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RR.L - Preliminary 2013 Rolls-Royce Holdings PLC Earnings Presentation

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PRESENTATION

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Good morning, everyone. It's nine o'clock so I'm going to suggest that we start. Thank you for joining us today. Let me start by introducing my colleagues from the Board; Mark Morris, Chief Financial Officer; Colin Smith, Director of Engineering and Technology; and Jim Guyette, President, Rolls-Royce North America.

I'm pleased that we are joined by our Chairman, Ian Davis, who is in the audience. I said that rather hesitatingly, because I haven't actually seen him this morning. I am pleased that we are not joined by our Chairman. I think our Chairman Ian Davis is going to be here.

Those of you who haven't met him, you know that we replaced Simon Robertson, Sir Simon Robertson, retired last year and Ian Davis replaced him. I know that he'll be joining us shortly. And what I would suggest at the end of the presentations, Q&As, you don't all flock around me and Mark. Ian Davis, our new Chairman, who is not here at the moment is the person you really want to speak to.

So I'm going to give you an overview of our performance in 2013 and provide some longer-term context and then I'm going to cover guidance for 2014. This forecasts a pause in growth for reasons that are particular to this year and I'm going to spend a few minutes explaining them. Mark will then talk you through the numbers and then we'll have a Q&A.

So let's start with 2013, which I would describe as a good year with plenty of positives and, as always, some areas where we need to improve. This performance required a great deal of hard work by our staff and by our partners and suppliers, so I would like to thank everyone who contributed to these results.

I suggest that the first number on the slide is the most important one. Our order book increased by 19% to GBP71.6b, or up 16% excluding Tognum that has now been renamed Rolls-Royce Power Systems, a division that also includes Bergen.

This record figure confirms our trajectory for significant long-term growth and demonstrates the confidence that our customers continue to place in our technology. The book includes orders for more than 1,600 XWBs, our best-selling Trent engine. But of course that is in the future.

Group revenue was up by 27%, 6% excluding Tognum. Profit was up 23%, 11% excluding Tognum. The 13% increase in payment to shareholders reflects the belief we have in the fundamental strength of the business as well as its future prospects.

I hope by now you are familiar with the four Cs that provide a focus for our business; customer, concentration, cost and cash. Each of these is a journey rather than a destination and our mindset needs to be one of continuous improvement. On customer, we've made big improvements with plenty more to do.

To give you some examples, in 2013 we achieved a 100% on-time delivery in Civil Large Engines for the first time ever, the first time ever. By the end of the year our Corporate & Regional jet business also achieved a 100% on-time delivery and in Marine delivery was 96% on time, up from 55% last year and just 10% two years ago.

There has also been progress on quality, with Airbus, one of our most important aerospace customers, registering improved quality metrics, and BP, a major customer in our energy business, now placing us among their most highly-ranked suppliers.

Tangible progress on quality and delivery strengthens customer relationships and makes discussions about future business much easier. It is also an essential first step to achieving better financial performance as delivering product on time and at the right quality reduces inventory and lowers cost.

I am delighted with the progress on our biggest program, the Trent XWB that has completed more than 200 test flights and more than 6,000 testing hours. The engine is performing well and will power the Airbus A350 into service later this year.

Concentration means deciding where to invest for future growth and where not. I am completely clear that we need to stand on two strong legs and that requires continued investment in both of our technology platforms, gas turbines and reciprocating engines.

We clearly have a strong Civil Aerospace business that is already assured of substantial growth. In three years' time we will be producing twice as many Trent engines as we are today. So while we need to keep investing in gas turbines and we also -- we also look for opportunities to expand in reciprocating engines, both to maintain balance in our portfolio and to generate the cash required in the much longer-cycle gas turbine business.

Back in 2011 we invested in Tognum to add scale, reach and capability to our reciprocating engine business. This is an important business and has proved a good investment. I spend a good deal of time there, most recently last week. I have been extremely impressed by Tognum's quality of management, customer insight and high-speed engine technology.

It will not have escaped your notice that we also entered preliminary talks about the acquisition of Wartsila. This would have added to our portfolio of medium-speed engines, with applications in marine and land power. On January 9 we announced that these talks have ended. We aim to strengthen our medium-speed engine portfolio and we will continue to look at options to achieve that.

Turning to cost, you'll have heard me say before, but it's worth repeating, the aerospace industry is, quite rightly, strictly regulated. That means it takes both time and tenacity to drive cost out from the business. And you will not be surprised to hear me say that we are not where we need to be.

But, while the pace of change may be slower than we would like, there are a number of areas where progress is being made. We have reduced indirect headcount by 11%, beating our own target of 10%, with more to come in the current year. Unit cost is down in Marine, Energy and Power Systems, although slightly higher in our Aerospace divisions.

We are building new, more efficient facilities and capacity that will support a doubling in production of Trent engines. We are moving production away from high-cost countries, negotiating terms with our suppliers and consolidating our supply chain. We are improving productivity and designing cost reduction into our engines.

Our cash inflow was GBP359m. We've put great focus on inventory, so it's good to see stock turns improving from 3 to 3.4. There's more to do, but by way of context this is among the largest one-year improvements recorded and the highest stock turn we have yet achieved. All of these actions will deliver benefits in time. So overall we've made headway on the four Cs and these are the areas where I will continue to focus.

Because this is a long-term business, to understand it properly you need to take a long-term view, looking back as well as forward. So, for example, in 2003 it is interesting to note the revenue fell by 3%, but taking the long view you can see that revenues have almost trebled in the decade since.

Profit growth over the same period has been even stronger and, of course, the order book, that has quadrupled, now stands at record levels, underpinning growth for years to come.

So we turn to 2014, where we've guided for flat revenue and profit. This is a break in a 10-year trend that will be followed by a return to growth in 2015, so it requires some explanation. Let's look at revenue and profit in turn.

On revenue there are two main drivers. First, after two years of impressive growth we will see defence revenue decline by between 15% and 20%. This will take revenue from its current record back to 2010 levels. Growth will return in 2015.

This one-year decline is the consequence of well-publicized cuts in defence spending among major customers and completion of the delivery phase of two important export programs. The $1bn multi-year agreement announced yesterday with Lockheed Martin to supply nearly 600 engines for Super Hercules aircraft underpins our confidence that growth will resume from a new base in 2015.

Second, the largest part of our Marine business, Offshore, will not produce the growth we've seen in 2013. This is because customer investment decisions are being deferred. And, I do believe that they are being deferred rather than lost.

In terms of profit, Defence profit down 15% to 20% clearly has an impact. But we also find ourselves fighting headwinds of lower capitalization, lower entry fees and negative foreign exchange, alongside higher restructuring costs that will produce cost benefits in the future.

