A turnaround in financial performance

"Accelerated revenue growth, a step change in profitability and positive free cash flow."

Tim Weller, Chief Financial Officer

Overview

Improved adjusted revenue[1] growth was in line with our expectations, with an acceleration across the year from 1% in the first half to 4% in the second half. This was driven by strong growth in the Public Service and Portfolio divisions and stabilisation of revenues in the Experience division.

Public Service revenue growth was underpinned by new wins such as the Northern Ireland teachers IT refresh contract and annualisation of the Royal Navy training contract offset by revenue reductions in some Local Public Service contracts. Experience revenue was impacted by significant prior year contract losses, offset by new wins, including those in International and with ScottishPower.

Growth in our transactional business was mainly driven by Portfolio, including the Travel and Enforcement businesses, which continued their recovery following Covid-related constraints.

From 1 January 2022, the Board has limited the items excluded from the adjusted results to business exits, amortisation and impairment of acquired intangibles, impairment of goodwill and certain fair value adjustments which impact net finance income/expense. This presentation

Summary of financial performance

	Financial highlights					
	Reported results – continuing operations			Adjusted[1] results – continuing operations		
	31 December 2022	31 December 2021	Reported YOY change	31 December 2022	31 December 2021	Adjusted YOY change
Revenue	**£3,014.6m**	£3,182.5m	(5.3)%	**£2,845.8m**	£2,777.8m	2.4%
Operating profit/(loss)	**£(79.6)m**	£(86.6)m	8%	**£102.9m**	£(77.7)m	n/a
EBITDA	**£235.7m**	£222.3m	6%	**£238.8m**	£143.0m	67%
Profit/(loss) before tax	**£61.4m**	£285.6m	(79)%	**£73.8m**	£(122.8)m	n/a
Earnings/(loss) per share	**4.47p**	13.33p	(67)%	**6.20p**	(7.74)p	n/a
Cash generated from/(used by) operations*	**£117.8m**	£(148.5)m	n/a	**£116.5m**	£(109.7)m	n/a
Free cash flow*	**£24.5m**	£(264.3)m	n/a	**£29.0m**	£(218.6)m	n/a
Net debt	**£(482.4)m**	£(879.8)m	£397.4m	**£(482.4)m**	£(879.8)m	£397.4m
Net financial debt (pre-IFRS 16)	**£(84.9)m**	£(431.4)m	£346.5m	**£(84.9)m**	£(431.4)m	£346.5m

* Cash generated from operations adjusted results and free cash flow adjusted results are free cash flow before business exits and cash generated from operations before business exits respectively (refer to note 2.10)

1. Refer to APMs on pages 229 to 231.

provides a more representative measure of the underlying performance of the business following completion of the Group-wide transformation. The comparatives have been re-presented on the same basis, with significant restructuring (£147.5m), contract-related provisions and impairments (£43.1m) and certain litigation and claims (credit £2.3m) now included within adjusted results for the year ended 31 December 2021.

The increase in adjusted profit before tax[1] reflects the above change in presentation, and therefore benefits from the reduction in restructuring costs and contract-related provisions and impairments, as well as the benefit of revenue growth. In 2021, the Group received £4.9m of funding under the coronavirus job retention scheme made available by the Government to help ease the employment impact of Covid-19. In May 2022, we announced the Group's intention to repay the 2021 furlough-related income at the end of the Group's publicly stated disposal programme and no later than the end of June 2023. An accrual has been recognised for this repayment in the year ended 31 December 2022.

The decrease in reported profit before tax arose as the increase in adjusted profit before tax[1] was more than offset by an increase in impairments of goodwill, a reduction in operating profit from business exits and a lower gain on the sale of businesses.

From 1 January 2022, the Board considers free cash flow and cash generated from operations before business exits each to be alternative performance measures that provide a more representative measure of the sustainable cash flow of the Group following completion of the Group-wide transformation.

