



**Rolls-Royce**

## **Resilience in a challenging environment**

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Finance Director  
- Paris 2009**



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## Agenda

**Group Overview**

Financial Position

Short term issues and mitigation

Summary



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## A Global leader in Power Systems



- A broadly based Power Systems integration business
- Global access, few competitors and high barriers to entry
- Technology rich, with strong understanding of customers' requirements

**Capability and technology - significant barriers to entry**



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# Broadening our portfolio



**Underpinning long-term growth**



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## Technology creates opportunities



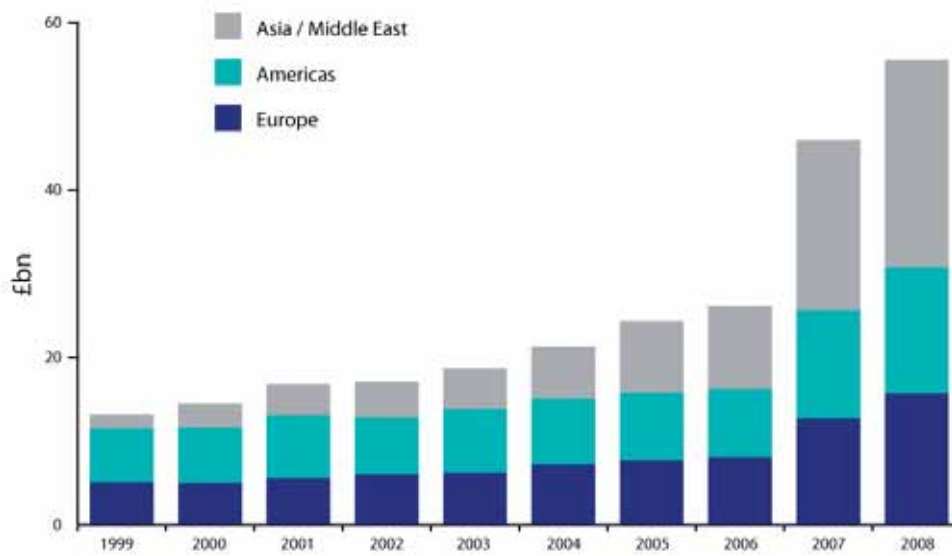
- Core technologies and systems integration skills create high barriers to entry
- Expanding and developing Energy and Marine opportunities
  - Oil & Gas and compression
  - Power generation – Nuclear and other low carbon technologies
  - Mixture of organic growth, partnerships and acquisitions



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## Long term visibility

Order book\* ~ £55.5bn

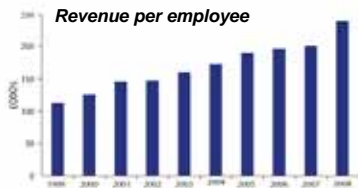


\*Order book stated on a constant currency basis



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## World class operational capability



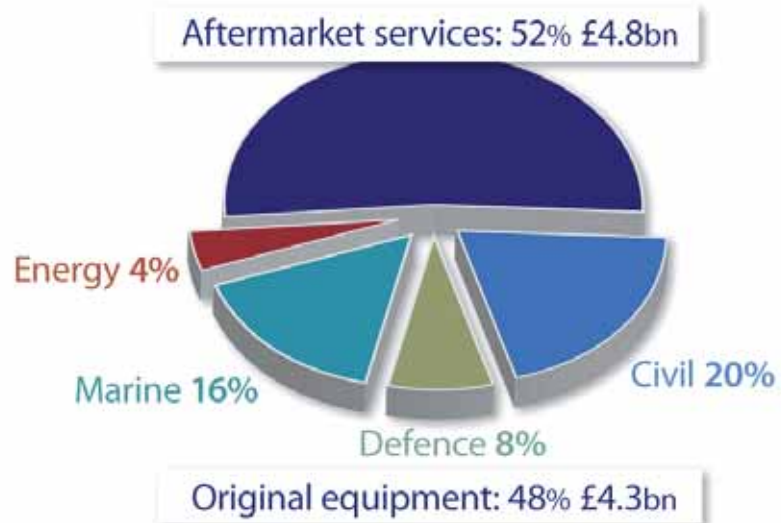
- Investing in focused factories – 50% less space; 30% more output
- Revenue/employee up 8% compound since 1998
- More flexible and capable supply chain
- Early action on cost

