Rolls Royce Investor Briefing

Farnborough Airshow – 20 July 2010

Mike Terrett – Group Chief Operating Officer:

Good morning everybody. Thanks for coming out to London, and I'm sorry we've got you a darkened room, but the presentations will be better that way. This is and Air Show week, obviously a huge amount of focus on Aerospace, so that's why Dan Korte and Mark King will give presentations on our Aerospace Businesses.

What I'd like to do today is to give a sort of group picture and touch a little on Marine and Energy because we are much more than just an Aerospace Company. I'll keep it brief so that we can focus on the other two, but I'll give you an overview of both those businesses at the beginning here. That's the agenda. We'll come back to Q&As at the end as we already said.

No apologies for using this chart. This is a chart that largely has been unchanged for many, many years, and it's a strategy that we are executing, and that is what we have been doing for many years, and it is a long term business and a long term strategy.

We've added a couple of words to it, Mission Critical, and because more and more we realise and understand and our customers realise and understand that everything we do for them is Mission Critical. It's a very defence type phrase, but it applies in all of our sectors, from Marine and Energy and clearly Civil Aerospace.

It also really becomes very clear to us, and it's very clear to many our air framers and engine makers, how hard it is to do some of the stuff that we do. Now, that's a challenge for us when we're executing and it's a challenge we relish, and we learn and we get better and we get fitter, but it's also a barrier to entry for others who aim to enter our business, and our view is that we continue to invest in our technology, our people, and our capability to keep, A, satisfying our customers and being the best at what we do, and also to make it harder for others to come into our business.

It also provides a huge platform for service development.

When you become very trusted to use your intellectual property, your people, and your capabilities, and your processes to help your customers, they welcome you in with an intimacy that allows you to actually do more for them.

You will all have seen this in the operations room up in Derby and

elsewhere, where we are deeply intimate with the customers, but there's also a platform and an ability that we have to go into other sectors and provide and grow the same sort of long term service capability working on Mission Critical and getting closer to our customers.

Our investment levels are at record highs. I'll talk about that a little later, and the business is being transformed as a result of that, and if I just take a look at the last decade, you know, by every measure in our sectors we've grown, the order book being the most significant, the order

book obviously being one of the lead indicators.

Revenue has grown, profits have grown, and I'll come back to this, our productivity has improved. We're delivering the same... double the business with about the same number of employees, albeit at a very different distribution where those workers are and what they do, so by all measures a decade of growth in our different sectors.

The shape of the company has changed. As I said, we have 40,000 people but a lot more overseas, a lot more locations overseas. Just to give you some idea of the sort of global nature of our business, in our Rolls Royce Deutschland facility in Berlin, which does about 400 or 500 engines a year, which some of you will have visited, we have 40 nationalities in that one location, many of them multilingual.

We're growing in Asia. Our order book is spread as you can see now, 1999 to 2009 the order book in Asia and the Middle East is bigger, significantly bigger now than the whole of the order book ten years ago and we've got a much more balanced geographic spread of our customers as well as a broader portfolio. We also have a much more geographic spread of our footprint which has continued to be more diverse.

We're building facilities around the world. I've got nearly 60 major property projects in hand. We'll show you pictures of the two most significant ones in Singapore and in Virginia.

Both of those are going really well, and we'll be up and running inside two years. The buildings all have roofs on and they're hives of activity, so our geographic spread is becoming very significant.

Often we tend to focus in the West on sort of European and North American trends, but the growth in some parts of Asia is still quite breathtaking in terms of market opportunities. China alone, if you compare China with the US. The US has 18 cities over a million people. China has 118 cities over a million people. A million people would be in the place where airports start to become sustainable.

Those of you who visit China get it. Other parts of Asia are also growing, so having the spread, being close to the markets, having suppliers in the

market, and being globally spread is very important for us. Over the last ten years our strategy in all our sectors is fundamentally the same, which is to develop, innovate, and turn that into product, to sell that product, and then to service the product, of course there is a lag in that.

It's a bit like looking at the light from the stars that are coming. It set off a long time ago, but for us the aftermarket that we're servicing now, which has shown this growth over the last ten years, is off a base of original equipment that was delivered obviously before that and developed before that, so when you think about the growth of the company, what we're actually invested in today providing the future original equipment deliveries and the future growth, and as I'll show on a later chart we have an unprecedented amount of new product being developed.