Cash generated from operations before business exits[1] increased by £226.2m to £116.5m benefiting from the improvement in adjusted profit[1] explained above, a reduction in repayments in respect of the Government's VAT deferral scheme and a £43.6m reduction in pension deficit contributions as the Group reverts to the agreed deficit contributions set as part of the 2020 triennial funding agreement with the pension scheme trustees.

Free cash flow before business exits[1] for the year ended 31 December 2022 was an inflow of £29.0m (2021: £218.6m outflow). The improvement primarily reflected the above increase in cash generated from operations before business exits[1], and a reduction in net interest paid in respect of leases and private placement loan notes.

As part of our drive for simplification of the business, and strengthening the balance sheet, we continue to seek to dispose of a number of non-core businesses. During the year we completed the disposal of eight businesses, realising total proceeds net of disposal costs of £463.4m (including settlement of intercompany balances on completion) with net cash proceeds of £387.9m reflecting the cash held in the disposed entities on completion.

These disposals form part of the Board-approved disposal programme. The sale processes have been launched for the remaining pillars in the Portfolio division. The Group expects to use the proceeds from this disposal programme to repay debt, to make accelerated deficit reduction contributions to the Group's defined benefit pension scheme and to invest in driving growth in the remaining core businesses. During the year, we repaid £226.7m of private placement loan notes and made pension deficit contributions of £38.6m (£30.0m regular contributions and £8.6m acceleration of agreed contributions triggered by disposals).

Liquidity as at 31 December 2022 was £405.2m, made up of £288.4m of the undrawn element of our committed revolving credit facility (RCF) and £116.8m of unrestricted cash and cash equivalents net of overdrafts. In July 2022, we extended the RCF to 31 August 2024.

Adjusted results

Capita reports results on an adjusted basis to aid understanding of business performance. The Board has adopted a policy of disclosing separately those items that it considers are outside the underlying operating results for the particular period under review and against which the Group's performance is assessed internally. In the directors' judgement, these items need to be disclosed separately by virtue of their nature, size and/or incidence for users of the financial statements to obtain an understanding of the financial information and the underlying in-period performance of the business.

In accordance with the above policy, the trading results of business exits, along with the non-trading expenses and gain or loss on disposals, have been excluded from adjusted results. To enable a like-for-like comparison of adjusted results, the 2021 comparatives have been re-presented to exclude 2022 business exits. As at 31 December 2022, the following businesses met this threshold and were classified as business exits and therefore excluded from adjusted results in both 2022 and 2021: ESS, AXELOS, Life Insurance and Pensions Servicing business in Ireland, AMT Sybex, Secure Solutions and Services, the Speciality Insurance business, Trustmarque, Real Estate and Infrastructure Consultancy, Optima Legal Services, Pay360 and Capita Translation and Interpreting.

Reconciliations between adjusted and reported operating profit, profit before tax and free cash flow before business exits are provided on the following pages and in the notes to the financial statements.

1. Refer to APMs on pages 229 to 231.

Adjusted revenue

Adjusted revenue[1] growth of 2.4% was in line with expectations. The adjusted revenue[1] was impacted by the following:

- **Public Service (2.5% growth):** growth from contract wins, including a contract to supply laptops to teachers in Northern Ireland as well as the annualised benefit of the Royal Navy training contract, increased growth in existing contracts in Central Government, and completion of a full test cycle on STA, offsetting handbacks in Local Government;
- **Experience (0.9% growth):** stabilisation in revenue, with the impact of significant prior year contract losses offset by positive revenue contributions in particular from new client wins in International and with ScottishPower; and
- **Portfolio (10.3% growth):** growth in transactional revenue mainly from Travel and Enforcement following the turnaround in these Covid-19 impacted businesses.

Order book

The Group's consolidated order book was £5,805.2m at 31 December 2022 (2021: £6,115.4m). Additions from contract wins, scope changes and indexation in 2022 (£2,110.2m), including the BBC and freenet AG extensions within Experience, and Personal Independence Payments and TfL Road User Charging within Public Service, were offset by the reduction from revenue recognised in the year (£2,132.3m), contract terminations (£8.1m) and business disposals (£280.0m).

