Capita

FY23 Results Presentation Transcript:

Adolfo Hernandez – *Capita – Chief Executive Officer*

Good morning, everyone. Thanks for being here today, I know this is a bit of an anticipated afternoon with the budget, so I do appreciate everybody taking the time to join me and our CFO, Tim Weller, who you all know well. I'm the new CEO of the company, I've been in the business for seven weeks. Sometimes that seven weeks has seemed a little bit longer than just the seven weeks, but it's really, really good to be here.

Today we have to cover the FY23 results, we're going to cover with you what worked well, where we made progress and also equally the areas where we didn't make that much progress. I will also, at the end of Tim's presentation, give you an overview of what I have seen and observed and learnt and we're starting to act on over the past seven weeks. But before we do that, I thought I'd better introduce myself for those of you I haven't worked with over the last few years.

I guess I was working until the day before I joined Capita for AWS. I was the Vice President responsible for the global telecoms business, so in that capacity, the vision that I led globally, we had to work with the world's largest telecom companies, arguably some of the world's largest companies, to help them accelerate the digital transformation, exit legacy, migrate, evolve the culture so that they could become digital first and cloud native. Help them with the very taxing requirements when it came to security, confidentiality, scalability, reliability and everything that is so important in telecoms.

I've spent half of my career in software, half of my career in services, always in the boundary of seeing how you could apply software to modernise services, or how you can build services wrappers around software to augment value. I've worked with public companies, I've worked with private-public companies, private companies.

I've worked for the - serving governments around the world and also commercial companies. Through my time, I've had senior leadership responsibilities in multinationals like IBM, Sun Microsystems, Alcatel-Lucent and been the CEO of a public traded company here in London, SDL plc, also the CEO of a private equity company. When you put together all of these skills, built over a 30-year career, I feel like I've been predestined for this role in Capita and that many of these skills will be extremely relevant to what we need to do here over the next few years.

Some of you may be asking why did he join Capita of all the places out there? Well, I guess just the first one is the huge opportunity for digital transformation. The reality is that, as I have experienced with AWS and most recently at Capita, most organisations, whether they are government agencies, telecom companies, utilities and many other sectors, they are really at the beginning of a digital transformation. Digital transformation, moving to the cloud, is all still on its infancy and it's a great opportunity and I want us to be there. I think it's a great opportunity to take Capita from what it is to that position, because there are significant opportunities.

The second reason why I joined is when you look at a company, you also look at the impact that the company has and it is very difficult to find a company that has a bigger impact on society and the fabric of society than Capita. We impact the lives of millions of people in Europe every day.

I was last week meeting customers and some of our colleagues in Ireland and I learned that we touch every single one of the Republic of Ireland's households daily, several times. Front office and back office of water provision, back office of electricity provision, front office, back office, customer support of gas and sometimes also telecoms.

If I look at my own experience living here in West London, if I need to deal with my council out of hours, that service is provided by Capita. My children pay their council tax to Capita. We enable the GPs, the pharmacists, the opticians that we use. We work with our forces in this country to keep the country safe. The pensions that I've built over the years, they are supported by Capita, so chances are if I pick up the phone, I'm talking to a Capita colleague, etc. That sort of fabric defines the list of customers that we have.

We have a list of customers that is second to none, it's really our crown jewel. They serve relationships that are not started last year or last quarter, they come from multiple years, sometimes over several decades. We've been working really hard, we deliver for them. Admittedly it hasn't always been smooth, it hasn't always been without challenges, but as I've gone around talking to our customers everybody acknowledges that we are super critical to their success and that we have always worked hard to do what it takes to get things to work.

The final reason that you look at as a CEO joining a new company is alignment. Alignment with the Board, alignment with the vision of the Chairman and then subsequently with the executive team as to what needs to be done. I found that there was 100% alignment around challenges, but most importantly the vision around the opportunities that we see ahead. You could ask me what's seven weeks in? Well, seven weeks in, I am even more excited than when I joined. There are some challenges at hand but there are a lot of pretty good opportunities that I will cover later on, that are going to keep us busy and hopefully are going to deliver share value creation over the next few years. I'll come back in a minute, but before we do that, Tim, will you please take us through the 2023 financial details?

Tim Weller – *Capita – Chief Financial Officer*

Thanks, Adolfo. Morning, everyone. As usual, our results are presented on an adjusted basis unless stated otherwise. In line with our half year presentation, cyber incident-related costs have been excluded from adjusted profit. Additionally, given the exceptional nature of the cost reduction programme announced in November 2023, the associated costs have also been excluded.

Finally, as we noted at the half year, following feedback from investors we've revised the definition of our free cash flow measures and these are now presented after deducting the capital element of lease payments and receipts. The comparators have been re-presented on the same basis.

