

FINAL TRANSCRIPT

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GFS.L - Half Year 2011 G4S plc Earnings Conference Call

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PRESENTATION

Nick Buckles - *G4S plc - Group Chief Executive*

Well, good morning, everybody. Welcome to our half-year results announcement. I don't like to change a winning formula, so pretty much the same agenda as we have had for the last seven years. I'll start with the results highlights. Trevor will come on and talk about the financials. I'll come back and do a bit of a review of the businesses and strategy. And then we'll finish with a Q&A session first of all here in the room and then on the phone lines.

So pretty good set of results overall, I would say. Turnover up 5% to nearly GBP3.8b. Organic turnover growth has picked up nicely for the first half, running around 5%, with new markets a key driver there, coming in at about 9%. And actually if you split out Iraq, the loss of that large contract last year, it would be nearer 13%. So getting back to the mid teens that we previously experienced.

Operating profits up 3% and the margin around 6.4%, slightly down on last year, but still a pretty strong performance.

Headline cash looked a little disappointing, but actually it's down to a couple of large contracts with the US government. Trevor will talk more about that, but we certainly expect to be up on that 85% for the year end.

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Earnings per share up higher due to good management of tax, interest, etc. So 8% up, 10% as published. And the interim dividend we've recommended goes up 8% as well. So the 13th half year of earnings growth through what's been quite a troublesome economic period.

I'd now like to pass you back to Trevor to talk about finance.

Trevor Dighton - G4S plc - CFO

Thanks very much, Nick, and good morning, everybody. As usual, this presentation shows the half year compared to 2010 half year at current exchange rates. As Nick has already said, our total turnover for this half was up by over 5% to GBP3.8b and nearly all of this was organic growth. Growth in the Secure Solutions part of the business was 6.5%, which includes about 0.5% from acquisitions. Growth in Cash Solutions was flat as continued low interest rates impacted our customers' need for the efficient circulation of cash and as a result of generally reduced services during the economic downturn.

Looking at the total turnover geographically, new markets continued to show good levels of top-line growth at nearly 11% for the half, including the impact from our acquisitions in Brazil in the middle of last year. Growth in both North America and especially Europe has picked up since 2010 to 3.8% and 2.7% respectively.

Looking in a bit more detail at just organic growth for the half year, new markets continues strongly at 9% in total across both product areas, in spite of the Middle East being flat due to the ending of the Army contract in Iraq late last year. Secure Solutions grew by 6% overall, with 4% growth in both Europe and North America. Cash Solutions organic growth was negative in developed markets and 1% in total. We're still getting 8% organic growth in our new markets Cash Solutions businesses.

The Group margin was down by 0.1% compared to the same period last year, impacted by a 1 percentage point decline in Cash Solutions. This business has implemented some significant cost control initiatives and efficiency improvements to mitigate the effects of negative growth in a product area where fixed costs are relatively high. It's very encouraging to see margins in Secure Solutions slightly up on last year.

Geographically, all three main areas showed a very small margin decrease. This is entirely Cash Solutions driven. You can see from the announcement that Secure Solutions margins were slightly higher in Europe and were maintained in North America and the new markets.

PBITA in the half has increased by GBP6m or 2.6% to GBP239m. Secure Solutions was up GBP16m and Cash Solutions down GBP7m, mainly down to our business reduction in Romania. Nick will explain profit trends later in more detail.

By geography, PBITA growth was flat in developed markets for the first half this year, with the improvement coming from new markets.

The P&L to June in total looks like this. In this slide, the prior year is shown at 2010 exchange rates. PBITA is GBP239m, as we've already seen, and interest of GBP47m is slightly lower than last year, giving profit before tax and amortization of GBP192m, which is GBP4m ahead of the comparative.

Pensions increase is a bookkeeping entry rather than a real cash payment and is GBP1m positive compared to GBP3m negative in 2010. The IASB is changing the way this number is calculated in the near future, but we've always excluded it from any of our key performance measures and will continue to do so.

Tax is GBP30m. And the only new discontinued operation this year is a small one in Russia. Profit after tax is up GBP14m, which is 13%, to GBP118m.



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This tax charge analysis shows that the effective tax rate on the real numbers has reduced again to 22%. This is in accordance with accounting standards based upon the anticipated rate for the full year.

As I indicated at the 2010 year-end announcement, we've made further progress on eliminating fiscal inefficiencies. And in this chart you can see how there's been a gradual improvement in the effective tax rate over the years down to the current level.

This EPS slide shows that there's a relatively small impact from currency exchange rate movements between the first six months of 2010 and 2011. At constant FX rates, we are GBP6m up on PBITA compared to GBP1m ahead at actual FX. Tax pre-amortization is below last year due to the reduction in the effective rate at GBP42m. Non-controlling interests, which is the new name for minorities, are GBP10m.

And the balance sheet's quite similar in many ways to both June and December last year. Goodwill and intangibles totaled GBP2.5b and dominate the balance sheet. The main movements are that net debt has increased by GBP150m since December, with current assets increasing by GBP117m. Overall net assets have increased by GBP26m since the year end.

Operating cash flow. This is slightly below our target but there is a very simple explanation. There are two US government contracts that -- they both have overdue balances combined of GBP45m, the largest being the Kabul Embassy contract. If these contracts had paid on time, our half-year cash flow would have been the best for years, at 80%. Remember our target is 75% at the half year and 85% for the full year. The log jam has now been cleared with these contracts. Remember, we operate through a foreign ownership structure and are a little restricted on direct access to the US government, and the money has started to flow through. We are confident that the full-year 85% target will be met.

