

FINAL TRANSCRIPT

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RTOKY - Rentokil Initial plc Trading Update Conference Call

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CORPORATE PARTICIPANTS

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Rentokil Initial - CEO

Andrew Macfarlane

Rentokil Initial - CFO

CONFERENCE CALL PARTICIPANTS

Karl Green

Credit Suisse - Analyst

Mark Shepperd

UBS - Analyst

Andrew Ripper

Merrill Lynch - Analyst

Laurent Brunelle

Exane BNP Paribas - Analyst

PRESENTATION

Operator

Good day ladies and gentlemen, and welcome to the Rentokil Initial third quarter trading update conference call. (Operator Instructions). At this time, I would like to turn the call over to your host today, Mr. Flynn. Please go ahead, sir.

Doug Flynn - Rentokil Initial - CEO

Thank you. Good morning, and thanks for joining the call today. With me I have Andrew Macfarlane, our Chief Financial Officer. I will run through the third quarter financial and operational highlights, and then we will take any questions you may have.

In summary, results for the third quarter are in line with our expectations. And as anticipated, both revenue and profit are up year-on-year. Looking ahead, we expect the fourth quarter, which is seasonally stronger for the Group, to see continued growth in profit. And our outlook remains unchanged.

In today's third quarter trading update, we reported that all divisions increased revenues. Organic growth in the quarter was up 4.1%, and we saw overall revenue growth up 25.3%. And for the year to date, revenues were up 23.8%.

Third quarter Group operating profit was up 6.9%. Adjusted operating profit was up 18.1% and adjusted operating profit before tax was up 21.1%.

Now, if we exclude the estimated interest benefit from the sale of Electronic Security, adjusted profit before income tax was up 5.3% in the quarter.

Now, I think it's worth highlighting that our statutory pre-tax profit, which is down 4.2% in the quarter, is increasingly impacted by an increase in amortization of intangibles other than goodwill, which arises because of the acquisition activity across the Group.

Now, turning to some of the key divisional performances, our Asia Pacific division had a strong quarter, with adjusted operating profit up 28.3% and organic revenue growth of 14.1%. In Beijing, our Pest Control business has become the recommended

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preferred supplier for this winter's Clean Beijing campaign ahead of the Olympics. And this is the first time that a foreign pest control company has been recommended as a preferred supplier.

City Link continues to perform well, with network turnover up 3.5% during the quarter, and 5.6% for the year to date. The integration of Target Express remains on track and will continue through 2008. We have a phased approach to integration whereby the IT integration and introduction of hand-held scanners is followed by the physical integration of the depots.

The systems and scanners enable all parcel movements to be fully traceable, in real time, by customers using the City Link website. City Link derives approximately 70% of annual revenues from the business-to-business market, and this has shown good year-on-year growth through the first three quarters, and also good levels of retention.

The business-to-consumer segment softened over the quarter, and that is a continuation of the trend highlighted at the interim stage.

And for the next few weeks the business is rightly focused on the peak Christmas trading period, and City Link expects to deliver over 9m items in December.

Now, we've continued to make solid progress in our Textiles and Washrooms Services division, with profit in the quarter up 4.5% on the prior year. Textiles and Washrooms is ahead of last year in the key markets of Germany, The Netherlands, France and Belgium.

The business in France has responded well to initiatives to better develop the Washrooms business, together with a number of higher margin specialist areas. In the U.K., we announced the closure of two sites which will allow us to complete the rationalization of the branch and processing infrastructure.

And finally, the Rentokil Pest Control division delivered the expected improvement in performance. Revenue in the quarter increased by 9.1%, with organic revenue up 4.3%. We continue to invest in this growing sector. During the quarter, we secured the clear Number 1 position in the Spanish pest control market through the acquisition of Ambius. And we also completed the acquisition of Presto-X in North America.

Now, the Company's by no means the finished article, but today's results demonstrate tangible progress towards the Group's objective of demonstrating sustainable, profits growth.

The operational improvements we've made across the Group are now starting to drive bottom-line performance. There's more to be done in this regard, but that said, Rentokil Initial is well positioned to build on our solid Q3 performance in 2008 and beyond. Thank you. We'll now take any questions you may have.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). We now take our first question from Karl Green from Credit Suisse. Please go ahead.

Karl Green - Credit Suisse - Analyst

Thank you. Good morning gentlemen. I've got a couple of questions if I can. Firstly, on the City Link performance, could you identify the quarter's growth in the B2B segment, and also in B2C as well? You did refer to a strong performance in B2B there. And also could you indicate what the exit rates were in the final month of the quarter?