Turning to the financial overview, although the 2023 results are in line with our trading update in December, we would be the first to acknowledge that Capita's financial performance is not where it needs to be. Our revenue growth, profit margins and free cash flow lag behind our peers. We've taken action and as set out in this morning's announcement, we'll be taking further action across 2024 to drive financial performance improvement.

In terms of the other main headlines from the results, we've now finalised the £500 million Portfolio disposal programme with January 2024's completion of the sale of Fera. We significantly extended our funding maturity profile by renewing our revolving credit facility to the end of 2026 and through the issuance of private placement notes with three and five-year maturities.

We've reached agreement with the pension scheme trustees on the 2023 triennial valuation, with no further deficit contributions from 2025 onwards. We're on track to deliver the previously announced £60 million annualised cost savings by the end of the first quarter of this year and we announced this morning we'll be implementing further cost saving actions, which will deliver an additional £100 million of annualised efficiencies by the middle of 2025.

Moving to the next slide for our financial highlights. Full year revenue growth was 1.3%. This reflected a marginal increase in revenues in our Public Service division with stronger growth in the Experience division. We saw growth in operating profit, profit before tax and EBITDA, reflecting the flow through to profit from the revenue one-offs and a stepdown in cost from bonuses and variable pay.

The growth in operating profit was partly offset at the profit before tax level by £16 million of increased finance costs, reflecting the high interest rate environment and run-off of low coupon debt. Earnings per share reduced to 1.7p, the step up in profit before tax was offset by a £24 million increase in the current tax charge in 2023, reflecting an £18 million charge in respect of losses not recognised for tax purposes.

It's worth noting that there's an offsetting current tax credit of £90 million on pension deficit contributions that is recognised in the statement of other comprehensive income rather than the income statement. Despite this high effective tax rate in the income statement, the underlying cash tax is much lower. We anticipate cash tax payments in 2024 of less than £10 million.

Free cash outflow reflected the decrease in cash generated from operations, which I'll talk about later, the cost of the cyber incident and increased capital expenditure in line with previous guidance. The increase in net debt to £546 million reflects the free cash outflow offset by the £63 million benefit from disposals completed in the year and the continued reduction in our leased property estate.

As usual, in the appendices to the slides we provide a fuller analysis of the financials, but the next few slides summarise the performance of our two divisions. First of all, looking at Capita Public, we saw a marginal increase in revenue in the year reflecting scope increases on a number of our contracts such as Royal Navy training, improving volumes on our Personal Independence Payments contract and a step up in revenues as a result of the application of indexation across our contract portfolio.

These effects were offset by previously announced hand-backs and losses within our Local Public Service business, which saw a 14% or £56 million revenue reduction year-on-year and the non-recurrence of the £17 million contract in 2022 to provide teachers' laptops in Northern Ireland. These contract exits suppressed operating profit, which reduced 4.7% compared with 2022.

We saw a small improvement in EBITDA, with operating cash flow up by 4.7% as a result of higher operating cash flows reflecting the flow through of scope increases and tight working capital management.

The next slide summarises the key wins and opportunities currently within the Public Service division. In 2023, the division saw an increase in total contract value sold of more than 50%, in part reflecting the delay in award dates from 2022 to 2023 of a small number of material contracts following changes within the UK Government in the last few months of 2022.

Contract wins in 2023 include expanded scopes with the Department for Work and Pensions to deliver Functional Assessment Services and with the Department for Education to administer the Disabled Students Allowance. There were material new wins, the City of London Police and a further extension to 2026 of the Recruiting Partnering Project, a contract with the British Army. The division's book-to-bill ratio improved to 1.3x from 0.8x in 2022.

The division's weighted pipeline reduced by £400 million as a result of the strong TCV performance. The division's renewal win rate decreased 41% following the loss of the Ministry of Justice and Standards and Testing Agency contracts, in both cases lost on price as we continue to maintain our disciplined approach to contract bidding and pricing. Across all opportunities bid for in the year, the win rate was 65%, broadly in line with the prior year.

Moving on to Experience on the next slide, where we saw revenue growth of 2.5% driven by improved trading in our non-UK businesses, indexation and the one-off benefit relating to a commercial settlement in the closed book life and pensions business. This growth was partly offset by contract losses, primarily the mortgage services contract with the Co-operative Bank, the loss of which we announced in December 2021, which came to an end in late 2022 having generated revenue of £47 million in that year.

The division delivered a 42.6% increase in operating profit, reflecting the £24 million benefit of the closed book life and pension settlement, coupled with high interest rate driven revenues in our pensions business, partly offset by the flow through of contract losses and the continued attrition in the remaining closed book life and pensions business.

