



**G4S**

**Interim Management Statement**

**Conference Call**

**15th May 2012**

## **G4S - Interim Management Statement Conference Call - 15th May 2012**

### **G4S**

#### **SPEAKERS**

**Helen Parris, Director of Investor Relations**

**Nick Buckles, Chief Executive Officer**

**Trevor Dighton, Chief Financial Officer**

#### **QUESTIONS FROM**

**Rob Plant, JP Morgan**

**Jaime Brandwood, UBS**

**Andy Grobler, Credit Suisse**

**Laurent Brunelle, Exane BNP Paribas**

**Paul Checketts, Barclays Capital**

***Introduction***

**Helen Parris, Director Investor Relations**

Thank you, good morning everyone and welcome to our Interim Management Statement conference call. In a moment Nick Buckles, our CEO, will take you through the key points of the statement and then Trevor Dighton, our CFO, will make some brief comments on our financial position and then we'll open up the call for some Q&A.

As this is just an update on current trading we don't intend to get into a great amount of detail on specific countries today. We will update you in more detail on the growth opportunities for the Group at the Capital Markets Day next week on the 22nd of May and at our half year results, which are published on the 28th of August. So I'd now like to hand over to Nick who will give you a brief summary of today's statement

.....

***Presentation***

**Nick Buckles, Chief Executive Officer**

Good morning everybody. As you can see from our statement this morning we have seen revenues grow 7.5% at constant exchange rates and 6.7% at actual exchange rates - with sterling's strength expected to have a more significant impact as the year progresses.

We have continued to see a step up in organic growth in our developed markets and continued strong growth in developing markets. Overall organic growth was strong at 7% which we're very pleased with, with 4% in developed markets and developing markets continuing to grow strongly at around 11%. If you exclude the Olympic Games increase year on year organic growth was around 6%.

In the Secure Solutions products some of the strongest performing businesses in developed markets in the first quarter were the UK, where we took on Manned Security on the MoJ contract, the US where we took on Chrysler - sorry General Motors and some additional work for Bank of America and Canada where we took on the CATSA Aviation contract. The UK Government business was still slightly negative due to the lost contracts part of the way through 2011. It will be strongly positive going forward.

In Europe the best performing countries were Belgium, Norway and Finland. Eastern Europe continues to be challenging with further revenue declines in markets such as Romania and Hungary and of course Greece is still fairly problematic, although we are seeing better growth this year than last.

In terms of growth in developing markets Secure Solutions, very good in Latin America as you'd expect, some high inflation driving some strong double digit growth in Argentina, Brazil and Peru, but also very good in the Middle East and Africa.

In Cash Solutions we continue to deliver good organic growth of around 10% in developing markets and we were positive in developed. The businesses in the Middle East and Asia have all grown particularly well.

In developed markets the organic growth was affected in Cash Services by the loss of the HSBC contract in the UK about three quarters of the way through last year, but we have started the new contract with RBS a few weeks ago, so we do expect to see a strong improvement in growth and margins in the second half.

But overall margins for the three months were down 0.4% as we expected, due mainly - almost entirely actually to contract start up phasing in the UK Cash Solution business as I just mentioned. The UK Government business, where we're starting outside the Olympics, about £180 to £200m revenue in the first quarter and April and also the US Government, where as I mentioned at the results announcement, funding for demining and just government funding overall has become quite tough. And actually our US Government business was minus 12% organic growth domestically.

I'll now hand you over to Trevor to make some comments on the finances.

.....

***Financial Update***

**Trevor Dighton, Chief Financial Officer**

Thanks a lot Nick. As you remember from the full year our financial position remains strong and we've got significant current headroom from committed funds. A few weeks ago we raised €600m for five years in the public bond market, which will be used for general corporate purposes and to pay down short term bank borrowings.

We haven't made any acquisitions in the year so far, but we're working on a number of opportunities and still expect to spend around the £200m for the full year.

With our continued focus on debtor management, cash flow also remains strong and we're on track to hit our cash conversion target of 85% of PBITA for the full year.

I'll just hand you back to Nick for some final remarks before opening the call for Q&A.

.....

***Presentation***

**Nick Buckles, Chief Executive Officer**

Thanks Trev. So the businesses continue to perform well and we are very encouraged by the pipeline of opportunities we see ahead and we will go through them in more detail with you at the Capital Markets Day. And we do expect to improve the margin performance in the second half ahead of the four terms decline we've seen so far.

