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RTO.L - Rentokil Initial plc Q3 Trading Update Conference Call

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PRESENTATION

Operator

Good day, and welcome to the Q3 trading update conference call. For your information, today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Andy Ransom. Please go ahead, sir.

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Thank you very much. Good morning, everyone. This is Andy Ransom speaking, Chief Executive of Rentokil Initial. I'm here with Jeremy Townsend, our Chief Financial Officer. I will now give you a short run through of the main points from our Q3 trading update; after that, we'll be happy to take any questions.

If I start first with the key financial highlights for the quarter, all numbers here are at constant exchange, our Group revenue's increased by 3.8%, with organic revenue growth of 1% coming from our core international businesses.

Adjusted operating profit grew by 3%, largely reflecting good performances from North America, which continues to benefit from our acquisition of the Western Exterminator business; but was also supported by good profit contribution from the UK, in particular.

Cash flow of GBP50.4 million was a strong improvement on last year's GBP29.3 million, and we anticipate further improvement in our cash flow in the fourth quarter.

Overall, I'm particularly pleased by our core businesses' improvement in organic revenue growth in the quarter, which was achieved despite the ongoing difficult trading conditions, particularly in Europe.

It's also worth noting that we took advantage of favorable bond market conditions to issue a 3.25% coupon, EUR350 million bond on the October 7. This is going to be used to refinance the Group's EUR500 million bond, which matures in March of next year; and, in doing so, will reduce our average cost of debt to below 4%, and will also reduce our interest costs by over GBP10 million per annum.

Turning now to each of our operations, in the west region, which includes our big North American and UK operations, revenue was up 19.1% for the nine months to September, with profit up by 14.5%, or GBP4.3 million; again, reflecting the positive impact of the Western acquisition made in Q4 last year. The integration of Western continues to go well, with most of the work due to be completed by the end of the year.

Asia continues to perform very well with profits up by 35% year to date on revenue growth of 7.5%. This is supported by strong double-digit growth from our operations in the emerging markets of India, China, and Vietnam.

Our east region, which comprises our businesses in Europe and the Pacific, saw profit decline by 1.2%, on a revenue decline of 1.9%, in the first nine months. This was driven by a weak performance in Benelux, the Netherlands in particular, but also by a softening in trading conditions in France and in Germany. Pricing pressure in the workwear category continues to impact our margins, as it has done all year.

In initial facilities, revenues declined by 3.9% year to date, with profits down 9.4%. This is due to the planned withdrawal from low margin single-site contracts in the UK; from lower job revenues in technical services; and from delays in the award of anticipated new contracts over the summer. Those new contracts have now largely come through, and some GBP25 million of new business was secured at the end of Q3.

As we're now approaching the end of our major restructuring and investment program, my focus is now on converting these efforts into improved profitability and into better cash generation.

Our overheads are coming down; savings in 2014 from central and divisional overheads estimated at GBP10 million per annum. The businesses are becoming more efficient, and during next year our restructuring costs and our CapEx will also reduce. I'll give further details on my plans to deliver sustainable revenue and profit growth, and increased cash flow, at the prelims in February.

Finally, turning now to the outlook for the fourth quarter, we're expecting trading conditions and ongoing business performance to remain largely unchanged over the remainder of the year.

With that, I'll hand back to the operator, Caroline; and Jeremy, and I will be very happy to take any questions. Caroline?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Robert Plant, JPMorgan.

Robert Plant - *JPMorgan - Analyst*

Three questions, relating to organic growth, please. You make reference in the statement to a core organic growth of 1%, and you say that's international growth just now. What is that excluding, please? Relating to that, on a like-for-like basis, Q2 to Q3, can you give us the trend in organic growth?

And also, when I read the statement, you give the nine-month category at actual exchange rates. I wondered if you could give us the categories at organic growth for Q3 and Q2, so we can see the trend, please.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Robert, the third question, was that on revenue, or on profit?

Robert Plant - *JPMorgan - Analyst*

On revenue, please, Jeremy. So, I'd like to see what each division is doing.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, so, on a core Group basis including IF, organic growth in the third quarter is about minus 1%.