EBITDA grew at a much slower rate than operating profit, as the division's depreciation and amortisation charges stepped down, reflecting the reduced level of assets utilised under the new VMO2 contract. Despite the increase in operating profit, operating cash flow reduced by 9.4% and cash conversion by 3.4 percentage points reflecting the non-cash nature of the commercial settlement, partly offset by the phasing of cash flows on the new Virgin Media O2 contract.

Turning to the key wins and opportunities in Experience, over 2023 Experience secured new wins with total contract value of £1.1 billion. This included the new Virgin Media O2 contract replacing our longstanding O2 contract and wins with the Civil Service Pension Scheme, National Transport Authority in Ireland and Santander. The book-to-bill ratio for the division was 0.9x, down from 1.2x in the prior year.

Our new and expanded scope win rate increased from 17% in 2022 to 53% in 2023 and the reduced renewal rate in 2023 of 61% reflected the Teachers' Pension contract, which once again we lost on price. The order book for the division decreased by £0.2 billion but this does not include framework agreements such as the new Virgin Media O2 contract, because these do not meet the criteria for order book recognition.

Key pipeline opportunities for the division include potential contracts with Scottish Power, SAGA, Vattenfall and a number of European telecommunication companies. We're devoting significant resources to growing the division's pipeline of opportunities in 2024.

On the next slide we provide the reconciliation between adjusted and reported results before tax. Outside the adjusted result, the reported numbers reflect a number of nontrading items, including the losses on disposal and goodwill impairments arising from the remaining Portfolio business exits. Costs arising as a result of the March 2023 cyber incident, including specialist professional fees, recovery and remediation costs and investment to reinforce Capita's cybersecurity environment in line with previously stated expectations. Lastly, the redundancy and other costs totalling £23 million and property impairment charges of £31 million arising from the significant cost reduction programme we announced at the end of November last year.

Moving now to cash flow and net debt. Cash conversion for the Group reduced from 63% in 2022 to 45% in 2023. As disclosed in last year's results, 2022's operating cash flow saw a £28 million benefit from the step up in usage of our nonrecourse trade receivables financing facilities. Whereas this year we saw a £9 million reduction in usage.

The noncash unwind of the Group's deferred income balance, reduced to £82 million from the average of £100 million in 2021 and 2022. Following the completion of the O2 contract, we expect the deferred income unwind to take a further stepdown in 2024 to a level broadly half of that seen in 2023, based on the current contractual profile. It's a somewhat technical piece of contract accounting, but the good news from the stepdown is that it should be beneficial to operating cash conversion in 2024.

Pension deficit contributions of £30 million were made in the year in accordance with the funding plan agreed as part of the 2020 triennial review and the cash cost incurred in respect of the cyber incident amounted to £20 million. Whilst we recognise an income statement change of £23 million in respect of redundancy and other costs arising from the cost reduction programme announced in November, only £6 million of these costs impacted on cash flows in the year.

As we flagged at the start of the year 2023 saw a step up in capital expenditure of over £20 million, as we continue to invest in technology, to enhance efficiency, customer service and client offerings. Net capital lease payments continue to reduce, reflecting our ongoing property rationalisation programme, which helped to offset the headwinds from inflation linked rent increases.

The free cash outflow of £115 million was partially offset by the net cash flow benefit from the Portfolio disposals completed in the year and as we set out in the final bullet point in the slide, in January 2024 we received a further £51 million in net cash on completion of the Fera disposal.

The next slide shows the liquidity position and funding maturity profile. The Group was undrawn on its revolving credit facility at the year end and this, coupled with the unrestricted cash balances on hand at 31 December, resulted in liquidity of £282 million. Whilst this is significantly lower than the position at the end of the 2022, it's a level we're comfortable with considering that we have no maturing debt in 2024 and that the extension of the revolving credit facility to 2026 and the £100 million private placement issuance that both took place in the middle of 2023 has significantly extended our funding maturity profile.

The Board's medium-term leverage target remains for net financial debt, pre-IFRS 16, to EBITDA to remain around 1x. As we note in the final bullet point, proforma leverage at 31 December reflecting the Fera disposal is 0.9x net debt to EBITDA in line with that target.

Now this slide sets out the key moving parts expected to help us transition from the substantial free cash outflow seen in 2023 to the goal of delivering positive free cash flow from 2025 onwards. Firstly, we saw a series of one-off cash drags in 2023 that will not recur in 2025. The most significant of these was the £30 million of pension deficit contributions which will reduce to just over £20 million in 2024 and then zero in 2025 and beyond, following completion of the 2023 triennial funding agreement of the trustees late last year, closely followed by the £20 million of cash costs for the cyber incident.

