

Rolls-Royce Holdings plc Half-Yearly Results July 2011

Speaker key

JR	John Rishton
AS	Andrew Shilston
MT	Mike Terrett
ES	Ed Stacey
RM	Rami Myerson
DP	David Perry
HB	Harry Breach
SM	Sandy Morris
AG	Andrew Gollan
BF	Ben Fidler
ZK	Zafar Khan
CF	Celine Fornaro
RV	Rupinder Vig

Time-code	Speaker	Speech
00:00:00	JR	Let's make a start. Good morning. Thank you for coming. Welcome to Rolls-Royce's first half results. Given the very busy reporting day across our sector and the fact that this is our half year results, we intend to keep this short and focused. I will give an overview, Andrew Shilston will then take you through the financials and then in a break with tradition, we're
00:00:24		going to go home. Or alternatively, we could take questions. I want to cover the three topics before I hand over to Andrew. Firstly, to share my views on our business, give you a flavour of what I've been doing since I arrived, I'll make a few comments about the future. Secondly, highlight significant first half achievements. And thirdly, review the key financial
00:00:50		indicators that demonstrate the strong health of the business and the strong start that we've made to 2011. I joined the board of Rolls-Royce as a non-executive in 2007. I took on the role of CEO in April of this year. My time as non-executive gave me a good understanding of the breadth of the business. And since taking on an executive position, I've
00:01:18		concentrated on improving the depth of my knowledge by

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		visiting many of our facilities and meeting with many Rolls-Royce employees and our customers. My overview would be that this is an extraordinary company with extraordinary products and extraordinary people. Everywhere I've been, I've met with people at all levels and without exception, they
00:01:42		have been proud of the company, passionate and professional with an enthusiasm I have not seen in other businesses. The customers I have met have generally been complimentary about what we do and how we do it, but it is clear that on a number of occasions, we could have done better. So we need to sharpen our focus on the customer. Rolls-Royce has a
00:02:07		number of striking characteristics, a very long-cycle business, a huge order book that provides good long-term visibility in a number of our sectors, an exceptional brand and a strategy that has been in place for many years and has been followed consistently and proved its resilience. I supported that strategy as a non-executive and I support it now as Chief
00:02:34		Executive. Sir John Rose and his team have done an amazing job over the last decade in transforming the business and creating choices about where we grow in future. So I see my role as firstly ensuring that we deliver the promises we have already made. And as you know, we believe that revenues will double over the next decade from organic
00:02:58		growth alone. This is a complex and long-term task. We are investing in new facilities, new technology and recruiting new people. It is also clear that we must focus on execution, cost, cash conversion and efficiency. We must ensure that we are competitive on all fronts everywhere. The second main element of my role is to examine the options for future
00:03:28		growth so that we can make the right choices. So in summary, my take-away from my first few months is shown on the slide. Great people, great products, right strategy, a strong balance sheet. We need to sharpen our focus on customer, cash and costs, deliver the promises that we've already made and choices about how and where we grow in
00:03:55		the future. Turning to the first half of 2011, I think that there have been two really important decisions taken so far this year that will shape the agenda for many years to come. Firstly, the selection of the enhanced Trent XWB to be the exclusive engine to power the airbus A350-1000. This builds on our strong position in wide body aircraft and sets the stage
00:04:25		for significant growth if those engines are delivered and operated over the next few decades. This aircraft will be a

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		powerful, long-term growth driver for our Civil business and the Group. Secondly, our joint offer with Daimler for Tognum that is progressing well. This will add breadth and depth to our Marine and Energy businesses. We will bring significant
00:04:51		systems integration and aftermarket capabilities to an already successful business. Tognum possesses a particularly strong diesel portfolio that will complement our own diesel and gas engine technologies, allowing us to double the revenues of the business in much less than a decade. In addition, we have continued to invest in refreshing and growing our facilities
00:05:16		and strengthening our supply chain. You will have seen that we've invested more than £600 million on capex and on research and product development in the first half. These investments include the continued development of new facilities in the US and Singapore, both of which have started initial production and pre-production, and the extension of
00:05:40		our services network as we grow our global capabilities to support customers. For example, we have opened new Marine centres in Holland, Poland and Namibia and further extended our Civil overhaul facility in Hong Kong. As you will have read, we are confirming the full-year guidance that we gave in February for 2011 in terms of revenue and profit
00:06:05		growth. And, excluding the Tognum acquisition, the core business will generate a modest cash inflow. As you can see from this slide, overall a strong performance in the first half. The headlines are a record order book, up 4% to £61.4 billion. We won new orders, 8.7 billion in the first half with around 75% coming from Civil Aerospace where we continue
00:06:37		to take around half of the lucrative wide-body market with new orders on four different Trent engine types for customers in Europe, the Middle East and Asia. Orders in Marine and Energy were similar to last year, but some sectors, notably oil and gas, will be second half biased. We remain encouraged by what is going on in both offshore exploration and production
00:07:05		and land-based pipeline and transportation activities. For example, investment announcements from Petrobras and BG Group make it clear that there will be good opportunities to support the development and extraction of new reserves around the world. The order book, once again, serves to highlight the global nature and the rapid growth in our market-position
00:07:27		over the last few years. Today, 47% relates to Asia and the