For the other elements of cash flow, CapEx was GBP53m for the half year, which is below last year's GBP70m and represents only 72% of depreciation. This is a result of continued tight control, although there is also a timing element here and we would expect the full-year CapEx to approximate the depreciation charge, as it did in 2010.

The statutory definition of operating cash flow is different and the reconciliation to our management definition is shown in this slide. Capital expenditure is excluded and tax paid included. Tax paid of GBP42m in the half was a little above 2010. Also included in the statutory definition of operating cash flow are discontinued items and additional deficit reduction pension payments, which were GBP19m in the half year.

Here is the rest of the cash flow. We take off interest of GBP64m, which is higher than the P&L charge at the half year because of the timing of interest payments on public bonds. CapEx spend, as we saw before, was GBP53m, and dividends GBP66m. Net acquisition cash spend was GBP57m.

Our main acquisitions in the half year were Cotswold and Guidance, adding to our Security Solutions capability in the UK, and MCH, adding to our Cash Solutions capability in the Netherlands. The spend shown here includes the recognition of deferred consideration, so it's slightly different from what is included in the cash paid shown in the previous slide. We also paid GBP13m in the period in deferred consideration in respect of Fidelity, the Cash Solutions acquisition that we made in South Africa in 2007.

There's been no significant change to the financing slide since the Capital Markets Day, which shows the maturity of our financing arrangements, with no major repayments until 2016. Our headroom at the half year was GBP341m.

On pensions there have been some ups and downs, but the net pension position at June has hardly changed since December, with a post-tax deficit on the IAS 19 calculation of GBP184m. On July 5 we closed the UK scheme to future accruals in order to limit the Group's exposure to possible future growth in pension liabilities. It doesn't impact the deficit calculation, but it does reduce volatility in the future a little.



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On dividends, we have a policy of increasing dividends broadly in line with earnings, as you know. And as you've seen, EPS increased by 8% for the half year. And we're declaring an interim dividend of 3.42p per share, in line with the EPS growth as further confirmation of the confidence that we have in the future. This continues the dividend growth trend. Remember we have a 19% average annual dividend growth since 2004.

Okay. So Nick will now take you through the business review.

Nick Buckles - G4S plc - Group Chief Executive

Thanks very much, Trev. So first of all, looking at Secure Solutions, and, as Trevor mentioned, I would say it was a very strong performance in the first half. And remember the organic growth was around 6% and we saw a slight increase in the margin, which I think is a great trend to have, really driven by a particularly strong performance from the UK business, but overall good performances all round in terms of profitability and growth.

Looking more specifically at different countries within Secure Solutions, you can see there the UK and Ireland -- the UK and Ireland margin pushing up three-tenths. That's really down to the fact that Ireland was very poor the first half of last year, if you remember. Had to make some major restructuring. But also the Care and Justice business in the UK has got some very strong margin improvements coming through.

In terms of growth, as we can see there, some great growth from Utility Services, around 20% organic growth there. Integrated Services, which is our government FM business, grew about 16%. And the UK commercial business, driven by this DWP extension, grew about 10% as well. So some very good performances there all round in the UK.

I would say the UK outsourcing trends on UK government, they do change week by week, month by month. We do keep the market abreast of where we see those changes, but I would say we're probably most positive now than we've been about UK government opportunities. Clearly there's a program now for prison market testing. We'll be starting two contracts in the next few months; we're bidding on another eight. We think there will be further work coming out of probation, police custody suites definitely looking to outsource. In fact we've been shortlisted down to two for the whole back office support for the Lincolnshire Police on facilities management, which is a great outcome.

Welfare to Work program being extended to workless families. And the whole management of asylum seekers in terms of transportation and accommodation, we've been shortlisted on that too. So I think it's a very, very healthy pipeline indeed. And the contracts we've won will more than offset the loss of the Court Services contracts, which finishes next weekend.

But of course, Ireland better than last year but still very tough. But overall, as you saw there, the UK and Ireland results, very good.

This moves us on to Continental Europe. Good performance, good pick-up in organic growth, really driven by some good wins in Belgium, but also other countries too. We have focused hard on controlling costs, particularly overhead costs. But in terms of pay reviews it's only Norway really where we've had a significant increase of around 4%. The rest have been in the 2% to 2.5% mark and we've had no issues passing those through to customers.

Systems market still quite tough. Places like Greece, lesser extent Denmark, but also Hungary, still tough in terms of systems, but obviously baked into these numbers.

And Eastern Europe overall has certainly made a recovery. Still slightly negative in terms of growth, but certainly significantly better than this time last year. And also good turnaround in Sweden. A loss-making business first half of last year and showing about a 3% or 4% profitability this year.

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And the final slide there really, Belgium, great growth. Norway, strong growth, close to double digits and a very good performance in Israel. So very pleased overall with the Continental Europe business, really back on the map there, I would say.

Moving on to North America, similar picture, accelerating organic growth. We've got about 8% growth in the commercial sector in the US. It's around 4% on manned security, so it's been strongly driven by systems business, strong double-digit growth there. Nuclear up for the first time for a number of years, around 8%. And also compliance and investigations business up around 20%. So very strong growth there in commercial.

In terms of US government, we had a major reduction last year for a base services contract in Washington. We had a pretty poor view of where we thought the growth was going to be in the US government this year, but certainly the first half has been a lot better than expected. It's slightly negative, but I think our view is that we should be positive by the end of the year for the US domestic business, if you strip out Afghanistan and Iraq. So pretty good performance.