Robert Plant - *JPMorgan - Analyst*

And what would that have been in Q2, please, Jeremy?

Jeremy Townsend - *Rentokil Initial plc - CFO*

The organic growth for the Q2 number, I'll just get that to you in a moment, about minus 1% for the continuing Group, including IF.

Robert Plant - *JPMorgan - Analyst*

So, minus 1% to minus 1%. Therefore, the thing that's been excluded, when you talk about 1.0% growth, is IFS?

Jeremy Townsend - *Rentokil Initial plc - CFO*

That's right.

Robert Plant - *JPMorgan - Analyst*

Yes, okay.

Jeremy Townsend - *Rentokil Initial plc - CFO*

That's right. Can you repeat your second question, Robert?

Robert Plant - *JPMorgan - Analyst*

Second one was about the per category. It would be nice to have, for Q2 and for Q3, what the organic growth rates were, for example, for pest control, hygiene, work wear, etc.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, I haven't got those separated out. But what I can tell you is directionally, where the strength was coming from was some improvement in the hygiene numbers, and reasonable strong growth in pest control. Work wear was reasonably flat. And, clearly, we had, on a core Group basis, [FM] was down a little.

Robert Plant - *JPMorgan - Analyst*

Great. Thank you, Jeremy.

Operator

George Gregory, UBS.

George Gregory - *UBS - Analyst*

Two from me, please. Firstly, Jeremy, just on the net interest cost, I think, Andy, you mentioned that the interest cost should reduce by GBP10 million per annum. What should we, therefore, be plugging in for 2014? Is it a year-on-year reduction of GBP10 million, or will that, for one reason or another, not impact?

Second question, overhead costs are said to reduce by GBP10 million per annum. I think consensus probably has about GBP80 million, or so, in the other line for EBITDA. Should we, therefore, assume that drops to GBP70 million in 2014, please? Thanks.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Hi, George. What I'm expecting on actual exchange rates is, given that we've moved the guidance for interest costs for 2013 to end up in the GBP59 million to GBP60 million range, I would anticipate, subject to net debt levels, based on the current underlying rate, that, that will come down by GBP10 million.

And similar for the overheads; that, in terms of that guidance of around GBP80 million, I think I would expect that number to be GBP70 million for 2014. That's right.

George Gregory - *UBS - Analyst*

Perfect. And just on that net interest, in addition to the GBP10 million reduction in the average interest cost, should we not also unwind that GBP1.5 million re-fi cost that impacts this year?

Jeremy Townsend - *Rentokil Initial plc - CFO*

I'm including that in the piece. So what you've got, in Q1 we don't get the benefit. It's not until April that we get the benefit, so we've got the double running cost until the bond matures.

There's an annual reduction underlying cost, so you're right, that's partly offset by the Q1 impact. So, what I'm going to on a net/net basis, we should be taking the number from just about GBP60 million to just about GBP50 million in 2014.

George Gregory - *UBS - Analyst*

Okay, very clear. Thanks.

Operator

Caroline De La Soujeole, Cantor Fitzgerald.

Caroline De La Soujeole - *Cantor Fitzgerald - Analyst*

I have three questions; one of which has already been answered, on organic growth.

The other two, one is on initial facilities. You're talking about delays in the award of contracts over the summer. I just want to get a feel, have these opportunities gone away, or could they come back? And therefore, would you expect to see an improvement in the fourth quarter trading performance on IF?

The second question is on hygiene. If I'm not mistaken, you've launched a new range in the third quarter; just wondering if you could talk about how the rollout is progressing, please.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, on IF, the contracts, when we talked about IF at the half year, we had a pipeline of about GBP30 million. GBP25 million of that has been realized towards the end of Q3, going into Q4. That should help the top line, will help underlying performance. Offsetting that, though, is we have had some margin erosion in IF in the third quarter, and I'd expect that to continue to flow through into Q4.

So, while the top line is strengthened by the new contract wins, my expectation is, given the margin pressure, Q4 performance will be broadly in line with Q3, and it won't be until 2014 until we start to see the benefit of those contracts working their way through to the bottom line.

