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# RTOKY - Interim 2010 Rentokil Initial plc Earnings Presentation

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## CORPORATE PARTICIPANTS

**Katharine Rycroft**
*Rentokil Initial plc - IR*

**Alan Brown**
*Rentokil Initial plc - CEO*

## CONFERENCE CALL PARTICIPANTS

**Jaime Brandwood**
*UBS - Analyst*

**Mike Murphy**
*Numis Securities - Analyst*

**Andrew Ripper**
*Bank of America Merrill Lynch - Analyst*

**Tom Sykes**
*Deutsche Bank - Analyst*

**David Hancock**
*Morgan Stanley - Analyst*

**Rajesh Kumar**
*HSBC - Analyst*

## PRESENTATION

**Katharine Rycroft** - *Rentokil Initial plc - IR*

Good morning, everyone, and welcome to Rentokil Initial's interim results for 2010. If I could just make a couple of announcements before we start. Firstly, may I draw your attention to the previous slide which is our Safe Harbor clause in relation to forward-looking statements. Secondly, this presentation is being recorded and webcast live so please could you switch off any mobile phones. And finally, as I'm told there is no fire alarm planned for today if you hear one please take it seriously and proceed to the fire exit at the back of the room.

Now please may I hand over to Alan Brown, our Chief Executive?

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**Alan Brown** - *Rentokil Initial plc - CEO*

Morning, everyone. Thank you for coming. Good to see you again. I'm going to give you a fairly short presentation and open up for questions and answers.

So highlights for the first half of the year for Rentokil Initial. 39% increase in adjusted profit before tax. It was 38% in Q2 so it's been pretty consistent so far though I must say we are now lapping the last of the easy quarters. We started to perform a little bit better from Q3 onwards last year so I don't expect to be seeing these levels of incremental profit quarter on quarter going forward. But, nevertheless, it's very nice to be able to deliver a very big and consistent profit increase in the first half over 2009.

Revenue decline continuing, improving trends in Q2 as you will see. I think we declined 3% or 4% in Q1 and declined just under 1% in Q2. So we're making some progress though not quite as good as I would like. Cost savings, however, are running ahead of plan. We delivered GBP40m in the first half compared to our GBP75m full year target so that's looking pretty good. Cash flow I'm really quite happy with though it's not as good as last year. Last year as you're well aware, those who follow us, was quite exceptional as we managed to drag back our days sales outstanding from 61 to ultimately 49 for the year. We're hovering around about 51 at the moment for DSO and that's a pretty good number and I'm pretty confident we'll get to the 47 DSO target we set ourselves for the full year.

Net debt continued to fall, GBP1,044m at the half-year and it's now pretty clear that setting aside any disasters we'll be well below GBP1b by the end of this year. And I'm also pleased to say the pension fund deficit has reduced on an IAS 19 basis to only GBP19m at the half year. So all of those important tidying-up issues around the balance sheet are going very well for us at the moment.

Customer retention also moving quite well, I'll come back to that later on. And we continue to work our way very strongly on our growth agenda. As I've said many times, I don't expect that this work will deliver strongly in 2010; it really is an agenda to get ourselves in a position to show consistent growth from 2011 onwards. Again, I'll come back and talk about that.

So I think the message really for Q2, in particular, I'd like to state is that it's a pretty good performance in a period of particularly high structural change. I'll come back and emphasize that point as we go through the divisional highlights. But in the meantime just a quick run through the numbers here. I think I've talked about most of them. You can see, for example, profit up 37% from quarter two in the middle of the chart, 38% year to date. Again, I think everything else was pretty well covered in the highlights.

Now let me give you a quick run-through to the divisions. Textiles and Washrooms first, the drop in revenue of 1.7% really highlights difficult trading conditions in Continental Europe, particularly for Textiles and Washrooms, also for Pest as it happens, and particularly in France and Benelux.

Now, in France, our business has undergone a big structural change in terms of its sales organization. We have decided to move away from salesmen really running from the individual processing units to a proper sales function for France led by a sales director which we hope will enable us to roll out best practice much more effectively across our sales operation. Clearly, this is leading to some disruption in the short term but I'm pleased to say that in June we started to see sales performance going somewhat better and I'm hoping that trend will continue in the second half of the year in France. But apart from that, no getting away from the fact that there are pricing pressures in the marketplace.

Our Benelux business I've talked about several times. It is I think now of all the businesses across the Group it's the one that's receiving the most attention. It's the one problem child we really have across the Group and though that's not good, given where we were two years ago it's not far off a miracle.

Now, despite all of these issues, profits up 12.5% in the first half of the year through good work on cost control. Retention is not satisfactory and we're having to work on that. But it is the exception in the Group, as you'll see later on, retention is going very well elsewhere. Restructuring programs going fine, some glitches in Belgium in the implementation but we'll be over that in a couple of months.

Pest Control has been the most consistent performer in recent times and as I was saying to Andy Ransom a week or two ago it's really rather nice to have a division which has no problem children at the moment and is running pretty consistently across the world. UK Pest has been absolutely terrific. I did not think I'd be able to stand here 12 months ago and say profit up 25% or the fact that we're now back into revenue growth. North America is going well. Libya, I'm very pleased to say we're now back on track in terms of getting payments and that looks now to have stabilized albeit at a lower level of profitability than previously and going well. Retention is terrific.

Asia Pacific, difficult set of numbers to interpret. You'll just have to believe me here a bit. The revenue is down but there's a lot of one-off issues like the Hong Kong contract that we got out of Q2 2009. Profit level is up 6%. I've split here the commentary into two, into Asia and into Pacific, because they're quite different businesses of course.

So if I talk about Asia, I think the important thing to note here is that revenue was underlying up about 1%. We're still seeing weakness in the fumigation business but the really good news here is we're now getting traction in China in our commercial business which has been growing very strongly from a very small base but if we're able to maintain this momentum I think we're at the beginnings of a really quite exciting story for China. Not quite as advanced in India, I have to say, but China I'm very pleased about. Retention up to 81.5%, you have to discount the very low number in June last year because that reflected the loss of the non-profit making Hong Kong contract.

