

16 November 2016

**ROLLS-ROYCE HOLDS CAPITAL MARKETS DAY
EXPECTATIONS FOR 2016 UNCHANGED
GOOD PROGRESS WITH TRANSFORMATION PROGRAMME
PLANNED UPDATE OF STRATEGIC PRIORITIES UNDERWAY**

Rolls-Royce is today holding a capital markets event in the UK. Hosted by Warren East, Chief Executive, and David Smith, Chief Financial Officer, the event will provide an update on current trading, progress with transformation, the next steps in reviewing how Rolls-Royce will deliver enhanced shareholder value in the long-term, and provide a further update on the expected changes resulting from implementation of the IFRS 15 accounting standard.

Commenting on the objectives of the day as a whole, Warren East said: *“This event marks an important milestone for Rolls-Royce. We have made significant progress over the last twelve months implementing the findings of our operating review, including key changes to the management and structure of our company. At the same time, we are taking actions that are adding pace and simplicity to our processes. The businesses are highly engaged and focused on their revised priorities, and today the market will have the chance to hear directly from the business managers charged with delivering the transformation.”*

“As my presentation sets out, we have an outstanding portfolio of businesses with highly differentiated products and services that, with appropriate investment, are well positioned to create significant value long into the future, despite some near-term market-led challenges.”

“As I set out in November last year, it is now time to look further ahead. Together with my new team, our focus is turning towards the Group’s long-term goals. Over the next few months we will be evaluating our strengths and investment opportunities, to define an appropriate vision for the business and the best way we can deliver sustainable shareholder value. I look forward to sharing more about our strategic priorities in 2017.”

Highlights from Warren East’s presentation include:

- Outlook for 2016 unchanged
- Good progress with 2016 strategic priorities:
 - Transformation programme well on track; cost savings now expected to be at the top end of the £150-200m target range
 - Significant changes made to senior management headcount and underlying cost base
 - Key senior appointments made
- Update of strategic priorities underway to evaluate the best way to deliver enhanced shareholder value in the long term

Highlights from David Smith’s presentation include:

- 2016: performance progressing in line with expectations set out in November 2015
- 2017: near-term market outlook mixed; long-term order book remains at near record levels
- IFRS 15 accounting treatment confirmed for Civil Aerospace; estimated revenue and profit changes quantified for FY15; cash flow not impacted by new standard

Other members of the executive leadership team presenting during the day include Presidents of the businesses, together with selected members of their teams. As well as short presentations, the business teams will be hosting a number of smaller break-out sessions, structured around our strategic priorities of delivering engineering, operational and aftermarket excellence. The teams will be highlighting some of the many activities that are underway to deliver the improvements required to achieve a significantly enhanced performance. Each team has prepared a video discussing the session's materials which will be available as part of the event's webcast.

Highlights from the business breakouts include:

Engineering Excellence

- Power Systems: focused product development, including gas engine and growing integrated system capabilities
- Nuclear: next generation R&D and broadening civil nuclear capability providing optionality and geographic growth opportunities

Operational Excellence

- Civil Aerospace: investing in production capacity and advanced manufacturing; reducing footprint and working collaboratively with suppliers to drive cost efficiencies; combined with continuous improvement programmes
- Marine: responding to market challenges by lowering fixed cost base and making focused investment to support growth opportunities

Aftermarket Excellence

- Civil Aerospace: delivering customer value through enhancing services choice; developing services infrastructure; and focused assistance for aircraft transitions
- Defence: driving aftermarket value through innovation to extend engine lifecycles; enhancing services value at a lower cost; and improving customer intimacy

IFRS 15 update

In addition, a breakout session on IFRS 15 will provide further detail on implementation of the new accounting standard, and an additional opportunity for analysts and investors to explore some of the new standard's implications for Rolls-Royce.