The combination of these events produces a result for 2014 that goes against the long-term trend. But for the reasons I've explained, and supported by our record order book, we remain confident that this is a pause in growth not a change in direction.

So, in summary, then, 2013 a good year with a healthy increase in order book underpinning long-term growth. The four Cs; a big improvement on customer; concentration, making sure we have two strong legs to stand on; cost, not good enough despite encouraging progress in places; cash, an increase in stock turns and a cash inflow. 2014, a pause before growth resumes in 2015 as our defence business rebases and as orders in marine offshore take longer to come through.

Now Mark will take you through the numbers.

Mark Morris *- Rolls-Royce Holdings PLC - CFO*

Thanks John and good morning to you all. I'm going to talk about the Group highlights and business performance and then I'll move on to provide some guidance for 2014.

You will recall for most of 2013 we guided Tognum separately to the rest of the Group. Today we have split out Tognum so that you can make the right comparisons in our key metrics. As usual, I'll restrict my comments to the underlying performance.

So, as John says, 2013 has been a good year for the Group with some mixed performances in our businesses. As I step back and look at the progress that we've made in some of the key areas, such as on-time delivery, inventory and headcount reductions, I'm really pleased. But there are some areas, like unit cost, where progress has been slower than I would have like and we'll touch upon those areas in just a moment.

But first, looking at the financials for 2013, we've made good progress with growth in the order book, revenue and profit and generated a cash inflow of GBP359m.

The order book stands at a record GBP71.6b, having grown 19% during the year, with a record order intake of GBP27bn. This includes a GBP2.5bn order intake from Tognum and GBP18.9bn from our Civil business and reflects a very successful year for our Trent XWB program.

Our order book provides good visibility of future growth and underpins our confidence to invest. Order cover for 2014 is around 75% and similar to last year. Revenue increased 27% to GBP15.5bn, GBP2.6bn of that was Tognum. The remaining 6% increase reflects 7% growth in OE with good revenue growth in Defence and Marine and a 4% growth in services.

Profit is up 23% to GBP1.8bn, including GBP180m from Tognum. The 11% growth excluding Tognum reflects strong margins in Defence, the benefit of IAE restructuring and a lower R&D charge. These positives have been partially offset by price pressure in our Marine business and slow progress on cost reduction in our Civil business.

Tognum did well in a challenging environment. The management team demonstrated strong market insight, calling the market exactly right and hitting guidance. Remember that Tognum's profit contribution to the Group reflects transition from a joint venture in 2012 to full consolidation in 2013.

I'm pleased with our cash performance, particularly the improvements we've made in inventory turns, rising from 3 to 3.4 times excluding Tognum. We've had a good flow of deposits and overall broadly flat working capital and higher volume.

We still have more work to do on working capital and I'm confident we can get our inventory turns even higher. Finally, we've increased the full-year payment to shareholders by 13% to 22p, reflecting our confidence in the business underpinned by our record order book.

So now let's turn to the key components of profit growth. Our trading performance was mixed. The benefit of volume growth this year has been eroded predominantly by higher costs in Civil, price pressure in Marine and a number of one-offs. I will talk about these items as we go through the segments.

The year-on-year benefit of the new trading arrangements with IAE, which you will recall was effective from the end of June 2012, was around GBP112m. On entry fees you will remember that at the half year the year-on-year increase was GBP76m, and some of you may be surprised to see only GBP26m today.

We have changed our accounting policy to match our policy for capitalized development costs, so some of those entry fees have now been deferred. You'll see the impact of this accounting change when we look at our Civil results. And you can find all the details on this change in note 1 of the press release.

On R&D, although we spent slightly more in 2013, our R&D charge was down GBP56m. This was primarily because we started capitalizing the XWB development costs following certification. This will reverse in 2014 as the XWB enters service and we continue to invest in R&D. So you can expect a higher charge in 2014.

Restructuring costs increased by GBP37m to GBP54m, reflecting indirect headcount reductions and facility consolidations that will improve our future financial performance. This will continue in 2014. You can expect a similar increase in restructuring charges as we drive down costs.

Turning now to cash, I'm going to pick out the major themes in this chart, which you're all familiar with. Net working capital improved slightly, reflecting a good second-half performance on inventory and higher deposits from our growing order book. We've made good progress on inventory and we will build on that success again this year.

For 2014, the phasing of investments and trading will be weighted towards the second half, so expect a cash outflow at the half year. CapEx on software was GBP650m and included major projects such as new test beds in the US and Germany, new blade and disc facilities in the UK and US and a new test and assembly facility in Brazil.

The remaining balance, of about GBP400m, relates to higher development certification and recoverable engine costs. We expect CapEx to be flat in 2014. So the result is a free cash flow of GBP669m prior to the payment of dividends. Our focus will be to further improve working capital as we drive inventory turns up.

As I said earlier, we are pleased with our cash performance of GBP312m, or GBP359m including Tognum. The Tognum cash flow of GBP47m is after paying a GBP60m dividend to our joint venture partner, Daimler.

So, turning to the Civil business, our Civil business has seen strong order intake, confirming the confidence our customers have in our technology and products. Our biggest program, the XWB, is performing well and will go into service in the fourth quarter of 2014.

Revenue increased 3%. OE growth of 3% reflects a 20% increase in business jet engines and a small increase in Trent deliveries. This was suppressed by Trent 1000 launch pricing and lower V2500 revenue, mainly as a consequence of transferring more parts to Pratt & Whitney.

After market revenue increased 3%, slightly lower than the 5% growth in the installed thrust, this reflects a 20% decline in RB211 revenue as these engines retire or fly fewer hours, resulting in fewer shop visits and part sales.

Now turning to profit, which increased by 14%, this reflects a number of things: higher volume; the benefit from IAE; a lower R&D charge as we capitalize XWB costs; and, higher entry fees, although this benefit was reduced by our new accounting policy. The improvements were offset by higher unit costs and costs to support the XWB's entry into service.

On unit costs in Civil, the performance in the year has been slower than we would have liked, but we are confident that the actions taken in 2013 will yield savings in 2014 and beyond. Changes in design and manufacturing require certification and new tooling, and this takes time.A number of our new factories are not yet running at full capacity, but we know the fixed-cost absorption will improve as production ramps up.

Let me give you an example:In our Singapore facility last year, we produced 41 engines. In the next few years, production capacity will be over 200, so fixed cost absorption will improve. We're also working hard with our suppliers to drive down costs. We've had some successes in 2013 and there will be more this year. So there's a lot going on and cost remains an area of intense focus that we are actively addressing on a number of fronts.

Looking ahead to 2014 in Civil, we expect modest growth in revenue and good growth in profit. Revenue growth will be tempered by fewer business jet engine deliveries, having come off a record year. We also expect launch pricing and RB211 retirements to further dampen growth.