Adjusted profit before tax

Adjusted profit before tax[1] increased in 2022. The adjusted profit before tax[1] was driven by the following:

- **Public Service:** benefits from the wins in 2022, the annualised benefit of the Royal Navy training contract and the non-recurrence of Electronic Monitoring programme costs in 2021; offset by a reduction on the British Army recruitment contract (RPP) resulting from transition to the next phase of service delivery;
- **Experience:** flow through of prior year losses including 3UK, William Hill and in the closed book Life & Pensions business. 2021 was impacted by provisions and impairments in the closed book Life & Pensions business and completion of significant restructuring;
- **Portfolio:** benefits from post Covid-19 recovery in transactional businesses and the non-repeat of 2021 restructuring costs; offset by operational investment in certain businesses; and
- **Capita plc:** benefits from the end of the transformation programme (2021 included £128.0m of significant restructuring) and efficiencies realised; offset by the effect of the announced intention to repay the 2021 furlough-related income.

Adjusted revenue[1] bridge by division

	Public Service £m	Experience £m	Portfolio £m	Total £m
Year ended 31 December 2021	1,410.4	1,140.9	226.5	2,777.8
Net growth	34.9	9.8	23.3	68.0
Year ended 31 December 2022	**1,445.3**	**1,150.7**	**249.8**	**2,845.8**

Adjusted profit before tax[1] bridge by division

	Public Service £m	Experience £m	Portfolio £m	Capita plc £m	Total £m
Year ended 31 December 2021	93.2	8.9	(0.1)	(224.8)	(122.8)
Net growth/(reduction)	(1.7)	29.6	16.3	152.4	196.6
Year ended 31 December 2022	**91.5**	**38.5**	**16.2**	**(72.4)**	**73.8**

Cash generated from operations and free cash flow

Adjusted EBITDA[1] increased by 67% reflecting the improvement in adjusted profit[1] explained above and the significant reduction in depreciation, amortisation and impairment of property, plant and equipment and intangible assets, largely driven by the Group's property rationalisation programme.

Cash generated from operations before business exits[1] benefited from the improvement in adjusted EBITDA[1], a lower working capital outflow compared with 2021, materially lower deferred VAT repayments and pension deficit contributions; offset by a reduction in non-cash and other adjustments.

The lower working capital outflow arises from contracts moving into the operational phase and increased utilisation of non-recourse trade receivables financing in 2022.

The reduction in non-cash and other adjustments reflects utilisation of customer contract provisions in 2022 compared with provision recognition in 2021, and the utilisation of the remaining restructuring provision.

Free cash flow before business exits[1] for the year ended 31 December 2022 was an inflow of £29.0m (2021: outflow £218.6m). The improvement reflected the above increase in cash generated from operations before business exits[1], a reduction in capital expenditure, and net interest paid in respect of leases and the Group's private placement loan notes.

Adjusted operating cash conversion[1] increased to 68% (2021: 48%).

1. Refer to APMs on pages 229 to 231.

Reported results

Adjusted to reported profit

As noted above, to aid understanding of our underlying performance, adjusted operating profit[1] and adjusted profit before tax[1] exclude a number of specific items, including the amortisation and impairment of acquired intangibles and goodwill, and the impact of business exits.

Impairment of goodwill

In preparing the half-yearly condensed consolidated financial statements at 30 June 2022, and these consolidated financial statements at 31 December 2022, the Group undertook detailed impairment reviews.

At 30 June 2022 a goodwill impairment of £92.5m was recognised in respect of the People and Property CGUs, and at 31 December 2022 a further goodwill impairment of £76.5m was recognised in respect of the People, Travel and Business Solutions CGUs, in the Group's Portfolio division. The impairments reflected the difference between the expected net proceeds at disposal and the cash flows the Group had previously projected it would generate if it held these businesses into perpetuity. The difference has arisen due to the potential for acquirers factoring in additional investment and costs required to run the businesses on a standalone basis, coupled with general macroeconomic conditions.

