

# CAPITA

## Transforming Capita

April 2018

*Simplify*

*Strengthen*

*Succeed*



## Summary of today's announcements

- 2017 results in line, no change to 2018 profit guidance
- Multi-year transformation programme
  - Simplify, Strengthen, Succeed
  - At least £200m of sustainable FCF in 2020\*
- £701m rights issue\*\*

## Strong fundamentals, significant improvement with better execution

### Capita has a strong platform

- Great people and track record of innovation
- Leader in long term, secular growth markets

### Recently prone to self-inflicted problems

- Short-term decision making
- Under-invested
- Poor operational discipline
- Acquisitions offset weak organic growth
- Stretched balance sheet



Simplify

Strengthen

Succeed

# Significant financial transformation

<b>Greater efficiency</b>	Annualised initial cost out of £175m by 2020 One-off cost of £150m to achieve
<b>Greater focus</b>	£300m disposal proceeds in 2018 More planned over next 2-3 years
<b>Greater investment</b>	Up to £500m over next three years
<b>Stronger balance sheet</b>	Leverage target of 1-2x*
<b>Stronger performance</b>	Double digit EBIT margins within three years
<b>Sustainable FCF</b>	At least £200m of sustainable annual free cash flow in 2020**

\* Adjusted net debt to adjusted EBITDA, pre adoption of IFRS 16 \*\* before exceptional and restructuring charges and additional voluntary pension contributions

# FY 2017 summary

Nick Greatorex



# Overview of FY 2017 financial performance

- Underlying 2017 profits in line with expectations
  - Restructuring costs fell from £57m in 2016 to £18m in 2017
- Capita Asset Services treated as discontinued operation
- Early adopted IFRS 15 from 1/1/17
- Reported loss impacted by significant non-underlying items
- Free cash flow constrained in second half
- No final dividend

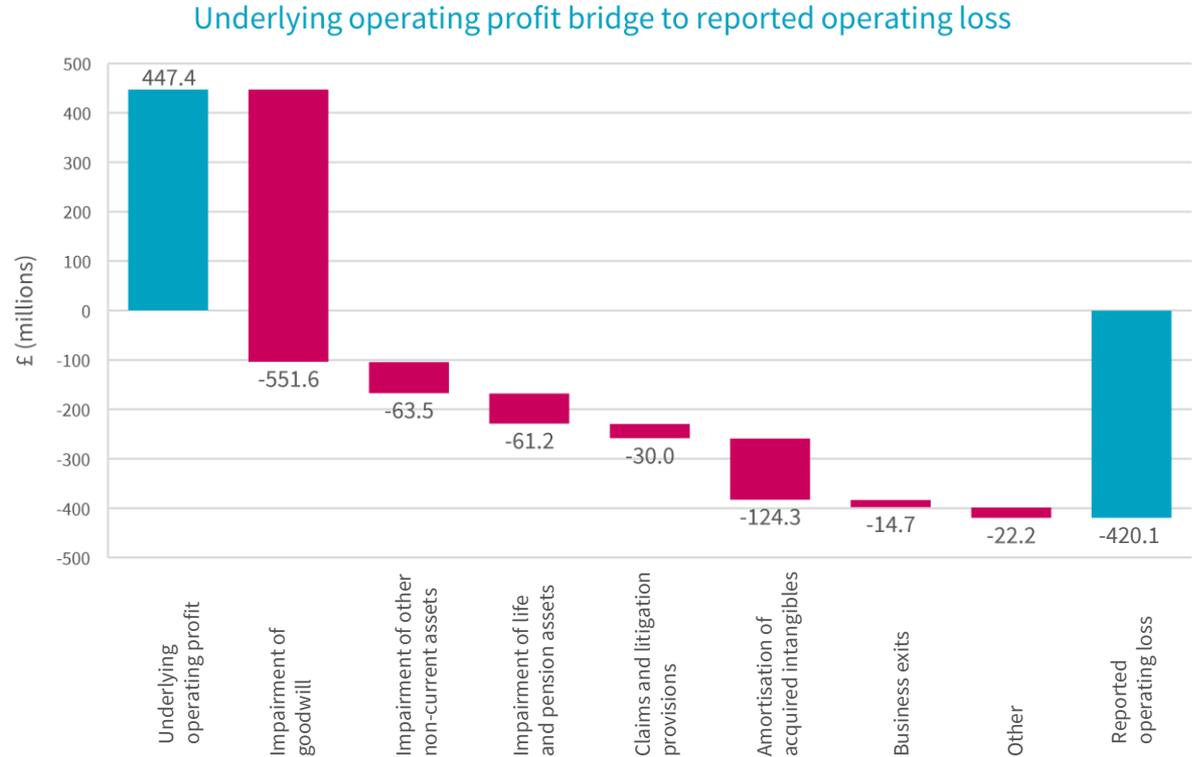
## Underlying income statement summary (£m)

	12 months to 31 December 2017*	12 months to 31 December 2016*	% Change
Revenue	<b>4,167.9</b>	4,357.3	(4.3)%
Operating profit	<b>447.4</b>	334.6	33.7%
Operating profit margin	<b>10.7%</b>	7.7%	—
Interest	<b>(64.4)</b>	(66.1)	(2.6)%
Profit before tax	<b>383.0</b>	268.5	42.6%
Profit attributable to shareholders	<b>303.6</b>	210.6	44.2%
Basic eps (pence)	<b>45.61</b>	31.68	44.0%