### Expanding and improving operational capability



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## Balanced business portfolio – 2008 £9.1bn



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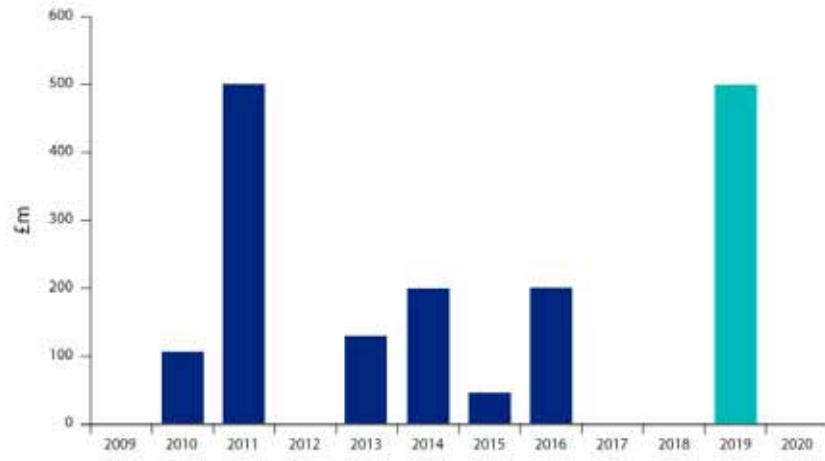
## Financial Strength

- **Continue to preserve flexibility**
  - Strong credit rating – committed to maintaining A rating
- **Pensions**
  - Early action taken to address pension deficit and future volatility
- **Foreign exchange**
  - Rates moving in our favour
- **Customer and supplier financing**
  - Greater demand but manageable
- **TotalCare contracts**



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## Debt maturities



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## Pension risks substantially reduced

- Early action taken to address deficit and future volatility
  - UK defined benefit schemes closed to new members in 2007
  - £500m special injection in 2007, more than 80% LDI asset base
- UK schemes - Significant IAS 19 pension surplus ~ £1.4bn
  - IAS19 Valuation driven by AA discount rates
  - UK Schemes ~ surplus £408m recognised on the balance sheet
- Triennial actuarial evaluation underway for largest scheme
- No material change to funding contributions expected



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## Foreign exchange

- **Long term hedging strategy continued**

- Circa \$40bn exposure over 10 yrs
- Cover increased in H1– capitalising on improving rates
- 2009 achieved rate similar to 2008
- Improving achieved rate from 2009

- **Translation and “mark to market” impacting reported performance**

- Income statement - mark to market – non cash
- Balance sheet – working capital, cash, financial instruments



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## Customer finance – delivered (Contingent liabilities)

- Not a core activity
  - Gross and net relatively stable since 2002 (Chart - appendix)
- **At 31 Dec 2008:** - Gross \$1,086m, Net \$222m, Stressed \$354m
  - **Credit Backstops** – Gross \$480m, Net \$142m, Stressed \$167m
    - 15 Customers and 154 Aircraft
  - **AVG's** – Gross \$606m, Net \$80m, Stressed \$187m
    - 17 Customers and 246 aircraft over 12 years



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## Customer finance – new business (Contingent liabilities)

- Credit markets
  - Export Credit Agencies more supportive and increasing capacity
  - Bank market continues to dominate as primary source of financing
  - Smaller leasing players increasing activity
- Close contact and understanding of customer demands
  - Knowledge/relationships with customers, banks, leasing Co's
- Manageable short term commitments—circa \$400m (gross) to end 2010
- Additional customer requests are discretionary



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## Why do we offer TotalCare ?