Pacific business better than it looks. Though the numbers look a little bit ordinary in terms of revenue and profit the underlying trend in this business is strong and I'm expecting a good second half of the year and they're now into growth in June in terms of net gain in both Washroom and Pest. I think we've really got the makings of a really good business in Australia and New Zealand. And Fiji, actually, I haven't been there yet but that's on my travel list. Going to do really well. Andy's -- Mr. Ransom's there already, of course, he gets to these places I don't quite reach.

Now Ambius, let me just say that, as you know, this business has been knocked around a bit by economic conditions. I think the important point in this chart is the last point, that we're actually -- when I say close to I think in June we actually were in net gain in Ambius across the business which really signals, I think, that we're past the bottom of Ambius and we're hoping that we'll be back on the way up in the second half and beyond.

City Link, well, well. City Link has matched revenue in the first half. We remain confident of revenue growth in the second half as I intimated at the full-year results. Operating losses have reduced again. And I think that the report on City Link is tried hard, done a lot of structural change, hasn't quite yet got the profit delivery that we would like to get. And the reasons for this I think are very operational. I'm delighted with the structural change; we've managed to reduce the depot numbers again, we'll be down to 71 as we indicated by the end of the year. I'm really pleased on July 23 we managed to close the Wednesbury Hub and centralize all of our hub operations in Coventry together with some big regional depots which are handling some regional traffic as well. And we've done that with very limited adverse impact on customer service. Well, the customer service has degraded a little bit in recent weeks, half a percent or thereabouts, but we'll get that back very, very quickly.

So all the structural stuff and all the IT stuff is going extremely well for us. I think what's really holding us back at the moment is the real detail for planning. With all of the changes we've made to the hub structure we're not getting the deliveries out of the depots early enough in the late evening to get them into the center to get them back out to the delivering depots in the morning and at the moment it's taking us too long to load up the vans for the local deliveries at 7 o'clock in the morning. I saw some data early this week which indicated that the time between putting the first parcel on the van at the depot in the morning and the time elapsed by the time we get to the first delivery point is two hours which is just far too long. It's taking us two hours from the first van, the truck to delivering to the first customer. And we know why that's happening. There are lots of little bits and pieces that need to be sorted out which are almost inevitable I think when you're doing such a big change as we've been doing over the last few months.

So we'll get there. And I think that then will help us get on top of the excess costs we've been incurring on sub-contractors which we've had to bring in to help us deal with these local inefficiencies. But the really great news is the direction is right and I think we'll have things sorted out in time for the Christmas season which starts around about October.

The other really good news I think in City Link is about -- just to refer you to the last bullet point here is that there has been strong industry recognition of the big improvement that City Link made. We got the top award at the Motor Transport Awards a few weeks ago for customer service which in my view is still not where it needs to be but it does show we've made really quite a remarkable turnaround in perception of the business over the last 18 months.

IFS has had a very strong profit quarter as you can see, up 48%, 28% year to date. A lot of good work on restructuring and there's much more to come I have to say. I'm really quite excited about some of the plans we've got for IFS which I'll be able to outline to you later on in the year.

So I think we're in a good place there. We've got successful implementation of the London Underground contract which you remember I announced about a quarter ago. And I'm also very pleased that we were able to acquire Knightsbridge Guarding and their associated front-of-house business called Perception in July and that is looking a very good business indeed. It will offer us in my view a significant opportunity to extend our services to existing customers both in London and later on across the UK.

We've got still some issues in the business. Pricing competition is very tough and despite the fact we've won some big contracts we've also lost some contracts so there's a lot more work to be done and I'm delighted also that Peter Lloyd, having -- really retiring in September, is going to be succeeded by a senior executive from Serco who comes in on September 1, Mike Brown. And I think that will help us to handle some of the bigger contract business that we're now pitching for in the IFS division.

Back to some numbers. Operating cash flow, maybe a couple of numbers I should explain here in the operating cash flow in half one compared to half one 2009. Adjusted PBITA is brought forward. Depreciation looks a bit high here, GBP116m compared to GBP108m. That includes GBP12m of impairment on two items; one, the Wednesbury Hub and secondly, we are just at the point of agreeing the sale of our Spanish linen basis where we've taken a write-down as well. That linen business has revenue of about EUR16m and is loss-making. And that business -- hopefully we'll be able to announce the sale of that in the next few days. But we have at this stage taken a write-down. As I say the two write-downs in total are GBP12m so the underlying depreciation number is about GBP104m -- GBP103m, GBP104m.

The second number perhaps I should just focus on a little bit is working capital. You see a GBP49m outflow compared to a GBP29m inflow last year. That's for two reasons really. The GBP29m inflow last year was quite exceptional because of the reasons I mentioned earlier, the reduction in DSO. We won't be able to repeat that of course in this year. But the other factor is that we've got about GBP25m of restructuring cash costs flowing out in the first half through redundancy, particularly in Textiles and Washrooms in Europe. The CapEx number looks pretty good as you can see and as I've indicated for some time I did feel that our structural level of CapEx expenditure going forward is going to fall.

Free cash flow, I don't think there's an awful lot to add here. This just confirms the closing net debt situation, GBP1,043m. And as I said before, I'd expect this to come in now well below GBP1b at the year end, depending a little bit on ForEx movements. A lot of our net debt is held in euro, about 65% is euro-denominated and with the weakening of the euro though it holds us back a bit on the profit line it's helping us a lot in terms of our balance sheet exposure.

So there you are, a quick run through the results. Now an equally quick romp through the strategy update. No big changes, as you would expect. This is the traffic light chart I've shown before and we've made a slight change in coloring here, I've now upgraded cost and cash to a green traffic light given the consistency of cost and cash delivery we're now achieving. We're still amber in developing capability, still a lot to do there, and we're still red in terms of profitable growth and that will remain red until we see some positive on the top line.