And then in terms of international accounts, starting to get some real traction there, with extensions to the contract with Hewlett Packard, Shell, BP and Agilent.

Moving on to Canada, good performance. Around 6% or 7% growth. But the big win there was CATSA; we won one of the four regions. The aviation contract, that's going to be about GBP50m a year. That'll put Canada's organic growth up 30%-plus and hopefully add around 2% or 3% organic growth points to North America next year.

Moving on to new markets, always a strong performer, but some great performances. India, 20%-plus organic growth. Kazakhstan, over 20%. Really come strong this year, Kazakhstan. And Malaysia, around 25%.

Moving into the Middle East, Qatar was our business of the year last year and over the last couple of years in terms of growth and margin. That continues to grow strongly. And with the re-let contract in Kabul, Afghanistan is showing very strong growth too, despite the UK part of that contracting.

In Iraq we signed a big contract with BP, the first of many oil contracts we expect to win in the Southern oilfields. And also in aviation, good progress, where UAE we're going to have a GBP6m or GBP7m contract there on the airport and also Qatar.

And then finally really another good example of strategy delivery, we're the preferred bidder on a PPP contract, FM in Alexandria in Egypt. So another good example too.

Moving on to other regions in new markets. South Africa continues to be disappointing. Minus 7% organic growth there, driven a little bit by systems but also manned security. But certainly the last couple of months in the half we've seen positive organic growth, which is the first time for a couple of years. So that's a good story going forward. And the margin has been much stronger there. Morocco, our star performer, with organic growth over 20%.

Latin America there, as expected, we thought it'd be around 15% growth. That's come in at 18%. So a great performance driven by Argentina, Colombia and Brazil, all of which were above 20%. And this is also an area which I'll come back to where we expect decent M&A activity in the near future.

Moving on to Cash Solutions, overall, as Trevor mentioned, we have got positive organic growth, which is strong, better, and certainly the second quarter we had about 2% organic growth overall, driven by a double-digit growth in new markets.

The margin has slipped, as we said it would at the IMS. And that's really a mixture of Romania coming down significantly from the loss of the contract there. And it is a network business. We had worked very hard on mitigating the lack of growth in developed markets in terms of network reductions, so -- but there has been a bit of an impact there.

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And finally, on the robberies side, really a tale of two sort of different stories there, one in developed markets that have been very good and very well controlled through new technology, but in developing markets, particularly Saudi, we've had a number of robberies, so that's where the margin has affected a little bit there.

Going into a little bit more detail, Belgium, as you know, we've taken over a large chunk of Brink's work as they exit the market. That's now been fully implemented by about June, delivering about 25% plus organic growth. I mentioned Romania. We're still hoping to restart some, but that's probably getting less likely. But we have downsized the cost base significantly there so we are running profitably, but obviously not to the level we had done previously.

UK organic growth still negative around minus 4%, really driven by the loss or the restructure, sorry, of the HBOS contract last year. But profit effect mitigated by good cost control. The G4Si, our international valuables business, 15%-plus organic growth, certainly helped by the recovery or the increase in the gold market, where we're shifting bullion around the world.

I think the positive point is that we are now back in conversations with a number of banks around outsourcing. I think their focus is back on cost reduction, what's their core business and what isn't. If you went back three to six months, there weren't any conversations going on, but now there are. So we do see opportunities coming back in terms of cash center outsourcing.

North America is just Canada, slightly disappointing there. The margin down to zero. We lost a chunk of BMO contract back end of last year. That's impacted the organic growth and has flowed through to the bottom line. But the competitive environment is okay. We haven't got any major rebids on the FIs due in the next couple of years, so we hope to rebuild those margins over the next six months or so.

CASH360 is going very well there. We've got a number of bids outstanding. And that we see as a means to get into the commercial market in Canada, where we're pretty light. We're mainly FI-based. But it's a good pipeline on CASH360.

New markets cash, as I mentioned, getting up to double-digit growth now in terms of the second quarter. Highlights, Hong Kong, 20% growth. Thailand, Malaysia, Morocco, Colombia, all these double-digit growth businesses, so that's good. Not so -- obviously not affected by interest rate reductions in these markets so we're starting to see some strong growth coming through. And, as I mentioned, still some robbery situations developed in places like South Africa and Saudi Arabia. And obviously they don't have to change a lot in new markets for them to have an impact on the margin.

Let's move on to the strategy itself in terms of delivery. As Trevor mentioned, not a big first half in terms of acquisitions; only a GBP42m spend. But we do still expect to spend GBP200m in any 12-month period. It depends how the deals fall in the second half, but we would still expect probably to spend that this year, but it might fall a little bit into next year.

The pipeline's good. We're looking at businesses in Brazil, Ecuador, Thailand, Malaysia, Korea and India, to name main countries we're looking at, but also, of course, any capability-building acquisitions we can make, particularly in the UK and Europe with our strong market positions there. And the focus pretty much the same, capability building in developed and really adding scale, potentially FM, in selected developing markets.

Same sort of return on investment criteria, still very confident we can hit those targets, and continue to evaluate larger deals, which we have done for the last few years or so.

And if you remember this slide from Capital Markets Day, where we see the industry trends, they haven't changed at all in the last few months. They're still very much where we believe the markets are going. And I'll come on and give you an example -- some examples of where we've seen that happen. So we certainly think industry will continue to consolidate on the market side. We still very much have the ambition and expectation that new markets is going to be a much larger part of our business in the future. Regulation is driving change, and government outsourcing is definitely picking up; there's no doubt about that.