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		Middle East, with that element alone now larger than the entire order book just five years ago. Underlying revenues grew by 4%, with services up 10% and a slight reduction in Original Equipment sales, mainly a function of the Marine slow down that we had signalled early this year.
00:07:55		Underlying profits grew by 28%, but benefited from a one-off settlement of some UK Defence contracts. Excluding this benefit, underlying profits were up 15%. The balance sheet remained strong; we finished the period with nearly £1.5 billion in cash after £82 million outflow from the start of the year. Average net cash fell to £780 million. Reflecting our
00:08:25		confidence in the strength and resilience of the business, the outlook for growth over the next few years and the opportunities we have to drive performance by focusing relentlessly on execution, we have increased the first half payment to shareholders by 8%. So in summary, a strong
00:08:43		first half. We are well-positioned and confident about the future. I believe that we must sharpen our focus on customers, cost and cash, deliver the promises that have been made, that will double the revenues over the next decade, and we have choices to make about future growth. Thank you.
00:09:14	AS	Right, well good morning. The flavour of this section is very much a case, I think, of this is largely all in line with guidance, so I'm going to be fairly brief. And I know there's a lot on today and you've got a lot of other companies to look at. As usual, I'll focus on the underlying results. The headline result is somewhat more eye-catching with the usual
00:09:35		revaluation movements in this half-year have been quite heavily positive. But all that detail's in the handout, just to reconcile between the headline numbers and what I'm going to talk about here. First of all, this familiar chart is looking at how profits have moved from one half year to the next. Taking foreign exchange, first of all, back in February we
00:10:01		said we would have the benefit of about a 6-9 cent improvement in the achieved rate through use of our hedge book over the full year and there's no change to that guidance. In the first half of the year, we had benefit from the hedge book of about \$36 million and that was offset by a small translation negative of about £13 million. I mention that
00:10:26		simply because we don't forecast translation differences and that is a change to or would affect previous guidance, that small £13 million number. With regard to R & D compared to previous guidance, we expect the full year to be up

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		around 20 million, something like that. About three quarters of that is spend and some of it is accounting effects. We knew,
00:10:49		obviously, that R & D this year, there'd be a heavier charge than last year. That guidance we gave back in February and that's mostly to do with the mix of activity moving away from the Trent 1000 to the engine for the Airbus A350. With regard to operating income, there's no change to full year guidance, so that negative there is exactly as we expected.
00:11:15		And then we move to the one-off items on the right hand side, the Industrial Trent provision that we made last year was a one-off. I think John's already alluded to that. And we have been in conversation with the MoD on contract terminations and there is some benefit arising from that as well. And I'll touch on that in the Defence sector in a moment. So turning to the
00:11:40		Civil business, first of all, continuing the very strong wide-body aircraft story, there's a lot of really good data in the back, in the appendices about market share by aircraft type, which I won't go into in detail now. I think you're familiar with that. But if you add it all up, we have a very strong market share story to tell of at least 50% in aggregate across the whole
00:12:0		market with much greater market share in some other product types. For example, the Airbus A350. Now we talk about installed thrust as a proxy for value, we've done that, I think, for quite some time now. Just to give you a sense of the strength of this Trent story that's emerging, or will emerge, over the next few years: we have about 140 million lbs of installed thrust in the Trent fleet today. And if you look at the
00:12:34		next 20 years and assume we get about 50% of the market, then we should deliver about another 700 million lbs of thrust over the next 20 years. And that isn't all in the distant future; we will double Trent deliveries in the next five years. So a very powerful story there coming through. Services
00:12:54		revenues, we guided that the full year would be up around 6 or 7%. We're not changing that. Of course, remember that in 2010, we had that Aviall logistics deal which meant that the year-on-year growth figure looks a little lower than it would if you... than if you had excluded that. If you unpick that services growth, we've had good double-digit growth in
00:13:19		our large engine TotalCare business and slightly slower growth in the smaller engines and time and material business. Yes, there is some recovery in time and material

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		activity, but to an extent this is going to happen later in the year as the arisings go through the overhaul shops. Worth just pointing out, I think, that because of the nature of our aftermarket business,
00:13:44		because it is so long-term contract-based, it tends to be more stable than some other companies who I think have been reporting quite significant quarter-on-quarter gains in their time and material business. The beauty of our long-term contract model is that we're much more stable and we get paid on an hourly basis, not on shop visits and that's a great benefit
00:14:05		I think both to the customer and to us because it produces predictability. Profits to date are more or less as we expected and compared to previous guidance, we'll see a small effect from the nuclear disaster in Japan that has caused some disruption to our supply chains and delayed deliveries into the factories and also delayed some overhaul activity and that's
00:14:31		going to cost us about £10 million or thereabouts over the full year. And there are some slightly higher R & D costs as well. Then finally, there's no change to our guidance on the effects of the Trent 900 event last year, so that's in line with what we said before. Turning to Defence on the two new development programmes for getting through to key milestones that's on
00:14:57		the TP 400 for the European A400M, their military transport aircraft, and the STOVL engine, likewise JSF development is proceeding satisfactorily. Work has largely stopped on the alternative engine for the Joint Strike Fighter while GE and ourselves consider our options. The programme isn't completely stopped in the language that's used in the United
00:15:23		States because if that happens, all the tooling and everything else is destroyed. That has not happened. So I think there are still further conversations to be had between GE and ourselves and the US government about where this programme goes. But for the time being, funding has been stopped. The transport sector continue to be a very strong theme I think
00:15:41		we've talked about for quite a number of half year periods over the last two or three years. And we're also pursuing export opportunities and service ideas to offset UK/US slowdown in some procurement programmes. Obviously the first half is dominated by the profit effect of settling these contracts that were cancelled by the UK MoD and I think BAE
00:16:08		was in a similar position, they talked about that earlier on

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		today. So other than this one-off, the full year will be largely as we expected in profit terms. Now turning to Marine, some good news in the Naval sector. We don't talk a lot about that usually, but we've won, as you can see here, the first order on
00:16:29		the Littoral Combat Ship programme for ten ships, which is a major foothold for us now in the US Navy. And in the UK, we've had confirmation that the UK Government will support the next generation nuclear reactor, the PWR3 reactor for the next generation of nuclear subs. And that is a very, very long-term business as well. Turning to other areas of Marine,
00:16:53		we've definitely passed the inflection point on orders in the oil and gas sector, that's called the Offshore market, it's just taking a little bit longer than normal to get customers to sign on the dotted line, but there's no point... sorry, there's... it's clearly, it's quite clear that the inflection point has been passed and so we'll see some turnarounds, some significant
00:17:14		turn-around in Original Equipment deliveries. In Marine, they were down about 25% for the half year. They'll recover quite strongly over the second half of the year, so overall OE will be down about 10% in Marine which is plus or minus what we guided back in February. And services are growing at a good double-digit rate, about 11% and that's based on all the
00:17:38		work we've put in... been putting into dockside services presence around the world which has been very successful. Worth just pointing out here, I think, that we're not involved in the, the big bulk carrier market, container ship market. I think one or two other companies in the sector have had some issues in that piece of the marketplace. We're not in that, our game is
00:17:59		in specialised vessels, particularly involved with the oil and gas industry, which as you've heard already is pretty busy in deep-water offshore in exploration and production. The margins are benefiting from a greater percentage proportion of services in the revenue mix, but overall there's no real change to guidance for the full year. Turning to the last of the
00:18:23		four divisions, Energy, we continue to invest to improve products and in new businesses such as nuclear, fuel cells and tidal power. We still believe Civil Nuclear is worth pursuing, despite the Fukushima disaster in Japan. And the reason for that is our capability is unique and we're developing plans with the key reactor vendors and all the