Revenue will return to higher growth levels in 2015, driven by significant increases in Trent engine deliveries, including the XWB. The profit growth will reflect the cost reductions I've just talked about and volume growth after taking account of lower R&D capitalization and lower entry fees.

The TotalCare net debtors are increased by GBP270m, reflecting a combination of linked sales and engine overhauls. You can expect a similar increase in 2014. Many of you have asked about TotalCare accounting, and we'll be doing a briefing session this year at Farnborough.

So, to summarize Civil, a good year, especially on new orders. On cost, progress has been slower than we had hoped, but there has been a lot of activity which will begin to flow through this year.

Now let's take a look at Defence, which had a good year. Revenue was up 7% and profit increased 11%, driven by strong exports of EJ200 and Adour engines and lower R&D spend. Services revenue grew just 2%, reflecting lower flying hours and some retirements of older C130s.

Our 2013 performance in a tight budgetary environment sets a high bar for a 2014 comparison. Against the background of a declining order book and the completion of the delivery phase of a number of our major export programs, we expect a 15% to 20% decline in revenue and profit in 2014. This reflects lower deliveries of engines to power the C130Js, V22 Ospreys and Typhoon, as well as fewer Adour kits.

As always, it is important to put this into perspective. We've had two good years of revenue and profit growth that outperformed the market trend. For 2014, our guidance essentially brings us back to around 2010 revenue levels before revenue grows again in 2015.

The multi-year contract for the C130J engines we announced with Lockheed Martin yesterday is worth about $1bn and demonstrates the scale and the opportunities that still exist. Even with the revenue reduction we still expect to maintain broadly similar margins in 2014 as cost reductions kick in.

So, moving on to our Marine business, Marine had mixed results in a tough environment, with good revenue growth of 12%, offset on the profit side by price pressure. The order book grew 1%, reflecting lower order intake particularly in Offshore and Submarines.

Competition remains tough in both Offshore and in Merchant. There is considerable bid activity, but the pace has slowed on some projects because of project financing and capital expenditure phasing by some of our customers.

Our Marine business did a good job of reducing product costs by around 2% during the year. But, the benefits of volume and cost reduction have been eroded by price pressure and adverse mix, particularly in the aftermarket and infrastructure costs, as the Marine business rationalizes its footprint.

Looking ahead to 2014, we expect a modest reduction in revenue and modest growth in profit. Profit rises against a declining volume because of the cost reduction actions we've taken in 2013 and continued actions in 2014. We expect 2014 revenue to reduce driven by the lower order intake in 2013, particularly in Offshore, due to deferred customer investments.

Next, let's take a look at our Energy business. We've seen good growth in the order book with the GBP1.1bn order intake for the year predominantly in Oil & Gas, which provides good visibility for 2014. We have a well-established Oil & Gas business that makes up around two-thirds of the revenue and more than all of the profit in our Energy business.

Revenue increased 9%, driven by higher OE volumes in our Oil & Gas business. Profit increased GBP7m, reflecting higher volumes, partially offset by pricing pressure and continued investment in our Civil Nuclear business. In 2014, we expect further good growth in revenue and profit. But, as you can see, the margins remain poor in this business and this is an area we continue to work on.

Turning to our Power Systems business, we are pleased with the contribution Tognum has made and we are pleased with our investment. We continue to build on two strong technology platforms and Tognum has added significantly to the breadth of our reciprocating engine portfolio.

The chart shows the trading comparisons for Tognum. We saw good growth in the order book, with an intake of GBP2.7bn. Tognum had a tough first half and a good second half, exactly as we said. That strong performance in the second half was driven by sales in marine and agricultural markets that included the effect of customers buying ahead of new emissions legislation that came into effect this year.

Revenue was broadly flat. We saw good growth in our marine and industrial markets offset by lower revenue in oil and gas, mining and lower aftermarket sales. Profit was also broadly flat after a strong second-half recovery, which was helped by unit cost reductions too. In 2014, we expect modest growth in revenue and good growth in profit driven by marine engines and land power systems.

Turning now to our financial strength, we're in good shape. We have good liquidity and a strong investment grade, credit grade, rating. Our financial strength gives us flexibility and assures our customers that we will be there for the long term. And, as we've said before, we are committed to maintaining a strong investment grade credit rating.

So now, before talking about our guidance for 2014, it's worth highlighting that we've created two new reporting segments, Aerospace, and Marine & Industrial Power Systems, which we call MIPS. This reflects our two strong technology platforms of gas turbines and reciprocating engines.

Aerospace will comprise our Civil and Defence businesses, while Marine, Power Systems and our Energy business will now sit in MIPS. Our Energy business will now be called Energy & Nuclear and will include our nuclear Submarines business, which transfers from Marine.

Now turning to our guidance for 2014, which will include Tognum. 2014 will be a pause in growth not a change in direction. And, in 2015 growth will resume. At a Group level, we expect flat revenue and profit. On cash, we are guiding on a free cash flow basis, which is more consistent with market practice. For 2014, we expect free cash flow to be similar to 2013, which is around GBP780m.

Now looking at our guidance for each of the different businesses; Civil Aerospace, modest growth in revenue and good growth in profit; in Defence Aerospace, a 15% to 20% decline in revenue and profit; in Marine, a modest reduction in revenue and a modest increase in profit; in Energy & Nuclear, further good growth in revenue and profit; and, in Power Systems, modest growth in revenue and good growth in profit.

And, some additional guidance for you in 2014. Expect our cash and profit phasing to be H2 weighted, reflecting cost and restructuring initiatives underway, phasing of CapEx spend and our MIPS business, which is traditionally more H2 weighted.

CapEx for the year will be broadly flat. And, on R&D, expect a modest increase in spending but a higher P&L charge as we stop capitalizing the XWB. And, lastly, we expect an underlying tax rate of around 24%.

So let me close by being clear about our focus, the four Cs, customer, concentration, cost and cash. We have a GBP71.6bn order book. This is a concrete measure of the confidence our customers have in our products and technology. Delivering on the promises we have made is crucial and I am pleased with the progress.

On concentration, we have a long-term strategy that's been applied consistently over many years. We will continue to invest in our two strong technology platforms to deliver long-term profitable growth.

As a CFO you would expect me to be focused on cost and cash, and I am. Progress has been slower than I would have liked, and I get this. We understand that improving financial performance is key to our long-term success and we are engaged in many cost-reduction programs. These will drive down costs as they are sustained across the business and as volume, particularly in our Civil business, ramp up.

Rolls-Royce is an exciting place to be right now. There is a great deal going on, including the entry into service of our biggest-ever program and good momentum established towards improving our financial performance.