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Facilities Management is taking hold in some markets. There is still the need and will continue to be the need to look at the customers' cost base in terms of the current economic environment. And we're getting very good at helping them to mitigate cost. And international contracts are definitely increasing.

On the product service side, definitely innovation and technology is important, and I've got some examples of that. Risk management is key, and more so particularly on international accounts but also in terms of getting our margins improved. Global consistency is important. So let's just have a little look at how we're doing there.

In terms of consolidation, we've seen some elements of it. Certainly Securitas' attempt to acquire Niscayah, which looks like that might not happen. But certainly in our own expectation we expect to continue to consolidate the market, particularly in developing markets, and expect to spend at least GBP200m a year, and the pipeline is good.

In terms of new markets, 36% of profits already, 30% roughly of revenues. Some acquisition focus there, as I mentioned; a number of countries that we're looking at. And organic growth ex-Iraq back up to 13%-plus. And that's where we see the future going in terms of organic growth.

Some great wins in the ports, maritime and aviation sector. That's very much driven by regulation, and that's good for the industry; drives up standards and gives the global players a bigger opportunity to win, CATSA being a good example of that.

And as I've said a couple of times, the government outsourcing pipeline looking good. We think there's going to be a formal program of prison to private sector over the next couple of years. The eight prisons are obviously in process. I mentioned we're shortlisted for Lincolnshire Police. That's the first of a number of police forces we're looking to outsource back offices. We're delighted to be down to the last two on that. We've submitted a bit for Wiri, long-term PFI in New Zealand, 25-year contract. I mentioned Egypt.

And in terms of the EM pilots, with the acquisition of GML we have a very active pilot and rollout running in Saudi Arabia. Brazil certainly on the cards in terms of opportunity, Portugal, UAE and Cyprus. So definitely EM, which we see as the route into the care and justice market in a number of countries, is definitely picking up. And with, as I mentioned, the acquisition of GML, a lot more capability to win in overseas territories.

In terms of Facilities Management, certainly strong performance in the UK. That's probably the most developed in terms of FM and we're playing a major role in that. As I mentioned, the government business grew about 16% in the UK. And also in Saudi Arabia, double-digit growth there. But a number of other new markets where we think there's a good opportunity for us to play in the FM space.

Lots of examples of reengineering customer requirements to win business. And then in terms of international contracts, just to reiterate the point that we are getting growth from those international accounts. Having global coverage and global consistency is definitely a differentiator in that market.

Then in terms of innovation, certainly our technology helped us win the work program in the UK. Our in-house access control or integrated systems product Symmetry is certainly helping us win business in the US, commercial and US government. And you've seen and hear us talk about secure tracks and incident management for major companies that's definitely won us a number of major accounts in the US. And that continues to be developed in terms of global roll out.

In terms of Risk Management and Consultancy ports is definitely a growth area. The BP contract in Iraq I mentioned that's about GBP20m a year in terms of oil and gas. And of course, we are going to get much more involved in terms of Risk Management and Consulting in the whole Olympics contract as it ramps up over the next six months, definitely having consultancy capability will help us with that.



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And then, finally, global consistency CATSA a really good example of a multi-country G4S bidding team, working under the direction of a central team to win that contract. And more and more demand from customers for global consistency, and we are going to change our structure to make sure we can deliver a little bit more consistency on a global basis.

So, in summary, good improvement in growth organically across all regions and products, very good to see after a tough year last year when we were still positive, as you know, 2% growth but picking up to 5% is a good outcome and we certainly expect that to continue for the rest of the year.

New markets picking up nicely, still our objective to get to 50% of our group in new markets by 2018. Bidding looking good, healthy pipeline which I've mentioned. And a very exciting and strong M&A pipeline, and we could pick up that GBP200m over the next couple of years if the opportunities, as we see them, come to fruition.

And overall very confident in our outlook, reflected in our 8% dividend increase which as Trevor mentioned is the seventh or eighth year running we've increased our dividend.

So now I'm happy to take any questions firstly from the floor and then from the phone lines. I'll just sit down if you don't mind. One at the front here please, Rob.

QUESTIONS AND ANSWERS

Robert Plant - *JP Morgan - Analyst*

Rob Plant from JP Morgan, the GBP45m drove the outflow relating to the US contracts. It's quite a large figure. Can you split it between Kabul contract and tell us what the other contract was? And do you think you'll be able to get it all back by year end? Thank you.

Trevor Dighton - *G4S plc - CFO*

It's mainly the Kabul Embassy contract. About 90% of it is the Kabul Embassy contract. That really was just a bureaucratic wrangle. You know the story with the Kabul Embassy we -- it was a poor contract that we inherited from the Armor Group acquisition, and we were supposed to exit it at the end of last year.

And the US government got into a bit of a pickle about who was going to take it on, and then eventually asked us to take it on again. We said, yes, we will but only if it's a decent contract. So we extended it for the whole year, but it's taken us quite a few months to go through their bureaucracy to work out exactly how the billing was going to work and the contract was going to work.

And because it's a [foci] structure as well we couldn't really get heavily involved from here. So it's taken several months, as I say, just to get how the billing was going to work, nailed down with the US government. It's a great contract, now we are making decent money out of it, but it's taken us a little bit of time to get there.

Robert Plant - *JP Morgan - Analyst*

It still seems quite big for contract size --

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Trevor Dighton - G4S plc - CFO

It's the whole six months, it's the whole six months.