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		other participants in
00:18:48		the market. And I think that the quality of our brand, together with our capability, is meaning that we've got access to all the key players in that marketplace. Now as in Oil & Gas, in Marine, order enquiry is picking up but current revenue growth is mostly from services. So half your profit compared to last year clearly benefited from non-recurrence of the refit
00:19:14		cost on the Industrial Trents that didn't recur. And for the full year, we expect slightly lower profits than we previously guided, mostly due to slightly lower OE, some new Civil Nuclear spend and some other people-related cost, bid costs and the like. Brief update on Tognum, we're very pleased with the take-up of the joint bid for Tognum. We've achieved
00:19:42		very nearly 95% in aggregate acceptances to date, which is good. The regulatory process, especially with regard to all the anti-trust clearances, is going very well and we would expect completions sometime in the autumn. And after that, we'll follow on with the process to squeeze out the minorities. Now all that timeline is laid out in the appendix so that you
00:20:06		can see how that's all going to work. In terms of the financials this year, there'll be no significant effect on our numbers because completion happens later on in the year. We've only got half of the business and there's some bid costs, so there won't be much effect. But clearly from the 1st of January next year, we will get the full benefit of half of
00:20:27		Tognum's earnings incorporated into our numbers. Now, the precise accounting cosmetics of that will change as we go through the year and I won't go into the detail now. But economically, we will have an entitlement to half of the earnings of that company in terms of the way the accounts are presented. The other thing that I think is worth mentioning is
00:20:48		that although we can't formally have detailed conversations with the Tognum management until this transaction completes together with Daimler, there's no doubt that there is unanimity between Daimler, ourselves and Tognum about what needed to be done to move this whole business forward. And we're starting those conversations in the
00:21:10		most detailed way that we're permitted subject to not having completed the transaction. In terms of our balance sheet, as ever, a strong balance sheet is a key part of the Rolls-Royce story. You can see here we've got sufficient

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		resources to pay for our share of the Tognum acquisition from our own internal resources, we don't need to raise any more money and
00:21:34		the credit rating is secure. The rating agencies know about the Tognum acquisition, they've had a look at it and our credit rating is unchanged. The average cash figure is down a little bit on the first half last year and that's largely because the effect of the ODIM acquisition, which was about £150 million, has a much greater effect on the first half this year than it did
00:21:57		in the first half last year in terms of how the averages are calculated. Customer finance and supply chain finance position is largely unchanged and finally there are some changes to the methods of calculating pension liabilities and US healthcare liabilities that appear in the notes in the headline to underlying reconciliation. Now these are economic benefits that will be
00:22:22		beneficial to the company over many, many years, but we've not included them in the underlying result. Looking at cash flow, we're still investing heavily, as you can see here. There's no doubt that industrialising the growth in Trent deliveries over the next five years is going to require some physical investment that is reflected here in the financials.
00:22:46		The breakdown is all in the press release, the breakdown between intangibles and fixed assets and so forth, it's all in the handout. But for the full year, we expect to spend something like £800 million, that's currently our expectation. Working capital is a big subject, as I've said before, and I think the gross working capital balances in aggregate add up to
00:23:08		something like £14 billion. So you can see that relatively small movements in these numbers can have an effect on the business. What's been happening in the first half is that we've had some modest inventory build as we anticipate the entry into service for the Gulfstream G650, Boeing 787, and then you add to that the disruptive effect from the nuclear disaster
00:23:31		in Japan and the knock on effects in our supply chain, inventories in aggregate have gone up something like £200 million at the half year. Now some of that will unwind by the full year, but you can see that's one of the reasons why we've got a small negative on working capital. The M&A below the line relates to the purchase of a small number of Tognum shares.
00:23:52		Clearly that number is going to be a lot bigger at the full

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		year, but if you ignore that we expect a modest cash inflow for the full year. So to summarise full year guidance, we expect a mid single digit overall increase in revenues with the OE held back a little bit by a small decline in Marine. The Civil business we expect to recover strongly, as I've said earlier. The tone is
00:24:22		definitely getting better in Marine and Energy from oil and gas demand and the order flow rising from that. Although profits are likely to be flat for the full year. The one off item in Defence is largely offset by the small translation difference that I've alluded to, some R&D costs and the impact from
00:24:44		Japan, all of those effects occurring in other businesses. So net net, there's no overall change to guidance in profits and we expect a small cash inflow if you put Tognum investment to one side. So that's the end of the formal comments and I think we'll now take questions.
00:25:04	JR	Thanks, Andrew. Very happy to take questions. If you could say your name, who you work for and wait for the microphones that'll be coming around, then I will try to manage the question-taking as best I can. So who would like to ask the first question? Right at the very front? Thank you.
00:25:29	DP	Thank you, I'm David Perry from Goldman Sachs. I've got two questions. You mentioned customer, cash and cost reduction several times in your intro. Could you elaborate a little bit on the cost reduction piece? I mean Rolls has been doing this for a long time and normally Mike gives us an update, but where you think... what you think still can be
00:25:54		done, please? And the second question is Rolls has this fantastic story on the wide bodies coming, but that also gives you a bit of a profit headwind for the next few years. Do you think there's anything you can do to try and help overcome that profit headwind or it just has to work its course and we just have to be patient?
00:26:17	JR	Thanks, David. Couple of comments and maybe I'll ask Mike and Andrew to add to the comments that I make. Having travelled around the business and sat and talked with Mike, Andrew and the rest of the management team, I think that there is opportunity for us to sharpen our focus a little in the areas that you talked about. So customer, cash and cost being
00:26:44		those three C's. What that means is can we turn up the dial with some attention on those a little further? And certainly on the cash and the cost side, they have received significant attention over many years and Mike and the team have