So a quick summary of where we are, just picking up by exception. Again, I'd like to emphasize recognition for City Link's service improvement coming through. Maybe the bottom point I should also just emphasize in terms of future improvements, I'm very focused on much more proactive management of customers at the moment. I'm not happy with our response times to customer queries and we have a major pilot going on at the moment in City Link to improve the level of customer responsiveness which I hope then will be relevant across the Group. So, a lot to do still in terms of customer care.

Customer retention, however, is benefiting from the continued focus on service across the Group. This is a chart which shows the retention rates over the last six months on an annualized basis, there's a detailed definition in the results statement. But you can see here, I think, a general improvement in all divisions except Textiles and Washrooms which is really back where it was in June 2009, reflecting some of the issues I referred to in Continental Europe. So it's clearly a big priority, Textiles and Washrooms focus. But elsewhere I am pleased at the progress we're making generally.

Developing capability. This hopefully will be the last time that Katharine and I have to stand here by ourselves. Jeremy Townsend joins on March 31 and as I said before I'm delighted that Mike Brown will join us, taking over from Peter Lloyd as the divisional Managing Director for Facility Service.

Elsewhere by section perhaps I'll just highlight the merger of the Pest and Washrooms business in the UK. The Pest business has been running extremely well. The Washrooms business has dug itself out of a hole and I think now the businesses are strong enough to be merged. It's a merger which is really focusing primarily on growth rather than cost and I'll explain why in a moment when we move on to some of the growth charts. So we're very excited about the prospects for that rather larger merged entity in the UK.

Operational excellence, the third thrust. Clearly, we've made a lot of progress here, particularly in the turnaround businesses. Perhaps if I just look at the bottom two bullet points and emphasize some of the issues I've already commented on. I think that the structural change in City Link through the first half is higher than at any time in its history and has been done without dropping any major balls which is, I think, a testament to the improved controls and management we have in that business compared to where we were three years ago. And I would emphasize that the business has also made a lot of progress in terms of depot integration which was of course the original reason the business blew up late 2007. And the systems side is now a long way down the track with further improvements to come during the second half of this year which will enable us to greatly improve rescheduling. But there will still be further benefits to come through 2011 as we start to implement route optimization software. You might rightly say why wasn't this done five years ago but it wasn't so we've still got some benefits to come from that.

And we are piloting a system in actually Textiles and Washrooms at the moment called Ortec, it will also be piloted in City Link. And essentially what a sophisticated tool like Ortec does is two things. First of all, it enables you to strategically plan where you should be running routes. And that's not as easy as it sounds; it really requires quite a lot of computing technology to optimize the general shape of the routes you should be running. And the second thing it does then is on a daily basis enables the routes, the individual calls to be piloted for individual drivers. And that will give us much more consistent performance across our branches. It also, as a secondary consequence for City Link in particular, should enable us to give our customers estimated times of arrival, which we currently cannot do. So that will be a big added value factor, particularly in the B2C market in the industry.

Now initial pilots have been pretty encouraging in Germany in our Washrooms business. We did two pilots. We did one pilot in a branch which we knew was very well run and the benefits in terms of operations were actually fairly marginal, 2% to 3%. But they did give us big benefits in terms of administration and greatly reduced the administration in the branch and has enabled us to reduce headcount.

In the second pilot in the Hamburg branch in Washrooms, which we knew was not a well-run branch, we have seen benefits approaching 25% in terms of route productivity which is an enormous impact in operational costs together of course with the administration benefits.

So I think what it will do is, apart from the admin benefits, apart from the customer added value benefits and being able to communicate to our customers when we are going to service them, it will bring all of our branches up to a high level. So I'm really quite hopeful about the prospects for these tools when we are able to roll them out. The only thing holding us back is getting our back office systems up to a level where we can actually feed these route optimization tools. And I expect we'll be there by the end of the year in City Link.

Cost and cash continues to grow well, GBP40m year to date, we're running ahead of the GBP75m target. Cash flow, I think, is looking pretty good. I'm certainly confident we're going to beat our target of 100% plus cash conversion excluding restructuring costs. We've indicated also the cash restructuring costs will be a tad lower than we had expected, from GBP50m down to perhaps GBP40m for this year.

Elsewhere perhaps, just a comment on procurement savings, the potential for the garment savings that I've talked about on several occasions before seems to get even bigger the more we look into it but it is not an easy thing to get at, we have to build quite a lot of capability to be able to get at these savings. Capability in terms of being able to specify a standard range of products, which we're starting with but it's a big job, and capability in terms of the materials, the textiles themselves, being able to specify those, and then, thirdly, capability in terms of procurement. So we're trying to bring together those scales in our textiles business at the moment and we're now making some progress but it's taking time.

Then, finally, the fifth thrust is profitable growth. I'm going to spend a bit more time on this as you might expect. We've reconfigured our way of presenting this to you to try and make it more straightforward to understand. We've got three types of initiative. Those focusing on existing customers, focusing on retention and cross-selling; those initiatives focusing on attracting new customers, (inaudible) sales productivity and targeting; and then obviously new service lines, a couple of examples I'm going to talk about.

So let's just skip through some examples. The thing which has given us the most immediate traction has been the focus on existing customers and focus on retention and we've started to do such novel things as talking to our customers. And I assure you this is quite novel in Rentokil Initial. And that's actually working quite well. The customers are somewhat shocked that we talk to them. I'm talking about the small customers. But they seem to be generally very pleased about this. And that is working well and in my view is then helping us to understand early where we've got an issue and is helping us then be more responsive and to pick up on problems that we might not otherwise have picked up.

The methodology that I've also referred to before, the NPS, Net Promoter Score methodology, which is quite common in our service industry, is also proving very valuable indeed. We're able to get through this simple research methodology a very granular feeling for where our service is working and where it's not working, by branch, even by route on occasions. And that is enabling us at a granularity of detail we couldn't have done before to start to address specific problems with specific areas of service. So this is going -- simple stuff going quite well and it's really got beyond the pilot stage into implementation.