Thank you very much for listening and now we'll take your questions. Thank you.

QUESTION AND ANSWER

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Thanks, Mark. Okay, as usual, I will point to people and we'll go around. Everyone will get a chance at the questions. If you could say your name and your affiliation before you start and then we will take your questions. So we'll start right at the front, maybe with Ben.

Ben Fidler - ***Deutsche Bank - Analyst***

Yes, Ben from Deutsche here. Maybe kick us off with a couple of questions.

First one just on -- partly your slide, Mark, I guess on capital allocation, but also build again maybe, with your comment, John, about your desire to grow in medium-speed engines. What should we think about capital allocation, about M&A, about leverage? And about your comment about continuing to want to grow in medium speed engines, does that mean M&A, or is there organic opportunity to do that? That's the first question.

I can come out with the second one, or do you want to me ask it now? I'll ask the second one now?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Good idea, otherwise you'll lose the microphone.

Ben Fidler - ***Deutsche Bank - Analyst***

Well, shocking.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

This may be a good idea.

Ben Fidler - ***Deutsche Bank - Analyst***

The second one is just, and I recognize it's probably a slightly delicate topic, but just on this FRC issue, is the FRC looking into any other accounting issues, or does this draw a line under absolutely everything? There's no other issues we should be concerned about? Just if you can update us on what's actually going on there in discussions with the FRC. Thank you.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay, why don't I make a couple of comments and then ask Mark to speak on both of those topics? In terms of capital allocation, a couple of fundamentals that you're all familiar with. First of all, we think it's essential that we have a strong credit rating. We're a very long-term business and we need to maintain that.

In terms of M&A, it won't surprise you in the slightest that I'm not going to get sucked into any discussions or speculation about what we are or are not doing there. We've never talked about it in the past and I'm not going to talk about it today and I won't talk about it in the future.

So what I would say is, as we look at the business - and, again, it shouldn't be a great surprise - we look at it in terms of the gas turbines and the reciprocating engine businesses. We've got those two platforms and they have some similar characteristics in terms of the fact that they are complex, integrated power systems in the sense of an OE and an aftermarket.

And, they're also, I think, important in terms of the balance that they bring to the Group in terms of the different nature of the financials and the industries that they're in, whether it's shorter cycle, longer cycle, earlier cash generation, longer cash generation, more capital intensive, less capital intensive. So there is a mix there that I think is important. It's important to get that balance right.

In terms of the medium speed, as we look at our portfolio in Marine, which is a strong portfolio in terms of what we can offer to marine, an area that I think we need to strengthen is our medium-speed diesel portfolio, where we are relatively small.

So, if you look at the medium-speed diesel, the big players, clearly, Wartsila is a big player there. And, if we look at our Marine business, an attractive part of that portfolio that we need to strengthen is medium speed and it's important in terms of pull-through of other products. How do we strengthen that?

Well, as I said, there are various options there. Clearly, you're well aware that we considered an M&A approach and, as I said, those talks have stopped. In terms of other approaches we can certainly -- and we are working -- Colin can comment on this -- on developing engines, more engines in the medium speed in house, so dual-fuel engines, different medium-speed engines. So we're working on that as well.

Mark, I don't know if you want to make some more comments on capital allocation, or whether you'd like to talk about the FRC.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Well, I can do both. On capital allocation, I think one of the main drivers will be our sensitivity and desire to retain a strong investment grade rating. And I think from that you can infer some leverage levels. There's always a quantitative element that's put on these things, but there's a qualitative element that goes with the rating agencies as well.

And of course it's important too to understand that, like all these things, whilst we desire to maintain a certain rating it's not ultimately our gift to give. But obviously that sits in a context of them understanding our business and what we're doing.

So, that's the important driver in having a strong grade rating for us, as you know, just because we're a long-term business and we want to ensure that governments and customers know that we're going to be around to continue servicing them in 5, 10, 15, 20 years' time.

And, as John said, there are a number of factors we have to think about in capital allocation in terms of how we look across our businesses, where we've invested, where we haven't, where it's long versus short versus medium term, and all around the areas of how the capital is deployed and the sorts of return on capital employed and so forth. So, that gives you some idea, I think, on that.

Just turning now to the FRC, you made a reference and I thought -- I think the question was: are there any other ongoing enquiries? Obviously, do you want me to explain a little bit first about the FRC, the accounting change that we've done?

Ben Fidler - Deutsche Bank - Analyst

I'm happy for you to, but it's more around looking at further issues, whether it goes any wider than this one.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Well, look, a couple of things. I don't think it's unusual for companies from time to time to get enquiries from the FRC, and we're no exception. Clearly, we're not going to comment on any private discussions that we have with the FRC until such time as, like in all these things, there is something to say. So, on the FRC, that's what I would say.

If there was some specific question around the change in policy, which I think is explained in quite a lot of detail in note 1, I'm happy to talk about that as well. No, okay.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay, the next in the front again. We'll start at the front on this side and wind our way a little bit up and come back. I know Sandy likes to be at the end.

Christian Laughlin - ***Sanford C. Bernstein - Analyst***

Thank you. Christian Laughlin from Bernstein. Just one question regarding around the profit strength phasing next year, if you will. I was just wondering if you could provide some commentary on where you expect to see some tailwinds, some margin tailwinds in H2 just given that we should expect to see XWB ramping up and then, of course, T1000 running at higher production rates this year.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Yes. We don't normally get into detailed breakdown of half-year phasing, but what I would say is this: - and, as I alluded to in the presentation - a number of restructuring and cost-reduction initiatives, how we're spending CapEx, some movements in R&D, but also just when we look at our MIPS business generally, the volume load is generally a bit more second-half weighted and that's what will drive some of the profit phasing as well.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Could I just pick up a part there? You throw in there the XWB ramp up. Just to be clear, XWB engine volumes in 2014 are very small. Entry into service is this year and XWB really starts ramping up 2015 and, particularly, in 2016. So this is a small volume of engines next year in terms of XWB. So that's still coming, just to be clear on that point.

And the next. And we'll just go back one row. I think it's -- yes, the gentleman just behind Christian.

Steven Cahall - ***Royal Bank of Canada - Analyst***

Thank you. Steven Cahall from the Royal Bank of Canada. Maybe just a couple of questions on what we're expecting next year in Civil versus some of the trends this year. So maybe first, on IAE, do we expect any uplift next year? It looks like we didn't have any uplift versus 2012 and H2 of 2013, so maybe just what your assumption is there.