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		done a terrific job. We need to keep going down that journey and I think, you know, my observation coming in new is that, while
00:27:07		we're making good progress on that, we need to continue to make good progress on it. And I certainly want to make sure that within the organisation, those things are considered to be important to our future. But you should be under no misunderstanding that Mike and the team have done a terrific
00:27:24		job improving cost performance over many years. So this is about sharpening the focus, about turning that dial up a little bit, about making sure that everyone knows just how important it is as we start to reach a significant ramp-up. Mike, would you like to add anything?
00:27:43	MT	Thanks for that, John. Yes, I do give you an update and because the supply chain and operational stuff has a continuity about it, it doesn't change a lot from half to half. But it's probably worth reflecting that we've had several years where inflation pressures have outstripped our efforts on productivity. But as we guided this year, productivity efforts will be offset by inflationary pressures, which are still there,
00:28:09		which we know about, and Energy and materials. We're investing very heavily, as Andrew's just said, in a lot of these facilities, both new facilities that we've invested in, new facilities that our supply chain are invested in and also new machine tools and processes going into our existing facilities. These strands of activity on the product side are coming to
00:28:35		fruition but clearly as you build a new facility, you put in new machine tools, there's a lag before you actually start to get the volume coming through and the benefits. And those will take some time. We're also heavily invested in IT processes and we've been doing this for a number of years and we're starting to accelerate that. And as John has said, a focus in the
00:29:01		organisation on delivering what we've promised and delivering not just to the customer, but also to our business plans is something that we're really focusing in on in the business. And John's encouraging us on that and that's great.
00:29:15	JR	Thanks, Mike. In terms of your second question about the wide bodies, the R&D headwind, I'm going to ask Andrew to make a few comments on that. Clearly the investments that we're making to support the ramp-up, particularly in the wide bodied area, clearly the investments we're making in

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		new products, the fact that we've had three new wide bodied
00:29:36		engines in very close succession results in the cost increases you see. But I think, you know, the beauty of the strategy that the team have put in place and the portfolio approach really shows its strength in that kind of environment where, you know, despite the economic turbulence that we've experienced over the last four or five years, despite the fact
00:29:59		that we've had these investments and we are set for growth, the overall group profitability and group revenues have progressed well through that period. Which is why I said during the course of my presentation that, you know, I supported the strategy when I was a non-executive and I continue to support it now. I think it's an extremely well
00:30:18		thought through, well implemented and well led strategy that gives significant benefit and helps to address the kind of issues that you're talking about which are inevitable when you are launching a significant new product. Andrew, would you like to...?
00:30:33	AS	Well, I think my colleagues have covered most of the issues now. What I would say on the portfolio point is that probably four or five years ago, we... if we were projecting forward to 2011, we wouldn't have envisaged anything like the quantity of Trent 700 engines going into production on the Airbus
00:30:53		A330. So I think part of the answer to the new product question is the aftermarket that's growing from the installed base and the portfolio effect that allowed us to enjoy the continuing life of what five years ago was considered to be an aircraft with a fairly limited life. But that's... I think we've
00:31:14		always said that, that we were in the market for lift. There is demand for lift in aggregate and if some programs are delayed or some capacity is delayed, then older programs tend to benefit. And I think that's what'll happen over the next few years.
00:31:31	JR	Thanks, Andrew. Okay, the next question, we've got another one right at the front? Thanks.
00:31:39	BF	Yes, Ben Fidler from Deutsche Bank. Three questions, please. Firstly, one for you, John, which is just to understand your aspirations, goals for where you think the margins might be capable of getting in the Civil Aerospace business in that today around 10%, some way below most of your peers in that area. What are your sort of own aspirations might be for

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00:32:01		that? The second question was just to understand, probably one for Andrew, really, your guidance for Marine being unchanged for the full year, which based on my scribbled notes from February seems to imply flat sales, flat EBIT, implication flat margin. You did a brilliant margin in the first half, 15% of Marine. Just wondering why that unwinds so
00:32:23		much at the margin level in H2 or whether it's just conservatism. And the third question was just to understand the R&D implications of the extra development, what you're going to have to do for the 350-1000 engine and where that leaves R&D and how we should think about that for the next couple of years?
00:32:43	JR	Thanks, Ben. Let me take the first one and maybe ask Andrew to... thoughts on two and three. I think, you know, in terms of margins, you know, if I look at our margins and look at some of our competitors' margins, if I look at the future potential revenue growth that we've talked about, it would be... it would be disappointing if we didn't improve
00:33:04		them over time. In terms of aspirations, I'm certainly not going to get into, you know, where I would hope, like or want them to be in this meeting. But as you would expect internally, that's something that we talk about quite a bit. But certainly with the doubling of revenues, it would... you would hope that they would improve. Andrew?
00:33:27	AS	Thank you. And I think on the Marine margin, probably the answer is that the margin expansion in the first half is because of the greater proportion of aftermarket, which has a higher margin. And what I said is that OE would recover quite significantly in the second half, so that mix is going to work slightly to our disfavour in the second half. In terms of R&D,
00:33:53		if you've inferred from my comment about R&D this year that that's associated with the A350s, that's not the case. It's small bits and pieces across the whole business. And what we've always said, looking at the R&D in total, is that it's the portfolio points that as the... for example, as the engine for the Boeing 787 goes into service, you've got more
00:34:17		engineering time to address the engine for the Airbus A350. So when you look at it in aggregate, as the old programs mature, you have more resource available for new. So I don't think you should assume that what was said in the past in R&D is really going to change in terms of overall numbers.
00:34:34	BF	So just to confirm, the implication from that in terms of resource is R&D stays flat. Is that what you're saying?