\*Excludes non-underlying items which include: business exits; intangible amortisation, impairments, net contingent consideration movements and other specific non-recurring items

## FY 2017 non-underlying items and reported operating loss\*

- Goodwill impairment reflects the outlook for 2018
- £63.5m of asset impairments relating to changes in both our clients and Capita's strategy
- £61.2m assets deemed to be impaired on major life and pensions client which is conducting a strategic review
- £30m provided for litigation costs in respect of legacy contracts in Real Estate and Employee Solutions



## FY 2017 cash flow highlights and leverage

- Working capital outflow of £312m
  - Deferred income declined in second half, reflecting low new business wins in 16-17
  - Partial elimination of cyclical working capital management
- Gross capital expenditure slightly reduced to £137m
- Underlying free cash flow of £38m
- Net debt decreased by £662m to £1117m, after proceeds from disposal of majority of Capita Asset Services division
- Net debt/EBITDA\*\* 2.27x at end 2017

Cash Flow highlights	£m 12 months to 31 December 2017	£m 12 months to 31 December 2016
Operating profit*	447.4	334.6
Depreciation and amortisation	83.4	87.5
Movements in working capital	(311.8)	220.0
Net interest paid	(54.2)	(59.6)
Taxation	9.5	(53.7)
Capital expenditure	(137.2)	(140.3)
Underlying free cash flow	38.0	397.3

Net debt £m	At 31 Dec 2016	Cash movements	Non-cash movements	At 31 Dec 2017
Loan notes	1,596.4	(126.2)	11.9	1,482.1
Cash in bank	(565.8)	90.5	(3.1)	(478.4)
Bank loans	650.0	(550.0)		100.0
Finance leases	2.3	(2.1)		0.2
Deferred consideration	10.8	(10.8)	13.1	13.1
Fixed rate swaps	85.1	(84.6)	(0.5)	—
Total net debt	1,778.8	(683.2)	21.4	1,117.0
Net debt/EBITDA**				2.27

\* Excludes non-underlying items which include: business exits; intangible amortisation, impairments, net contingent consideration movements and other specific non-recurring items

\*\*Net debt/EBITDA based on defined debt covenants calculation. For details please see Alternative Performance Measures

## Current trading and 2018 guidance

- Underlying pre-tax profits, before significant new contracts and restructuring costs, expected to be between £270m and £300m in 2018
- First quarter trading consistent with full year guidance
- Free cash outflow expected in 2018
  - Further reduction in deferred income £130m
  - Final unwind of cyclical working capital management £130m
  - Known commitments £300m
- Amendment agreed with US PP noteholders

# Transformation plan

Jon Lewis



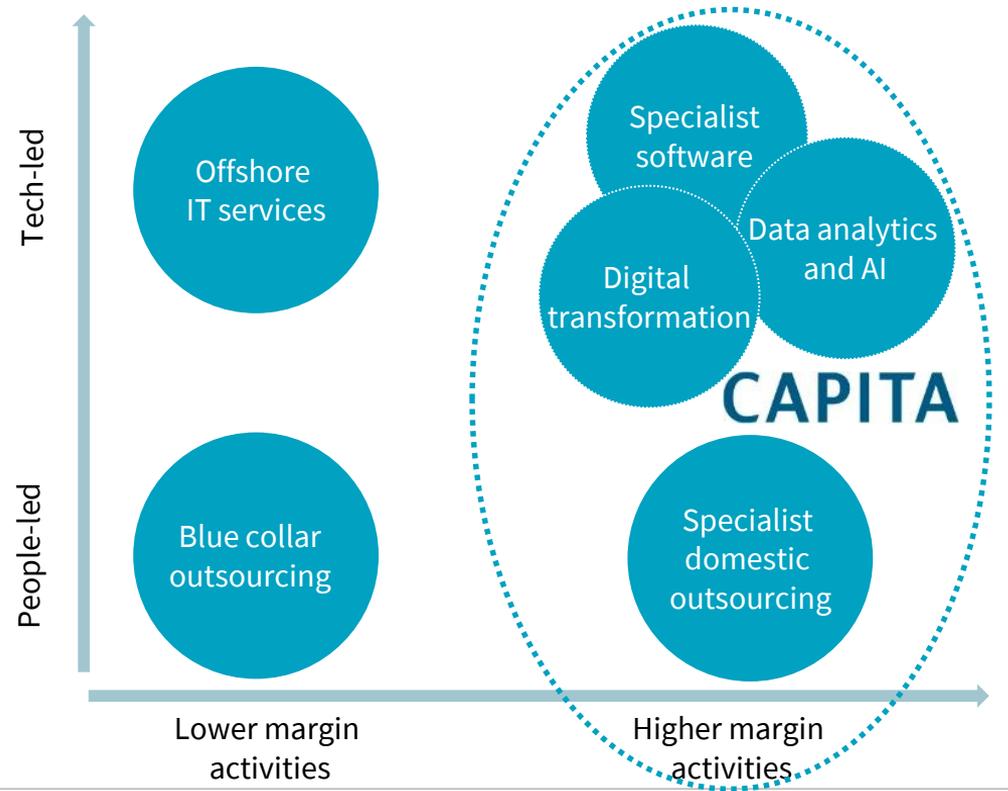
# Capita has a strong platform to build on