Nick Buckles - G4S plc - Group Chief Executive

I think I mentioned the organic growth in Afghanistan even though the UK part has dropped quite rapidly, that contract is around GBP70m GBP80m a year now, the US Afghanistan contract.

Trevor Dighton - G4S plc - CFO

So we couldn't effectively bill for that six months. We were perfectly relaxed about it because we knew that it was just going through the process, but it just took a bit of time to nail down.

And since then it has been put in place, the process has been put in place and the invoices are flying out to the US government, and the money has started to flow back in. We've had the first chunk of that money in now. So we really are completely convinced and happy that it will come in by the end of the year.

And the other one is a similar sort of story on the -- another contract, but that's only a small element of the total.

Nick Buckles - G4S plc - Group Chief Executive

At the front.

Kean Marden - RBS - Analyst

Morning guys, it's Kean Marden from RBS. Could you give us a little more background on sort of the evolution of the UK custody suites, because it feels as if your -- you've become a little bit more optimistic on basically how the bid profile is starting to emerge in that area.

Nick Buckles - G4S plc - Group Chief Executive

The police forces generally, as you know, are under significant, really significant budget pressure in terms of cost reduction, very real and very significant. And becoming much more open minded around the role the private sector can play in helping them through that cost reduction process. And it really depends on the appetite of the police forces to how much they're looking to outsource. But certainly on the Lincolnshire bid it's a fairly substantial part of process and infrastructure that we are bidding on.

And what we expect is that they're really the lead force of about seven or eight, and if we win that contract we think there is an active pipeline that will follow thereafter in that whole sort of process.

And that's really the whole of back offices. Then alongside that there's a couple of other police forces where we are bidding to actually build and run new police custody suites by consolidation of existing facilities. So the whole police area we see a lot more growth opportunity and real growth opportunity.

But also other areas of government, as I mentioned, the whole -- the contract called Compass which is running the program for managing the people that run the transportation and accommodation for asylum seekers, big contract that we expect to win a part of, so good news all round I would say.

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Kean Marden - RBS - Analyst

You mentioned over the last sort of three to six months there was potentially the opportunity for a bit of a pause in the UK revenue growth in Q3. Obviously you had the phasing of sort of contracts coming out. So it looks as if the prisoner escorting contracts are going to get handed over at the end of August. Is there anything there, i.e. London riots or maybe that would potentially plug that gap for you or are you still looking for a bit of dip in momentum in Q3?

Nick Buckles - G4S plc - Group Chief Executive

I think if one examines that in a little more detail in thinking it through it's probably not going to be a huge impact in Q3 because it's only one month. So I'd imagine with the new work we've coming on in Q4, buildup for Olympics, that hopefully it will be smoothed out. I don't think we'll have a massive dip, but I think it will be a bit slower in the third and fourth quarter because of the court services contract.

But going into the new year in the UK with all the startups we've got still pretty positive by the end of the first quarter next year. It really depends how they pan out. But the Olympics contract clearly is going to start building up as well.

Kean Marden - RBS - Analyst

And then final quick one, should we put anything for Romania this year at all?

Nick Buckles - G4S plc - Group Chief Executive

I wouldn't. Second row, we'll work backwards.

David Brockton - Espirito Santo - Analyst

Morning, it's David Brockton from Espirito Santo. Could I ask just a question around the cash solutions business, you talked about the efficiencies and the cost you've taken out of that business? Would you be able to flesh that out a bit more maybe quantify the extent of cost and give us a feel for I guess scope for further margin erosion within that business?

Nick Buckles - G4S plc - Group Chief Executive

As I mentioned, it's quite a few moving parts in there. In terms of in developed markets, yes, we haven't had a lot of growth and we've had to take cost out because of revenue reductions, say for the UK, a good example, but robberies have come down. And that's probably a permanent, hopefully, should never say that, a permanent reduction in robberies.

But in terms of the cost base itself you can't sort of point to the fact that we've closed 10 branches or laid off 300 people. It's very much just tailoring the cost base according to the revenue, which you have to do actively because it's clearly a fixed cost type of business.

But I don't think -- it's not possible to say in these countries we've done X, Y and Z and that's the ongoing impact. What I would say is where the margin has come down by 1% overall don't expect it to come down anymore. And as the revenue starts to come through and pick up, I expect the margin over time and it won't be an overnight return, but there is no reason why the margins won't return in Cash Solutions once the growth comes back.



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So we've worked at reducing the cost base overall where the countries have got revenue reductions to make sure we haven't lost profitability and margin. But no overall program basically.

David Brockton - *Espirito Santo - Analyst*

Thanks.

Mike Allen - *Panmure Gordon - Analyst*

A quick one from Mike Allen from Panmure Gordon. Just on the acquisition strategy, I guess if you look at what you've paid for deals in the past with some of the bolt-ons you may pay 7 to 8 times EBIT and a bit more for the strategic acquisitions. Are those valuation multiples likely to remain the same over the next 12, 18 months or has there been an increase or decrease in what you expect to pay for acquisitions?

Nick Buckles - *G4S plc - Group Chief Executive*

It depends on the business clearly and the country, but I would say the majority cases in developing markets the multiples are still very much at that level and sometimes lower, depending on the sophistication of the market itself.

But as I've mentioned before in some of the more sort of admired markets I would say like India, maybe Thailand, maybe Brazil the sort of desirability of assets is high, and so the multiples could get into sort of 10 to 12 times on occasions in those markets.