These two, when coupled with the £5 million furlough repayment and £6 million of restructuring spend, mean that 2023's £115 million free cash outflow was impacted by £66 million of items which should not recur in 2025. Removing these items gets us to a clean rebased 2023 free cash outflow of £54 million.

We then have the two waves of cost reduction programmes, the first of which we announced in November last year focused mainly around indirect support, function and overhead activities, the implementation of which is nearing completion and yielding a bottom line benefit of £60 million on an annualised basis.

The second, announced this morning, we'll be taking action over the period to mid-2025 which will be focused not only on overhead and indirect activities, but also encompasses efficiency opportunities identified in operational support, supply chain and technology. This wave 2 programme is expected to deliver incremental savings of £100 million on an annualised basis by mid-2025.

We'll be providing more detail on this second wave of the programme at our Capital Markets event in June. Whilst we expect to reinvest a proportion of the benefit from wave 2 of the cost reduction programme in enhancing our customer proposition, absent any other moving parts such as the potential benefit from revenue growth and contract margin expansion, the cumulative impact of both efficiency programmes should see the Group transitioning to positive free cash flow generation from 2025.

My penultimate slide sets out our outlook for 2024 from a financial perspective. Given the changes we need to implement over the next few months, I'd characterise 2024 as being a transitional year from a financial perspective, as we put in place the building blocks for a materially improved financial performance in 2025 and beyond. As such, we expect revenue to be broadly in line with 2023, driven by a low to mid-single digit percentage revenue decline in Experience, reflecting continued attrition in the closed book life and pension business, offset by revenue growth of a similar percentage from Public Service as contracts won in 2023 move into the execution phase.

Adjusted EBIT margins are expected to show modest expansion, as we see a bottom-line benefit from our ongoing cost reduction programmes. We still expect the Group to be cash consumptive in 2024 and are currently estimating £70 million to £90 million of free cash outflow in the year, principally reflecting improved operating cash conversion normalising to 60% to 70%. In part benefiting from the lower deferred income release I talked about earlier, the nonrecurrence of cyber incident costs offset by cash restructuring costs of around £50 million expected to be incurred in delivery of the cost efficiency programmes.

As a result, we expect net financial debt to increase over the course of the year, but for this to be partially offset in terms of total net debt by the ongoing effect of our property rationalisation programme.

On the phasing front, we expect revenue to decline in H1, reflecting the one-off benefits in the first half of 2023, with revenue growth to be delivered in the second half. As we execute the cost reduction programme, we expect the free cash outflow to be heavily weighted to the first half of the year, with the margin benefit seen in the second half. As you'd expect, we're planning to set out our longer-term financial targets at our Capital Markets Day in June.

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Finally, this slide recaps what I talked about in the overview slide at the start of my presentation. Knowing how much all of you hang on my every word, I won't reiterate all the points. Suffice it to say that we're taking far reaching action to seek to get Capita's financial performance back to where it needs to be. With that, I'll hand back to Adolfo.

Adolfo Hernandez – *Capita – Chief Executive Officer*

Thank you, Tim. Okay, I think as Tim made very clear, our financial performance is not what it needs to be and I think the case for change is self-evident. We need to turn this to a more positive and improving financial position. Let me talk about my onboarding, my familiarisation. Over the past seven weeks I have spent most of my time listening, because I think it was super important to spend time listening and learning from customers, from colleagues, from partners and do as much as I could directly and through some work with commissions and really get to the bottom of what's really happening with the operations.

Internally, I've spent a significant amount of time with our colleagues, our colleagues who are day in and day out in the middle of operations. They love their customers, they know their business processes really well. I have been positively impressed by how they do it, I've been listening to some of the calls in the call centres, how they handle things, how passionate they feel about the outcomes and sometimes how much they feel that dual identity of yes, they may be working for Capita but they're part of the customer engagement. That has provided really valuable insight.

I also started engaging online with colleagues on a variety of topics, bidirectional, unscripted, unfiltered. Overall, I've been getting a lot of free advice on what's working, what's not working so well and what we need to improve. I've also spent time with our top leadership teams, probably roughly engaged with the top 100 leaders in the business and trying to understand where are the business opportunities. Where do we win and why, where do we lose and why, what are we doing well, what feedback are we getting and ultimately where do we generate profits and cash and whether it's a sustainable business going forward.

You've read the release, you probably imagine that I spent a fair amount of time with our technology teams understanding our technology state, understanding the legacy, understanding the migrations that have taken place, what's mid-flight, what's planned. Understanding the work that was being done on stacks, rationalisations, convergence and architectures, gen AI and a number of topics that are super relevant.

But above all, I think what I've been trying to understand is as we look at this business going forward and this industry, where are the problems that our customers are trying to solve and where do they need help and where do they feel that we have a role to play. I'm trying to get that in a concise fashion so that we can get on with addressing it.