Andy Ransom - *Rentokil Initial plc - Chief Executive*

I'll pick up the signature one, Caroline. A little bit anecdotal at this stage, but we were trying to do three things with the signature launch. Fairly obvious, I suppose, sell more; sell at a better price point; and sell at a higher penetration level per customer.

We've launched, on a rolling launch basis, in over 30 markets now. The feedback that we're getting from the sales force is terrific. They love the product. The evidence, as I say, is somewhat anecdotal at the moment, but it would appear that we are selling more, on average, in each of the markets. We are selling at a better price point, and we're also upping the number of service lines per customer.

So, all three of the core metrics that we were looking for evidence of a successful launch appear, at this stage, to be tracking in the right direction, but it's too early to give any indication. These sort of programs take quite a lot of time to work all the way through the portfolio, so it'll probably be some time before we can put dollars on the effectiveness of the rollout, but so far, so good.

Caroline De La Soujeole - *Cantor Fitzgerald - Analyst*

Understood. Perfect. Thanks.

Operator

Andrew Ripper, Merrill Lynch.

Andrew Ripper - *BofA Merrill Lynch - Analyst*

I've got two, please. Jeremy, just want to finish off a couple of structure questions. Obviously, the bond you've just issued is EUR350 million; the bond that matures in March is EUR500 million. In terms of the difference, do you have sufficient gross cash, or will you just draw down the RCF, in terms of paying out for the EUR500 million that's out next March?

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, Andrew, we will have a reasonable amount of cash to fund it. But I would expect, depending on the availability of the working capital, we tend to have availability of about GBP100 million in working capital. There will be some draw down on the RCF from time to time, but it will be a relatively small draw down. Because we did EUR350 million, we may be calling on the RCF, but it'll be --

Andrew Ripper - *BofA Merrill Lynch - Analyst*

Marginal.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Swings and roundabouts. I would suspect, by the year end, for example, given the seasonality of the cash flow, we probably won't be drawing on the RCF by the end of 2014, everything else being equal.

Andrew Ripper - *BofA Merrill Lynch - Analyst*

Okay. Then in terms of CapEx, there's obviously a reference that CapEx is likely to be lower in 2014 than 2013, can you give us a sense of order of magnitude? And where will CapEx -- what are you cutting back on in terms of CapEx?

Jeremy Townsend - *Rentokil Initial plc - CFO*

Sure, so we're guiding for the current year to GBP230 million to GBP 240 million. That's above the historic level, as we've been investing in the transformation program, IT projects, as well as the restructuring.

We're currently in the middle of the planning process at the moment, and putting our plans together for 2014, and we'll obviously be able to give more detail at the prelims. But I guess I'd be disappointed, Andrew, if I couldn't reduce that by GBP20 million as we come to the end of the structuring, and particularly manage some of the infrastructure investment.

We'll still be rolling things out, delivering the new tools into the business, but then, I'd have thought, there's at least a GBP20 million reduction there to be had.

Andrew Ripper - *BofA Merrill Lynch - Analyst*

Okay, thank you. And I've got two for Andy. Andy, on your summary at the front of the press release today you talk about converting the restructuring investment phase into improved profitability, which is a fairly generic phrase.

I appreciate you're going to provide more color around strategy and business plans in February, but I just wonder, in terms of driving profits forward, are you more interested in top line, gross margin, cost, combination of all three? Where is the emphasis going to be over the next couple of years?

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Well, you correctly called it, Andrew, that more details to follow next year. But clearly, the biggest challenge for the Group has been driving organic revenue growth. We're not coming off that focus. We absolutely remain committed to driving organic revenue growth. I'll talk more about that at the prelims, as to where I think we can get that, and I'll give you some detail then.

In the meantime, I am of the view that we can do a fair bit more to drive profit out of the business. So, the answer, is it all three, yes, of course, it's all three. We'll be going for top line, we'll be looking at gross margin, as well as cost below gross margin. But really, the program's going to be about focus; it's going to be about effectiveness; it's going to be about pace of execution. We will be looking for improvements right through the P&L, but I'll give you a lot more detail at the prelims.