### Customers:

- Predictable costs
- Supports outsourcing
- Flexible contract design
- Risk transfer

### Rolls-Royce:

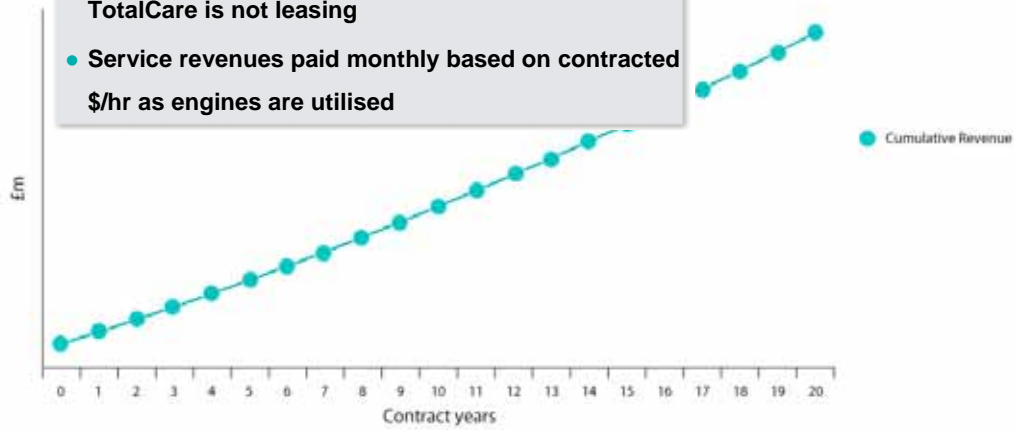
- Expand revenue opportunity
- Manage overhaul load
- Incentivise cost reduction
- Best positioned to manage risk



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## TotalCare – Cumulative contract revenues

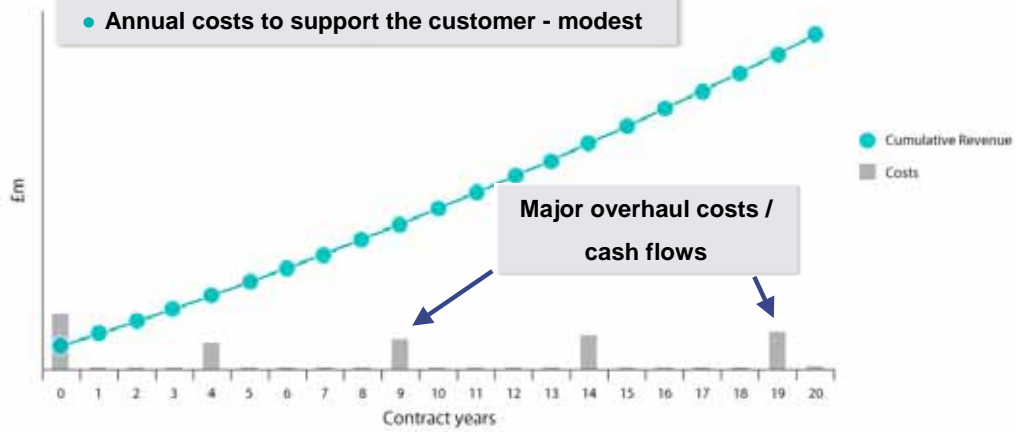
- Revenues from OE sale and through life services
- Engines paid for via PDP's and at engine delivery – TotalCare is not leasing
- Service revenues paid monthly based on contracted \$/hr as engines are utilised



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## TotalCare - Costs

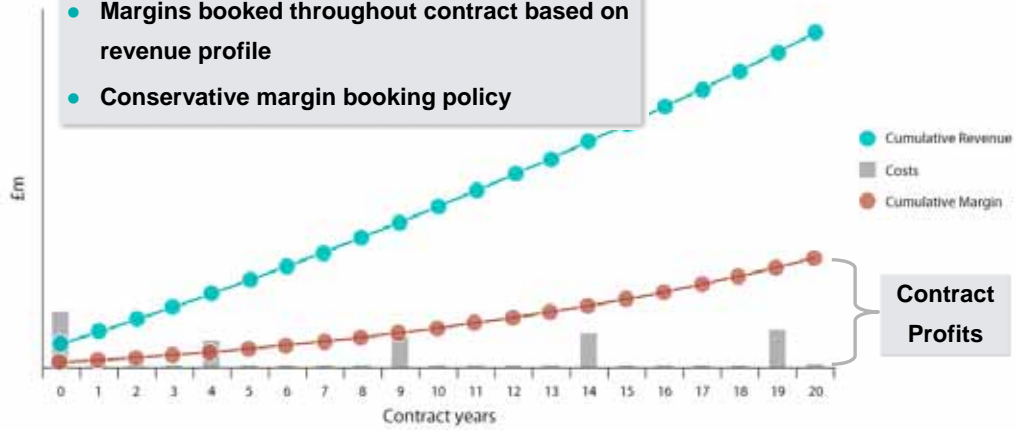
- Overhaul costs and cash flows lumpy – driven by frequency and scope of intervention
- Annual costs to support the customer - modest