So thanks very much for your attention we're not happy to take any questions.

.....

**Telephone Operator**

Thank you. Ladies and gentlemen if you'd like to ask a question please press \*1 on your telephone keypad now. And our first question comes from the line of Rob Plant from JP Morgan. Please go ahead.

**Rob Plant, JP Morgan**

Morning Nick, Trevor and Helen. On the margin as you said people expected the worst performance in Q1, but when you look across the rest of this year do you think the full year margin will be flat, will it be down a bit, up a bit and how does it pan out quarter by quarter please?

---

**Nick Buckles, Chief Executive Officer**

We expect that variance to sort of reduce as we go through the year, you know down to the reasons I mentioned. We've got UK Cash business which we expect to significantly improve second half v. first, there won't be a big change in the second quarter v. first but certainly second half onwards. UK Government - all those start up issues will work their way through by about August time I would say, so we'll see a much stronger second half.

The US Government piece, there's a bit more work to do there. As I mentioned the demining business has actually halved its revenue year on year, so that's a significant downturn in revenue and a big profit impact from that. But we are working through a big restructuring programme in both the UK and the US demining in the next couple of months so we'll start to see an improvement there. But the underlying US Government margin won't improve back to prior year levels we don't believe during this year. So there's been quite a bit decline there.

But elsewhere the underlying business is still performing well; developing markets are growing strongly at higher margins. And so the prognosis really - and as we've said before - is a 7% margin for the next couple of years is our expectation give or a take a little bit basically, but with organic growth picking up significantly during the second half of this year.

You know looking at the different regions the UK is definitely going to be significantly stronger because the lost contracts fall away at the half year. US Government will get better from the minus 12%. US Commercial has been very strongly double digit that will probably come off a little bit because it's been incredibly strong. Canada will remain high for the year, developing markets will still be double digit and stronger and so all we can see is stronger organic growth going forward.

So I hope that answers the question overall.

---

**Rob Plant, JP Morgan**

Yeah, thanks Nick.

---

**Telephone Operator**

Thank you. And our next question comes from the line of Jaime Brandwood from UBS. Please go ahead.

.....

**Jaime Brandwood, UBS**

Morning, Nick I just wanted to just check something that you said - did you say that UK Government was still slightly negative year on year in Q1?

.....

**Nick Buckles, Chief Executive Officer**

Yes that's true.

.....

**Jaime Brandwood, UBS**

And are you expecting - you know given the phasing of the MoJ and other contracts for the UK Government growth ex Olympics to move into positive territory in Q2?

.....

**Nick Buckles, Chief Executive Officer**

Yes, because we've got Lincolnshire Police starting on the 1st of April and we've got Compass starting as well.

.....

**Jaime Brandwood, UBS**

Okay and in terms of the start-up contracts that you mentioned in the UK, I mean do you have a sense - you said these start-up costs will start to drop out as of August, do you have a sense for the first half as a whole in terms of some rough quantification of these UK Government start-up costs, what that might be?

.....

**Nick Buckles, Chief Executive Officer**

It's not so much start-up costs it's contract phasing. So basically if you imagine our first half of last year we had a Court Services contract annualising at £80m plus with double digit margins and we had a D&E contract which went through to about April of £50m annualised at decent margins but not double digit. And on both those contracts there were some exit benefits as well, in the second half more than the first half. So that's what we're really talking about. And the contracts we're starting up are all pretty much break even for the first three months, purely from the fact - you know you price these contracts on long term margins, they're seven year contracts and you don't expect to hit the ground running with big margins basically.

.....

**Jaime Brandwood, UBS**

No absolutely. And what's the latest that you're hearing on the electronic tagging renewal in terms of when we might hear more on that?

**Nick Buckles, Chief Executive Officer**

Well the contract, as we've mentioned before is broken down in a different way ...

.....

**Jaime Brandwood, UBS**

Exactly yeah.

.....

**Nick Buckles, Chief Executive Officer**

... supply, etc, etc. We're just working through the process, I don't think they'll - I mean the start date for the contract won't be until the mid-point of next year or between Easter and summer next year so there's a long way to go still through that.

.....