The second one looks pretty complex in this chart but really not that complex I think. This happens to be a map of Brighton. You see Brighton Pier down here. What we have done is to highlight in the blue squares the Washroom customers in the center of Brighton and the red squares are the Pest Control customers in central Brighton. And there is, as you can, well, you can't see from this chart but I can assure you there is very little overlap indeed between those customers. So with the merger of the Pest and Washrooms business in the UK we have a very obvious and real opportunity to embark on some cross-selling, building on the relations we have with washrooms customers to sell pest services and vice versa with pest customers to sell washroom services.

And through the simple use of some simple technology, we're able to bring this to life for the sales people, quite graphically, about where they should go calling. Early days yet, no clear results coming through but we're really looking very much forward to seeing whether we can capitalize on this pretty obvious opportunity for the business. This is the UK example; we're also trying it in other markets.

This is a bit more technical. The graphic here is actually a graphic from a screen from an iPad-type device, which we're piloting in the UK, which we're really using in front of small customers to sell pest treatments but it will also be relevant to washroom treatments. It's a very straightforward tool and I think enables us to instill a more standard approach to selling in our business and also enables us to get very rigorous control of pricing. The pilots in New Zealand which started this one or two years ago have gone quite well, we're now introducing a more sophisticated model to the UK market.

So another initiative which we've just started, a very, very simple one. It's our first foray into Internet transactions. It's a click-and-pay opportunity for wasps. If you have a wasp net problem, you want to have it treated very quickly you can go online and within 24 hours we can have a technician on site for a fixed price to deal with your wasps nest. We also look to extend this service into certain other fairly straightforward pest control initiatives, ones that don't really require a surveyor to come and survey the opportunity.

I think that this is a small example of something which we obviously want to extend also to other parts of our business, particularly City Link, where I think there is a good opportunity to move forward with simple transaction services. Again, what's held us back in this area has been getting the infrastructure of our information systems lined up to be able to offer a service like this online. But there'll be more to come in this area in due course.

Another example of an area we're focusing on is bids and tenders. This is an area of weakness for Rentokil Initial. As you know, our core market has been and remains SMEs but there is also good business to be had with bigger customers and we're having to learn our way in terms of bidding and tendering and we're trying to professionalize this particular aspect of marketing our services across the Group. IFS, of course, has a particular need to do well here but also increasingly our Pest and Washrooms businesses are getting into more and more bids and tenders. So a lot of work going on here as well.

Indoor sales I've talked about before. We've had some early experience in pilots. It's proving quite challenging to optimize the blend of skills one needs to do indoor sales to work with the field sales representatives but we're quite convinced this is the way to go to drive sales productivity which at the moment is unsatisfactory across most divisions in the Group. So we're going to extend the indoor sales pilot and we very much hope that we will find a way to optimize this particular technique over the next few months.

So if I now then turn to some of the new service lines. Manned Guarding I've already highlighted. And the reason for going back into Manned Guarding is this time to offer it as a joined-up service, not a standalone service as Rentokil used to do, a joined-up service with our cleaning and catering offerings in the UK market. You can see that the scale of the market is large. Manned Guarding is the third-biggest FM market in the UK. Cleaning accounts for 19%, catering for 18% and manned guarding for 14%. And the trend for certain customers to move to FM services is inexorable. This was a weakness in our offering. We have bought with Knightsbridge a very high quality business. It's a small business focused on high end City of London clients. Very similar in a way to Lancaster, the cleaning company we bought, in terms of its market focus. It offers us a really excellent basis for developing our Manned Guarding offering, initially of course in London but then beyond into the provinces.

And, then, a final small example from our Pest division which is investing pretty heavily in extending its service lines. Entotherm is a heat treatment process where you heat up the whole of an area and is particularly successful in dealing with bed bugs and insects with a very, very high success rate and has won awards in the UK for best innovation in the private sector, rightly so in our view.

So there you are, a quick romp through the growth agenda. Let me close the presentation part of this event with a view of outlook. Trading conditions have been now pretty consistent for the last nine months. Europe continues to be challenging, particularly on pricing. Cost savings are however giving us momentum to continue to drive earnings and running ahead of the GBP75m full year target. City Link has had its challenges in the first half of the year in terms of profit delivery but the restructuring is going very well and I would expect that by quarter four, City Link will be performing very strongly indeed. But the profitability will be weighted heavily towards Q4 also because of course of the success, [noted] success we've had in the B2C market which tends to be a Q4 biased market.

Net debt is continuing to fall and we would be pretty confident we will be perhaps significantly below GBP1b by the end of the year. We continue to focus heavily on the growth pilots and growth generally. We don't expect any material movement in the top line in 2010 but we are very much determined to deliver revenue growth in 2011.

And I think, in summary, our full-year expectations are unchanged for the business though we do point you to the potential adverse impact of the weakening euro on translation of results into sterling. That adverse impact at current exchange rates could be GBP10m but is offset to a significant extent by the strength of some of the other currencies such as the Aussie dollar and the South African rand. But there is, at the moment, we'd say an adverse impact of about GBP5m overall on our currency basket in terms of translation of results. But other than that we're not changing our expectations for the year as a whole.

So with that I think I'll hand it over to you and be very happy to take any questions you might have.

## QUESTIONS AND ANSWERS

**Katharine Rycroft** - *Rentokil Initial plc - IR*

If you could just wait for the microphone to be handed to you and also if you could state your name and institution. Okay, then if we start with Jaime.

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**Jaime Brandwood** - *UBS - Analyst*

Morning, it's Jaime Brandwood from UBS. I just wondered if I could start by asking about the merger you're implementing in UK Pest Control and UK Washroom and you started saying that you'll perhaps investigate that elsewhere as well. Is it a case of trying it first in the UK and the potentially rolling it out elsewhere in other countries where you've got both Pest and Washroom?

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**Alan Brown** - *Rentokil Initial plc - CEO*

Jaime, thanks for your question. No, it's not. We have run combined operations in the Islands for many years, the Caribbean in particular and Fiji and such like, very, very small and they've been successful. And what I was really fascinated by when I visited them was that if one looked at the customer overlap between Washrooms and Pest in these island operations it was about 30%. If you look at the overlap in our independent business where we don't run them together it's about 7%. Now, one has to allow for the fact that the customer market in Islands is a bit more captive perhaps than some of the larger geographies so I don't think one can make an automatic readout that you can get an increase in cross-selling by 23%, but nevertheless, the trend was clear.