And then similarly, on the RB211, if you can give us maybe any color about what retirement rates were in 2013 and what's the expectation for that trend in 2014, because it does look like it accelerated in terms of retirements in 2013. Thank you.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Okay. On IAE, let's try and put this one to bed. For the full year, as I've said, there's a GBP112m uplift. And again, if you recall, if you go back to 2012 we had half year of what I'll call 'the Old World' and then half year of 'the New World'. And your observation is right. There was no uptick in the second half.

Going forward we are not going to break out IAE any more. It just gets too difficult. We're working off assumptions of the old model back from 2012 and we don't know what they would be today. What I will say, is that generally, as we move forward, the uplift will reduce. And I think we've given you that guidance before.

On RB211 retirements for this year - sorry, for 2013 - we said the impact was a reduction for RB211 revenues of about 20%, and that will continue as we go forward. And, again, this isn't a surprise to us. We factored in that there's always some movements a little bit backwards and forwards, but we are anticipating that as it goes [up] we'll start to see some retirements.

And of course, one of the things that we're keen to do is ensure that by lowering the cost of overhauls and so forth we can extend the lives of those. But it's in our planning.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Right at the front on this side.

Nick Cunningham *- Agency Partners - Analyst*

It's Nick Cunningham from Agency Partners. I hope this doesn't seem too aggressive, but it falls to me --

John Rishton *- Rolls-Royce Holdings PLC - CEO*

If it's very aggressive I'm not going to answer..

Nick Cunningham *- Agency Partners - Analyst*

Well, you can always shut me up.

John Rishton *- Rolls-Royce Holdings PLC - CEO*

Yes, okay.

Nick Cunningham *- Agency Partners - Analyst*

But Defence has been, if you like, almost anomalously strong for several years. And we've kept on asking about that; can this go on. And you haven't been specific in response.

But I think the takeaway has been that it's sustainable. But now we're looking at a 15% to 20% decline at one-year notice, which is unusual for a large company to do that. So I'm just wondering what happened and what -- why was it not flagged earlier?

And I have another couple. Shall I ask them?

John Rishton *- Rolls-Royce Holdings PLC - CEO*

Please ask them all, yes.

Nick Cunningham *- Agency Partners - Analyst*

Thanks. On the change in RRSP treatment I'm just wondering why the FRC recommendation was only half adopted. What's the thinking behind your decision to adopt a different treatment from them?

And, finally, and this probably just displays my own ignorance, but why is the minority so small? One would have thought that half of Tognum would generate a much bigger P&L minority. As I say, that's probably just me.

John Rishton *- Rolls-Royce Holdings PLC - CEO*

I'm going to ask Jim on Defence. I think, in part, the answer to the Defence question, though, is we have given in-year guidance and you run into that which is, well, do we make -- how do you handle that? But we give in-year guidance now. Clearly, this time we've started talking a little bit about the future and I think that that's made us think a little bit more carefully about how we manage that.

So what I would say is what we are trying and we're heading in the direction of - and I know again it'll be slower than many of you would like - trying to get more transparent about a whole variety of issues, including length of time potentially and details around it.

And, as Mark said, we'll have a session on the TCA accounting at Farnborough. But I think in a nutshell that's the answer to that. But, Jim, maybe if you can make a few comments on Defence that may be helpful.

Jim Guyette - ***Rolls-Royce Holdings PLC - President, Rolls-Royce North America***

Thank you. And what I'd like to do, if I may, is take your narrow question and maybe provide a little more color to the Defence story, because I think it would be helpful to all of you. And I suspect it's one of the primary issues of concern. Let's start with a couple of points of background.

Let's go back five years and let's look at our revenue and profits. Our revenue improved 54% over the last five years, profits 96%. Now, this is against a backdrop of a very, very difficult defence budget situation - US, UK and a couple of other jurisdictions as well. So, it is outsized performance given the backdrop of a tough, turbulent environment.

And the reason that we were able to do so well is product portfolio, mix and also some contracts that served us through that difficult period. What we're now finding is that the defence reductions are beginning to bite. And they didn't begin to bite just this year. If we go back and look, our order book has been decreasing over the last three years, so I think quite a signal that things were going to catch up with us. And they have.

Last year it was the aftermarket business that did not do as well as one would have hoped or as we have done in the past and, if you look, it only increased 2%. So that's where we took the first hit. And it was in reduced line and it was also with respect to some airplanes that had been retired. So this year it's now manifesting itself in OE. And I'll cover that in just a second. But I'd like to provide a couple of other points that might be helpful to you.

If you look at the US for a moment, last year I provided a tutorial on sequestration. My colleagues have asked that I don't do that again this year, but we can do it later if you would like. We do have a defence budget for the first time in several years in the US, and that's good news.

The other good news is for this one year it put aside the effects of sequestration, only for one year. The other good news is that it is a $12bn improvement over where sequestration would have been. The bad news is the defence budget is $40bn less than the President requested. So again a little bit of gain here, but not as much as the Defence Department thought it needed to run its business.

The other thing that I would point out to you, again, for background, is you look at the political situation in the US, yesterday House of Representatives passed legislation on debt ceiling, another signal of stability, and that will carry us through March of next year. So I think that's helpful.

The other point that I would raise is this is a year of mid-term elections, so every member of the House is up for re-election, a third of the senate. And I think it means that there is probably less room for political mischief. People are going to be on their better behavior. Now, what does that mean for sequestration next year? Don't know, but I suspect, again, better behavior.

If I could then move to another aspect of this, we have in my view good clarity on 2014 and we're having increased clarity on 2015. The next bit of information that we will have will come on March 4 when the President releases his budget to the Congress. We'll have a much better sense of what's in, what's out.

Usually we know about this in February. It's been delayed a month, so we're a month behind in all of that. But still, I think we understand pretty well what 2015 will look like. There are puts and takes, but a better understanding.

If I were to again walk you through now the OE side of what is happening to us, again we're going to concentrate on the US, because that's where the volatility is today. The C-130J, it is our bread-and-butter airplane. We have been at a high watermark on deliveries of C-130[J]s. This year it will drop approximately 30%. You heard the announcement of the new order, a five-year order that will bring us up above this year but not back up to the high watermark.

V-22 Osprey has been an award winner for us over the last couple of years, and that drops by more than half this year. And we would anticipate that that levels off. Now, there's going to be some prospect for perhaps some sales to Israel and some other countries that would be nice upside but, for us, we think we know where we are. And of course A400M is delivering. We have now JSF starting to deliver. There are some opportunities in the tanker world that we're also having a look at.

The other side of this equation is cost, and a very, very important element of what is happening in Defence. Simply said, we are resizing the business. We're attacking every single element of cost.

Overheads; over the last three years we pulled overhead down 20%. This year we're bringing our production costs, our manpower on the shop floor, down 15%. That's almost 500 people. Most of that is in the US and almost all of those people will be off the payroll within two weeks. So it's not a plan. It is a reality.