As I look at what I've seen, I think we have some really strong foundations to build on. However, there is a little bit of rebuild that is necessary. Why am I saying this? I talked about my customers' surprise when I came in, I knew it was strong but I have to say going around it's something I'm really proud of. That list of customers with whom we work and how closely we are integrated in their operational and strategic fabric. There is an open invitation for us to be more part of that strategic fabric and help them drive some of the changes that they need to drive.

I talked about the passion that I see in our colleagues out there and that is true. It's just great to see the shine in their eyes as they're describing what is it that they're doing, how they're doing it and they're also equally passionate about some things that we should be able to improve when it comes to productivity, repetitive tasks and automation. When I look at our customers, the landscape of our customers is one where they have more and more complex problems to solve and they have less and less resources.

The pace of change is such that for them to enrich a human interaction with a productivity copilot is a massive undertaking. For them to think about content summarisation and meta tagging and having that delivered as a service is super complex. To look at all the data and unlock the value of the data behind their operations is both super valuable and super complex. I look at the role that technology has to play as the pace of change and I look at the size of the market, so I have concluded that the opportunity for a trusted partner like Capita, who's trusted delivering outcomes, delivering that veneer around key projects and combining that with technical capabilities is there, is very real.

As I said at the beginning, this is an incipient industry, the opportunity is there for the taking. Some people have made some moves, we've started making some, but everything is just at the beginning, so really excited about what we've got. But I did say that this is - we've got to rebuild, because to deliver on what we can deliver and to really monetise that opportunity we're going to have to change a few things. It's not going to be immediate, it's not going to be easy, it's going to take grit, it's going to take determination and it's going to take above all execution, but I believe we can do.

So you're going to ask me okay, what are the things that you would like to change? Well first of all, I think I'd like a little bit of clarity and intentionality as to what do we want to be known for. What are we going to do intentionally for whom and how, that's the refocusing of what we do. We produce huge outcomes, but one of the reasons why this is not showing in the numbers is because we produce maybe too many outcomes, so we need to refocus.

The second thing we need to change is simplification. We need to simplify, simplify and simplify. How do we operate, how do we run this business, we need to just become leaner, we need to become more agile. We need to be more replicable, we need to capture the knowledge of what we do well and where we do it well and use it everywhere else. So the whole topic of simplification is going to be a key one.

Then the third thing that we need to do is we need to inject a lot of technology into the business. Technology that is present, but we need to make it more pervasive and we need to make it pervasive everywhere. It's on two fronts, so we have the internal use of technology capabilities that are available there today for us to deliver a better service, for us to be more efficient, for us to deliver a better working environment for our colleagues. But also using technology as part of our value proposition so that we are more relevant and more differentiated in front of our customers, so that we can be more profitable and grow more as we shift into faster growing segments of the market.

So seven weeks in, I wish I had all the answers today. We are working, everybody in the management team, the executive team, it's just really pulling all the stops so that we can come up with a firm plan and strategic plan that we're going to share with you on the Capital Markets event in June. But it would be unfair not to share with you at this stage some of the early key moves, so let me just give you an early preview of what we're going to move.

First and foremost, we have to become a more efficient business and we have to spend less. As Tim made the case earlier, we're just simply spending too much to run this business and cost is the single biggest inhibitor of the free cash flow generation. That needs action and we're taking action today. Some of you say well, you're taking action too early. No, I'm not, I'm being decisive, but the team had already started looking at this last year. There was work that was underway, there was analysis, there was opportunity that was identified.

We've gone as an executive team, looked at this, we believe that we can do it and we should get going today. This cost, well it should be cost removal, I should say, it will be painful in the short term, it will pay off in the medium term, it will pay off in multiple ways. Obviously, it will help our free cash flow generation over time, it will help us with the profitability and I think those two things are good for everyone. It's good for shareholders, it's good for colleagues and it's good for our customers. But it will also give us a little bit of wind when it comes to revenue growth.

Tim has talked about the pricing discipline that we've had last year and that's great, but one of the challenges of the pricing discipline is our cost base was too high. If we have a more competitive cost base and we're still disciplined around pricing, we should be able to win more deals.

The second thing that it's going to mean is we're going to reuse a number of things a lot more. I fail to see why the call centre that we use for a government department in the United Kingdom to serve citizens on a particular service has to be different from the call centre we use to serve a telecoms company in Central Europe, or different from the call centre that we use in Ireland to serve a utility. 80% should be the same, should be the same technology, the same services, it should be out of the box and then we personalise the experience and the remaining 20%. It's just an example of opportunities that we have here.