<p><b>Talented people</b></p>	<p>70,000 people trusted to deliver business critical services every day Committed and entrepreneurial</p>			
<p><b>Established innovator</b></p>	<p>Processes – eg O2 SIM exchange, smart auto-enrolment for The Pensions Regulator Technology – top 5 UK software company – proprietary IP such as Knowledgepool, SIMS8 Commercial – gainshare models</p>			
<p><b>Blue chip clients</b></p>				
<p><b>Market leadership in our chosen markets</b></p>	<p>Learning process outsourcing #1 Recruitment process outsourcing #2 Local government services #1</p>		<p>UK customer management #1 DACH* customer management #2 UK Education software #1</p>	
<p><b>Long-term growth potential</b></p>	<p>&gt;70% of FY17 revenues from long term contracts; £8.2bn order book Diverse sources of revenue across private / public sector clients Addressable markets growing – with largely untapped international opportunity</p>			

\* DACH is Germany and Switzerland

# Capita's sweet spot is technology-led complex activities

- Outsourcing is not an homogenous market
- Capita is focused on technology-led complex activities
- Large, long-term, secular growth segment
- Opportunity for Capita
  - Build out existing strengths
  - Take advantage of existing barriers to entry
  - Deliver appropriate margin



## Track record of high impact relationships with blue-chip clients



- Trusted partner for 26 years
  - £1.2bn TCV 10-year partnership signed in 2013
  - £100m investment to deliver digital transformation
- Capita is helping to deliver a core element of O<sub>2</sub> strategy
  - Moving O<sub>2</sub> up the Customer Satisfaction Index, increasing revenue opportunities for O<sub>2</sub>
- Capita is compensated by sharing in O<sub>2</sub> success

*Our partnership underpins O2's customer-led strategy*



- Sky needed a more “intelligent” employee portal - more accurate, relevant, personal and creative
- 2015 install of Orbit, Capita’s digital employee platform
  - Unique insights gained through use of data analytics
  - New “My Sky Rewards” platform and AI-enabled functionality
- Capita supported Sky’s strategy to improve employee engagement

*Full “Hire to retire” offering now an opportunity*



- Delivering Automatic Enrolment (AE) since 2011
- In 2015 Capita’s insight led to revised strategy for 1.25m smaller employers to be a more tailored, more efficient, self-service
- Coping with higher demand at the same time as delivering higher customer satisfaction
  - over 750 employers self-segment every day

*Innovation delivering efficiency and customer satisfaction*

Our vision for Capita

Our people become trusted partners for our clients

creating value

by developing reliable and efficient solutions,  
innovating and delivering unique insight

delighting customers

# Our plan is to do fewer things, better



## Simplify

Focus on strong positions with growth potential  
Align organisation around growth markets  
Use common, scalable capabilities  
Cost base



## Strengthen

Leadership and governance  
Up to £500m investment in asset base, tech, people  
Win more of the right work  
Balance sheet