Refer to note 3.4 to the consolidated financial statements for further details.

Business exits

Business exits include the effects of businesses that have been disposed of or exited during the period and the results of businesses held-for-sale at the reporting date.

In addition, business exits include the exit costs, including professional fees, salary costs and separation planning costs, relating to further planned disposals for which the held-for-sale and business exit criteria were not met at 31 December 2022.

In accordance with our policy, the trading results of these businesses, along with the non-trading expenses and gain on disposal, were classified as business exits and therefore excluded from adjusted results. To enable a like-for-like comparison of adjusted results, the 2021 comparatives have been re-presented to exclude the 2022 business exits.

Adjusted operating profit to free cash flow before business exits[1]

	2022 £m	2021 £m
Adjusted operating profit/(loss)[1]	**102.9**	(77.7)
Add: depreciation/amortisation and impairment of property, plant and equipment and intangible assets	**135.9**	220.7
Adjusted EBITDA[1]	**238.8**	143.0
Working capital	**(32.7)**	(113.6)
Non-cash and other adjustments	**(44.7)**	38.6
Operating cash flow before business exits[1]	**161.4**	68.0
Deferred VAT repayment	**(14.9)**	(104.1)
Pension deficit contributions	**(30.0)**	(73.6)
Cash generated from/(used by) operations before business exits[1]	**116.5**	(109.7)
Net capital expenditure	**(43.6)**	(51.2)
Interest/tax paid	**(43.9)**	(57.7)
Free cash flow before business exits[1]	**29.0**	(218.6)

Reported to adjusted[1] profit bridge

	Operating profit/(loss)		Profit/(loss) before tax	
	2022 £m	2021 £m	2022 £m	2021 £m
Reported	**(79.6)**	(86.6)	**61.4**	285.6
Amortisation and impairment of acquired intangibles	**5.1**	7.7	**5.1**	7.7
Impairment of goodwill	**169.0**	11.5	**169.0**	11.5
Net finance costs	**—**	—	**(3.4)**	1.4
Business exits	**8.4**	(10.3)	**(158.3)**	(429.0)
Adjusted	**102.9**	(77.7)	**73.8**	(122.8)

1. Refer to APMs on pages 229 to 231.

At 31 December 2022 business exits primarily comprised:

Business	Disposal completed on
AMT Sybex	1 January 2022
Secure Solutions and Services	3 January 2022
Trustmarque	31 March 2022
Speciality Insurance	29 April 2022
Real Estate and Infrastructure Consultancy	22 September 2022
Optima Legal Services	30 November 2022
Pay360	1 December 2022
Capita Translation and Interpreting	29 December 2022

Further businesses are planned for disposal as part of the Group's simplification strategy. However, given the status of the relevant disposal processes, the businesses did not meet the criteria to be classified as assets held-for-sale at 31 December 2022 and, accordingly their trading results are included within adjusted results.

Further detail of the specific items charged in arriving at reported operating profit and profit before tax for 2022 is provided in note 2.4 of the consolidated financial statements.

Taxation

The reported income tax credit for the year of £14.6m (2021: charge £61.5m) and the adjusted income tax credit for the year of £31.8m (2021: charge of £4.0m) reflect the recognition of additional deferred tax assets of £36.7m (net of a £16.7m change in the deferred tax asset estimate due to the reduction in future taxable profits on disposal of taxable entities, reflected in the tax arising on business exits). These losses mainly arose due to the adoption of IFRS 15, Covid-19 related downward pressures on the profits and tax deductible restructuring costs in previous years.

Free cash flow to free cash flow before business exits

Free cash flow was lower than free cash flow before business exits[1] principally reflecting pension deficit contributions triggered by the disposal of Trustmarque and AXELOS, offset by free cash flows generated by business exits.

Movements in net debt

Net debt at 31 December 2022 was £482.4m (2021: £879.8m). The substantial reduction in net debt reflects the benefit of the Group's positive free cash flow generation, the proceeds from disposals, coupled with the impact of the ongoing programme of leased property estate exits.