The second thing is digitation of offerings, I talked a lot about that. Yes, internally but also externally and I think there, there are a number of dimensions. So (1) our offerings shouldn't be a one-off; they should be built on common platforms, they should be replicable. Because the beauty of that is obviously you're more efficient, but you're also faster. If you're able to do that you also get scale and speed and scale means money. Speed and scale also means happy customers and less frustrated employees, so we need that technology at the core.

Data, we have a ton of data, we produce a lot of data as we operate with our customers, but we haven't been able to unlock the value of that data fully yet. Sometimes it's because of where it sits in the system, sometimes it's just the interface, sometimes it's because the mindset hasn't been there. Sometimes the process wasn't created, sometimes it was too hard internally to do it. We need to unlock that data.

Third is gen AI. When you have such a disparate business based on multiple contracts, where have so many different activities, front office, back office, cross concentric where we are processing large amounts of data, where we're doing a lot of document processing, where we're trying to identify trends. Gen AI targeted for use cases is perfect, I've spent the last few years doing that and enabling customers to do that and you can see the use cases. We've talked over the last couple of weeks all about the work we've been doing with the British Army recruitment, I think that's a great case.

How do you use large language models and natural language processing to process huge medical files and really get productivity improvements. Those are looking at medical files and getting productivity improvements of over 30%. You start finding some of these use cases everywhere, you can see the impact. Think also about us, we have 47,000 colleagues inside the Company. Imagine the power of being able to use gen AI technologies for qualifications, for CV qualifications, use them totally to match people to jobs, make the whole recruitment process more efficient.

The onboarding, getting people to production faster, maybe in a week, not in six weeks. Giving them a better tool so that we retain them and we don't have the cost of churn. Think about the impact of that over time dropping through the bottom line.

(3) We are not going to build a big software capability as we have attempted in the past. We are going to leverage hyperscalers, we are going to leverage large technology providers who are building scalable, reliable, advanced, innovative services that you can switch on and off. We're going to put a veneer around that of that Capita specific, because while the technology in its raw inception is there, most customers do not have the prowess and the time to keep implementing that themselves, sustaining it, managing it and managing that digital outcome. That's going to be a big shift in the strategy.

(4) I want to talk about delivery and precision in delivery. I think many of you might know the history of Capita. A few years ago, when there were a few well-known contracts where we have onerous clauses or delivery challenges that cost us over £200 million accumulatively. Thankfully, Jon and the team got on with that and many of those were largely addressed.

I have to thank my colleagues at Capita for managing to deliver over the last couple of years consistently KPIs in excess of 90%. We've been able to deliver also the customer Net Promoter Score of 16 in what you would agree was a really challenging 2023 environment. But we can do better and we should do better, because every time we have delivery mishaps we eat away into the customer franchise and the goodwill and it costs us money and it costs us time and it costs us frustration, so precision in delivery will be super important going forward.

Last but not least, governance and evolving the culture. When dealing with the situation I just described, problems a few years ago, it was right that we inserted into the business a reasonably robust governance framework to make sure that no onerous contracts were signed and everything was done truly by the book and it served a purpose. But if you fast forward to 2023 and 2024, some of that may be heavy-handed, some of that belts and braces across everything has slowed down the execution of the organisation.

Most importantly, the emergence of many committees has created an environment where ownership is utterly fragmented among the 20 people who are on the call. I like to operate in an environment that is more agile, where we have a clear execution framework where everybody is aware of who's empowered to make the decision. What authority do they have, the delegation of authority, but then they're also accountable for delivering that outcome.

So expect no radical change, but expect to see a more modern, appropriate, balanced model of freedom and empowerment emerging into the culture. The culture will become more one of accountability and empowerment, so that we can have smaller teams making the right decisions and only escalating up things that warrant that. In working with my executive team, we believe that that's very clearly required. We also need to introduce speed and pace into what we do.

If reusing and replication is important, and it's one of my key points, we have to have a true one Capita mentality and not just work down in our contract world and try to export and import best practices from different parts of the world. Obviously, we have to become more cost and cash conscious in our culture. Last but not least, I think we need to bring more honesty, empathy and call things for what they are. As an executive team we're totally committed to do that going forward. As I said, a lot more in June when we unveil that.

You will hear the same themes from the strategy components in June. Just reassure you that a lot of 2024 we need to do is the immediate priorities of execution that Tim just outlined. But we're also going to be making the early moves to enable the strategy so we can start seeing the fruits and the benefit of that coming through in 2025 and beyond. I could argue and say that we have to get leaner, to get fitter, to get stronger, to grow and it will be in that sequence, but this is not about optimising one particular year; this is about building a valuable company for years to come.