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And my second question just confirmed interest, now that you're three quarters of the way through the year. Could you give a specific number in terms of guidance for the interest charge for full year '07, including the benefits of the sale of Electronic Security, please?

Doug Flynn - *Rentokil Initial - CEO*

Okay. I think Andrew's going to take this question?

Andrew Macfarlane - *Rentokil Initial - CFO*

Yes. Obviously when we pick up a parcel, customers don't always tell us whether it's B2B or B2C, so we do our best to identify the traffic patterns by the delivery address. We can most easily monitor what's going on in, let's say, the top 50 accounts across City Link. And over the course of the year, we have not lost any of those top 50 accounts.

What we've identified is that B2B is growing very, very strongly, high single-digit growth year-on-year. B2C, however, is softer, and we're seeing a fairly consistent pattern of down-trading across our major B2C accounts. So when you look at the traffic patterns in the network, B2B would normally peak round about this time of year, and we are seeing that. We have not yet seen a big pickup in B2C volumes. So we think this is symptomatic of a late Christmas.

In terms of the interest charge, I think Q4 will be fairly similar to Q3.

Karl Green - *Credit Suisse - Analyst*

Okay, thanks. Just to -- sorry, just going back to the City Link, so it's B2B which is the majority of the business is growing high single-digit?

Andrew Macfarlane - *Rentokil Initial - CFO*

Yes.

Karl Green - *Credit Suisse - Analyst*

And the network's grown 3.5% in the third quarter? Is that suggesting B2C has gone negative?

Andrew Macfarlane - *Rentokil Initial - CFO*

Certainly for the top accounts, it has. What we are -- what we find it difficult to do at the moment, because of some systems constraints, is identify all of our customers, of which we have several thousand, as to whether they're typically B2B or B2C. But if they're typical, then yes, it's going backwards.

Karl Green - *Credit Suisse - Analyst*

Okay. Thank you.

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Operator

(Operator Instructions). We now take our next question from Mark Shepperd from UBS. Please go ahead.

Mark Shepperd - UBS - Analyst

Morning gentlemen. I'd just like to get my head round the seasonality of the Asia Pacific business, because if I understand correctly, this is a business which is growing in underlying terms, and you're building it by acquisitions quite rapidly. But the Q3 numbers are less than the Q2 numbers.

So is there a strong seasonal element there? I remember you saying earlier in the year that the Q1 is depressed because of the Chinese New Year. Why is Q3 less than Q2? Are there some one-offs that are not being reported there, or -- And if there are, how big are they?

Doug Flynn - Rentokil Initial - CEO

I think -- certainly one of the factors is -- as we integrate Pink, we have -- we've got to the point where we're now able to rationalize some of our service routes. So this quarter, we have let some of the service technicians go, for example.

I think it's very hard to look at Asia Pacific, quarter-to-quarter, and expect a smooth progression, because we make so many acquisitions. Depending on the timing of what we have to do for integration, then it can just cause the numbers to move quarter-to-quarter. I think what you should look for in Asia Pacific is a general, longer-term trend of steady growth.

What -- because we make so many acquisitions, the integration costs of bolt-ons, we just treat as business as usual. And that's one of the things that just causes the numbers sometimes to be a bit volatile. We're really only pulling out integration costs for big things like Target Express.

Mark Shepperd - UBS - Analyst

Right. Okay. Thanks.

Operator

(Operator Instructions). We now take our next question from Andrew Ripper from Merrill Lynch. Please go ahead.

Andrew Ripper - Merrill Lynch - Analyst

Morning, chaps. I've got a few questions, if I may. Just given that Mark asked it, just to finish off on that point, your Asia Pac organic growth, I think you talked about 14% today. And in Q2, you talked about 22.

So can you just -- I understand, Andrew, what you're saying about the profits and the integration costs, but in terms of the organic graph, is there any reason why that should have dropped off? Is there a phasing issue in relation to the new Hong Kong contract, which obviously is a big part of organic growth this year? Could you explain that?

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Doug Flynn - Rentokil Initial - CEO

I think there are issues around measuring quarterly organic growth anyway, and it really needs longer periods of time than just a quarter, because they -- while it all adds up, it does wobble around a bit. And I wouldn't read too much into each individual quarter, Andrew.

Andrew Ripper - Merrill Lynch - Analyst

Okay.

Doug Flynn - Rentokil Initial - CEO

It's -- I'd rather look at a -- maybe a rolling 12-month period might be better.

Andrew Ripper - Merrill Lynch - Analyst

Yes, okay. You're happy with the momentum going into 2008?

Doug Flynn - Rentokil Initial - CEO

I'm absolutely happy with it.