But really off the back of the fact the reason they're highly valued is they are growing at 20% plus. So you've got to look at the overall returns within the three-year period, and they still look very good.

Mike Allen - *Panmure Gordon - Analyst*

And just on the organic growth for Cash Systems as well, I think you flagged that Q2 organic growth rate was about 2%. Do you think that the organic growth has troughed now at these levels or do you see further scope for acceleration or likely to remain 1% or 2%?

Nick Buckles - *G4S plc - Group Chief Executive*

I pretty much -- I certainly expect it to pick up in the second half. We have got one issue in the UK where we've got a major contract coming out towards the end of the year, but we do expect to replace that with new business. But that's the only caveat I'd have on that. Apart from that the underlying growth will definitely improve throughout the second half.

Mike Allen - *Panmure Gordon - Analyst*

Just a final one from me in terms of indexation in both parts of the business, does it account for about 50% of the organic growth in each case or do the dynamics differ slightly in each business?

Nick Buckles - *G4S plc - Group Chief Executive*

I'd think it was at least 50%, 50% to 60% on average I would say at the moment.

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Mike Allen - Panmure Gordon - Analyst

That's great, thanks.

Nick Buckles - G4S plc - Group Chief Executive

Do you want to move back a row.

Jaime Brandwood - UBS - Analyst

Morning, Jaime Brandwood from UBS. Just if I can start by asking I think, Nick, you mentioned that excluding Iraq the emerging market or new markets growth was 13%. That's including the cash business is it, that's the whole of the emerging markets?

Nick Buckles - G4S plc - Group Chief Executive

Yes

Jaime Brandwood - UBS - Analyst

And so looking at just Iraq can you quantify for us exactly what the revenue was in the first half versus first half last year, and what some of the major moving parts there in terms of the downsizing of the UK-related business.

Nick Buckles - G4S plc - Group Chief Executive

Well, if you do the math you can probably work it out because it's the sum of the difference between 9% and 13% on new markets revenue. So I -- it must be the equivalent of (multiple speakers).

Jaime Brandwood - UBS - Analyst

How small is Iraq now I guess?

Nick Buckles - G4S plc - Group Chief Executive

It's the loss of the one contract I'm talking about particularly. Iraq is running at about -- I need to put my glasses on, yes, it's down to only GBP20m in all.

Jaime Brandwood - UBS - Analyst

GBP20m okay. And then just looking at the comment you made there about the contract loss in the UK Cash Handling, you are referring to the contract you lost to Loomis I guess?

Nick Buckles - G4S plc - Group Chief Executive

Correct.

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Jaime Brandwood - UBS - Analyst

Right. And how are you feeling generally? I think you've been trying to push through fairly significant price increases in UK Cash Handling this year, 4% or 5% to cover the wage increases. How are you feeling generally about market share in that market? Is Loomis mounting something of a comeback, or are you feeling fairly relaxed?

Nick Buckles - G4S plc - Group Chief Executive

I would say that I've said over the years that we've had a very strong market position in the UK, and Loomis have been pretty weak. I would say in the last 12 months they've got their act together and they are a reasonable alternative now operationally, clearly not as good as us, but a reasonable alternative.

And so before I don't think there was a lot of chance that for a bank or a financial institution they'd move their business very easily. I think there is a probability now, but certainly I would say we are significantly stronger.

But there is not really a massive pricing issue. The pricing hasn't been good in the UK for five years basically I would say. I mean looking at pricing a retail service is probably the same price as it was when I ran the company 16 years ago. Clearly there's been massive changes in operational structure down from three man, two man, one man crews.

So it's not been a buoyant pricing environment for five years, and I think my view is it certainly needs to be a more buoyant pricing environment in the future, and it's something we need to look at.

Jaime Brandwood - UBS - Analyst

Have you concluded that posture in terms of that sort of 5% wage --?

Nick Buckles - G4S plc - Group Chief Executive

Yes.

Jaime Brandwood - UBS - Analyst

You have okay. And then just quickly on the indexation point again, just the strong growth that you had in both Asia and LatAm Secure Solutions how much of that was wage related, wage inflation related?

Nick Buckles - G4S plc - Group Chief Executive

Latin America is probably of the sort of 17%, 18% probably more than 10% definitely, Argentina is a massively inflationary environment so it's -- I wouldn't know exactly the number but it's certainly more than 50% of the increase.

Jaime Brandwood - UBS - Analyst

And Asia meaningful there or what?

Nick Buckles - G4S plc - Group Chief Executive

Less than half I would say there.

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Jaime Brandwood - UBS - Analyst

Okay. Very lastly can you tell us who else is down to the last two with you on Lincolnshire?

Nick Buckles - G4S plc - Group Chief Executive

Reliance.

Jaime Brandwood - UBS - Analyst

Reliance, thanks.

Nick Buckles - G4S plc - Group Chief Executive

Next row -- sorry on this one, Julian in the middle here. Come from this side.

Julian Cater - Collins Stewart - Analyst

Morning, it's Julian Cater from Collins Stewart. Two related questions please. There is clearly a lot of opportunity in the UK government space, but can you talk a bit more about the competitive environment and particularly the apparent desire of the government to introduce new competition into a number of the sectors?

And the second question is in relation to the eight prisons that you said you were bidding for what would you regard as a par score in terms of number of wins in that space?