Using 2015 as an example, the team evaluated how the standard would have changed revenue and profit for Civil Aerospace if it had been applied to that year:

- Cumulative profit and cash flow recognised over the life cycle of a product is not changed by the new standard
- Changes to the timing of revenue and profit recognition:
 - Original Equipment: to more closely reflect the cash received on original equipment sales
 - Aftermarket: to reflect the timing of actual work done to provide aftermarket services, irrespective of the commercial value of implicit performance commitments (this new aftermarket approach is known as the 'input' method)
- Changes result in adverse notional adjustments to Civil Aerospace revenues and operating profit in 2015 of £0.7bn for original equipment (OE) sales and £0.2bn for aftermarket (AM)

- Drivers of change in revenue and profit largely led by:
 - Elimination of linked profit on OE accounting
 - Removal of the 'capitalisation' of linked and unlinked engine losses and adjustments in both OE and AM accounting for the related 'depreciation'
 - Reduction in the magnitude of beneficial long-term contract accounting adjustments
 - When applied to CorporateCare® service packages in business aviation, the input method required by the new standard also has an adverse effect on the timing of AM revenue and profit recognition (included in the above notional adjustments)
- From a balance sheet perspective, if IFRS 15 had been applied to the 2015 closing TotalCare® net asset and Capitalised Aftermarket Rights balances then approximately £3.5bn of transition adjustments (before tax) would have been applied to reduce shareholder reserves

The new standard will be adopted in 2018. The 2017 reported results, which will be initially prepared and reported under existing standards, will be restated in the 2018 results to reflect the changes introduced in the new standard.

Commenting on IFRS 15, David Smith added: *"The new standard provides a number of benefits to the business. As it brings profit performance for OE more in line with cash generation, it will put a sharper focus on improving productivity across our manufacturing activities. At the same time, the change to aftermarket accounting, particularly in Civil Aerospace, reinforces our focus on cash flows, as we look to improve further our strong reputation for customer service by maximising engine availability while minimising cost."*

Talking more widely, David Smith added: *"As set out in November last year, we are committed to improving disclosure and transparency and will continue to work with our different stakeholders to ensure they understand the detail of these accounting changes. We remain committed to a robust financial policy, focused on maintaining a strong investment-grade credit rating."*

Update on current trading

During the course of today's presentation Rolls-Royce is providing an update on current trading, the outlook for 2016 and recent market developments. Highlights include:

- **Trading in line with overall expectations; some market conditions remain challenging**
 - 2016 outlook unchanged for revenue, profit and cash; free cash flow still expected to be in the range of £(100)-(300)m
 - Transactional foreign exchange benefits from weaker sterling and life cycle cost reductions expected to more than offset higher engineering and programme costs in Civil Aerospace
 - Other businesses overall in line with expectations, despite mixed market conditions
- **Market outlook mixed**
 - Civil Aerospace large engine demand remains strong, reflecting strength of XWB order backlog; demand for business aviation original equipment weakening further; parked aircraft numbers stable with transitions now secured for many earlier parked aircraft
 - Defence outlook remains positive overall supported by good aftermarket opportunities
 - Power systems markets mixed reflecting weaker demand for industrial engines and service, although marine and power generation remain steady
 - No signs of recovery yet in offshore oil & gas markets for Marine and OE order book remains very weak; further revenue weakness expected in 2017

- Nuclear expected to benefit from improved submarine activity; progress developing civil nuclear opportunities but limited near-term upside
- **Transformation activities proceeding well**
 - Transformation programme well on track to achieve upper end of planned £150-200m pa cost saving target; full run rate savings expected to benefit 2018 performance
 - Significant changes made to senior management headcount and underlying cost base
 - 2016: c.£50m benefit with incremental savings of £90-120m expected in 2017
 - 2016 exceptional costs unchanged at £75-100m

Commenting on current trading, Warren East said: *“We have made steady progress in 2016 to date, delivering a ramp up in large engine production and implementing the first stage of our transformation programme. At the same time we have managed well mixed markets for our Marine and Power Systems businesses. Overall, we remain comfortable that our expectations for profit and free cash flow remain achievable.”*

Rolls-Royce’s full year results for 2016 will be published on 14 February 2017.

This announcement has been determined to contain inside information.

Details of webcast and internet accessible materials

<http://edge.media-server.com/m/p/hbhieo58>

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Photographs and broadcast-standard video are available at www.rolls-royce.com.
 A PDF copy of this report can be downloaded from www.rolls-royce.com/investors.

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