So we have now, in addition to the Islands merged our operations, particularly in Italy, we did that about nine months, we've also done it to a lesser extent in the Nordics, but Italy we've done it in and the Italian merger has been pretty successful. I think I may have commented it in a previously meeting that we found in Italy that the customer, the combined customer list of the Pest and Washrooms business was about 13,000 and which only 1,000 were shared. So they're now really going for it in terms of looking at the cross-selling opportunities, as well as the cost synergies which is obviously derived as well.

So the evidence we've got from those operations which have always been combined, together with the Italian pilot, has encouraged us to then extend this on a much bigger scale into the UK market.

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**Jaime Brandwood** - *UBS - Analyst*

Yes, that was the second thing I was going to ask for, obviously, there's revenue synergy, what about the cost synergy? Is it feasible to run the operation using the same vans, using the same kind of --?

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**Alan Brown** - *Rentokil Initial plc - CEO*

No, you cannot combine at the service level. What you can combine at of course are locations and we have 44 Pest locations and 19 Washroom locations so we'll be looking to get further synergies there and clearly at the senior management level, IT, Finance, HR, all will be combined. So there will be some cost savings coming through from that but I would emphasize that the major reason for this merger is to drive revenue.

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**Jaime Brandwood** - *UBS - Analyst*

And moving quickly onto parcels, the volume trend there, 4% for the H1 period, 2% in Q1, therefore around 6% in Q2. Can you talk a little bit about that acceleration? Is that purely that you had less weather impacts? Is that you're taking market share, for example, are HDN-DHL, having issues that maybe are enabling you to take share? Any sense for why that acceleration is coming through?

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**Alan Brown** - *Rentokil Initial plc - CEO*

The weather effect clearly has had an impact in Q1, you're right about that. I think Q2 isn't representative of how things will go for the rest of the year, certainly up until Q4, Q4 is such a special case. I would say that the market has been characterized by a degree of unusual stability in terms of customer portfolios. We have lost very little business and we've actually won very little business in the first half of the year and I would say that is not untypical of what we're seeing across the industry after quite a high degree of churn in 2008/2009.

So I think that although we would expect the growth to come through in the second half of the year quite strongly is related to our customer mix, Jaime, because our customer mix is quite well positioned towards the B2C market which continues to grow very strongly at the seasonal piece. The drawback is that it's quite seasonal so I think the customer mix is right and it would be the growth of our existing customers which will drive the consignment growth in the second half of the year.

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**Jaime Brandwood** - *UBS - Analyst*

Last time I remember an update I think B2C was about 30% of City Link revenue.

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**Alan Brown** - *Rentokil Initial plc - CEO*

41%.

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**Jaime Brandwood** - *UBS - Analyst*

41%, great. And then very lastly, dividend policy, as you reach a position towards the end of the year where net debt to EBITDA is going to be at 2 times or possibly even slightly under 2 times, what makes you think about potentially reinstating the dividend?

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**Alan Brown** - *Rentokil Initial plc - CEO*

Shareholders make me think about that and I suspect that when we get into the yearend results and all that the Board will be looking closely at why not to reinstate the dividend rather than to continue the current policy. So I think you're right, I think with net debt below GBP1b, the only other thing -- at the yearend time I think, I'm pretty sure to happen, I think the only other thing taking place now is our credit rating. Standard & Poor's still have us on a BBB- negative outlook which I would certainly hope that they're going to review. So assuming they do review that and assuming that net debt does come in below GBP1b then I would that thought that there would be a strong argument for reinstating the dividend early next year.

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**Jaime Brandwood** - *UBS - Analyst*

Thanks very much.

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**Katharine Rycroft** - *Rentokil Initial plc - IR*

Mike?

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**Mike Murphy** - *Numis Securities - Analyst*

Mike Murphy at Numis Securities. Alan, can you just say on the cost savings whether there's scope to raise that GBP75m for the full year given that you're running ahead of target? And can you also say whether parts of that GBP75m have changed at all between, City Link as I remember was the main cost saving, and the other divisions?

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**Alan Brown** - *Rentokil Initial plc - CEO*

Yes, Mike, clearly, we're heading towards GBP80m plus or about that, but I wouldn't want you just to write that in because equally clearly, the revenue line is proving a little more challenging that we thought three months ago, but I think the two should be able to counteract each other.

In terms of the source of the saving, no material change. I think that what we're seeing is that a lot of the small projects are delivering, we're getting more small projects coming through so the City Link savings will be down a bit, but things like Olympic are providing incremental savings as the Group really gets to the savings mentality and takes it to heart. So we're seeing a lot of smaller savings coming through smaller projects as well as the big ones.

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**Mike Murphy** - *Numis Securities - Analyst*

Okay and can I just follow on from that on the sales side. Clearly, actually through the first half has been disappointing relative to where you thought you might be, only by small fractions but clearly, actually it has been more difficult. Have you consciously accelerated cost savings through the half year period knowing actually that you're struggling in terms of the top line?

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**Alan Brown** - *Rentokil Initial plc - CEO*

No, I haven't had to go in with heavy-handedness, it's not particularly my style, it's just really been coming through to be honest with you. So we've not said, "Right, we've got to pull this lever harder," it just has naturally flowed through. I find that it works best if I'm trying to focus on things which are nine to 12 months ahead rather than trying to influence what the business is doing three or four weeks ahead to be honest with you. So it's just naturally flowed through.

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**Mike Murphy** - *Numis Securities - Analyst*

Okay and just one final question if I may on those cost savings. If one were to look out at 2012 do you still feel that there is scope for further cost savings or are your managers telling you that we've had two years of cost savings and really actually they want to get on with the growth agenda in terms of driving top line growth? Because, talking to other Chief Executives it becomes clear actually that the employees start to get a little bit irritated about, or managers get irritated that it's all cost, cost, cost and really actually they're looking to drive the top line?