Andrew Ripper - Merrill Lynch - Analyst

Okay, fine. Well, alright. Well just going then to cover more important issues. On Textile and Washroom, obviously you're making some quite significant changes to the U.K. business in the second half.

Can you give us any sort of sense of how low the base is going to be, in terms of U.K. profits this year? And can you just confirm that -- obviously we've had three years of change in this business. Are you basically saying, by the end of January '08, guys, that's it, clean basis on which to try to return the business to growth next year?

Doug Flynn - Rentokil Initial - CEO

Well, let me answer that last part first. The answer to that is yes. By the end of January, we should have a clean basis to go forward from. The new processing plant at Bromsgrove, I had a look at last week.

That goes live, I think it is next week. So that is -- that's very close to being commissioned live. We've been able to come out publicly with the closure of the plants at Bradford and Chorley. There's a plant that will go live, I think it is in December in Reading. And then the other plant goes live in Glasgow in January.

Andrew Ripper - Merrill Lynch - Analyst

Yes.

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Doug Flynn - Rentokil Initial - CEO

And so by the end of January, we should have Bradford and Chorley closed. There may be one further branch reshaping that has to occur at the -- that might be post-January. But that's not going to be a big deal in the scheme of things. The scale of the business is going to be sub-80m --

Andrew Ripper - Merrill Lynch - Analyst

Yes.

Doug Flynn - Rentokil Initial - CEO

In terms of revenue by the end of the year, and --

Andrew Macfarlane - Rentokil Initial - CFO

At the moment, we're -- I think the business has reached its low point. It's posting -- it is obviously still profitable, and its quarter-on-quarter profits are pretty stable at the moment. So we think this is the bottom.

Andrew Ripper - Merrill Lynch - Analyst

Yes. Okay. But in terms of -- obviously you've got some one-off costs in the second half of this year. If you include them, is it zero to 5m for this year, something in that order of magnitude?

Doug Flynn - Rentokil Initial - CEO

I don't think there's much point in taking the one-off costs in. Quite frankly, they are more now -- they're closer to being investment in maintaining the business.

Andrew Ripper - Merrill Lynch - Analyst

Yes.

Doug Flynn - Rentokil Initial - CEO

I would -- we've declared the overall one-off costs for that division, and they're related to the plant in --

Andrew Ripper - Merrill Lynch - Analyst

Okay.

Doug Flynn - Rentokil Initial - CEO

Belgium, in Lokeren, and this U.K. business. So --

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Andrew Ripper - Merrill Lynch - Analyst

Okay, fine. I don't want to (inaudible) on that.

Doug Flynn - Rentokil Initial - CEO

Yes.

Andrew Ripper - Merrill Lynch - Analyst

And then in France, you've made an overall comment about the performance of Europe being cash-strong. Can you make more specific comments about the trends you're seeing in France, please. I know in the first half you had an acceleration of sales growth. Is that continuing into the second half?

Doug Flynn - Rentokil Initial - CEO

The things that are going very strongly in France is we're doing really well in Washrooms, because that's where they're putting on quite strong growth. And similarly in some other specialty areas, including some hospitals areas. Where we have the probably less than stellar has been the conventional Industrial Garments area, which has shown growth, but not spectacular growth.

So, overall the business is going pretty well, but some parts of the business are really quite strong.

Andrew Ripper - Merrill Lynch - Analyst

Yes. Okay. And then on the Pest Control business, you had very good pool growth, if you annualize it. Is that a precursor to accelerating sales growth in the fourth quarter and early next year? Or is there sort of a seasonal effect because (inaudible) is quite strong summer season, and that's growing relative to the European and U.K. businesses?

Doug Flynn - Rentokil Initial - CEO

I think a big part of it is seasonal. But certainly businesses, like in U.K., we're now seeing reasonably steady growth above prior periods. And we certainly expect the U.K. business to be in profit growth in 2008, and they're there or thereabouts on a monthly run rate now.

Andrew Ripper - Merrill Lynch - Analyst

Okay. And then just a final thing on the FN business, two points. There's obviously quite high terminations in the quarter. Could you explain those?

And could you just quantify the profit on the business disposal, please?

Doug Flynn - Rentokil Initial - CEO

Andrew.

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Andrew Macfarlane - *Rentokil Initial - CFO*

I think (inaudible) the Cleaning business in particular is finding the commercial environment quite tough, particularly in the retail sector. Terminations (inaudible) tend to be quite lumpy in this business. We've gone for a number of quarters without getting big contract losses. We happen to have a couple of larger ones where we lost parts of contracts in this quarter, and that's obviously blipped the number. But as I say, it is a pretty tough commercial environment. You see, we've referred to some productivity initiatives, which we've got underway to try and offset that.