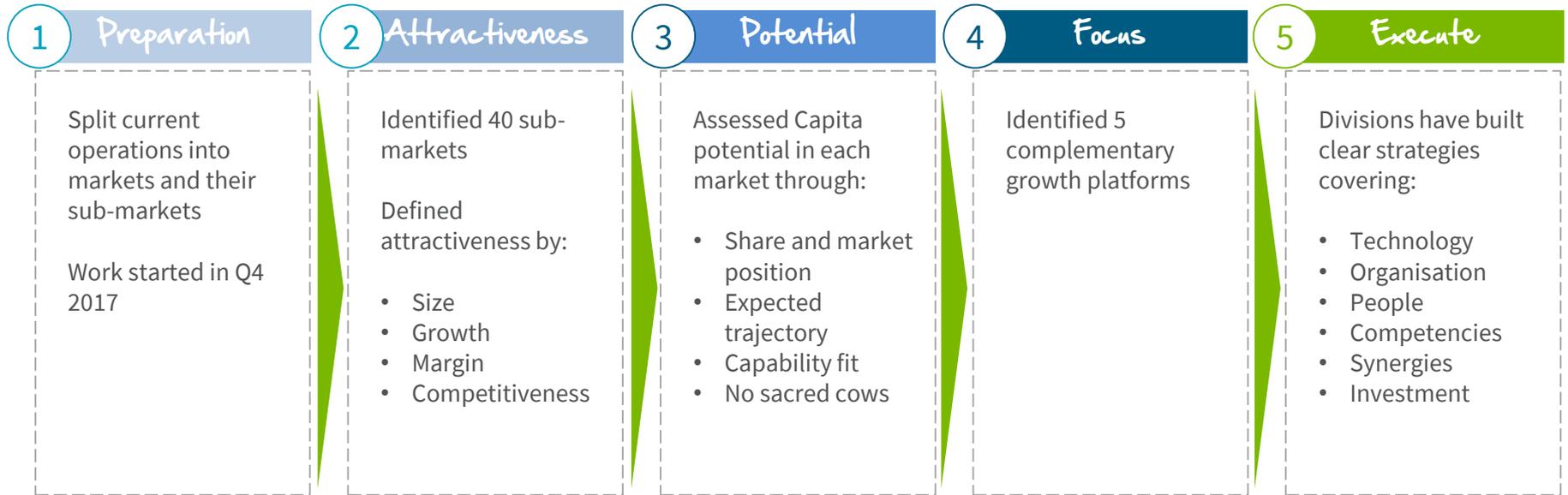
## Succeed

More predictable, lower risk

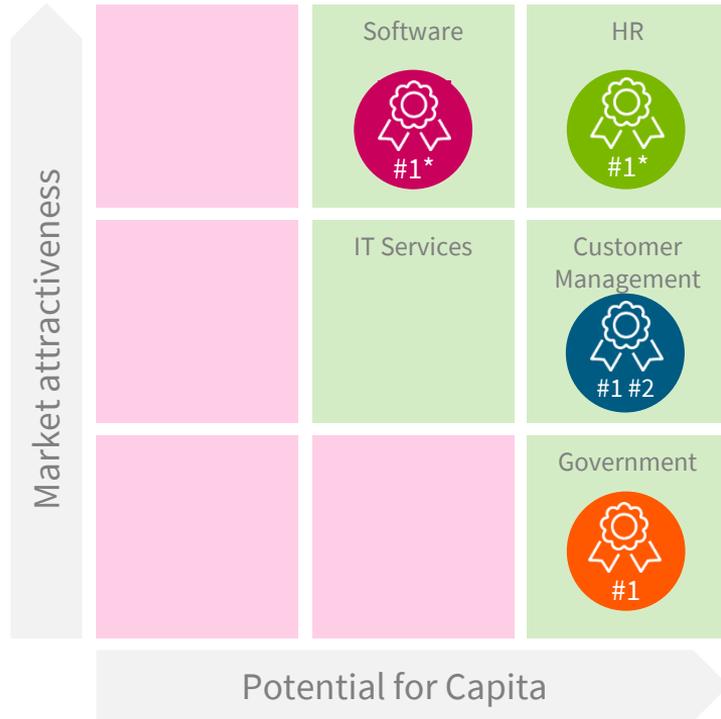
At least £200m of sustainable free cash flow in 2020\*

\* before exceptional and restructuring charges and additional voluntary pension contributions

# Simplify: focus on strong positions with growth potential (1)



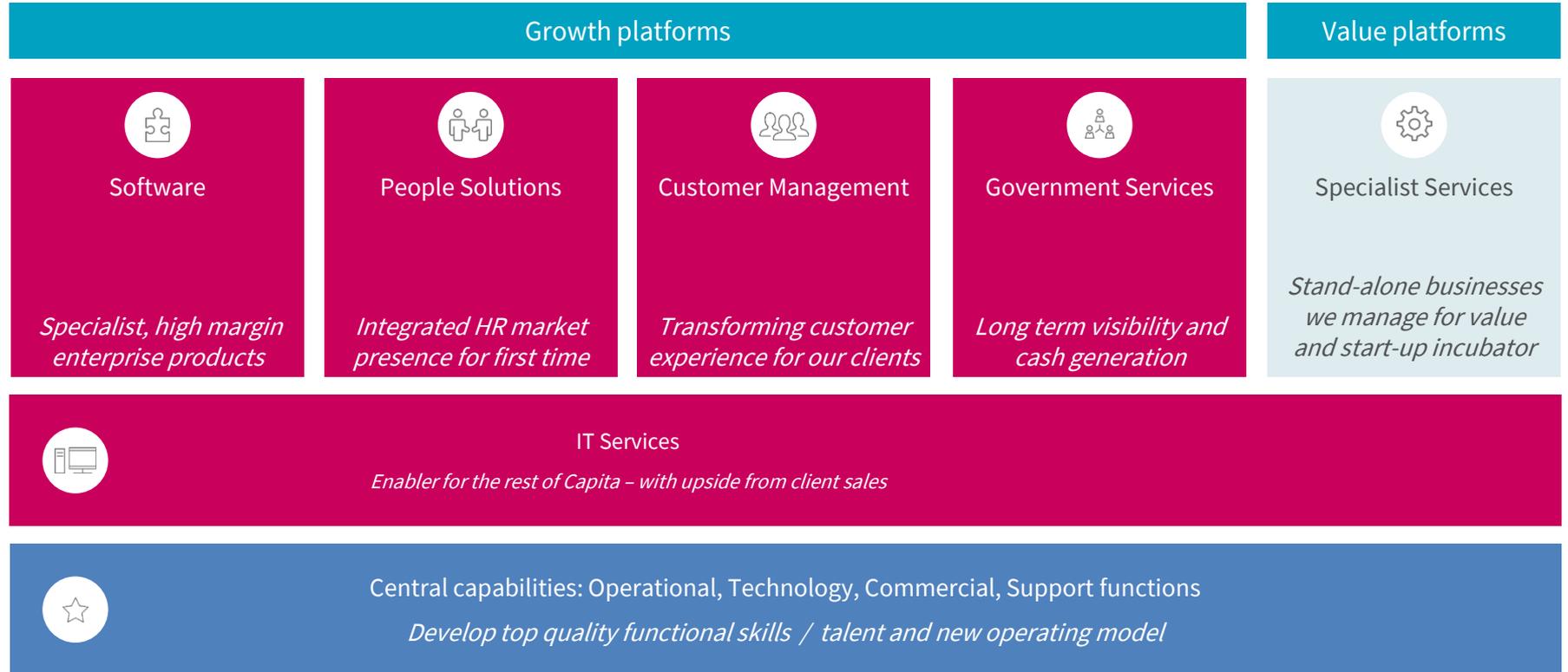
## Simplify: focus on strong positions with growth potential (2)