Free cash flow to free cash flow before business exits[1]

	2022 £m	2021 £m
Free cash flow	**24.5**	(264.3)
Business exits	**(4.1)**	(36.2)
Pension deficit contributions triggered by disposals	**8.6**	81.9
Free cash flow before business exits[1]	**29.0**	(218.6)

Net debt

	2022 £m	2021 £m
Opening net debt	**(879.8)**	(1,077.1)
Cash movement in net debt	438.2	232.1
Non-cash movements	(40.8)	(34.8)
Closing net debt	**(482.4)**	(879.8)
Remove closing IFRS 16 impact	397.5	448.4
Net financial debt (pre-IFRS 16)	**(84.9)**	(431.4)
Cash and cash equivalents net of overdrafts	177.2	101.5
Financial debt net of swaps	(262.1)	(532.9)
Net financial debt/adjusted EBITDA[1] (both pre-IFRS 16)	**0.5x**	3.7x
Net debt (post-IFRS 16)/adjusted EBITDA[1]	**2.0x**	4.1x

1. Refer to APMs on pages 229 to 231.

Net financial debt (pre-IFRS 16) reduced by £346.5m to £84.9m at 31 December 2022, resulting in a net financial debt to adjusted EBITDA[1] (both pre-IFRS 16) ratio of 0.5x. Over the medium term, following the completion of our Portfolio divestment programme, we will be targeting a net financial debt to adjusted EBITDA[1] (both pre-IFRS 16) ratio for Capita of ≤1.0x.

The Group was compliant with all debt covenants at 31 December 2022.

Capital and financial risk management

Liquidity remains a key area of focus for the Group. Financial instruments used to fund operations and to manage liquidity comprise US private placement loan notes, euro fixed-rate bearer notes, revolving credit facility (RCF), leases and overdrafts.

In July 2022, the Group signed an extension of the £300m forward start RCF with its lending banks for a further twelve months to August 2024. The new facility commenced on 31 August 2022 upon the expiry of the previous RCF and provides the Group with committed liquidity for the cash fluctuations of the business cycle and an allowance for contingencies, and incorporates provisions such that it will partially reduce in quantum as a consequence of specified transactions. The RCF was not drawn upon at 31 December 2022 and had a total committed value of £288.4m.

In addition, the Group has in place a non-recourse invoice discounting facility, utilisation of which has become economically more favourable than drawing under the RCF as prevailing interest rates have increased. As such, the Group has increased its use of the facility across the year with the value of invoices sold under the facility at 31 December 2022 of £44.4m (2021: £16.4m).

At 31 December 2022, the Group had £177.2m of cash and cash equivalents net of overdrafts, and £285.5m of private placement loan notes and fixed-rate bearer notes. These debt instruments mature over the period to 2027, with repayment of £66.3m of maturities in 2023 which are expected to be funded through the Group's existing facilities, cash and cash equivalents and from the proceeds of the Group's ongoing divestment programme without the need to obtain new financing. As such, a measured approach will be taken to any potential refinancing with time taken to implement a longer-term debt solution at the appropriate moment.

Going concern

The Board closely monitors the Group's funding position throughout the year, including compliance with covenants and available facilities to ensure it has sufficient headroom to fund operations. In addition, to support the going concern assumption, the Board conducts a robust assessment of the projections, considering also the committed facilities available to the Group.

The Group and Parent Company continue to adopt the going concern basis in preparing these consolidated financial statements as set out in section 1 to the consolidated financial statements.

1. Refer to APMs on pages 229 to 231.

Liquidity

	2022 £m	2021 £m
Revolving credit facility (RCF)	**288.4**	385.7
Less: drawing on committed facilities	—	(40.0)
Undrawn committed facilities	**288.4**	345.7
Net cash, cash equivalents net of overdrafts	177.2	101.5
Less: restricted cash*	(60.4)	(54.8)
Liquidity	**405.2**	392.4

* Restricted cash includes cash required to be held under FCA regulations and cash held in foreign bank accounts.