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# Progressive margin recognition

- Business case establishes expected return/margin on contract
- Margins booked throughout contract based on revenue profile
- Conservative margin booking policy



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## TotalCare – Risk management

- **Major assumptions**

- Utilisation
- Material and labour cost assumptions, inflation, FX
- Frequency and scope of overhaul

- **Contract management**

- Ongoing fleet management
- Contract reviews on every contract each 6 months

- **Experience over a decade**

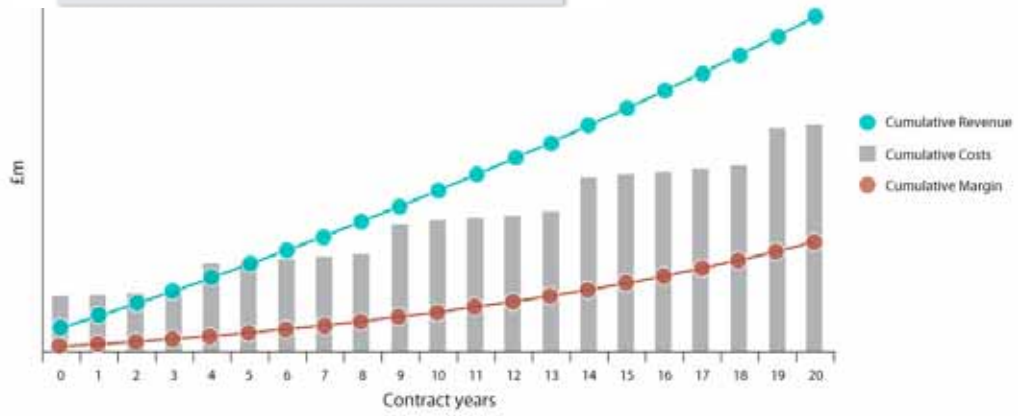
- TotalCare for the widebody since since 1997
- Contracts delivering against expectations
- Margin recognition increasing as contract matures



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# TotalCare – Income statement

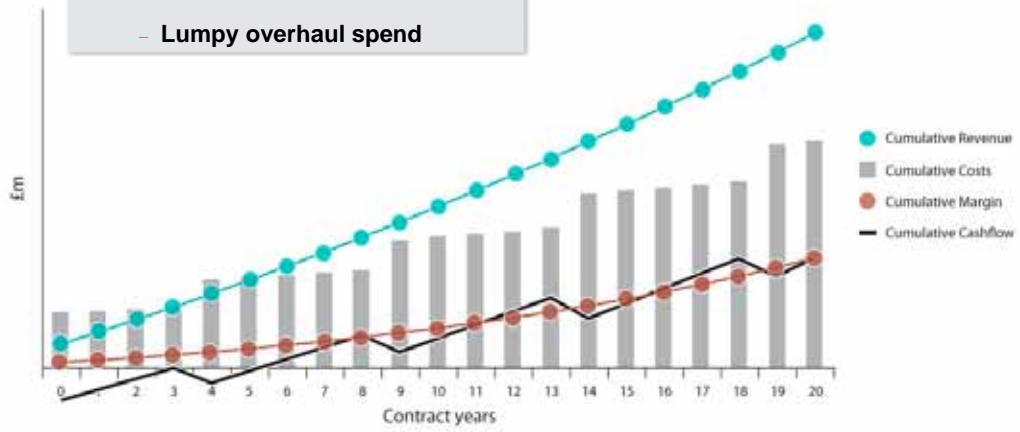
- Margins booked progressively over time reflecting latest view of contract outcome



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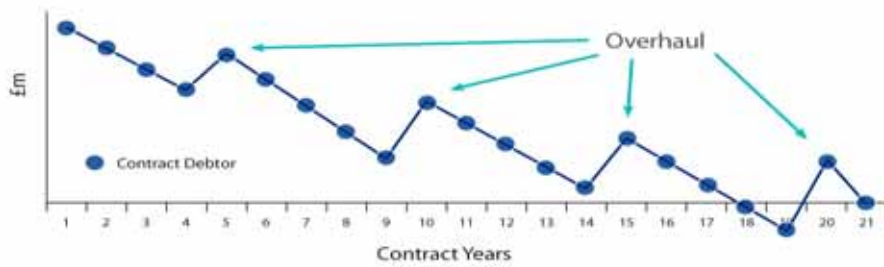
# Income Statement Vs Cash flow