- 
  - #1 in UK education software
  - #1 in UK utilities software
  - #1 in UK 'blue-light' software
- 
  - #1 in UK LPO
  - #2 in UK RPO
  - #1 in UK benefits administration
- 
  - #1 in UK customer management
  - #2 in Germany & Switzerland
- 
  - #1 for local authorities
  - #1 for central government

Growth 3yr CAGR**	Current market size	Market share
+8%	£15bn	3%
+5%	£5bn	10%
+4%	£7bn	11%
+4%	£7bn	13%

# Simplify: organisation around growth markets



## Simplify: cost base



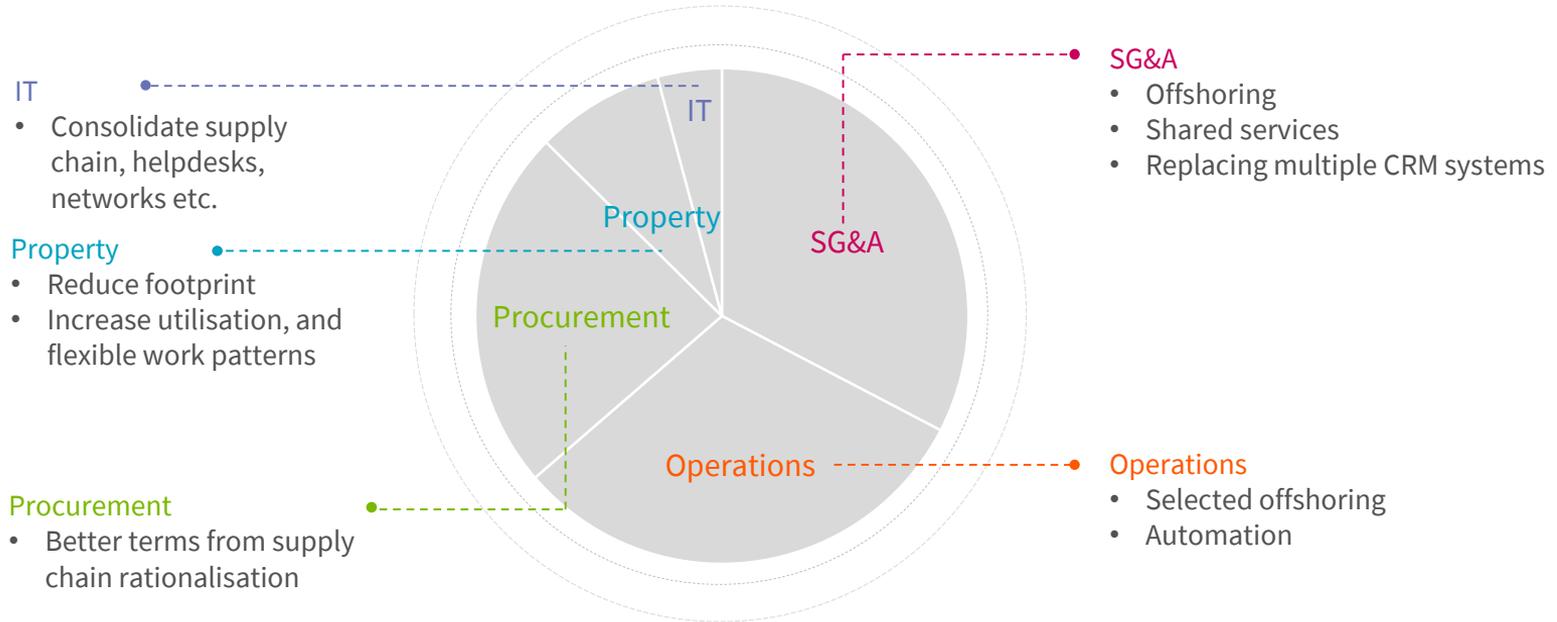
- SG&A is c50% higher as % of sales against industry benchmarks
- Currently Capita has c250 separate profit centres, legacy of policy, organic diversification and acquisitions
- Duplicated costs rather than benefits from scale, and widespread wooden dollars
- Four months into a detailed bottom-up exercise – significant cost saving opportunities identified – work ongoing

*Acquisition-led growth: limited economies of scale achieved*

Source: Bain analysis of benchmark data and S&P CapitalIQ financial information, benchmark refers to selected BPO peer group of companies

# Simplify: initial cost saving target of £175m by 2020

- Initial target of £175m cost out by 2020, with one-off cost of £150m to achieve
  - 2018 - £70m cost out – cost to achieve of £40m
- Potential to reduce costs further over the longer term