Viability assessment

The Board's assessment of viability over the Group's three-year business planning time horizon is summarised in the viability statement on page 64.

Pensions

Contributions during the year to the Capita Pension and Life Assurance Scheme (the Scheme) have been in line with the contribution schedule agreed with the Trustee of the Scheme following the 31 March 2020 triennial valuation. This includes the acceleration of deficit reduction contributions (£8.6m) triggered due to the disposal of Capita entities during the year.

The net defined benefit pension position for accounting purposes moved from a small net asset at the start of the year (£5.8m) to a larger net asset by 31 December 2022 (£39.6m). The main reasons for this movement were the £38.6m of deficit funding contributions paid into the Scheme (plus a net £0.2m deficit funding contribution in respect of other schemes). Both the value attributed to the pension liabilities and the value of the assets fell materially over the year predominantly due to the material increase in the yields available on both long-dated Government and corporate bonds. Due to the investment strategy adopted by the Trustee of the Scheme the impact of these changes has been broadly hedged so that the value of the assets has moved to a similar degree to the value of the liabilities. Despite the economic events in Q3 2022 that led the Bank of England to purchase Government bonds, the Scheme's Fiduciary Manager confirmed that the Scheme had sufficient liquid assets to meet collateral calls to maintain its hedged positions throughout the year, as well as confirming that there is sufficient buffer against future adverse movements.

The net defined benefit pension position for accounting purposes moved from a small net asset at the start of the year (£5.8m) to a larger net asset by 31 December 2022 (£39.6m)

The valuation of the Scheme liabilities (and assumptions used) for funding purposes (the actuarial valuation) are specific to the circumstances of the Scheme. It differs from the valuation and assumptions used for accounting purposes, which are set out in IAS 19 and shown in these financial statements. The main difference is in assumption principles being used based in the different regulatory requirements of the valuations. Management estimates that at 31 December 2022 the net asset of the Scheme on a funding basis (ie the funding assumption principles adopted for the full actuarial valuation at 31 March 2020 updated for market conditions at 31 December 2022) was approximately £40.0m (2021: net asset £40.0m) on a technical provisions basis. The Trustee of the Scheme has also agreed a secondary more prudent funding target to enable it to reduce the reliance the Scheme has on the covenant of the Group. On this basis, at 31 December 2022, the funding level was around 96% (or a net liability of £50m). The deficit of £50m is expected to be met by a mixture of the remaining deficit contributions and asset outperformance.

The next triennial valuation of the Scheme is due as at 31 March 2023, where the Trustee of the Scheme and the Company will review the contributions being paid to the Scheme. The 2023 triennial valuation is expected to be completed in 2024.

Consolidated balance sheet

At 31 December 2022 the consolidated net assets were £352.7m (2021: net assets £296.5m).

The movement is predominantly driven by the gain on the sale of businesses offset by the goodwill impairment recognised during the year, and the increase in the net pension asset referred to above.

Parent company balance sheet

The company's market capitalisation was significantly less than the net assets of the parent company at 31 December 2022 and the Directors gave consideration as to why this might be the case and whether assets on the parent company balance sheet may be impaired. The factors considered included: the differing basis of valuations (point in time nature of the market capitalisation and that third parties value the services sector on income statement multiples versus long-term view using a discounted cash flow for the basis of impairment testing under accounting standards), sum-of-the-parts view and the multiples achieved on recent disposals, and that the sector may be trading at or below book value with the market making a general assessment of the sector and all companies within the sector which can ignore the liquidity profile and specific risks of an entity.

Management's estimate of the value in use of the Group used in the testing of goodwill and intangibles for impairment at 31 December 2022 gave a value for the Group that exceeded the market capitalisation at that date, and supported the parent company net assets. An impairment test was performed at 31 December 2022 in respect of the parent company's investments in subsidiaries and amounts owed by subsidiary undertakings. A £7.0m impairment was identified in respect of the parent company's investments in subsidiaries, and an impairment of £30.1m was recognised in respect of amounts owed by subsidiaries.