We're now moving on product cost. What can we do to reduce product cost? Aggressive actions there as well. Those take time to implement, but they're under way. We're looking at production footprint. How do we consolidate? How do we reduce? Again, actions under way. So there's a cost element to this. We have got to resize, reshape the business to today's defence reality.

And lastly, John, I would also mention just for the group that we're out in the international marketplace looking to see what we can do too to sell equipment, and we're working with our platform suppliers.

And then there is the aftermarket. And one of the things that we're focused on in this kind of an environment is how do we help our customers do more with less. An example of that, we have a new product upgrade for the T56 engine that serves the legacy C-130s. It is now a program of record in the US; very, very helpful.

And what we do is upgrade the engine. And what it provides the customer is somewhere between a 10% and 15% reduction in fuel. And so with a small investment there is a big gain. So we're looking for every opportunity again to help those customers that we have do more with less in a budget-constrained environment.

So I apologize for a long answer, but I did think that since defence was a headline item that perhaps it might be helpful to handle it in a comprehensive way. To answer your direct question, yes, we saw it coming, reflected in order book declining.

John Rishton *- Rolls-Royce Holdings PLC - CEO*

Thanks, Jim. Mark.

Mark Morris *- Rolls-Royce Holdings PLC - CFO*

Right, FRC, I think the key thing here is that risk and revenue sharing partnerships, which you're familiar with, Nick, are not directly covered by any particular standard under IFRS, so it requires judgment in arriving at what we believe is the right treatment. And ultimately it's like all these things. There's a level of interpretation and, as we've alluded to, we've been in discussions with the FRC.

We have a view on how we think it should be interpreted. They have another. There are both -- good arguments for both, but when we looked at it and looked at the difference in terms of where we ended up we concluded that it was relatively immaterial. But for us it's important that we stand behind what we believe is the right accounting treatment. And that's the position that we've taken. And for us it's consistent with what the rest of the industry does.

John Rishton *- Rolls-Royce Holdings PLC - CEO*

I think what we found was the discussions with the FRC were extremely constructive and helpful and they made us really reflect on what we saw and how it works. So I think it was really helpful in terms of getting us to think clearly about something that we hadn't perhaps thought as clearly about in the past. So they were good discussions, I think very constructive and useful.

Mark Morris *- Rolls-Royce Holdings PLC - CFO*

Absolutely.

John Rishton *- Rolls-Royce Holdings PLC - CEO*

Mark, you had a question on minorities as well.

Mark Morris *- Rolls-Royce Holdings PLC - CFO*

Yes. I'm not quite sure I fully understood the question. But obviously Tognum has moved from being JV accounted to fully accounted. I think if it was a techie question we'll take it offline.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay. We'll do that. Next let's just go back to this side. Those of you sitting at the back will learn you have to sit at the front in future.

David Perry - ***JPMorgan - Analyst***

It's David Perry from JPMorgan. Two questions please. The first one, John, just this issue of medium-speed diesel engines where you think Rolls needs to become stronger. When we were given the presentation on Tognum that was the major raison d'etre, if I understood it correctly, so can you just explain why Tognum isn't meeting the need and why you felt the need to have talks with Wartsila please?

And the second one goes back to Ben's question right at the beginning about the FRC talks, because I think we can't really ignore it and for you, Mark, to say they're private discussions are you absolutely rock-solid sure that there will be no forced changes to TotalCare accounting going forward?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay, let me take the first one. What has become clear, and maybe it's been clear all along, is that we need to do a much better job explaining our non-civil business to many people, which is an issue for us rather than an issue for you, if that makes sense.

So one of the things that we'll be doing later this year is we will have an investor meeting on our Marine and reciprocating engine business, and it isn't just about Marine. There's a land power part to it as well. So we need to make sure that you understand that business I think much more clearly than you do. And we recognize that that's something that we haven't been particularly good at doing.

And to clarify that point, Tognum is the high-speed diesel engine company rather than a medium-speed. So if you look at reciprocating engines in simple terms you've got three speeds, low, medium and high. Low is something that you put in huge vessels and you build them into the vessel at the place where the vessel is in simple terms. I'm making this overly simple.

Medium speed is what we make at Bergen and what Wartsila is good at and has a very large market share. Tognum is a high-speed diesel engine. And if you look at the different engines that it makes there I think, Mark, it goes about 28,000 engines, 20,000 of which are what we would call low-power, high-speed engines, which are primarily for Daimler.

And there's 8,000 which go to a variety of different sources at different sizes, whether that's agricultural equipment, construction equipment, the oil and gas industry etc., etc., so they've got a very diversified customer base. But the fundamental difference is high speed, medium speed, low speed, Tognum high speed. Medium speed is an area that we need to build our portfolio.

David Perry - ***JPMorgan - Analyst***

Thank you. And just to clarify, sorry, because clearly I've phrased the question wrongly, I think back at the Tognum meeting -- sorry, back at the Tognum meeting the point was you were not interested in that medium-speed area. I know it was your predecessor. But the point was always about the niche boats not in a commodity market and you wanted the Tognum high-speed to clarify the gas turbine capability that Rolls had already in marine.

So I'll just -- I'll ask the question correctly. Why the need to move into the medium-speed market that previously, maybe by previous management, wasn't perceived as important?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay. So I'll answer it slightly different. I think that, one, Tognum is a good acquisition. As I've said in my presentation, the management team are doing a terrific job. They did a terrific job last year. I'm sure they will this year. And we are getting the benefits that we foresaw when we made that acquisition.

As I said, I was there last week. And one of the things that I go through when I go there is to look at where we're getting the revenue synergies that we spoke about and how well they're progressing. And we're doing well. And we've got a detailed plan on that with lots of detailed examples of where that's working. So as an acquisition I am comfortable that that was a good acquisition and a good plan.

In terms of medium-speed, though, it doesn't address some of the issues that I think we have; we think we have in terms of Marine and the growing land power business. So irrespective of what was understood or said in the past, to be clear, we believe that we need to strengthen our medium-speed diesel engine businesses.

FRC, Mark.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Okay. We have a huge number of accounting policies that we apply. We are confident with all the ones that we apply. They are viewed and vetted by our auditors. And in relation to TCA accounting we are confident with that one. And like I said to Ben, in terms of conversations or inquiries with the FRC it's not unusual for companies to have them. But like I said, in any respect, conversations that go on between companies and the FRC are private.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay. Let's go back one more at the side.

Ed Stacey - ***Espirito Santo - Analyst***

Hi, it's Ed Stacey from Espirito Santo, just one question, which is cost savings in 2014. When I look at both Civil and Marine you're talking about some margin negative effects. So in Civil you're saying you've got the RB11s coming out of service and you've got launch pricing, so both pricing and mix problems.