## Strengthen: we will invest up to £500m over the next three years

Investment	Initiatives	Benefits
Organisation capability	<ul style="list-style-type: none"><li>• Attract, develop and retain talent</li><li>• New operating model</li></ul>	<ul style="list-style-type: none"><li>• Better decision making and more predictable business</li></ul>
Services & Products	<ul style="list-style-type: none"><li>• Technologies common across businesses ; eg data analytics and robotic process automation</li><li>• Existing platforms/products to retain competitiveness; eg SaaS enablement</li></ul>	<ul style="list-style-type: none"><li>• Competitive, scalable, repeatable, platforms to deliver strategy</li></ul>
IT systems & infrastructure	<ul style="list-style-type: none"><li>• Ensure meet commitments in existing contracts; eg data centre upgrades</li><li>• Functional IT systems to support business better; eg SAP, single CRM</li></ul>	<ul style="list-style-type: none"><li>• Necessary to repair under-investment</li><li>• More cost effective, more flexible, more secure, more reliable foundations</li><li>• Better decision making and more predictable business</li></ul>

# Strengthen: focus on winning the work we can execute well

1

## Re-ignite sales

### Create opportunities

Allocate sales resource and responsibility to divisions

Create opportunities – not just respond to RFPs

Focus on repeatable, scalable products/offerings

Embrace account management

2

## Win the right work

### Enhanced pre-bid contract review committee

Led by CEO and CFO

Complete alignment with operational, strategic and financial goals, including:

- Commercial terms
- Capability assessment
- Implementation and operational plan
- Life-time cash generation
- Potential risks and liabilities

3

## Do the right work

### Enhanced post-win operational approach

A common governance / programme management method to deliver new contracts

Provides a set of reusable services, capabilities, processes and tools

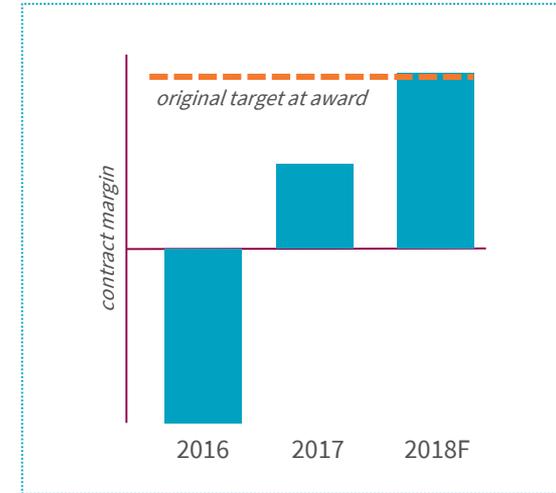
Managed by an experienced team of programme management experts

*New structure and discipline to transform how we win and deliver for clients*

## Strengthen: fixing poorly performing contracts

- Very limited number of challenging contracts
- Result of too much focus on revenue, poor risk analysis and poor execution
- Capita has become adept at fixing these
- New policy and procedures to stop this cycle

On track to deliver a major turnaround in performance with TFL



## Strengthen: balance sheet

- Target 1-2x adjusted net debt to adjusted EBITDA leverage pre adoption of IFRS 16
  - Result of review of peer group, client base and business mix
- Decisions taken
  - Raise £701m new equity\*
  - Non-core disposals - expected proceeds of £300m in 2018
  - Further disposals planned over next 2-3 years
- Accelerated US PPN repayments
  - £150m from rights issue proceeds, and up to £150m from expected disposal proceeds
- Review diversity of debt funding over next 2 years
- Commitment to reduce pension deficit over medium term
- Consider dividends once the business is generating sustainable cash flow

## Succeed: our plans for each division

	<i>Simplify</i>	<i>Strengthen</i>	<i>Succeed</i>
<b>Software</b>	Develop a shared backbone across our products	Invest in adjacent product offerings, pilot US market	Drive profitable growth and expand internationally
<b>People Solutions</b>	Leverage integrated business structure	Invest in products, platforms, partnerships and analytics	Outperform market and improve cash generation
<b>Customer Management</b>	Roll out best practice consistently	Extend our lead in analytics, automation and transformation	Extend UK market leadership, turnaround DACH* margin
<b>Government Services</b>	Focus our portfolio on proven, scalable offerings	Build out partnerships and innovation (inc BPaaS)	Deliver contracts and reliable cash flow
<b>IT Services</b>	Leverage single platform, and focus on customer	Upgrade data centres, investment into cloud, SD Wan	Fix the basics and support Capita's technology ambitions
<b>Specialist Services</b>	18 operating units - mostly stand-alone operations Managed on a portfolio basis		Delivering plan to maximise value for each

\* DACH is Germany and Switzerland

# Succeed: new culture and behaviours, leadership

## *New approach right through the organisation*

- New Executive Committee (Exco) has been created
  - Includes division and function heads
- New approach to engagement with all staff
- Comprehensive plan to develop new culture
  - Single set of behavioural values
  - New 'Managers and Leaders' programme
- New approach to incentive plans
  - Improve retention
  - Engage key talent
  - Drive performance improvement
  - Long term shareholder value creation