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	AS	Well as you know, we don't... we don't give multi-year guidance, but what I'm telling you, there's not going to be a significant change to resource levels.
	BF	Okay, thank you very much.
00:34:48	JR	If I could just raise this up on the A350 exclusive for the 1000. You know, I think that's a really, really important win for Rolls-Royce and I certainly look at that as a very positive thing really in how strong our position on the wide bodied market is and in the total A350 fleet as well. So I have to say I think it's an exceptionally positive, positive position to be in. So the next question? Again, we'll just sort of keep at the front-ish. Yes? That's it, yes. Oh.
00:35:26	ZK	Good morning, it's Zafar Khan from Societe Generale. One for you, John, just trying to understand really your strategy on the engines for the narrow body. Clearly very well strategy on the wide body, very good position, but I'm really struggling to understand where you're going to go on the narrow bodies. So if you could help us with that, I'd be very grateful.
00:35:46	JR	Okay, on the narrow body. A couple of comments. First of all, I think that, you know, our decision not to go on the re-engined Airbus was a sensible decision from a business case perspective. You know, if we weigh up where we want to invest our money and the returns that we can make, our view was from a simply financial... on a financial basis, that
00:36:15		there were areas that we could do better on. So I think that was a sensible and rational decision. In terms of what Boeing now seem to be saying about re-engining rather than a new aircraft, as you're all aware, CFM is certainly exclusive on the 737. My understanding, but it is only my understanding would be that that wouldn't change with the re-engining. So
00:36:37		that doesn't alter the position going forward. So that's where we are. I'm comfortable with the position that we're on narrow bodies. If you look further ahead for new aircraft, I think we would take, naturally as you would expect, take a serious look at that and would envisage that that would be something
00:36:57		that we would be interested in. So the fact that we're not on the NEO and nothing's changed on the 737, you shouldn't read into that that that's not a part of the market that we wouldn't be interested in. But I'm comfortable, personally, with the position that we're currently in in that market when I

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00:37:12		look at the other things that we invested our money in and our position on the wide body, for example, in Civil... but also across the broader spectrum. So if you take into account the Marine business, the Tognum acquisition, those kind of things, for me it's a rational and sensible business decision.
00:37:28	ZK	So should I assume that you are still interested in the smaller engine and narrow body's still very much part of the longer term plan?
	JR	Yes, you should take into account the fact that, yes, that's a part of the market that is an important part of the market and it's certainly one that we would look very seriously at as and
00:37:45		when new aircraft are considered. You shouldn't take into account... you should not draw the conclusion that, because we're not on the re-engine NEO, that we have exited that market. That would be completely the wrong conclusion to draw from that.
	ZK	Thank you.
00:38:04	CF	Good morning, Celine Fornaro, Bank of America and Merrill Lynch. Two questions, if I may, on services? The first one is on the aftermarket for Civil Aerospace, the guidance for the full year. So on H1, you know, you grow probably slightly better than your average full year guidance. Why should we expect to slow down in H2? Is there a specific reason for
00:38:25		that? And also if you could just give a bit more colour on the performance between the large engines on time and material and maybe the business jet, if that's coming back or we're seeing the first green shoots? And the second question, still on services, in the Marine business, is given the
00:38:41		strong growth but the OE recovering, how should we think about the split? You know, services versus OE, you know, where it is today and where is it going? And also, when you open these new centres in services, how quickly after that do you generate, you know, service business or you gain.
00:38:38		And the second question, still on services in the Marine business, is given the strong growth, about the OE recovering, how should we think about the splits, you know, services versus OE, you know, where it is today and where is it going, also, when you open these new centres in services, how quickly after that do you generate, you know, service business, or you gain market share?
	JR	Thank you for that series of questions. Andrew, if you could help me out with those, that would be excellent.

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00:39:10	AS	It's quite an exciting menu to work my way through. Okay, well let's pick up on the Civil Aerospace aftermarket first of all. I did point out that we had the Aviall deal in the second half of last year, which, when you're looking at the year-on-year growth, all tended to press that percentage for the second half of the year. So I think that's probably the answer to that point. In terms of small engines, I don't think there's anything more to the guidance I've already given. I mean, we expect good double-digit growth in our large engine TotalCare business, and in smaller engines it's fairly flat, and we're seeing some of the older V2500 engines, or the older aircraft gradually going out of service, maintenance events perhaps I think are stretching out I think, Safrane was seeing some of that, and in other respects, on business jets, it's pretty much steady as she goes.
00:40:12		So I think that's why, despite the fact that the large engine story is very strong, when you add it all up, and produce the overall Civil business result, it's down around 6% or 7%. Looking at Marine, well I think the story on services is pretty clear, that it's growing at a nice double-digit rate, there's every reason to assume we can continue to make that grow, just by virtue of greater dockside presence and the growth in installed base, and so we don't any target any split, to, you know, aftermarket, it is what it is, it's just a result. I think I suggested that the tone in OE is getting better, so OE in Marine in the second half will be better than the first half, and obviously we will update that guidance in the new year as we go looking into 2012.
00:41:09		In terms of the new centres that we put into our service network, the benefit is pretty rapid, because mostly it derives from putting service engineers on the dockside, and the service engineers get into the vessels pretty quickly, and so they are earning money almost from the date that you commission the factories. So that's quite a nice position to be in, it's not a heavy investment, long term payback story at all, quite short cycle.
	JR	Thanks. Next question.
00:41:43	ES	It's Ed Stacey from Espirito Santo, just one question, and it's for John, on the three Cs, the customer one, and the need to sharpen the focus on the customer. I guess in the last sort of 12, 18 months we had the event on the A380, and maybe that sort of raises some issues, but we probably think of that as being kind of an extraordinary event. In more general terms, is there something you're doing wrong currently in the way that you support your customers, and something