Andrew Ripper - *BofA Merrill Lynch - Analyst*

Thank you. Then secondly for you, in terms of the portfolio [published], you guys traded a multiple that's significantly lower than some of your peers, particularly in the US; and then Berenson close to home. What's your position as far as the portfolio is concerned? Are you committed to all of the business units? Or would you have an open mind if a deal was to appear that would enhance value versus whether -- the valuation of the Group, as it's currently constituted?

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Yes, very fair question, Andrew. I think a former boss of mine once said that he'd sell any business in the portfolio if the right value proposition was tabled. At one level, I think you always have to have an open mind to where is the best opportunity to create the best value for shareholders.

Again, in Feb, I'll give more detail as to where I see the priorities and the opportunities, both for investing in the portfolio through acquisitions, some modest divestments as well.

In the case of IF, we've taken the step of running that business more independently. We've said that there's been speculation about that in the past. Our intention there is to run that business well, to run it hard, but we'll keep an open mind, going forward, as to the long-term future ownership of that business.

But for the time being, the portfolio remains as is. Again, I'll give you a bit more detail, a lot more detail in Feb as to where the focus areas are going to be.

Andrew Ripper - *BofA Merrill Lynch - Analyst*

Yes, okay. Thanks very much.

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Thanks, Andrew.

Operator

Mike Murphy, Numis.

Mike Murphy - *Numis Securities - Analyst*

You mention in the statement that as you approach the end of your major restructuring investment program. Can you say now whether you feel, Andy, looking forward, that we won't have these perennial GBP50 million/GBP60 million of restructuring costs? Also, can you say at what level they might be? And if they are at a small level, will you take them above the line, rather than have them as, say, a perennial item?

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Yes, thanks, Mike. I can say, definitively, we will not have GBP50 million/GBP60 million restructuring charges on a perennial basis, for sure. We are absolutely focused in that space. It's going to be a material reduction, not really able to give you a figure of that at the moment, but it will come down substantially from those sorts of levels.

The issue of where do we take those charges is something that Jeremy, myself, and the Board will discuss over the next few months. Again, I would expect to be able to give you a straight answer to that in Feb.

Jeremy, you want to add to that?

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, I think that's right. I think the key issue, Mike, is to get the numbers down, and then we'll look at the disclosure, to whether they go above the line, or below the line, and, again, we'll be very clear in Feb.

One of the issues is we're trying to keep the reporting of our numbers as consistent as possible because we're aware there's been a number of changes over the time. But equally, we don't want to be making too many changes going forward, either.

So, we'll look at it very carefully. We're looking at all of our reporting framework, and we'll come back to you at the prelims, letting you know on that. But I'd just reiterate what Andy said, there will be a significant reduction; I think that's the key thing.

Mike Murphy - *Numis Securities - Analyst*

Yes, but, as you say, in your own comments, as we approach the end, is the end, in your mind, December, or is the end middle of next year, or end of next year? I'm just trying to get a sense of when all of these major restructuring figures are going to fall out the numbers.

Jeremy Townsend - *Rentokil Initial plc - CFO*

There's still some projects ongoing, so they don't come to a sudden halt, and there's still a bit of work to do, but it will be substantially completed within 2014, that's for sure.

Mike Murphy - *Numis Securities - Analyst*

Okay. Thank you.

Operator

Sylvia Foteva, Deutsche Bank.

Sylvia Foteva - *Deutsche Bank - Analyst*

I want to ask three questions, please, on M&A. At the interims, we were left with the impression that M&A will continue to be a very important part of your strategy. Can you just comment on the pipeline, and which areas and divisions you're looking to add to?

Then, on the contract portfolio, that one table was not in this quarterly release. I was just wondering whether you can give us any details on pricing additions, terminations that you are doing.

And then finally, in France, are you seeing any benefit from the [SCSC] tax credit, please? Thanks.

Andy Ransom - *Rentokil Initial plc - Chief Executive*

I'll take the first one. M&A, Sylvia, yes, we've got a very healthy pipeline of potential deals, with quite a number of open conversations at any one point in time. The prime areas that we are most focused on are Latin America, in particular Brazil; North America, to infill some of the remaining gaps in our city strategy there; and parts of the Middle East. So, those are three of our top targets.