## *New leadership team incentive plans*

- New incentive package for Exco aligned to transformation
- Short term plan (STIP)
  - Financial measures (PBT, FCF, cost out)
  - Personal objectives aligned with strategy
  - No awards in 2018, if bottom of the range profit forecast not achieved
- CEO/CFO, as above, except ½ of any award in stock is subject to withholding period
- Long term plan (LTIP)
  - To be aligned with strategy and shareholders' interests
  - Shareholder consultation planned later this year

# Succeed: transformation led by things that we control

Driver	Contributor to value creation by 2020	In our control
Cost out	High	✓
Complete contract turnarounds	High	✓
Reduced finance costs	Medium	✓
Market trends	Medium	✓
New investments	Low	✓

*Huge value from doing the basics better*

# Our plan is to do fewer things, better



## Simplify

Focus on strong positions with growth potential  
Align organisation around growth markets  
Use common, scalable capabilities  
Cost base



## Strengthen

Leadership and governance  
Up to £500m investment in asset base, tech, people  
Win more of the right work  
Balance sheet



## Succeed

More predictable, lower risk

At least £200m of sustainable free cash flow in 2020\*

\* before exceptional and restructuring charges and additional voluntary pension contributions

# Divisional introductions



# Customer Management: at a glance



## What we do

- Manage multi-channel customer contact operations for clients
  - Customer service, technical support, sales & retentions, collections and escalated case management
  - Voice, webchat, messaging, IVR, social media & online support
- Differentiated partnership model: outcome-based, risk transfer, deep BPO

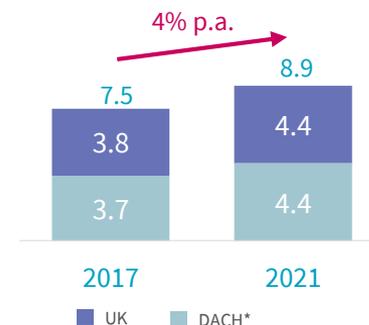
## Major clients



## Our market

- £7bn addressable market
  - UK: £3.8bn
  - Germany and Switzerland (DACH), £3.7bn
- 16% market share in UK and 6% in DACH\*
- Large, focused customer management players e.g. Teleperformance, Webhelp, Convergys

UK and DACH\* market size (£bn)



## Key facts

- 22,000 employees, across 17 sites, in 7 countries
- Services in 16 languages
- FY17 Revenue £0.8bn\*\*

# Customer Management: strategic imperatives



## Simplify



Standardise best practice and provide consistent service offerings



Deepen partnerships with leading technology providers to enhance automation / digital capability



Expand and prioritise use of offshoring where possible to reduce costs

## Strengthen



Improve our infrastructure and tools



Invest in analytics capability



Build on leading market share in retail, and telecommunications / media



Expand further into transport and travel, financial services and automotive

# People Solutions: at a glance



## What we do

- Provide a suite of HR offerings, supporting the employment life cycle from hiring to retiring
- Focus on recruitment, learning and benefits, and pensions administration; supported by proprietary platforms Tessel, Orbit and Hartlink
- Provide attraction, screening, performance management and payroll services
- Offer cross HR advisory services, helping customers understand how recruitment, learning and benefits interact

## Major clients

- 6,000 clients across private and public sectors
- Direct CxO relationships across private and public sector



## Our market

- UK £5bn market
- #1 with 21% market share in Learning Process Outsourcing
- #2 with 12% market share in Recruitment Process Outsourcing
- #1 with 6% market share in Benefits Administration
- Competitors include Alexander Mann, QA and AON Hewitt



## Key facts

- Interacts with 1 in 4 of the UK's working population
- Manages 1,500 pension schemes, with 5.2m members
- FY17 Revenue £0.5bn\*

# People Solutions: strategic imperatives



## Simplify

-  Reorganise and consolidate into a single HR business
-  Create single sales engine
-  Remove redundant costs
-  Standardise data extraction and management tools for all business units

## Strengthen

-  Upgrade core products and platforms
-  Strengthen analytics capability
-  Productise and replicate successful solutions
-  Develop partnerships with key ERP providers to ensure our solutions can integrate with customer infrastructure

# Software: at a glance



## What we do

- Develop specialist enterprise software, in markets with distinctive product offerings, with focus on
  - Education
  - Emergency services
  - Hospitals and healthcare
  - Local government
  - Professional services
  - Utilities
- Develop products which serve similar needs across different industries, such as workforce management, enterprise resource management and payments
- Form a distinctive component of the wider tech-enabled Capita service offering
- 5% international revenue; scope for expansion, including pilot US market

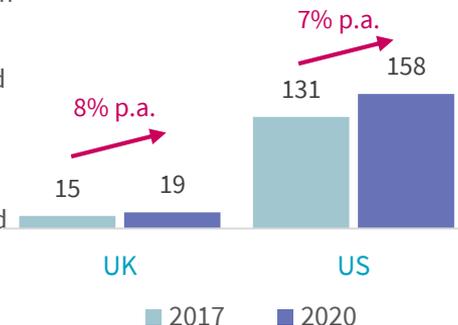
## Major clients



## Our market

- Overall UK software market ~£15bn with 8% growth
- Top 5 player
- Horizontal markets dominated by global giants (e.g., Oracle, Microsoft, SAP)
- Vertical specialist markets are more complex and fragmented with different competitors in each