That's keeping us very busy in terms of our capital investment, people, R&D, flight test programmes. You can see them all this afternoon. It keeps us very busy, but the vast majority of those investments are for products we

aren't really delivering in any volume yet if at all, and that product will then deliver for many years and then be serviced for many years thereafter, and it's on that basis that we see the sort of continuing long term trend to improve and double the size in a decade, and it's being franked by the fact that we did it in the last decade.

The eagle eyed in the room will spot 9/11 and will spot Iraq and SARS and will spot Lehman Brothers in this trend, but actually the broad picture is consistent steady growth.

We've ended up with a well balanced business. I think this chart you've seen many times, but it's just worth pointing out that Civil Original Equipment, whilst,

and I used to run Civil and we love the Civil business, the Civil Original Equipment is only 18% of turnover, and that's for corporate, regional, narrowbody, and wide body. It's big, and we're big in all those businesses, but actually our Marine original equipment is a similar portion of our revenue.

Aftermarket services clearly, that's, you know, about half the turnover of the company and Civil is a big part of that but we are a much, much more balanced business as we grow. Now I'm going to move on and talk briefly about the two other businesses that aren't really featuring at the show; Marine and Energy. I'll first talk about the Marine business.

We will be hosting a Marine seminar later this year, likely to be October or November, and I'd urge you, if you want a fuller picture of Rolls Royce, to take part in that, it's a fascinating business. Obviously we've got the four sectors there; Naval Surface, Submarines, Oil and Gas, and Merchant, and the Marine business is far more about the total power system supply than

about just prime mover engines.

You know, we have a lot of kit that goes onto these vessels, and if I can just talk about the UT vessel, the one that you see in the sort of bottom part of the picture on the left, these service the offshore industry, and we can have as much as 60% of the value of the ship be delivered by Rolls Royce, ranging from the design, to the control system, to the winches, the thrusters, the propulsors, the power systems and the system that integrates the whole ship.

We like to think Farnborough is high tech, but really, if you want to go and see what high tech really is, go and sit on the deck of one of these UT vessels. It is very impressive. You sit there with 360 degree vision. It's a beautiful environment. It's all polished wood/mahogany, but everywhere you can see there's maybe as many as 30 different displays of where you are, how the ship's operated.

The captain's chair, which we do, is the control system which keeps this ship, which can be ten decks up above the ocean, keeps it within a metre and a half in position in high winds and waves, and that's all done by satellite signals and control in the ship, we provide that system integration.

What we're actually able to do, and Colin Smith and his engineering team have actually been able to leverage some of that system integration back into the other parts of our business, particularly into energy brought into the Aerospace.

It's very sophisticated stuff and it allows us to actually be very intimate with the customers, so the Marine capability is a lot more about power systems and it lends itself to significant understanding and greater intimacy with the customer, and the agenda in Marine is really only going to go in one direction for a number of reasons, environmental pressures, the green agenda, the clean agenda, plays very much to our strengths with the environmentally friendly gas engines and diesel, reduced oil content we use in our Aerospace code to improve propellers and delivering significant improvements in efficiency in the Marine business, and cleaner fuels.

The heavier, less clean fuels that are in use in Merchant and are gradually going to over time be replaced by more clean efficient units.

We completed the ODIM acquisition. As you know we completed that earlier this year. That takes us further into the various bits of high tech kit that the offshore industry needs, including seismic surveys, and the service opportunity is very significant.

There's a sophistication on the boats and the way in which they're operated is not matched yet in the Marine business by the sophistication of the service offering, and we see that what we've done in the Civil business,

done in the Defence business, as fantastic platforms for us to access a greater share over the time of the Marine business, and it is a conservative business, and they do like to deal with people they know and they like and they trust, and our brand name helps us enormously in that respect, so we're excited about Marine and we're also excited about energy, and the market itself I think is undeniable.

We've a very strong position in Oil and Gas and we intend to build on that and we think natural gas is going to be a bigger part of any energy requirement in the future because natural gas powered power stations in any form are generally at the top end of the efficiency scale and the clean scale, so we think that is going to continue.

Today we are small, as you know, in power generation, but we've got some fantastic products and technologies which we are seeking to thoughtfully exploit those products. In terms of gas turbines the Trent and RB211 have got small but respected positions and we will grow that.