We've also got some targets in cleanroom, which is the very technical end of the work wear category, which we talked about before.

And in most of the businesses we have targets, but we are developing a more differentiated approach to what sort of returns that we would expect, depending upon which part of the business they fit.

So, primary focus is on pest, and in the markets I've shared. But we do have some targets in many of the other parts, but taking a more differentiated approach.

On the portfolio, do you want to take that one?

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, (inaudible). Yes, on the portfolio, in terms of retention, retention's been reasonably robust. We've guided in the statement to the charges in Benelux, and IF; and in terms of terminations, that's been the core area, particularly in IF as we've managed our way out of the single-site contracts.

Pricing, again, we've guided to that in the statement. We have been under pricing pressure, again, particularly in Continental Europe, and really across the board, France, Benelux, and Germany; we've had some softening contracts as we were renewing them, as we have had in IF. I think a key challenge for 2014 is to look for us to be able to manage that margin pressure, and manage that price pressure that we're experiencing.

The third question, in terms of France, the French tax system, above the line and below the line, has been a somewhat challenging environment over the last two to three years. Below the line, I think it's the highest tax rate we face across all of our 50 countries in terms of corporation tax.

But there has been some beneficial impact of that social credit above the line in the year. You'll see from the French numbers in the statement that we are getting profit growth in France, despite the margin pressure, and that is helped, to an extent, by the credits that we've had in 2013.

Sylvia Foteva - *Deutsche Bank - Analyst*

Thank you.

Operator

Jane Sparrow, Barclays.

Jane Sparrow - *Barclays - Analyst*

It's just the one the decision to limit the deployment of some of the systems that you developed, and leading to the non-cash write-off.

Is the decision to not progress with those programs because they basically didn't turn out to be very good systems? Or is it because it's going to cost too much to implement them, and, therefore, it's a sort of job half done that will need to be picked up in the future? Can you just talk me through the reasons behind that decision?

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Yes, Jane, one of the things, I suppose, most incoming CEOs do is take a good, fresh look at lots of ongoing things. I took a really hard look across all of the programs and projects that were part way through implementation and in the vast majority of them concluded that they were very good projects and performing well.

In the case of these projects, it was my judgment, based on more detailed analysis, that whilst the solutions were technically very good and they worked, the cost to deploy versus the benefits we would ultimately get that, that equation was not good enough, in my opinion, to justify the continued deployment, and, in some cases, further development.

So, a very hard clinical review concluded that some of the projects we would just be better off to limit deployment to where we had deployed, and to push on in a more focused way on finishing off the deployment of the other projects. It was a survival of the fittest, if you like, but a very tough review, and I think the right decision for the shareholder.

Jane Sparrow - *Barclays - Analyst*

Okay, thank you.

Operator

George Gregory, UBS.

George Gregory - *UBS - Analyst*

Sorry, one very quick follow up question, please. What are your expectations for working capital outflows this year? Also, any outer year thoughts you have on how working capital consumptive growth might be, please? Thanks.

Jeremy Townsend - *Rentokil Initial plc - CFO*

Hi, George. Yes, we guided all year to 20 to minus 30. I think that I'd hold with that range, but my expectation is nearer minus 30 than minus 20. We are a 2 billion plus business, so trying to land working capital on a -- even within a range of GBP10 million, it can be a bit challenging for a CFO in 50 countries. But that would be the guidance.

Going forward, working in our favor is an increased push to get people onto direct debits, and an increased professionalization of our cash collection. One of the projects we will be continuing to roll out is some sophisticated software that we use for managing receivables and collections.

Going against that is the fact that, increasingly, we're moving to key accounts, large accounts. One of the big pushes in 2014 is for driving our key account sales in America. But increasingly, as a business we're looking to grow what traditionally Rentokil has been, an SME in the small customer base, and grow a much bigger key account base, national account base, and those national account customers tend to have longer payment terms.