- Cash flow reflects:
  - Progress through the contract
  - Lumpy overhaul spend



## TotalCare – Net debtor

- Balance sheet at any point reflects mismatch between cash revenues, cash costs and margins booked
- Lumpy overhaul spend increases debtor as incremental costs not recovered from customer but charged through hourly rate



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## A strong financial position

- Robust financial position and credit rating with debt maturities well spread
- Flexibility to respond to investment opportunities
- Reduced volatility in UK pension schemes
- Customer and supplier financing concerns manageable



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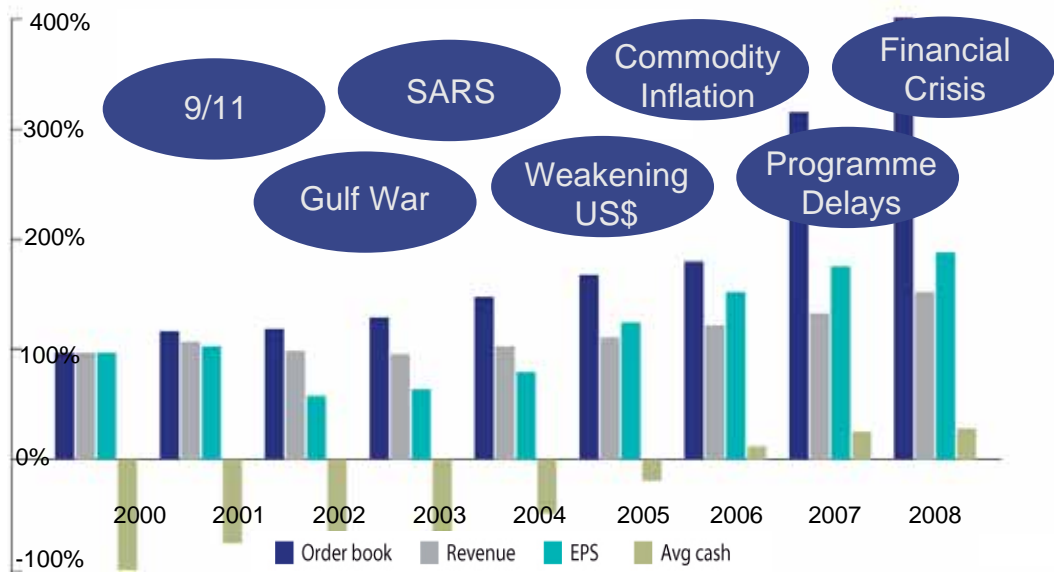
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## Managing challenges



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## A business transformed

	2000	2008
● Revenue (£bn)	5.9	9.1
● Aftermarket (£bn)	2.2	4.8
● UPBT (£m)	436	880
● Avg Net (Debt)/Cash (£m)	(1,323)	375
● Order book (£bn)	17.1	55.5



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## **A challenging environment: managing what we can influence**

- Make – Buy strategy
- Cost reduction, efficiency and productivity
- Matching capacity with reduced demand
- Cash management, working capital and inventory



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## A strong power systems company

- Broad geographical product and service portfolio in growing markets
- Customer knowledge, technology and systems integration create opportunities
- Robust financial position
- Continuing to invest for future growth
- Early action on cost in 2008, continuing in 2009



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## Safe Harbour Statement

This Annual Results Announcement contains certain forward-looking statements. These forward-looking statements can be identified by the fact that they do not relate only to historical or current facts. In particular, all statements that express forecasts, expectations and projections with respect to future matters, including trends in results of operations, margins, growth rates, overall market trends, the impact of interest or exchange rates, the availability of financing to the Company, anticipated cost savings or synergies and the completion of the Company's strategic transactions, are forward-looking statements. By their nature, these statements and forecasts involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements and forecasts. The forward-looking statements reflect the knowledge and information available at the date of preparation of this Annual Results Announcement, and will not be updated during the year. Nothing in this Annual Results Announcement should be construed as a profit forecast.



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