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		you need to change? Could you maybe give an example of what you do you mean by the need to sharpen the focus on the customer?
00:42:12	JR	I don't think there's anything we're doing wrong in terms of our customer, and again, if I go back to the success the business has had in terms of winning business across all its sectors, it's quite clear that we have good relationships with our customers. As I've said, I've met most of ...the customers that I've met have all been very complimentary. So what do I mean? I think, as with all things, there are some things that we can sharpen up upon, there are things that we need to improve, around, and some of it is in quite some detail.
00:42:50		I think coming from a different business background, you know, I come from a business to consumer background, rather than a business to business background, and in those businesses the organisations tend to be more customer in their mind, in everything that they do. So I think there's a little bit of ...it isn't quite the same in the business to business, which I understand, but I think that, you know, there's some areas that we can tweak, some areas that we can improve our attention on our customers.
00:43:25		I've been discussing that with my colleagues, and I think there's a general view that that is the case, but this doesn't mean that anything was necessarily wrong, I think this is an area that we can improve and get better at, rather than it's wrong so we must change it. I think we do it generally very, very well. So in many ways, I'd go back to the answer that I gave on cost, which is, this is an area where I would just like to turn up the dial a little bit, turn up a little bit of attention, and put a little bit more focus on that area than maybe there has been. That doesn't mean that it was bad or wrong in the past.
	ES	Thanks.
	JR	We'll come right back to the front again, and then we will drift backwards.
00:44:05	RM	Rami Myerson from UBS. Just two quick questions, you talked about the inflection point in Marine, and on the ordering taken, Marine activity and order interest, can you tell us what you are seeing so far year to date, and potentially the interest going forward to the end of the year, and if I understood correctly, there's an Advance 2 to Advance 3, or Advantage 2 to Advantage 3, engines currently under development for the narrow body replacement after American's decision to re-engine with the CFM Leap-X

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		engine, does that mean that that has been pushed to the right, and development that will be deferred until you see the potential for new narrow body aircraft?
00:44:50	JR	Let's start with the second one first, Mike, I don't know if you want to make some comments about that?
00:44:55	MT	Yes, basically Advance 2 to Advance 3, we have technology programmes, and the technologies that we develop are applicable at different thrusts, so clearly you know, compressors, turbines, and so on, and so the programmes that we have feed all of our programmes, both Civil and Defence, but certainly across all the Civil portfolio. So we don't see change in our technology programmes at all as a result of this. The other thing to remind everybody is the Trent XWB is demonstrating now the world's most efficient performance, from the data that we have. So in terms of technology, we're actually living on the cutting edge of that on a daily basis. The technology that lies behind future developments has applications in current programmes as well as in future programmes.
00:45:47	AS	Just on the Marine order point, I think actually, if you look at the press release, there's probably all that we need to say on that subject, but just to pick out of a few highlights. We took a billion pounds' worth of orders in the first half, and the point about the Marine business is that it's quite fragmented, it's not like the Civil Aerospace business where individual orders can be worth very large amounts of money and they're worth announcing individually. Marine orders tend to be small, but they aggregate up to quite big numbers. But just some examples here, about the UT decision and system integration packages to oil and gas sets, we've won more than a hundred million of orders in four or five different countries all over the world, and this is another example here, an order for six UT offshore supply vessels by the Blue Sea Group.
00:46:40		So there's a lot going on, and it's all over the world, and what's driving it is the same thing, it's activity in the deep water oil and gas sector, which is driven partly by the oil price and partly by the fact that there are very few places that oil companies can invest to own oil reserves other than offshore.
	JR	Right in the middle, and then we will definitely come further back.
00:47:05	RV	Yes, Rupinder Vig from Morgan Stanley. Two questions, perhaps one for John first, you know, going back to the three Cs, if we think about cash, how quickly should we be able to

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		<p>see improvements in cash given we've got ongoing headwinds such as new programme investment, we've got the inventory bill that we talked about, so how near-term and objective can that be to sharpen on cash, if you like, and then a question for Mike, perhaps, on the operational side, we've talked today about doubling Trent production in five years. Are the resources in place to be able to do that, what else needs to happen, so you know, what are the big challenges from that perspective, to be able to get to a stage where you can double the production in five years on Trent?</p>
00:47:45	JR	<p>Thanks. One of the dangers with being the new guy, as soon as you mention something, it becomes the sort of flavour of the month internally and externally, so let me reemphasise, this is about sharpening our focus, just pushing a little harder on it. I mean one of the things that, if I read any of your reports, over a long period of time, that you would talk about, I think is cash and cash conversion. So I don't think I'm sort of, breaking new boundaries by suggesting that we could maybe increase our focus on cash, and there are clearly a number of areas that we can look to, and there are clearly a number of headwinds that we have faced, some that we will continue to face. So the question is, how do you get the organisation more interested in cash?</p>
00:48:25		<p>Again, this is about, you know, sharpening the focus rather than turning a switch that was off on. Andrew and the team have been very focussed on cash, but nevertheless, I think it's an area that we could usefully get some more people in the organisation more interested in, and that will be beneficial. So again, sort of, I run the gauntlet in terms of, sort of, you've already termed it the three Cs, I can already read tomorrow's reports, thank you very much indeed. Again, this is about, you know, sort of my views and just increasing the emphasis in a few places on a few topics, none of which, in my view, would surprise you in the slightest, if I read your reports in total. Mike.</p>
00:49:20	MT	<p>Okay thank you. Well, it's a big subject to talk about, preparation for the growth in Trent, but just a few things to put into context. First of all, the significant ramp up of new product is clearly the Trent 1000 and the Trent XWB, although there is a not insubstantial ramp-up still on the Trent 700, as was mentioned earlier. So as you know, from the airframers' requirements, that ramp-up is, you know, starting now on the 787, and will really start in a couple of years' time on the XWB. So, it's not sort of a totally immediate thing to ramp-up to the full rates.</p>