Nick Buckles - G4S plc - Group Chief Executive

We've talked about the government outsourcing and competitive environment before, and our view is much the same that, yes, the government got a declared intention to introduce new players, but they've obviously got to be new players with credentials and a sound balance sheet and size and scale. So I think when they talk about making the market a much easier place to do business they are trying to introduce smaller players, but I think that's going to be very difficult for them just because of the expertise and sometimes investment required.

But clearly the example of Court Services moving over to a new player it's a week or so away, I'd rather talk about that once we see what the outcome is in terms of the operational delivery. My view would be they've saved enough money through the tendering process not to have to switch suppliers, and I think that's a lesson that they'll look at in the future. But I don't know where they are going to be at the moment on that.

I think it depends on the department, some of the departments are not awarding on price and some are. And as I've said before if it's a second or third generation I think the view is that it's easier to switch, but I think we'll see how that works in the future. I know that there has been huge operational issues on the transfer of the D&E contract that we lost in May. So, we'll wait and see what happens on that.

And the second point, that's a very good question. I would hope I would expect that we should win 25%. That's not an unreasonable expectation. If we don't, we don't. But I think that would be the minimum we should set out stall out for. And if anyone from our business is listening on the call they know their target now don't they?



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Julian Cater - Collins Stewart - Analyst

Great, thank you.

Paul Checketts - Barclays Capital - Analyst

Hi, it's Paul Checketts from Barclays Capital. It's -- your language on the outsourcing of cash services to central banks and commercial banks has interestingly warmed up quite a lot. Can you remind us of the potential in that market please?

Nick Buckles - G4S plc - Group Chief Executive

Yes, it's -- if you think of the UK scenario which really is the most developed outsourcing market on all services, but particularly on cash as well, and the numbers aren't going to be precise but just to give you an idea.

We believe that ATM and cash center outsourcing doubles the size of a market basically from the pure transportation perspective. So the UK -- if you look at the UK cash solutions market relative to GDP, relative to population its two or three times bigger than most other markets on a proportional basis. And the UK is the only market really, maybe Spain that's gone through that evolution. So on cash solutions alone most markets can double in size if we get into cash center and ATM outsourcing.

In terms of pure numbers the UK cash outsourcing business that we run is about GBP70m or GBP80m. The opportunity that's still in-house is probably a similar number. And the amount of businesses with a competitor which is owned by the banks is probably a similar number as well. So you are probably talking in our market about GBP300m odd for cash center outsourcing. And that hasn't really evolved in any of the other countries. So I'd say typically the cash outsourcing -- cash center outsourcing and ATM management is at least as big as the traditional market.

That's why we've always been very bullish about cash solutions growth in the longer term. When people talk about reduction in money supply, etc., etc., it really isn't the issue; the issue is how quickly we can convince banks through regulation, through central bank intervention to outsource cash centers basically.

Paul Checketts - Barclays Capital - Analyst

And on the central bank side.

Nick Buckles - G4S plc - Group Chief Executive

Clearly the UK have made that decision a number of years ago. The Dutch central bank are going through a similar process, but I think that looks like the banks are probably going to take on the outsourcing role there themselves.

So there's various stages of evolution. We can get a sort of full report done on that if required. But we know we have this small consulting company we own called SMI which consults with central banks on how they manage cash. So clearly their objective is to persuade as many as possible that moving into the hands of the operator is the best thing to do.

Paul Checketts - Barclays Capital - Analyst

And lastly if I can on the PPP contract in Alexandria is there any security components involved, and would we know some of the other bidders that were involved?

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Nick Buckles - G4S plc - Group Chief Executive

Yes. I think we got to preferred bidder fairly quickly. It comes down to where our key differentiator is that we've got a global network with very good relationships with regulators and governments. So, once the decision is made to look at using the private sector we are in a very strong position. I think clearly if we can put people in front of those customers that have done it in the developed market it's a much easier decision for them to make. So it wasn't a huge process, so I think we went to preferred bidder pretty quickly.

The security element is probably 10% to 15%. But as I say in developing markets facilities management or even bundled services is definitely a key market trend.

Paul Checketts - Barclays Capital - Analyst

Thanks.

Nick Buckles - G4S plc - Group Chief Executive

One in the middle here.

Andrew Ripper - Bank of America Merrill Lynch - Analyst

Hi there, it's Andrew Ripper from Merrill Lynch, a couple of questions. First of all, I wonder if you could make some comment in terms of gross margin trends for the secure solutions maybe for the major businesses, North America, UK, Benelux, are they stable up or down?

And in terms of new business coming through the larger contracts like CATSA, Olympics, maybe European Commission, thinking about Benelux, are the returns on those contracts sort of equivalent to the returns you're generating on the existing book of business please?

Nick Buckles - G4S plc - Group Chief Executive

Yes. I think throughout our organization the debate around gross and net margin goes on in every trading review basically. And if you look at it as a large contract making contribution to central costs that's one way of looking at gross margin, or if you look at the site-based contribution for a smaller contract that contributes to the sort of network overhead costs you've got in a business that's another view of gross margin.

So, it's a difficult question to answer. Gross margins have been coming down for many years. They typically were above 20% now their nearer 13% to 14% in a number of businesses. But that's partially due to the fact that contracts are larger and site-based contracts have got their own overheads so you don't need to make the same gross margins basically.

So if you looked at the gross margin of our Care and Justice business for example that would probably be lower than our Secure Solutions, but the net profit is higher. And it just does depend on the structure of the contracts and the overheads that you've got.

So the short answer is I'm sure the gross margin is coming down, but it's because we are winning large contracts with their own overheads which just have to contribute to central costs.