So, everything else being equal, my expectation would be for a growing business, and with an increasing mix of key accounts, we'll continue to have some outflow in terms of working capital in that GBP20 million to GBP30 million range.

George Gregory - *UBS - Analyst*

Perfect, thanks.

Operator

Rajesh Kumar, HSBC.

Rajesh Kumar - *HSBC - Analyst*

In terms of your CapEx, could we get a bit of sense on how you're planning to split it between textile, and now rest of the divisions?

Also, within the textile division, what proportion of your CapEx is textile? And what are textile prices doing in your supply chain?

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, hi there. In terms of the total CapEx spend, the amount we spend on textiles is in the region GBP100 million to GBP110 million. Given the level of growth in that business, and the volume growth, I'd expect that number to remain at a similar level going into 2014.

There is an element of the cost of the -- of the work wear business that's related to cotton and cotton prices, but it tends to be relatively small element of the piece. By the time you've designed the garment, procured it, made it, fitted it, sold it, shipped it the garment element tends to be a relatively small part.

In terms of cotton prices themselves, my understanding is actually the futures market has been reasonably favorable in recent months. But in the scheme of things, and compared to, for example, fuel prices and labor costs, that will have a small beneficial effect, but that's potentially outweighed by other cost inflation elsewhere.

I'm not expecting a big inflationary impact from the cotton prices, or deflationary impact. They key challenge for us is to continue to work on the whole supply chain, and drive procurement savings across the board.

But the quick answer is around about GBP100 million to GBP110 million for 2013, and 2014.

Rajesh Kumar - *HSBC - Analyst*

Okay, thank you very much. Just to get a bit more color on what you're saying, where do you actually produce these garments? Are these produced in emerging markets, where currency, and hence the wage cost in the landed textile, is going down?

Overall, I'm just trying to understand how much of it is driven by cost saving, and how much of it is driven by basically the underlying prices falling, in terms of next year's CapEx being guided down?

Jeremy Townsend - *Rentokil Initial plc - CFO*

Yes, the CapEx that we're addressing next year and reducing is really in the area where the non-equipment for rental. It's going to be more around IT investment, and some of the restructuring investment we've had in terms of addressing some of our older plant and machinery in the -- typically, in the textiles and hygiene area, France, Benelux, and Germany. But I don't anticipate the CapEx in relation to garments moving materially in 2014.

And in terms of the reduction in CapEx, that's really in the non-equipment for retail area, rather than the equipment for retail. My guidance would be that the amount we spend on it in 2014 will be broadly in line in 2013, everything else being equal.

Rajesh Kumar - *HSBC - Analyst*

That's very clear. Thank you very much.

Operator

Edward Donohue, One Investments.

Edward Donohue - *One Investments - Analyst*

A few questions, if I may. One, just an understanding of -- you've been with the organization five years now, and, therefore, you've seen all the nooks and crannies.

Bearing in mind that one of your targets is to basically get the organic growth up and running, what do you think really needs to happen to convert what you've got in the organization? And bearing in mind you've basically reengineered the sales force tracking, what's been going on over the last five years, since I've been looking at you guys?

I'm just trying to understand what is going to be different, going forward, so you'll be able to actually drive that organic growth. I appreciate that the external market is really tough, but I'm trying to understand what is in your self control, that you can actually get that top line going.

The other one is just the comment with regard to focus on key accounts. What is the margin profile of key accounts versus the SME in the past? Are we looking at an overall better margin profile, or less?

And the other one a bit more closer, in Continental Europe, on the time horizon. You were talking about Germany and France softening. What actually has happened post summer, because it seems to be the inverse of some comments coming out of other businesses with regard to those two geographies? Thanks.

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Thanks, Edward. I'll take the first two, and Jeremy, perhaps, cover the third. Absolutely right; yes, I have been in the business a little over five years and, therefore, know lots about most of the business, and less about one or two parts.

The areas that we will drive harder, going forward, first off, there's the geographic prioritization of where we can drive better-than-average levels of growth. Some of it will come from focusing in the right parts of the world, and focusing more heavily in the parts of the world that we can get really good growth, and putting our investment there.