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**Alan Brown** - *Rentokil Initial plc - CEO*

Well, I think any Chief Executive of a legitimate business which doesn't have to think about cost is a very lucky man indeed and I doubt that in my career I will be in that position. So I think that costs, like the poor, are always with is. So you've got to be consistently at it because it's ultimately, in my view, a core driver of competitiveness, you have to do it. So I stand by what I've said on several occasions that at this range, this distance away from 2011/2012 I'd have thought we'll deliver not less than GBP50m of cost savings in each of those years over and above what we're delivering this year. And I would hope we would get more than that, but that's what I'm saying at this stage. We have to be able to deliver the cost agenda and be able to deliver the growth agenda.

Now, where I would, however, agree with you is if you're doing things like closing a central hub, that is a big distraction and you can't really get on to a growth agenda when you're doing things like that. But I think we'll be through the big structural savings by and large by the end of this year and the cost savings then will come from a range of smaller projects which will be less intrusive on the growth agenda.

The other point I would make, which I think I would agree with that you're saying is, is that we have clamped down very hard on salary increases over the last two years. It's been, probably a 1% increase in salaries, there's a lot of people not taken any increases over the last two years and that is not a sustainable position. We will have to start to offer some increases in salary in 2011 and beyond, albeit we're looking to do that by linking any salary increases to productivity.

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**Mike Murphy** - *Numis Securities - Analyst*

Okay and then finally if I just may, just on that growth agenda, you say to show consistent growth from 2011 onwards, clearly using 2010 as the base, so i.e. yes, you expect to deliver growth in 2011, not 2011 being the base and growing 2012, 2013.

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**Alan Brown** - *Rentokil Initial plc - CEO*

That's correct. I still would be hopeful that we'll get very close if not to matching last year's revenue in 2010 subject to currency impacts, I mean there will be an adverse on the top line on currency impact, it could be GBP20m related to the GBP5m I talked to you about on profit, but other than that I think we'll get very close to matching last year's revenue and that then will be the base for growth.

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**Katharine Rycroft** - *Rentokil Initial plc - IR*

Andrew.

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**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

Morning, it's Andrew Ripper from Merrill Lynch. First question on termination rates where you put an interesting chart up on Page 15 showing some quite good recent improvements across the businesses, ex Textiles. I'm just wondering what your sense is of how much further you can push retention across the portfolio?

And then maybe you could explain a little bit more about why Textile and Washrooms is lagging? Is there any sort of disruption from the changes, restructuring that you've been undertaking or is it an economic effect, please?

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**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

Well, I think, Andrew, you wrung out of me on a previous occasion a target of about 85% retention rate and now with the advantage of seeing the graph it probably wasn't a bad guess because I think that a lot of the businesses are coming in at around 83% at the moment, if I understand the chart correctly. So I think to get to 85% would be a pretty good number and I think one or two people have said, "Well, the business used to do 86%, 87%" but I don't think the business was accounting accurately to be honest with you for retention rates in those days. Certainly now we take quite a difficult measure, we include in retention any downgrading of existing contracts whereas I think in a previous life we used to define it as complete loss of a customer and didn't take account of any reductions. So this is quite a tough measure we've got and, as I said before, I think 85% is looking like a good number to go for and there are four of the businesses now heading towards that.

With regards to Textiles and Washrooms, there a few things. I think the UK Washrooms business still needs to do better. It's come along way over the last 18 months but it can certainly do a lot better on customer retention. And the Benelux business, which I've pointed out on a number of occasions, has not been performing well and we've changed the whole management team in that business over the last three to four months. And that business I think was typical of a number of integral businesses which really had been ripped of capability over a number of years and now need to rebuild that capability.

So we've got a couple of hotspots where retention is not good which we've just got to work through but there's nothing systemic in it, it's more business specific in Textiles and Washrooms that we're trying to address. And there've been one or two losses in the French business which have, it's just big customers which are not typical.

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**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

Yes, and the trend of improvement in recent months is that basically payback on the improved service levels from '09 translating into keeping customers for longer?

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**Alan Brown** - *Rentokil Initial plc - CEO*

I would certainly like to think so. I think the work we're taking on customer care is also coming through. So the payback's taken a while but it's now looking pretty clear linkage between the range of service initiatives we've taken and retentions.

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**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

Okay. Then thinking about the pilots that you talked about today, it's obviously difficult for us to get a sense of how meaningful they could be if rolled out across the Group. I don't know whether you can give us any sense of timeline in terms of when they could be translated into division wise or Group wide initiatives? And as a follow through from that when they could impact upon the top line please?

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**Alan Brown** - *Rentokil Initial plc - CEO*

The pilots will run until they work or until we decide that they just can't work. So the customer care stuff is really working and we're now looking to implement that across a number of divisions. The improvement of retention rates and the improved understanding we're getting from our existing customer base is very high, so that has now been rolled out in a number of territories.

Some of the other stuff, particularly the indoor sales stuff needs a lot more optimization and I think that's going to have to go through several iterations before we really get that working properly. The other ones are in between, the tablet which we showed earlier I think is capable of fairly rapid rollout, if it works that will be an easier one to implement if it proves successful.

So I think, clearly I cannot give you guidance on individual pilots and I'm very reluctant to give you guidance on growth generally because it's just, I was thinking about it last night, it's a bit like trying to develop a DNA, a genetic way of running a business and my previous experience, particularly in China, was that you can get seven or eight bits of the DNA chain right but if you haven't got the ninth and tenth there things still don't run, then suddenly they click into place and off you go.

So my best guidance in all of this still is that we will see progress through 2011, that would be the best guidance I can give you and whether it's Q1, whether it's Q3 I don't know, but that's my feeling about when these things are going to come to fruition. Not just through these growth pilots but through some other initiatives we're taking as well.

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**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

Do you think nominal GDP growth is a reasonable sort of benchmark for prospective sales growth for next year?

**Alan Brown** - *Rentokil Initial plc - CEO*

Let me come back to that in February 2011.

**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

And just finally from me, the Pest Control organic growth just slipped a little bit in the second quarter. I think the US was pretty strong in Q1 and dropped off a little bit in Q2. What do you feel is the sort of momentum when you look at --?