**Jaime Brandwood, UBS**

And the acceleration that you're talking about for the Group as a whole in terms of this 7% organic growth building through the year, are you also expecting acceleration excluding the Olympics in terms of that underlying 6?

.....

**Nick Buckles, Chief Executive Officer**

Yeah, that's really what I was trying to allude to in the first answer. The only business we can see going backwards against where it is at the moment is probably Europe because we had a lot of good contracts start towards the end of the first quarter last year in places like Belgium and I think the organic growth in Europe was about 4 or 5% in the first quarter, that will fall away a little bit during the year but it's not significant.

We've also got the European Parliament contract coming off. So that's the only area, apart from that we just see the others improving basically.

.....

**Jaime Brandwood, UBS**

And very lastly in terms of the acceleration in emerging markets, is there anything else that you'd sort of pick out there other than the inflation in places like Argentina and Latin America more generally, is there anything else that's giving you confidence about that acceleration in emerging markets?

.....

**Nick Buckles, Chief Executive Officer**

I mean you know we've been working on the sectors now for a little while, with just our business plan process around the regions and you know the opportunities for mining and oil and gas are large contracts, as opposed to the past where we're putting on lots of small business in new markets there's a big opportunity to put on large contracts now. So I think that will start to make a big difference in the second half.

.....

**Jaime Brandwood, UBS**

So that pipeline is something that we might hear about a week from now?

.....

**Nick Buckles, Chief Executive Officer**

Yes.

.....

**Jaime Brandwood, UBS**

Perfect, thank you.

.....

**Telephone Operator**

Thank you. And our next question comes from the line of Andy from Credit Suisse. Please go ahead.

.....

**Andy Grobler, Credit Suisse**

Hi good morning. Just one question remaining; just on the US Government business you mentioned the demining contract which you'd lost at the end - or had got a lot smaller at the end of last year, what's the situation with the rest of that business in terms of scope and pricing, what are you seeing as of now?

.....

**Nick Buckles, Chief Executive Officer**

Yeah, we'll probably give a big more detail on it at the Capital Markets Day, possibly - we're still thinking it through at the moment. But you know this business runs behind a proxy structure, and basically there are sort of three elements of the business, there's US domestic high end security, which is the traditional business which we've been doing for 30 or 40 years, so Savannah River, Oak Ridge, etc. And that part of the business - there has been quite a lot of rebids in the last 12 months, pricing is very, very tight, and price with the US Government has become the predominant measure of contract award once you hit a fairly low technical barrier.

So undoubtedly some of the underlying domestic business is lower margin than it has been, not significantly, but definitely lower. And the budgets are being squeezed and so there are reductions to service and there's a very slow process of getting new contracts awarded basically for new business. But in this area of the business it's fairly mature, we've got about 70% market share and the margins a little bit tighter than they have been.

Then if you go into the facilities services part which is classified facility services with security at the core the domestic part of that - we've been bidding on a very large number of contracts, we're still awaiting a number of decisions. We expect to land some of those in the second half, or before the second half which will see the growth improving in the domestic side.

And then overseas in terms of base operations we've won a big contract in Diego Garcia, Bahrain and that's a big area of growth that we see which is integrated facilities on overseas US bases, which will really be the growth driver we think in the future.

But then if you add on the demining and dogs business K9, that came with the acquisition of RONCO a few years ago, that's had a fantastic run for a couple of years. Strong double digit margins, about \$100m revenue annualised. And it's not a case of a contract coming off it's a case of funding for humanitarian demining drying up completely. So whereas we were working for the United Nations, etc, on large demining humanitarian projects in Iraq, Afghanistan, Sudan, basically the funding just stopped. And so we were left with large tranches of employed workforce and assets, which basically we couldn't deploy. And it's the same with our UK demining business which reports into the UK risk management business, the funding has just completely dried up so we've had to take a lot of cost out to get the business back into shape. And that will definitely show some improvements in the second half.

But that underlying inability of the US Government to award contracts, particularly in the integrated facilities area and the fact that the underlying margin in the domestic businesses has come under some pressure has meant that that's probably our poorest performing business relatively year on year and there's a lot of work to do on it.

.....

**Andy Grobler, Credit Suisse**

Okay, thank you very much.

.....

**Telephone Operator**

Thank you. And our next question comes from the line of Laurent from Exane BNP. Please go ahead.

.....