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00:50:00		I will talk about the factories that we are building, around what we call our Make Components, because I can paint that picture more simply. But also, our suppliers and our partners are putting in similar investments. So let's just talk about, I will talk about three major Make Components first. You know, the fan blade and the assembly of the engine, that's clearly Make, we clearly make turbine blades and we clearly make the rotating discs. In those three areas, we've announced investments and some are now complete, to effectively duplicate capacity, but also duplicate it with modern methods and modern processes, which will also read across into our older facilities.
00:50:50		So if I just give you a quick update on those, in CrossPointe, Virginia, we are making discs, and that factory opened this first half, we've produced parts, these are production parts, and they're going through the production-proving process, but they are production parts that will fly. So that's a brand new facility in Virginia, the USA, and it looks great. In Singapore, we have two major facilities, as well as a hub complex, on what is actually a stunning aerospace park in Seletar Singapore. That will be officially opened next year, but at the moment, we are stocking it with machine tools, and are production-proving the processes to do two things.
00:51:40		One is to make wide chord fan blades for the Trent, which is clearly our iconic feature, and the thing you see as you get on an aeroplane, and secondly, to assemble large Trent engines. Again, total effect of doubling, doubling and more of existing capacity, which we're also investing in in the UK, and both of those are coming along really well, and we will ramp into production in line with the requirements for engines for the aeroplanes. We're also building a facility up in the north east of England, to replace essentially, an older facility in Sunderland, again, making discs, and we have announced that we will be investing in turbine blade machining capacity, again in the UK.
00:52:30		So, we are investing, and when we go around the world, we can see our partners investing and we can see our supply chain. We've carefully selected on these new programmes, to have a smaller number of bigger, more capable players. You know, it's a big task, you have to put the factories in place, you have to fill them with machine tools, then you recruit, improve the processes and the hard work then follows. And we're pretty excited with the progress, but it's a big task for us.
	JR	Okay, let's move further back, the gentleman in the white

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		shirt and then the one in the blue shirt.
00:53:05	AG	<p>Thank, Andrew Gollan from Investec. Two questions please, first one, easy financial one for Andrew. The hedge book has gone off a little bit, can you tell us what the average hedge rate is compared to the end of 2010, first question.</p> <p>Secondly, I think you mentioned, with regard to Tognum that you expect to double the revenues in a shorter period than ten years. Does that, are we talking about the combined businesses here, or are we talking about perhaps what you were expecting for perhaps, Rolls-Royce Marine and the other assets, before you put them together with Tognum's assets?</p>
00:53:45	JR	I will take the second one first. We talk about the total business Tognum doubling that in less than ten years, Andrew, doubling that in less than ten years. Andrew, do you want to talk about the hedge book?
00:53:55	AS	Yes, by all means. There's some information actually, in the press release, under Note F, but just for the benefit of the audience, the hedge book is now just over \$20 billion, the average book rate is about \$1.60 in the hedge book, and for those of you with a Reuters screen close to you, you will see that's fairly close to the forward rates that are currently available in the market.
	JR	Thank you, the gentleman just, that's the one.
00:54:25	JA	<p>Hello, Jason Adams from Nomura I guess I'm learning I've got to sit up front from now on, but just two questions. The first one for you John, on the Energy business. When you look at this business, do you think it's at a scale now where you're confident of growing it organically and delivering margins that would be acceptable to your shareholders, or do you think this one could be a focus for bolt-on acquisitions, and you need to get the scale up to compete, I'm wondering how you feel about the size of that business. The second one for you Andrew, on Civil Aerospace. You mention that the disruption caused by Japan is impacting profits by ten million, R&D is a little bit higher than expected, and then perhaps maybe there is even a negative translation impact that you didn't forecast, but yet you maintain guidance. So can we infer that perhaps the first half of the year delivered a little bit better trading than expected, and if so, where did that slight upside surprise come from within Civil Aero?</p> <p>Thanks.</p>
00:55:30	JR	Thanks Jason. On the Energy business, a couple of comments from me. First of all, clearly Energy, the Energy business is smaller than the other areas, secondly the

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		financial returns are, I think the euphemism is disappointing, and we need to address that. So I think the first thing that I would say is that we need to address the financial returns that we're getting from our Energy business, and we'd think carefully about how we can do that. As I said in my speech, the oil and gas part of that business looks pretty good, the power generation, less so. So we need to address that, is the first thing. The second thing is that clearly the acquisition we are making at Tognum is significant for the Energy business in total, and that will bring, to a certain extent, some scale, but of course, it's in a different part of the business, so it's the diesel engines part, rather than, to make it simple, gas turbine.
00:56:38		So, what I would say is, one, for our existing Energy business we need to fix the financials, and that's sort of something that I take on and we will look at very carefully. Exactly how we can do that, whether that is a, we need to be bigger, or a different answer, we will see. Secondly, the acquisition of Tognum will bring some scale to the Energy business, but in a slightly different way. Andrew, would you like to...
00:57:05	AS	Yes, I think, looking at the Civil business, we're in danger of micro-analysing a very large business. This is a business that can generate profits over a full year of close to half a billion, and we're talking about 10 or 15 million items here, which realistically, are more or less in the noise, so I don't think there's any sort of, detail, more detail that we should give you about the first half. What I would say is that, again, perhaps we are trying to be too precise with guidance. We did say, back in February, that we would expect the Civil business to produce a result about 25% up for the full year, I think you can see in the chart, we've said 20 to 25%. Frankly, realistically, there isn't change to guidance, I think we're trying to be too precise here in the outcome. The difference of a few percentage points in profitability in the Civil businesses is not capable of being forecasted, giving the huge array of products we have, the huge array of transactions, it's all in the noise.
	JR	Thanks Andrew. Any other...? Right down here at the front again. As you say, if you want to ask questions, it's clearly at the front you need to be. So next time we should fill the front with all Rolls Royce people, and then we will be okay.
00:58:28	SM	Well, I mean, this charming young people has pinched my seat. It's Sandy Morris, and I'm just trying to avoid circling back and asking the same question, about margins, but if we just were to look at Civil Aerospace, notwithstanding that we