In Marine you're saying Offshore is the bit that's a bit weaker than you thought, so that's, I guess, mix negative. And you're seeing there's fierce competition, so I guess we're worried about pricing there are as well. So I could imagine if you were doing nothing on cost savings then your margins would actually be down for both of those businesses.

And then when I look at -- okay, you're saying actually that both of them had decent profit growth. There must be a lot of cost savings. Can you tell me -- am I right that it's a really pretty big number and, if so, what is it that is nailed down and I can be confident that it comes through the cost savings?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Mark.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Okay. Yes, obviously our guidance for Civil, we've guided modest growth on revenue and good growth in profits. And I think what you're seeing there, and, as I alluded to in my presentation, is that obviously you're going to start seeing cost benefits coming through. And interestingly, in Civil, that's against the headwind of lower RRSP entry fees and lower capitalization. So there are a number of things here. As usual, there's a number of moving parts in this, which will include mix and various other things as well.

On the Marine side, yes, absolutely they took 2% out in 2013. We expect continued cost reduction on that front along with some restructuring and rationalization. Again, those will start to flow through as well. But that doesn't mean that the price pressure is coming off. That's obviously something that is still with us in the Marine side, in particular, commercial marine.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Yes.

Rupi Vig - ***Morgan Stanley - Analyst***

Yes, it's Rupi Vig from Morgan Stanley. Just two questions perhaps, one for John first. Just when I think about Defence, and perhaps Jim can weigh in with this as well, what is the right long-term margin in your Defence business? After we've had this reset in 2014, are we going to go back to a period over time where we get towards a low-teens margin, or can we maintain the margins where they are?

And then perhaps one for Mark around cash. When I look at the 2014 guidance, obviously, you're saying roughly the same sort of level. But if we have a good -- or some improvement, should I say, in working capital is there a chance that the cash comes in a little bit better, or -- especially if you've got flat CapEx as well? Thank you.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Well, I'm very impressed that you managed to find a topic that Jim didn't cover in his explanation of Defence, so congratulations on that.

I'm not sure that I can answer you what the right long-term margin is in our Defence business. Clearly, it depends on a whole variety of things. What we are clear about and what Jim did cover is that we need to manage the things that we can manage, which in this specific instance would be cost. And we need to make sure that we are as efficient as we possibly can be. And that's where our focus is.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Yes, I think in terms of cash I think the key thing to recognize obviously is the improvements. And certainly flat CapEx and on working capital what we've got to recognize there is - and I've signaled that - is when we look at the TCA net debtor rising by similar levels again.

So that's really what's bringing down some of the effect. We've got cost reduction under pinning cash that's being contra'd by, obviously, a rise in net TCA debtor. So that's why we're signaling around similar levels.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Let's just keep going back and then we'll come back down to the front here. We'll get there, trust me.

Zafar Khan - ***Societe Generale - Analyst***

It's Zafar Khan from Soc Gen. Just on the headcount reduction, the 11% you mentioned, could you give a little bit more detail on that, please, where that actually happened and what the numbers are in the different divisions now, and how they compare with 2012 year end?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Yes, Mark, I think -- Yes, Mark, please.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

I can't break it down by division. I don't think it's -- as we've indicated, this is all around what we call indirect. A large chunk of it would have been in the UK, but it's everywhere we're not direct. So 11% is the number we did from where we started back in October in 2012 as our benchmark. And it will continue. So that's -- but we're not going to break it down by division.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

How many in -- roughly how many people in total you think that was, Mark? About 1,000?

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

About 1,100, yes.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

About 1,100 people. And, as Mark said, this is in the overhead area. And, as I think I've explained to you, my view is that we've carried too much overhead. Like many material businesses, we've grown and we've carried too much overhead. We need to improve our efficiency a lot in this area, so we're driving process improvements in a whole variety of ways and will continue to do that.

So, if I look at simple things like transaction processing, where do we do that, how do we do it, how many people have we got doing it, how efficient are we doing it, those are the areas that we're getting to.

I think in terms of the costs you didn't see huge change in the costs in the year because, of course, we had the cost of restructuring offsetting the savings. And we should start to see the benefits of that coming through this year. But we're putting more restructuring in this year to drive more cost savings in the future and will drive similar numbers again this year.

Okay, next. Okay, let me come right out to the front again and a change with policy.

Chris Hallam - ***Goldman Sachs - Analyst***

Morning, it's Chris Hallam here from Goldman Sachs. Just one very quick question about your 2014 profit guidance, just how confident you are on that guidance. Because if Defence is down 15% to 20% and you're guiding for flat this implies your non-defence segment is growing low single digits. But 85% of that non-Defence segment you've said is good profit growth, so it seems you must be very confident on flat for the Group for this year?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Well, as I said, we give guidance every year and I think the track record at a Group level has been pretty good, which is a dangerous thing to say, obviously. And it's our best view as we look at out into the future. As with all these things, it's a projection into what's going to happen in the future, but it's certainly our best view, which we've been reasonably good at doing at the total level.

I think as you look into the various divisions you get some ups and downs which you inevitably do as you break down into the detail. But you wouldn't expect me to say anything other than we're pretty confident, otherwise we wouldn't have given it.

Let me go to Sandy, who's just twitched.

Sandy Morris ***Analyst***

And God, that's tired me out. Actually, Wellington boots on just in terms of our cost base in Civil, the simple average number of employees in 2012 was 21,500 and in 2013 it was 23,400. I know you've taken overhead out. We are clearly sitting on a massive chunk of production capacity that we aren't using. If we are assuming that engine deliveries aren't going -- Trents aren't going up markedly in 2014 versus 2013 despite 787, is that right?

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay, let me make a couple of comments there and Mark referred to this. And your point is well made, Sandy. So if we take the most obvious example, in Singapore last year we made 41 engines and it has the capacity to make an engine a day, so clearly that is a cost burden for us in the way that you're talking about.

Next year there will be a small ramp up in Singapore. But in total Trent engines do start to pick up next year, although there's a mix issue there in terms of Trent's large ones going up and the smaller ones going down a little bit, which is the way that we're forecasting it.

The issue for us is -- in terms of balancing that is preparing Singapore to take over the build of the Trent 1000 and the Trent 900 at the moment. Last year it just built 900. It'll start building 1000s this year. And then the buildup of the XWB, which, as I was saying earlier, is very small this year, starting in 2015 and then really ramping up 2015, 2016 in particular. And that's when we start to see that change in mix.

So if your question is am I carrying too much fixed cost and fixed overhead at the moment for the level of production, the answer is yes. And that's what Mark was saying, which is as production ramps up, particularly in civil, that will bring us benefits. If that's your question.