We also have a position in land based diesels again using the diesel business in Marine to further penetrate the power generation needs. The world is going to need more distributed power. It's unquestionable that the transmission losses and the infrastructure required for old fashioned grids are going to become challenging for many countries, and so more distributed power is going to be required.

We think we can play better in that market given our technology set, so you will hear more from us talking about energy in future presentations, and we will follow up, as we're going to do with Marine, on a seminar at a point in time. We're also keeping a very significant presence in looking at the low carbon opportunities.

I won't spend time today talking about civil nuclear. That may be something that, again, we follow up in the future, but we think it is inevitable that the world will find a way of building more nuclear power stations, and we've got the capabilities and we intend to use those capabilities in that sector, but that will take time.

We're continuing to invest in the technology in fuel cells, and we also are progressing our tidal pilot up in the North of Scotland, so we're keeping a foothold in those that we can then exploit because we think there are opportunities here in energy.

If I return to the most pertinent theme of the week in Farnborough, we've showed this chart to you before. These are just ten of the more spectacular things that happened in the last 12 months, in 2009, the first flights of different products, and I won't steal Dan or Mark's thunder by, trying to talk about all of these, but they all continuing to make progress with their development milestones.

You'll see some of them this afternoon. It is unprecedented. It's unprecedented for any company to have these number of first flights. In my operations job I'm engineering the company or tooling the company up to make these, so we're clearly investing a lot of capital. We're building facilities.

We doing and investing in a lot of R&D and a lot in people and IT to be able to ramp up to meet this production requirement that's coming and it's this that underpins the next decade, so we're investing in growth. We're investing at unprecedented levels and if I look at productivity, we've invested heavily in the last ten years to be able to deliver this level of growth.

As I said, we've doubled the size of the company with pretty much the same number of people, 40,000 people, but a very, very different mix. We've invested in tools to allow us to be more efficient. Those of you who have visited the operations room will have seen the scale of what we've developed there, but very broadly, up in Derby and also down in Bristol and elsewhere we are doing, with the same number of people, but working with much, much better IT tools and capabilities and processes, to manage that growth, and that sort of comes out in the left hand picture which just shows the productivity per employee. We're also investing in all of our facilities.

We've talked about that a number of times with you, but right at the front end of our manufacturing development we've partnered with other partners and governments around the world to produce and be big players in these advanced manufacturing centres.

The one in Sheffield is a fantastic place to visit if you ever get a chance. Some of you may have had a chance to look at the mobile version of that where the high speed machining, advanced machining techniques are being developed that we will flow into our supply chain and particularly our domestic facilities and become much more productive.

This one you can see here is going to be up in Glasgow. There's another one coming in the Midlands, also Bristol composites, and then in the US we're developing with the Commonwealth of Virginia, the advanced manufacturing centre to go on out Crosspointe site and a similar, slightly smaller one in Singapore.

Now, these are the equivalent, in manufacturing terms, to the research and development and research and technology we do to produce product. This is the R&D, if you like, for manufacturing, and it will take enormous time out of the manufacturing of some of the products that we have, and you know, when you're producing something that weighs nine tons, and, we aim to sell at the sort of prices we sell, you know, it's a lot of machining of high tech materials, and so it is a differentiator to be really good at that, and

that’s an investment that will pay back over many years. I also should say on that chart that many of our suppliers are also investing significant amounts of money.

If you travel to Japan or China you'll see whole new facilities that are being built on the back of our business plan for Trent and Trent XWB, and a point that, needs to be made, is that, being the only engine on the XWB has led us to actually have higher volumes earlier than we probably would have expected, so we're investing for rate growth as well as for new product.

In terms of long term growth I think I've made the case here that, we are a long term company. We invest in R&D, that becomes product, and then it becomes aftermarket, and it takes a long time. We all live in the future in Rolls Royce, so the things we're doing today are really, things that my successor will be standing up and talking about aftermarket revenues in many years’ time, so we do live in the future and that does require us to invest.

It’s high investment, but actually we feel confident that the product is coming through. In any given year we may not get the mix right, but actually when you look at what we're doing, what we're investing in, and the sort of markets that we're in we're confident that we will double our revenues over the next decade.

We don’t do forecasts for that but we're confident it will be an outcome and we will be a very exciting company over that time, and so at that point I'll finish the intro and hand over to Mark King.