So, part of it will be about being more selective. But, I have to say, a lot of it is going to come from some very good old fashioned blocking and tackling in terms of the sales force, and how we get the right level of focus across a very large organization.

I'm beginning to identify six levers for profitable organic revenue growth, and for each of those levers ensuring that all of the sales forces are properly equipped to do the job.

We've made great progress, I think, in some of the marketing and innovation pieces; around the selecting the right markets; selecting the right products and services; targeting the right level to the customers; getting the right propositions. We've made good progress there.

We now need to drive more progress through the right incentives for the sales force; getting better cross-selling; up-selling; density selling; range selling; sales effectiveness; sales efficiency.

So, there's a whole range of good old fashioned blocking and tackling that we just need to up our game across the organization. It's a combination of focus in the right parts of the business, and then real driving the activity levels across the sales force are the two main generic areas, I'd say, in answer to that question, Edward.

On the key --

Edward Donohue - *One Investments - Analyst*

Sorry, if I just come back on that, sorry to interrupt. But if you looked, and it's a terrible definition to say, between the Anglo-Saxon world and non-Anglo-Saxon world, and I'm excluding Asia in that part, where your success has been it's in the Anglo-Saxon world; US, UK. Do you believe that you've actually got the skill set in the sales force in Continental Europe to actually be able to achieve the KPIs that you need?

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Yes, I think we do, Edward. But I do think, and you covered it earlier, I think in Continental Western Europe the market conditions are tough, and, therefore, the sales force are having to work in those difficult conditions.

We have invested in the sales force quite a lot in terms of skills training, and tools, and techniques, and certainly I'm not satisfied. I would never say I'm satisfied. But I don't really see a material difference between the quality of the sales force and the level in sales activity differentiated between Continental Western Europe and the Anglo-Saxon parts of the world. I do think the main difference is the prevailing market conditions that we have at the moment.

Edward Donohue - *One Investments - Analyst*

Okay. And the key accounts?

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Yes, your question on key accounts, typically, you win key accounts at a lower margin than you win SME accounts. That would be typical. It's very difficult to generalize.

But the raison d'etre behind a lot of key accounts is if you can secure a large national contract that contributes to a density across the entire organization. So, that raises the overall level of profitability. But then typically, once you've won a national account the objective is to support those customers over the life of the contract, typically by up-selling further service lines into those customers. Quite often, the average level of margin on national accounts will improve over the life of the contract, and that's the typical intention.

Overall, no doubt that national accounts typically are won at a lower level of margin. But, over time, they do have average up, and they do contribute to the overall profitability of the organization by adding that density, as I say.

Edward Donohue - *One Investments - Analyst*

Okay. And then the next -- the other one was just with regard to France and Germany, the fact that you talk about a softening. Is that softening relative to the first half, or just to put that in some context, if that's possible?

Jeremy Townsend - *Rentokil Initial plc - CFO*

That's right. And it's our experience, clearly. To some extent, it depends on our customers, and the industries, and the sectors we're working with.

I think the softening is, as much as anything, in price pressure as it is in volume growth. That this isn't about necessarily contracts termination, so this isn't necessarily driven by unemployment, or us losing customers. This is more around, as we're renewing contracts, if you think about a cycle, we're renewing contracts that were previously cut three years ago. It's a relative pricing position relative to the price we struck with the customer three years ago, and where the market is versus how it's moved on in the year.

Our experience has been during the year we've come under more price pressure from the contracts that have renewed across -- Benelux, it had been an experience, and particularly in Holland throughout the year.

We've had some softening as well in France and Germany in the third quarter. We've got an automotive exposure in Germany, and some of those contracts have come under pricing pressure in the third quarter.

The other issue in Germany, which is a slightly different issue, just to flag, is in the pest business, in our German business, which is wrapped up in there, it was a particularly wet summer season in the German-speaking areas. I was in Switzerland in July and the pest season hadn't started there, given the relatively cold start to the summer.

So there is an element of, to Andy's point, the jobs that we get associated with some of our contracts, that you tend to get a better margin on those jobbing contracts, and we did have a relatively weak jobbing season.