**Laurent Brunelle, Exane BNP Paribas**

Good morning. Just a follow up on organic sales growth, can you maybe split the 7% achieved in Q1 between price inflation and volume? And is it fair to assume for the full year 10% organic sales growth including the Olympic Games as you mentioned that the organic sales growth is accelerating without the help of the Olympic Games contract? Thank you.

.....

**Nick Buckles, Chief Executive Officer**

I mean the price v. volume is always very difficult to ascertain, particularly as the only measure we have of inflation is retail price index across countries, and often wage inflation is either lower or significantly higher. In developing markets it's nearly always 50/50 between price and volume. I think in developed markets I would say that nearly all of it is volume growth, there's not a lot of indexation still coming through in a number

of territories. I don't know where that leads the overall Group probably of the 7% I would say 5% is volume and 2% is price probably.

.....

**Laurent Brunelle, Exane BNP Paribas**

Okay.

.....

**Nick Buckles, Chief Executive Officer**

Then in terms of organic growth you know we never give predications so I can't really answer that 10% plus question. But all I'm saying is it wasn't quite 7% in the first quarter we rounded it up a little bit, but we do expect that to improve during the year. The Olympics will add 2 to 3% as I said. We may get to 10%, we'll have to wait and see how it pans out basically.

.....

**Laurent Brunelle, Exane BNP Paribas**

Okay, thank you very much.

.....

**Telephone Operator**

Thank you. And our next question comes from the line of Paul Checketts from Barclays. Please go ahead.

.....

**Paul Checketts, Barclays Capital**

Morning, I've got three questions please. Firstly are you finished with the cost cutting programme in the Cash Solutions business in the developed markets now? And the second question is on any particular movements or imbalances in price and wages across the business that are going on at the minute? And lastly on Denmark and there are some reports that you are going to divest part of the business there. I'm sure you won't want to talk about specifics, but maybe you'd just remind us how the Danish business breaks down between Cash and Secure and some of the systems operations please?

.....

**Nick Buckles, Chief Executive Officer**

Right, three questions - the first one cost cutting really has been across the whole group it hasn't just been on Cash Solutions developed markets. So basically we announced at the year-end that we'd undertaken something called Project Meadow in the Group and that's a round of short term overhead cost reductions in region and group following down into the business units. Most of that is now complete, some will still be coming through - the rest through to the half year, but most of that is complete to underpin our second half and margin performance going forward.

The third area of Project Meadow - or Meadow Tree is basically about getting the right shape of overhead for the future businesses that will take a little bit longer, that's

something we're working through. The other area of cost reduction we're working on and it's only early days - is the whole procurement issue where we're trying to address about £500m of bought in cost from outside the Group; so good progress being made, still a lot of work to do but definitely a good start.

The second question on prices and wages, you know we've said before Europe is often the only place where we get these issues. We're not massive in any particular way in Europe. I'm not aware as we speak of any major issues in terms of price v. wage around the different continental markets. The only market that we've seen quite a big economic effect quite quickly is the Netherlands where organic growth has slowed to negative and quite a lot of short term reductions as well. So that's the only real big economic impact we've seen that's different from where we expected to be back in March.

And then the third point around Denmark. Denmark is a mixed Secure Solutions business, it doesn't have any Cash Solutions at all and it's about - sorry it's about 160 million a year revenue so it's a fairly substantial business. The Secure Solutions or Manned Security piece is about 30 million in that figure. The remainder is some sort of alarms business ranging from B2C to B2SME through to large systems. And as part of our overall look at divestments we've said that B2C and maybe small alarms isn't fundamental to our strategy, our strategy is very much on large contract wins, outsourcing and driving strong organic growth. So it's part of a number of businesses that we're looking at to see if there are some value creation opportunities in line with how we sort of dealt with it in Norway basically.

.....

**Paul Checketts, Barclays Capital**

That's great, thanks very much.

.....

**Telephone Operator**

Thank you. Ladies and gentlemen please be reminded if you do wish to ask a question please press \*1 on your telephone keypad now.

Okay, ladies and gentlemen if you do wish to ask a question please press \*1 on your telephone keypad now.

We have no further questions coming through.

.....

**Nick Buckles, Chief Executive Officer**

Well thanks everybody for joining the call, I'm very pleased with the start to our year and we look forward to seeing you next week. So thanks very much.

.....

END