**Alan Brown** - *Rentokil Initial plc - CEO*

Seasonal factors no more that that really. There's really nothing in it, it's just seasonal factors. I think the US had some quite strong impact from its distribution business in Q1, that's a business which provides pesticides to other companies, came off a little bit in Q2, but I think we see in the Pest business, setting aside Continental Europe, there is some momentum developing in terms of new business. So I think we're looking, the Pest business is our more stable business and I think we're pretty confident we'll get some growth this year.

**Andrew Ripper** - *Bank of America Merrill Lynch - Analyst*

Okay, thank you.

**Katharine Rycroft** - *Rentokil Initial plc - IR*

If we could go to Tom now please.

**Tom Sykes** - *Deutsche Bank - Analyst*

Morning, Tom Sykes from Deutsche Bank. I was just wondering, just on the City Link business you've obviously taken out the structural costs. Could you maybe just say the scale of the one-off or ad hoc costs that you're carrying for the operational issues that you see at the moment please?

**Alan Brown** - *Rentokil Initial plc - CEO*

We are running, in terms of that core, what we call C&D, the Collections and Delivery bit of the business, the small vans going around the country, we are incurring costs which in the first half of the year have been about GBP5m more than last year which reflects the amount of resource we've put in to preserve service while we've been going through this enormous structural change. Now, we've had big savings elsewhere, the whole infrastructure costs have come down substantially through the reduction of depots, so really big savings coming through, but that bit, that element of it is the one that I'm really unhappy about and that's the bit that the team is now focusing on to sort out in the second half of the year.

**Tom Sykes** - *Deutsche Bank - Analyst*

Right, but as a run rate if you sorted out the operational issues and optimized the time from parcel to delivery, what's the scale of reduction of those costs that you would expect? What's the endpoint you're trying to get to, given a flat revenue line this (multiple speakers).

**Alan Brown** - *Rentokil Initial plc - CEO*

Well, I could give you a conceptual number but I'm not going to because I want to wait and see whether there's things going to come through but I will give you clear guidance about City Link. I will say that we now anticipate that we'll delivering about GBP10m profit this year in City Link for the year as a whole, taking account of the revenue stream and getting a hold of the cost base in the second half of the year.

And I would repeat what I've said before that for me this looks like, in moderate to tough economic conditions a 5% margin business which we might not get to in 2011 but we'll be getting close to it in my view. I think we could go more than 5% if we get into a strong economic market where you get new growth, because obviously then the growth comes through very strongly in the bottom line if you start to get that. So I'll give you that general guidance rather than getting into the specifics of the C&D costs, Tom.

**Tom Sykes** - *Deutsche Bank - Analyst*

Okay, thank you. And I'm just slightly confused on your comments on the revenue just because you alluded to a couple of times that June was better and then you said, well, the great outlook was worse than it was three months ago when we were talking to you. Then you say your retention rates are better. So I'm not quite sure how that all stacks up to like-for-like growth in the second half because there seem to be some conflicting comments there. Do you expect that you'll still be running constant currency slightly negative in the second half or do you think that actually you can generate positive constant currency growth?

**Alan Brown** - *Rentokil Initial plc - CEO*

It's looking about (inaudible) for the year as the half which means positive in the second half.

**Tom Sykes** - *Deutsche Bank - Analyst*

Okay, thank you.

**Katharine Rycroft** - *Rentokil Initial plc - IR*

Could we have David please?

**David Hancock** - *Morgan Stanley - Analyst*

Thanks. David Hancock from Morgan Stanley. Around the question on dividend you said the Board would be looking at reasons not to pay, one of those reasons might be more acquisitions. Can you just talk about whether you want to add more capabilities within the Facility Services business to grow the Guarding offering more and Catering, I think, relative to how you characterized your market you're clearly overweight Cleaning and underweight the others.

**Alan Brown** - *Rentokil Initial plc - CEO*

Yes. Well, I think all the businesses in the sector have come from their own historic position and Compass and Sodexo have clearly come from a very strong position in Catering. Carillion and others come from strong positions in M&E so I think it's more about being able to offer a full range of services rather than trying to take a really big share of the new sectors. I think the big gain for us is being able to sell in then Guarding into our medium sized to larger customers across the portfolio and I don't think we have to go acquiring a lot more business to do that. I think it's much more economic for us to build an organic growth







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agenda on the back of the capability we now have. So I wouldn't be highlighting up a range of new acquisitions in the IFS business at all, I think this was an important gap to plug.

We do have a weakness I think in M&E to be honest with you, that business is really subscale at the moment, it's about a GBP9m business. That really is subscale. So if something came up in that area we might look for it but it would again be a similar size acquisition to a Lancaster or to Manned Guarding.

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**David Hancock** - *Morgan Stanley - Analyst*

Great thanks. Then just on cash flow, it looked like the DSOs cracked up a little bit in the first half but you said you're confident about getting down to the 47 for the full year. Can you just talk about why you have that confidence?

And on the restructuring costs, GBP10m lower than you'd previously thought, is that pushed back into next year or is that you think the costs will be slightly less?

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**Alan Brown** - *Rentokil Initial plc - CEO*

On the latter point the costs will be slightly less. That's not to say we won't have other programs with additional paybacks coming through next year, but it's not that we've got a deferment of expenditure on the projects we've planned for this year, that's not the case. The reason by the way we've managed to do this is we've been pretty successful in getting away the properties that we had. We've managed to move the properties on very quickly, the Wednesbury hub, for example, which closed on July 23, I think we sign next week the sale of the hub which is pretty good going. The price is not wonderful but in the current market it's better than we thought we'd get so it's gone. So that's why we've been a bit more successful in terms of the cash restructuring costs that we thought, getting the properties away quite quickly.

Sorry what was the first question again?

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**David Hancock** - *Morgan Stanley - Analyst*

It was around DSOs and --

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**Alan Brown** - *Rentokil Initial plc - CEO*

Oh yes, well, there's a seasonality factor in all of this and I think that alone will help us in the second half of the year and we've had some issues in some of our businesses through some of the restructuring which has held us back a bit. But I don't anticipate that will still be an issue at the year end.