But the bigger issue is in terms of the pricing of the new contracts, which have softened in France and Germany; in addition to the experience we've been having, particularly in Holland in the first half. It is a third quarter issue relative to the first half.

Edward Donohue - *One Investments - Analyst*

And if you look through the portfolio of contract renewals, have you cycled through a significant portion of those, or is that going to continue through Q4, and Q1, [as well] (multiple speakers)?

Jeremy Townsend - *Rentokil Initial plc - CFO*

The renewal basis is a continued basis. I think the best guidance we can give, which is what we're trying to say in the statement, is that at the moment our core would be, looking into quarter 4, we'd expect a similar set of circumstances.

This is quite -- well, there's an unemployment link, and there's a GDP link. I think we do see a reasonably good correlation over time between GDP performance and the strength of the economy. Clearly, the hope would be that, as you alluded, the GDPs, in both Continental Europe and the UK, improve as we head into 2014.

The feeling I get is while the expectation for GDP performance is out there in terms of improvement, it doesn't feel -- our experience is it's not quite flowing through yet. Clearly, we would benefit from improved GDP performance in Continental Europe, when that comes. But we're not experiencing that just yet, and it doesn't feel like we're going to see it in 2013. Clearly, we're hoping we'll see some of that in 2014.

Edward Donohue - *One Investments - Analyst*

Great. Thank you very much, indeed.

Operator

Hector Forsythe, Oriel.

Hector Forsythe *- Oriel Securities - Analyst*

Three, hopefully quick, questions on clarifications. When you're describing the business, you're using the word core. Can you define that, please?

Jeremy Townsend *- Rentokil Initial plc - CFO*

That's excluding initial facilities, Hector. We're calling our core businesses our core root-based businesses.

Hector Forsythe *- Oriel Securities - Analyst*

Okay, that's fine. One for Andy here. In terms of the structure of the business that he is -- that you're inheriting, can you just confirm that you're happy with that and we're not going to see any material changes? I think that you've probably alluded to that already, but I just want to clarify it.

Andy Ransom *- Rentokil Initial plc - Chief Executive*

Yes, directionally, happy. We've now fully got a regional organization structure, and I have no intention of moving away from a regional organization structure. There'll be a little bit of boundary realignment potentially, which I'll talk about later, but the shape of the organization is going to be run on a regional basis going forward. So, no radical change.

Hector Forsythe *- Oriel Securities - Analyst*

Okay, fine. I assume, therefore, no cost of -- no significant costs, other than your -- that you've outlined already?

Andy Ransom *- Rentokil Initial plc - Chief Executive*

No.

Hector Forsythe *- Oriel Securities - Analyst*

Okay, good. The final one is then on, previously, we've had cost savings of X each year has been outlined. There's currently a -- cost savings is in excess of a GBP40 million target. I note there's no narrative in the statement to that, would you like to pick that one up?

Jeremy Townsend *- Rentokil Initial plc - CFO*

Yes, so guidance on that unchanged for 2013. That GBP40 million, typically, has been driven out of the divisions.

The GBP10 million that we're articulating in terms of the overheads is in the divisional overhead line, the central overhead line that we report separately.

We'll come back, at the prelims, with any guidance on the divisional spend for any cost savings in the divisions for 2014, but I'd just reiterate the guidance we had in terms of the divisional savings for 2013 at this stage.

Hector Forsythe - *Oriel Securities - Analyst*

Okay. I was just wondering if it might drop -- that kind of guidance might just drop away in future.

Jeremy Townsend - *Rentokil Initial plc - CFO*

We'll have a look at that as part of the overall piece for 2014. One of the things I think we might want to get to is more of a net margin guidance, looking at cost inflation, price inflation, and cost savings, and think about that, but we'll come back to that at the prelims.

Hector Forsythe - *Oriel Securities - Analyst*

I think the latter would be more helpful. Thank you.

Operator

At this time, there are no further questions.

Andy Ransom - *Rentokil Initial plc - Chief Executive*

Terrific. Well, thank you very much, everyone, for joining today's call. We look forward to updating you again at the prelims in February. Have a good day.

Operator

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