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		<p>have rounding errors, the mix was pretty adverse in the first half. We had more R&D, we understand, in this business, but the margin is holding up pretty well, in those circumstances. Mike, in the meantime, is busy starting up factories left, right and centre. And fine, splendid stuff, and in the meantime, he's got launch programmes going through. I mean, without trying to ask the margin question again, there is a lot there that one could be encouraged by, for the future, if Mike or someone would help elaborate, you know, quite how challenging these start ups may be. It would be helpful, please.</p>
00:59:30	JR	<p>I will let Mike take it, but as I said earlier, I would agree with your synopsis, which is why it would be disappointing if we double our revenues and we don't improve the margins. Mike, do you want to make some comments?</p>
00:59:40	MT	<p>Well, it's always great to tell people how difficult your job is. But no, I think, I started explaining what we are doing around the world, I mean, when you're introducing new products, everybody will understand if you increase volume through a factory, you know, you're going to get some fixed head absorption benefits, as well as the opportunity to drive productivity out. Actually, if you're introducing a new product, you also have to actually put it through a proving process, take it down a learning curve, making sure that everything is set up, on relatively smaller volumes. So, there is a challenge in doing that, that is in the mix, you know, we're also, as I said, services revenues are growing, so that's helpful, but we're also actually launching products, and launching I've mentioned the Trent, we're also launching the BR725 which is going into volume production now, so that's again, in the BR710 world, which is still strong volumes, we're suddenly adding a new product, which is in the family, but nevertheless we have to learn it out.</p>
01:00:45		<p>So in the Civil business generally, there are learner challenges, through our factories. Those factories are shared factories, we're also putting TP400, and the LiftFan, through those factories as well, and there's learning on those. So it's a great challenge to have, it's one that we enjoy enormously, but you know, in a supply chain, you've got to manage new products, you've got to manage old products, and legacy products, and it's all in the mix. Trying to disentangle it on a half year half year basis, is not easy to do in a simple way, because it's part of a general mix, which is I think what Andrew's made a number of times. I don't know if that helps put a little bit of colour on the world that we live in, but it's a good challenge to have.</p>

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01:01:45	HB	<p>Harry Breach here from Barclays Capital. I will just ask two questions without three sub parts to each. Firstly, Andrew, you touched earlier on the Civil section, about materials being below the large engine TCA growth in the first half, so should we be thinking of that as having been sort of flattish, and what's the sort of profile looking like? You said better in the second half, does that mean up to the level of the large engine TCA revenue growth we've seen? And then turning over to Mike, Mike, there's been a lot of focus, I suppose this year really, on supply chain managing in the ramp-up, it's probably getting to be pretty top of the list of concerns. What can we take away to make us feel more comfortable, that part shortages and the supply chain, broadly, given how large and complex that is, can be better managed this time to mitigate shortage, quality, schedule issues, compared with previous ramps? Is there anything tangible we can sort of think about to make us feel better about it?</p>
01:02:57	AS	<p>Right, well, let me take the first of those questions on the time and material piece of our Civil aftermarket. I think your characterisation of the time and material performance in the first half as flattish is fine, I'm happy with, in terms of the second half, there's no doubt that the number of arisings, or bookings if you like, in the overall base network, is increasing. But I don't think that's going to cause the sort of double-digit increase that we've seen in the large engine long-term support contracts. It's because, you know, there's a very large installed base of engines, about 30%, as you know, are on time and materials, and so there are some areas of the fleet that are looking better, for example, the 524 engines, I think we've talked about, with one or two operators, we're seeing more demand for those overhauls, but then, we have quite a large number of engines where, you know, there may be little change in the second half. So I don't think you should expect sort of double-digit, necessarily, upturn in the second half on time and materials, but there will be some improvement.</p>
01:04:08	MT	<p>Okay, on the ramp up. I think if you are referring back to, you know, the challenges everybody faced in the last big cyclic turn of 2004, I think there needs to be a bit of context here, in that prior to 2004, there was an enormous dip in Civil, as a result of 9/11, the Iraq war and SARS. The ramp-up that occurred was, to a large extent, a ramp up in existing products and existing supply chains, that came on very quickly, must we remember. We've been planning this ramp up in Civil for some time, and rather sadly, we've had to wait a little bit on the 787 and the A380 delays, but we've had</p>

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		<p>plenty of visibility, we've put a lot of planning tools in place, we've carefully selected our suppliers, and have worked with them on production readiness, and continue to do so. We've also hedged our materials probably far more extensively, than we did back in 2004.</p>
01:05:10		<p>Now, having said that, you know, it is one of those things, if you're in my job, you lie awake and worry about, which is the right thing to be doing, constant attention to detail with suppliers, planning, making sure we're close to them. Particular attention to making sure the paths are production-ready, and are learnt out, and the processes are capable. So those sorts of things, we are heavily engaged with, in our production readiness programmes, and we will continue to do so.</p>
	HB	Thanks Mike.
	JR	Going round again, you see, it's the people at the front again.
01:05:48	DP	<p>Yes, thanks David Perry again. Can I just come back to Energy, just trying to understand the lower guidance. Andrew, I think in your presentation you said it was, the guidance was lower because of softer OE nuclear costs, and I think you said people costs, as I was scribbling away. Can you just elaborate on that, have you started doing some restructuring already?</p>
01:06:09	AS	<p>No, it's not restructuring, I mean, we're talking quite small numbers here, in the overall scheme of things. It's largely to do with, just having people to bid for new work. I mean, before you win orders, you need people to address the markets, so I think that's really what I'm talking about, it's not restructuring.</p>
01:06:28	DP	Sorry, I'm not sure I understood you, so you said, before you bid you need people?
01:06:31	AS	<p>Before you win orders, you have to have people to respond to requests for, you know, RFPs, requests for proposals, you have to have people to address the markets, so those are creating cost without revenue, and you have to incur that cost before you win the orders.</p>
01:06:49	DP	And you're talking about Power Gen or Oil & Gas?
01:06:51	AS	<p>Well, it's principally, I mean, it's in both. Oil & Gas has been more buoyant, as I said, the order enquiry level has definitely picked up. We have been bidding for Power Gen work, both from a diesel side and gas turbines, and it does require a certain amount of effort. So I think it's across both businesses really.</p>

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01:07:18	DP	Thank you.
01:07:26	BF	Just one final one from me, which was, maybe I missed it in the press release somewhere, but I just wondered if you could update us, Andrew, where the TCP net debt was at the end of the first half?
01:07:34	AS	Well, I'm so pleased, Ben, that you've asked me that question, and I think you will find the answer in the press release, and I will refer you, I will refer you to the note in a moment, when I have found it. And it is, where are we, it is on Note F, page 11 of the press release, and the short answer is, there's not much change.
01:08:10	JR	So hopefully that's discouraged any more questions. Are there any more? Okay, thanks very much for coming again this morning, I'll just summarise again, it was a strong first half, I think we're well positioned, we're confident about the future, and certainly, you know, my first few months in this company has been a terrific experience and I look forward to seeing you again at the full year. Thank you very much indeed.