and software and technology platforms.

-Ends-

This announcement contains inside information.

Analyst conference call, presentation, and replay:

Capita's Chief Executive, Andy Parker, and Group Finance Director, Nick Greatorex, will be hosting a conference call for analysts to dial into from 08:00 to 08:45 this morning alongside an online WebEx presentation. Please access the call and WebEx in time to allow for registration.

Please see details below:

Conference call:

Standard International Access: +44 (0) 20 3003 2666

Password: Capita0812

WebEx presentation:

To view the **presentation slides**, please go to:

<https://capitaevent.webex.com/capitaevent/onstage/g.php?MTID=e275548be800e60654e522519cdf23e04>

Password: Capita1

Replay:

Following the event, a replay of the call will be made available for 21 days after the call.

Dial-in: +44 (0) 20 8196 1998

Access code: 9532156#

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Goldman Sachs are advising Capita on the disposal of the CAS businesses

Goldman Sachs International, which is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority in the UK, is acting for Capita and no one else in connection with the potential sale of the Capita Asset Services division and will not be responsible to anyone other than Capita for providing the protections afforded to its clients, or for giving advice in connection with the potential sale of the Capita Asset Services division.

Capita is a leading UK provider of technology-enabled customer and business process services and integrated professional support services. With 75,000 people at over 500 sites, including 94 business centres across the UK, Europe, India and South Africa, Capita uses its expertise, infrastructure, and scale benefits to transform its clients' services, driving down costs and adding value. Capita is quoted on the London Stock Exchange (CPI.L), and is a constituent of the FTSE 100 with 2015 revenue of £4.7 billion. Further information on Capita can be found at: www.capita.com.