A company that is growing, that is growing in revenue and profits and in associated cash generation, where our employees are happy to come and stay and develop their careers. With customers who are equally happy as they are today, but they'll find us more relevant in this new industry transformation, digital transformation. Then ultimately one that is delivering more positive and improved financial performance than the one we've shared with you.

I've only been here a few weeks, but if you were to measure my passion when I arrived and my passion today, I am more passionate now than I was when I arrived. I was then, but I'm now seeing the true opportunities. Yes, this will remain a complex business, yes, there is a lot of work to do. Yes, this year is going to be painful, yes, I feel like we're going to have to work on really difficult things. But as I look at the opportunities and I look at the markets and I see what customers want us to do, that by far outweighs the complexity. I'm excited about the challenge and I feel honoured to have the opportunity to lead this great team into new areas. That's the end of my presentation and I think now handing over and you're going to moderate the Q&A.

James Rose – *Barclays*

Hi there, it's James Rose from Barclays, I've got two please, if I may. Firstly, Tim, on free cash flow guidance, I appreciate the more precise guidance range you've given for FY24. Do you have more visibility of 2024 than you've had in perhaps prior years? As ever, can you help us bridge from FY23, I think the rebased £54 million, to the FY24 guidance?

Then secondly, for Adolfo, very simply what does Capita need to do more of and what does it need to do less of?

Tim Weller – *Capita – Chief Financial Officer*

Okay, so on the free cash flow guidance, we are being more precise. Having completed the Portfolio disposal programme, having got our arms around what, as Adolfo says, is still a complex portfolio but essentially down to the two divisions with the corporate centre, it is an easier business to predict in terms of cash flow management. We've clearly got a grip on all of the individual contracts and have pretty good visibility.

In terms of that bridge from the £115 million-odd of free cash outflow in 2023 to the £70 million to £90 million, that includes - the £70 million to £90 million includes £50 million of the cost of delivering wave 1 and wave 2 of the cost out programme. So essentially, you're starting off with £115 million and then going back down to £30 million to £40 million or so of, in inverted commas, underlying free cash outflow.

Why is that getting so much better than the £115 million? Well, we haven't got the cost of the cyber incident in there, which is in the £115 million. We are seeing an improvement in cash conversion, principally reflecting the noncash nature of some of the things that have flowed through the income statement in 2023. In particular, the commercial settlements in Capita Experience. Strip those out and we're expecting cash conversion to move up from 45% in 2023 to that 60% to 70%.

We will continue to manage working capital very tightly. I wouldn't expect a material swing one way or the other in our usage of nonrecourse financing. As I said at the previous results announcement, at the margin it is our cheapest source of financing and we prefer to drawdown or utilise the nonrecourse financing facility rather than revolving credit facility and that you saw in our year end numbers.

But the main driver behind the underlying improvement in free cash flow is a greater level of cash-backed profits, as we see the benefit of the cost reduction programmes flowing through to the earnings of the Group and an improvement in cash conversion from no longer relying on a very substantial deferred income release. So 2023's deferred income release was over £80 million and we expect that to halve in 2024.

Adolfo Hernandez – *Capita – Chief Executive Officer*

Thank you. To your second question, what should we be doing more of and less of? I think I talked about some of that in the presentation. We need to be more intentional with the refocusing of activities and then just make sure that we replicate the things where we have the intention to be really good at and be known for. Just make sure that it's not in one particular contract or one particular vertical, but it happens across the Company. Equally we need to use a lot more technology, as I talked about, but not necessarily technology that we have to build, but to leverage partners and augment partners. I think that's a big difference.

Things that we should be doing a lot less of, I'd probably characterise as two things, less complexity and then we have to stop spending cash the way we do.

Chris Bamberry – *Peel Hunt*

Morning, Chris Bamberry, Peel Hunt. Where does Capita stand today in terms of its ability to address the threats and the opportunities of generative AI? Secondly, what are you seeing currently in terms of customer demand in CX across your key verticals? Finally, looking at that £100 million of new savings, what do you expect at end year savings for 2024 and 2025? Thank you.

Adolfo Hernandez – *Capita – Chief Executive Officer*

Okay, I'll take the first two. We're not starting from zero, that is the good news. We have - I talked about the particular use case that is public on British Army recruitment and gen AI and we are engaged in discussions and prototypes with customers in different parts of the value chain. Whether it's having an agent augmented copilots for productivity, or it's using some copilots for dealing with complaints, or looking at natural language processing for acceleration of training and most recently now we're also looking at efficiencies in our acquisition of talent and onboarding of that talent.

We have also enlisted the help of an independent company that is well advanced, for two reasons. Reason 1, from my past I know what's possible and I know what is happening out there, but obviously I think it's good to have somebody who's out there permanently and who has very experienced people around the world working with companies like ourselves and our customers around the world, so we can have access to those skills and those learnings.