The profit on disposal of the Dutch cleaning business is under £1m.

Andrew Ripper - *Merrill Lynch - Analyst*

Right. Thank you.

Operator

(Operator Instructions) We now take our next question from Laurent Brunelle from Exane. Please go ahead.

Laurent Brunelle - *Exane BNP Paribas - Analyst*

Yes. Good morning. Laurent Brunelle, Exane BNP Paribas. Two questions, if I may. First on Corporate activity. You have been, well (inaudible) very active in the past nine months. What do you expect moving forward? Do you still expect a lot of bolt-on acquisitions, please?

And second, can you just come back on the City Link performance? Just to understand, is it -- I mean the deceleration trend seen in Q3, is it a cyclical issue? Or is it more linked to the ongoing integration process with Target Express?

Doug Flynn - *Rentokil Initial - CEO*

Okay. On the Corporate activity, the areas we're principally focusing on are Asia Pacific and Pest Control. We're clearly not pursuing -- or certainly currently not pursuing acquisitions in the packing -- in the packages area. We've got more than enough on our plate integrating what we've already acquired.

The other area that we continue to explore is Textiles and Washrooms area. Were to make acquisitions, significant acquisitions in that area, they're likely to be larger than the things we've been doing in Pest Control and Asia Pacific. But during -- There are very few large targets out there in either Asia Pacific or in the Pest Control arena, you know, really anywhere around the world, certainly [anything] that we think might be available.

It's very difficult to predict and forecast what we might or might not buy. It really is a case of where strategy and opportunity collide. It is about making sure we've got the capacity, the management capacity, to undertake the acquisitions, to carry out the integration, and that we're not making massive change within the particular division at that time.

And the acquisitions we make have to meet pretty tight financial criteria as well. So we don't have -- We have a pipeline of prospective acquisitions, but we don't have a target value. It is about our financial capacity and it is about the strategy we're trying to pursue, and it is about the financial returns we're trying to get. So, it's -- If you'd like me to estimate what we think it is next year, I really can't do that. However, it wouldn't be unreasonable to assume it's probably going to be of a similar order. But that's not guidance. I just want -- It would not be an unreasonable thing to assume.

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As to City Link, we don't believe that the slowdown we're seeing on B2C has anything to do with the inevitable more internal focused process [we] go on with when you're carrying out a big integration. It is always a concern with you're carrying out significant integration processes that -- you worry that you might tend to take your eye off the customers. We don't think that's the case. And the reason, part of the reason, why we don't think that's the case is that none of the big customers have left us. And what we are seeing is some down-trading by those customers who are principally focused on the B2C areas.

So I don't think that's the situation. We don't have an absolute oversight of the rest of the industry though. So it would be interesting to see what the rest of the industry says by the end of the year, as to what's happened in the B2C area. So we see that as a cyclical thing, but (inaudible).

Laurent Brunelle - *Exane BNP Paribas - Analyst*

Okay. Thanks.

Operator

We will take our next question from Karl Green from Credit Suisse. Please go ahead.

Karl Green - *Credit Suisse - Analyst*

Yes. Thank you very much. A few follow-up questions, if I can. Relatively small, but just trying to get more clarity. In terms of the Wipers exit in the U.K., can you say what the Q4 '06 revenues were, just to get the comparable base for the coming quarter?

My second question was just on the U.K. Cleaning business. You talked about operating profit being flat, excluding acquisitions. What happened to revenues, just to get a sense of the margin relation, the underlying margin progression?

An also sticking with the Facilities Services as well, can you give the annualized revenues of the Catering contracts which you exited, please?

Doug Flynn - *Rentokil Initial - CEO*

Right. The Wipers business was about a 10m to 12m revenue business, and it was break-even. So it had done kind of 2.5m to 3m in the last quarter of last year.

Hold on a second, Karl. I'll see if I can find the answer on Facilities Services for you.

Revenue in the U.K. Cleaning business is strongly up, but it's obviously benefited from the acquisitions of Lancaster and InSitu. I think organically it's probably growing around about mid-single digits.

And in terms of Catering, I would have thought that over the course of the year we must have exited at least 20m revenue of contracted in (inaudible).

Karl Green - *Credit Suisse - Analyst*

Okay. Thank you.

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Operator

As we have no further questions, I would like to turn the call back to Mr. Flynn for any additional or closing remarks.

Doug Flynn - Rentokil Initial - CEO

Thanks very much, everybody, for joining the call. As I said earlier, we're pleased with the progress many of our businesses have made. And we'll brief you in February about the full year. Thanks very much and goodbye.

Operator

That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.

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