And the very last one is on pricing in City Link, some of your peers have talked a little bit more favorably in recent months about pricing in parcels in the UK and more broadly in Europe, can you just talk about whether you're seeing an easing of trends as well?

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**Alan Brown** - *Rentokil Initial plc - CEO*

I think there has been a slight easing in terms of specific negotiations with specific customers, we would have seen that, but it's pretty marginal. And we have a mix effect in our business, of course, with some of our bigger customers growing quite strongly. So I think for our business we're not likely to see a big change in the negative 4% trend in the second half of the year.

**David Hancock** - *Morgan Stanley - Analyst*

Perfect, thank you.

**Katharine Rycroft** - *Rentokil Initial plc - IR*

Will you pass to Rajesh please?

**Rajesh Kumar** - *HSBC - Analyst*

Hi, this is Rajesh Kumar from HSBC. Just one quick question on contract retention rates, clearly, they're coming up June to June, up 5% and that's good news. The question is, is that led by less reduction because last year you had a lot of reductions? Or is that led by more contract retention?

**Alan Brown** - *Rentokil Initial plc - CEO*

It's a combination of both and if I talk about Ambius clearly they've had better retention of customers last year in what was the relatively early stages of the economic downturn, a lot of customers just cancelled. So I think of some of the more essential services like the Textiles and Washrooms area there are still significant elements of reduction coming through which we're managing a bit better. So it's a combination of both. I don't have the details split between the two to be honest with you. So I would say last year we had more absolute loss of customers than this year but the blend is probably balanced this year a bit more towards contract reductions rather than losses.

**Rajesh Kumar** - *HSBC - Analyst*

Okay and in terms of reductions are you seeing larger accounts or smaller accounts and more number of accounts? As in, when we talk about a 20% churn, has the mix changed in terms of the churn size of each ticket?

**Alan Brown** - *Rentokil Initial plc - CEO*

It varies a lot by geography. In Textiles and Washrooms in Europe we've lost a few big customers, one in France, one in Benelux, those are the higher profile ones. But I would say that what's happening is that certainly the SME base is tending to stabilize and that is probably where we're now getting better retention rates, in the SME business. The bigger customers tend to be still very price sensitive with a lot of procurement activity going on. That was why I've emphasized the importance of the Goods and Tenders initiative we're taking in the business.

**Rajesh Kumar** - *HSBC - Analyst*

Okay and how much are your sales teams and service teams talking now? Because if they're talking that would mean that going forward contract retention rate can get better. So has that improved?

**Alan Brown** - *Rentokil Initial plc - CEO*

Well, the sales are really split into two different types of effort. One is managing existing customers with customer care initiative and clearly they are really working cheek by jowl with the service people. There's another group of sales people who are looking for new business and they are less connected with the service people.

**Rajesh Kumar** - *HSBC - Analyst*

That really helps.

**Katharine Rycroft** - *Rentokil Initial plc - IR*

Do we have any more? Yes, Mike?

**Mike Murphy** - *Numis Securities - Analyst*

Alan, just looking at City Link and you talked about the GBP4.6m higher distribution costs, I'm just looking at Q1 and Q2, I mean in Q1 you managed to get your costs down by GBP3.2m and they've gone up by GBP0.9m in Q2 on very similar revenue. So have those come through in high distribution costs or are they purely a Q2 phenomenon or was there some of that in Q1, I can't remember --?

**Alan Brown** - *Rentokil Initial plc - CEO*

No, no, it's been a consistent trend on year. I think the difference quarter-on-quarter is because of differences in cost last year rather than any change in trend this year. Okay, January you've got to set aside a bit because it was so extraordinary with all the snow, but the trend we've seen has really been month-by-month against budget, we've been consistently underperforming, we've been performing worse than budget in terms of cost from February through June in this particular area. So it's not that it's getting worse, it's just we're not making improvements we need to make at this stage.

But as I said before, I'll come back and emphasize the point, I think now we're really finished the big structural changes for the year and I think now we understand why we've had the issues we'll be able to address it in the third quarter.

**Mike Murphy** - *Numis Securities - Analyst*

And can I just follow on from that, do you feel that in the final quarter you could adapt your cost base a little bit more quickly than you have done in previous years, if you go back a couple of years there's GBP101m in Q4 and there was huge problems in terms of adapting to the changed volume environment. Have you been able to make it more flexible than it was in the past with subcontractors, etc.? Or will you still be prone to this trying to plan for those last six weeks which can be extremely difficult?

**Alan Brown** - *Rentokil Initial plc - CEO*

Of course, one has to gear up for significant resource in Q4, there's always then a variable element, but this year the underlying cost base, the fixed cost base will be so much lower than previous years, that will be the big advantage we'll have. So we'll be still having to gear up but from a much lower fixed cost base because of we'll be down to about 71 depots by that stage and one central hub. So I think the profitability in business in Q4 should be substantially ahead of last year because of that. We'll still have to gear up in terms of variable costs but the fixed costs will be much lower.

**Mike Murphy** - *Numis Securities - Analyst*

How much do you think, can you give us an idea of (technical difficulty) of that in terms of the --

**Alan Brown** - *Rentokil Initial plc - CEO*

Well, I've given you the guidance. I think that's sufficient, I've said that we would expect to make around about GBP10m this year and we'll make a marginal profit in Q3 and therefore you can work out by difference what you might expect then profit in Q4 to be.

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**Mike Murphy** - *Numis Securities - Analyst*

Yes, I'm just trying to look at the delta on that actually and (multiple speakers) but I appreciate it's, you've de-risked it in that respect but I can't see from the outside just how much because we don't have that idea of how much are the changes in the fixed costs.

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**Alan Brown** - *Rentokil Initial plc - CEO*

Right, well, some things have to remain a mystery in life, Mike, otherwise it wouldn't be exciting.

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**Katharine Rycroft** - *Rentokil Initial plc - IR*

Okay, I think that's it. Thank you very much, ladies and gentlemen.

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**Alan Brown** - *Rentokil Initial plc - CEO*

Thank you.

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