The second one is capacity. As we do everything that we need to do in 2024, getting that extra help, that bandwidth to executive and accelerate is there. But we're not starting from scratch.

To your second question, what's the demand? I think every customer that I have engaged with on the experience side, they want agents to be better equipped and they want less of the passing the call from agent to agent, for the customer not having to identify themselves three or four times. They want agents to have more information in real time. Customers, our customers, our clients want our agents to sound more like them and have the right tone of voice. They want to have more analytics on the call so that the average handle time is well understood. We can also profile better agents on different shifts for different types of questions, so the demands are huge. Those are in what's the art of the possible.

Going forward, many of them are saying actually why do I have two operations, one for the front office and one for the back office. Why don't I put the customer at the centre and create a 360 degree review of the customer and then the teams interact about that. We started the year well, you saw the latest RNS on our Central European telco customer that is enlarging there. Where there is a sector that is in transformation, I think the opportunities are there for us to take them.

Tim Weller – *Capita – Chief Financial Officer*

Then in terms of how much of the £100 million is going to drop to the bottom line in 2024, just to be clear about the £100 million, to reiterate the point I made in the presentation, we do expect to reinvest a proportion of that cost saving from the £100 million in enhancing our service offering and improving our technology and to a degree becoming more competitive, brackets, in price. That is different in nature from the £60 million, so the first £60 million, that is a bottom-line benefit, that's a net number. The £100 million is going to be a lower amount that actually drops to our bottom line.

In 2024, I mentioned in the presentation that we expect our EBIT margin to improve during 2024. To give a bit of guidance on that, it's 4% in 2023, maybe a 30 to 40 basis point improvement between 2023 and 2024. That is a mixture of some profit headwinds with a reduced level of deferred income release in 2024, which I talked about. A nonrecurrence of the commercial settlement in Capita Experience and actually there is no accrual in 2023 for a management bonus. Those three are the big headwinds.

Offsetting that is the bottom-line benefit from wave 1 of the cost out programme and wave 2. Mathematically when you run through those, there is more than £60 million that must be dropping to the bottom line in 2024 to show that margin improvement. I'm not being precise, quite deliberately, we're going to come back to this at the Capital Markets Day in June.

David Brockton – *Deutsche Numis*

Good morning, it's David Brockton from Deutsche Numis. Can I ask two questions as well and they do continue the theme of the prior questions? Adolfo, just to understand from your prior experience how easy you feel it is to drive an improvement in the tech estate within a business, how quickly we should expect to see this. Is it a function of waiting for new contracts before you can implement replicable processes, or can you run faster at it? That's the first question.

Then the second question, I think I've got the guidance all nailed, but just in respect of DI releases and unwind, looking at the pipeline for this year there are a few existing customers where there was an element of renewal or potentially expansion. Could that create an unexpected DI unwind that's not within the guidance that obviously could be higher profit? Thanks.

Adolfo Hernandez – *Capita – Chief Executive Officer*

Okay, on the ease of improvement, it is not immediate. As any change that is worth doing, it has some complexity attached to it. But this is what I learnt in my previous role. The digital transformations that are successful and these big migrations are only successful if the direction comes from the top. If it is a tech-driven initiative, we'll always find a number of reasons why it can't be done or it's not the right time to do it. I think you can all relate to many examples like that. But when it's driven from the top, when this is the strategy, it's not a question of it, it's a question of how and how quickly and you make it a core to your strategy, in my experience when I have seen some of the companies I was working with, they are successful.

There are use cases and areas and stacks that move at different speeds, so what we are going to be looking at is at prioritising two types of work. We're going to be prioritising the low hanging fruit and we're also going to be prioritising those that are going to have the biggest impact, even if it's not low hanging, because we need to get started, right? So those two are the ones that get there. But with determination, strategy and effectively there is no optionality, it just becomes a plan, we get in some help where required and I'm confident we will get this done.

Tim Weller – *Capita – Chief Financial Officer*

Then on the potential renewals in the pipeline, actually most of the pipeline opportunities we talked about in the results announcement are new or expansion, as opposed to renewals. 2024 is not quite like 2023 or 2022, where there were some very substantial renewals coming through.

You're right, that can result in the sort of thing we saw with the O2 rollover into the VMO2 contract, the big one-off deferred income release. That should not be the case, so we probably have a more predictable pattern of deferred income in 2024 than has been the case for the previous couple of years and I guided to halving of the DI release between 2023 and 2024.

Adolfo Hernandez – *Capita – Chief Executive Officer*

Thanks very much for being here. Thanks for the support over the period and look forward to working with you over years to come. Thank you.

Tim Weller – *Capita – Chief Financial Officer*

Thank you.