UK & US enterprise software markets\*, £bn



## Key facts

- Over 22,000 schools use Capita software
- Most local authorities use at least one Capita software product
- FY17 Revenue £0.4bn\*\*

# Software: strategic imperatives



## Simplify



Focus on carefully selected UK and international specialist markets



Develop reusable software tools



Market aligned sales force and improved go-to-market capability

## Strengthen



Invest in core products with distinctive offerings to defend position, and grow in existing and adjacent markets



Build best-in-class development centre to produce standardised software



Scaled, integrated, shared service functions



Expand selected products into US market

# Government Services: at a glance



## What we do

- Government's trusted partner for the delivery and transformation of tech-enabled business services
- Operate high-profile services that integrate multiple service capabilities to achieve government's policy outcomes
- Deliver support services to Local Authorities, schools and health organisations including
  - Collecting and making payments to citizens
  - Back-office processing
  - IT and digital transformation

## Major clients



## Our market

- Largest player
  - 11% share in Central
  - 15% share in Local
- Central: £3.5bn TCV\* addressable opportunities (excl. own re-bids) to 2020
- Local: Traditional large BPO deals in decline; transactional services and digital are growing
- Competitors include Capgemini, Atos, DXC, TCS, IBM, Sopra Steria, BT, Agilysys and Serco

### Opportunities for central government services\*\*, £bn



## Key facts

- Process 800,000 daily roadside detections for congestion charging from the camera network in London
- Carry out over 20,000 clinical assessments per month on behalf of DWP
- FY17 Revenue £0.9bn\*\*\*

\* Total Contract Value

\*\* This chart shows the weighted total contract value of Capita's qualified opportunities and then remaining total contract value of remaining addressable opportunities (excluding own re-bids), sourced by management estimates

\*\*\* Source: management accounting records

# Government Services: strategic imperatives



## Simplify



Focus on areas where Capita has distinct advantage, e.g.

- Disbursement and collections
- Scheme Administration & Licencing
- Service Integration



Deprioritise and avoid smaller, non-core, fragmented activities, e.g.

- Property and estate management
- Facilities management



Standardise and productise core capabilities

## Strengthen



Invest in our chosen core capabilities



Upgrade our transformation capabilities, introducing state-of-the-art capabilities in data analytics, robotics, automation



Build strategic relationships with external digital providers



Transform business development – focus on long-term client relationships



Build innovative business models using our existing capabilities and scale

# IT Services: at a glance



## What we do

- End-to-end enterprise IT outsourcing and transformation, including hosting for large / specialised public sector and select private customers
- End-to-end network outsourcing services, including voice and telephony, local and wide area network setup, maintenance, fault resolution and security
- Comprehensive managed IT support for educational institutions across the UK and Northern Ireland
- Extensive value added professional service portfolio including testing, data consulting and cybersecurity services

## Major clients

- Key markets: education, emergency services, local and central government, health and defence



## Our market

- Top 10 player UK
- Offering includes data centres, infrastructure, and networks
- Market polarising between large commoditised infrastructure business, and higher-margin value-add services
- Key competitors include IBM, DXC, CapGemini, and smaller specialists

UK IT outsourcing market\*, £bn



## Key facts

- Runs network connecting >5,000 public sector sites in Scotland
- Supports new Aircraft Carrier alliance, and Nuclear Decommissioning Authority
- FY17 Revenue £0.4bn\*\*



## Simplify



Simplify portfolio and structure



Create well-defined and modular product catalogue



Focus client base on internal customers, public sector, and medium-sized enterprises

## Strengthen



Investments for internal customers first, then external markets



Build technical and sales capabilities in higher growth and margin businesses



Invest in new networks technology, data centre upgrades, cloud capabilities and people



Customer experience

# Specialist Services: at a glance

## Scope and rationale

- Grouping of predominantly stand-alone businesses, which have minimal commonality with other divisions
- Managed to maximise value, allowing other divisions to focus on growth in their dedicated areas with no distractions
- Mix of cash generative, growth, challenged and non-core assets
- FY17 Revenue £1.1bn\*

## Main categories

- Financial and regulated services
- Miscellaneous specialist services
- Commercial ventures

## Disposals in progress



## Key constituents

- Life & pensions
- Insurance services
- Mortgage & collections



- Travel & events
- Real estate & infrastructure
- Managed print
- Hardware reselling



## Recap of financial guidance given today

- Initial target annualised cost out of £175m by 2020
  - One-off cost of £150m to achieve
- Investment of up to £500m over next three years
- Double digit EBIT margins within three years
- Adjusted net debt to adjusted EBITDA of 1-2x pre adoption of IFRS 16
- Non-core disposals - expected proceeds of £300m in 2018, further disposals planned over next 2-3 years
- Reduce pension deficit over medium term
- Consider dividends when generating sustainable free cash flow
- At least £200m of sustainable annual free cash flow in 2020\*

## Rights Issue – expected timetable

- **Publication of Prospectus** – 23<sup>rd</sup> April 2018
- **General Meeting** – 9<sup>th</sup> May 2018
- **Commencement of Nil Paid Trading** – 10<sup>th</sup> May 2018
- **Last date for Acceptance of Rights Issue** – 24<sup>th</sup> May 2018
- **Rump Placement** – 25<sup>th</sup> May 2018

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