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So if you take, CATSA is a prime example, it's multiple airports all with their own infrastructure, and it will contribute around 7% or 8% to head office costs which are 1% or 2%. It's that sort of level of contribution, but the gross margin, if you went down to who is actually running the scanners is probably 20% for example. But -- so you really need to look at the net margin trend, and the good news for us is it went up for the first time for a little while which was great.

Andrew Ripper - Bank of America Merrill Lynch - Analyst

Okay. And then the second question can you sort of talk -- give us a bit more color on the Olympics contract in terms of how it's going to ramp up? And maybe just thinking about the billing next year will you get a sort of a big chunk of revenue in Q3?

And also operationally obviously it's quite challenging in terms of the numbers of people you've got to go out and hire, you've got to go out and do that first before you sort of get paid. What sort of returns profile can we look at on the contract please?

Nick Buckles - G4S plc - Group Chief Executive

We are right in -- still in process in terms of negotiating how the contract will ramp up and staffing requirements. It's very difficult to answer that question. I'd probably be in a much better position to do that a bit later in the year.

I'm not trying to be difficult; I think it's just a very difficult question to answer because it depends on how big our role becomes ultimately. And clearly we've got to make sure that we get paid in line when we incur our costs. So it's a bit of an open area at the moment, but not one we are concerned about. There's big opportunity, but haven't really go the answer to that.

Andrew Ripper - Bank of America Merrill Lynch - Analyst

What are you expecting to bill in relation to the Olympics in the second half of this year?

Nick Buckles - G4S plc - Group Chief Executive

Same answer.

Andrew Ripper - Bank of America Merrill Lynch - Analyst

I'll come back and ask that one next year. Thanks very much.

David Hancock - Morgan Stanley - Analyst

Thanks. Morning, it's David Hancock from Morgan Stanley, just one please on the international justice opportunities, so you've talked in the statement about some of the electronic monitoring contracts coming up. Can you just talk about the scale of opportunities in that area around things like prisons internationally as well please?

Nick Buckles - G4S plc - Group Chief Executive

Yes. To be fair in terms of revenue and profits the EM opportunity doesn't really hit the scale from a group perspective. Certainly when you start them up in the pilots, they're mainly product supply and some monitoring.

Our ambition in all those pilots is to get into a full service model and the UK contract is about GBP50m a year. But they would probably start off as only a couple of million pounds a year in terms of product supply, GBP2m to GBP5m that sort of level.

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But that -- the reason we are excited about it A, they will become a full service model potentially. The profitability is very strong. And they are the entry model to actually get into a care and justice discussion with those various governments to prove the private sector can operate effectively. So strategically very important, the GML acquisition was very important to that strategy. As I say it leads to longer term care and justice.

In terms of the major prisons it's really back to the ones we've highlighted before. Wiri in New Zealand we've put the bid in for that. We are still waiting to progress on the four prison bids we've put in, in South Africa. There has been some opportunities in Peru which we are looking at, but they are the main ones at the moment.

Any more questions from the floor? Okay, we've got one question on the phone line if we could have that please.

Operator

Yes of course. Our question comes from the line of Laurent Brunelle of BNP Paribas in Paris. Please go ahead with your question, your line is now open.

Laurent Brunelle - *Exane BNP Paribas - Analyst*

Yes, good morning. I've got three questions if I may. First can you maybe give more color in terms of margin evolution for H2? Do you expect the 20 bps decline in H1 to reverse given, let's say, a more favorable mix effect?

Second can you give us your view on your ability to pass on wage costs to clients, especially in Europe and especially regarding what Securitas said recently?

And lastly, can you maybe split your 5% organic growth in H1 between volume and price. Thanks.

Nick Buckles - *G4S plc - Group Chief Executive*

Sure. Working backwards, yes, the 5% roughly is 50/50 between volume and price we think. It's very difficult to do a weighted average of cost in multiple countries, but that would feel about right.

Wage awards I mentioned on the call earlier that there have been wage awards in Europe typically around 2%, 2.5% but we've managed to pass them through without a big issue in most of those countries. We -- fortunately, we are not in France and Germany strategically [exit] to those countries which have been problematic. Spain clearly is not a market for us, which again is problematic.

And in Sweden, which I think has been an issue we are on a recovery story there. As I mentioned we are into profitability from a loss making situation, good management team in place and growing pretty well. But that's really coming from quite a poor position so no issues there to speak of.

The first question basically what we've been saying is we are confident for the estimates for this year. We don't expect them to go up. We don't expect them to go down. It's really up to the market to decide.

But certainly we -- the growth is picking up, but we wouldn't expect the margin to stay at the same level as last year which is what we've pretty much said with a 1% decline in Cash Solutions that will have an impact on the overall group margin. Where it ends up will be down to the growth, the mix and the actions we take in the second half.

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Laurent Brunelle - *Exane BNP Paribas - Analyst*

Okay. And moving into 2012 do you still expect to return to high single-digit growth organically despite current macro headwinds?

Nick Buckles - *G4S plc - Group Chief Executive*

It's a difficult question to answer. I don't think anybody is predicting 2012. All I would say is we always grow ahead of GDP trends. We grew the highest level above GDP trends on a lag basis during the recession. So we are still very confident we'll have a good year in 2012.

Laurent Brunelle - *Exane BNP Paribas - Analyst*

Okay, thanks.

Operator

Okay, if there are any further questions --.

Nick Buckles - *G4S plc - Group Chief Executive*

I think that concludes the meeting. Thanks very much for coming and I'll look forward to seeing you again soon. Thank you.

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