Sandy Morris ***Analyst***

Well, it is almost precisely. Because we muck about with unit cost in Civil but, give us a break, we're carrying a massive amount, so if you then were to --

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John Rishton ***- Rolls-Royce Holdings PLC - CEO***

…Get up here, Sandy, you're doing a good job for me.

Sandy Morris ***Analyst***

God, watch the share price if that happened. And therefore if you tell me that actually, notwithstanding that change is difficult, we are content with the progress we're making so that when we hit the button the business is in the shape you want it to be then I would regard that as a very encouraging comment. Are you going to make it?

John Rishton ***- Rolls-Royce Holdings PLC - CEO***

Yes, I would. So for us it's about shaping the business for the future. And in the future we're going to get extra benefits of volume. And when we start getting the capacity and the demand in balance we get that as a windfall. But if we've right-costed the business before we get there then we're in great shape, which I think is the point that you're making, and that's what we're striving to do.

Sandy Morris ***Analyst***

And you're happy?

John Rishton ***- Rolls-Royce Holdings PLC - CEO***

Yes.

Sandy Morris ***Analyst***

Right. And then a crude --

John Rishton ***- Rolls-Royce Holdings PLC - CEO***

Happy is not a word I ever use, by the way.

Sandy Morris ***Analyst***

Less miserable.

John Rishton ***- Rolls-Royce Holdings PLC - CEO***

Happy was 1974, about an hour and a half, and that was it. It's over. I'm confident; that's a much better word.

Sandy Morris ***Analyst***

God, you've had a charmed life.

And then, look, just blundering into TotalCare, where actually the disclosure has gone up a lot, now, the liabilities are a bit smaller than I'd imagined and it's just part of these accruals and spend. Just in broad terms how much did engine overhauls go up last year? And what's the trend in engine overhauls just so we can capture the cash spend, please?

Mark Morris ***- Rolls-Royce Holdings PLC - CFO***

Yes, I think the problem is there are so many moving parts here. And you've alluded. Last year GBP270m and, interestingly, about GBP240m of which was in the first half and only GBP30m of which was in the second half. And that just really reflects the various moving parts we have in and what contributes to the net TCA debtor.

And, again, we'll get into a little bit more of this when we get into Farnborough. But, yes, we had more shop visits and overhauls in H1 than we did in H2. And that's the main driver just because that drives the creditor down, which, in turn, creates the net debtor being high. That's the main reason behind it, Sandy. But you had a pretty good go at answering yourself just then, so --

Sandy Morris ***Analyst***

Yes, I do that and then go wrong.

Mark Morris ***- Rolls-Royce Holdings PLC - CFO***

Well, you're right.

Sandy Morris ***Analyst***

Thank you. Just could they go up again, or have we hit a maturity average level, because my sense is the spend has gone up a lot for the last two or three years as the fleet matured?

Mark Morris ***- Rolls-Royce Holdings PLC - CFO***

I think, with the levels of H1 and everything, it will continue. Obviously, they will ebb and flow from one H to another. It's just depending on how they schedule and where the aircraft are delivered and, more importantly, how the aircraft are used. Because you can't say that every aircraft has one coming in every five years.

If an aircraft is being worked harder it will be four years. So there's lots of moving parts that drive that. And of course, as you know, shop visits and overall costs are just one part of what makes up the net TCA debtor. But they will ebb and flow. But of course as you got more volume on the management they are going to grow over time; that's the reality.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Okay, there's one more here.

Andrew Gollan - ***Berenberg - Analyst***

Morning, Andrew Gollan from Berenberg. Two questions, one on aftermarket and one on revenue drivers. Civil aftermarket, could you possibly tell us the split or broad split now between TotalCare and time and materials? And within the time and materials a broad indication of how important the RB211 program is?

Secondly, on revenue drivers, a couple of sub-questions here. The launch pricing issue on T1000, presumably we knew about that, because these are agreements that were made some time back. Or is it a factor that's becoming more of a headwind than we thought? Or do we know where we're going with this issue for 2014 and 2015? And I guess the same applies to when we get into Trent XWB down the line.

And secondly, on V2500, I believe that was down year on year and I understand that to be parts and services supplied into the platform. Why was that lower, given that industry volumes were up, please?

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Okay, I think you got three questions there. On aftermarket the split is about 70/30.

On the issue about launch costs, yes, of course we know about them. They're contracted a number of years in advance. Lead times are typically 18 months, two years, and then right outs are five, six, seven as the set of deliveries will go through.

But, again, when we guide on profit that is just one element along with where are we on, if you're just looking at the OE element, what all the other deliveries are doing. And then particularly within Civil you've not just got Civil Large. You've also got the business jet engines, which traditionally have higher margin anyway because they fly less hours than the aftermarket, so the logical business analysis is you get more on the OE.

V2500, again, let's just remind ourselves of what we're doing. We continue to manufacture and supply parts and there's a transitioning process that's going on. And over time some of the parts that -- where we have sourced in supply will eventually transfer through to Pratt & Whitney.

We will continue manufacturing a number of parts and, again, even over time some of those will start to drift as well, which is why we originally guided it will start to come down over time. So that's the driver behind it. It's just as time's gone on there's been some parts transfers of what was coming in through us now and now what's been transferred and goes straight to Pratt & Whitney. So that's the driver.

On the -- previously, obviously, some of the parts where we've had more volume is just a function of what part sales are being driven, and you can forecast them, but what actually turns out may be different. And last year, for instance, we had a number of cases where more expensive parts were being ordered and more of them, which drove part of that revenue.

Andrew Gollan - ***Berenberg - Analyst***

And what proportion of Time and Materials does RB211 represent.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

I said that it's about 30 -- sorry, RB211? Off the top of my head I haven't got that, but we'll get that for you.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

It's obviously quite a significant.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Yes, it is. Within time and materials RB211s is going to be --

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Almost all of it.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Yes, I was going to say 70%, 80% I should think. Yes.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Yes. And the 70/30, Mark, just to be clear, is the total --

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Total.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

-- as opposed to the split of sales that we're getting at the moment, where we've got higher TotalCare and less time and materials.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

That's correct.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Yes.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

So it's just on the existing total installed base.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

So that's the total.

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Yes.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Now it's different.

Anything else from -- just one more from -- last one from Ben. This is last of the last.

Ben Fidler - ***Deutsche Bank - Analyst***

Sorry to come back with a few more and end on a low point maybe, but just a couple of follow-ups. Firstly, you mentioned there were some quite good deposit inflows that helped -- or deposit inflows, an item in the cash flow in 2013. Maybe you do disclose it and I just can't find it, but I wondered if you could share with us what that scale of deposit inflows was that helped in the free cash flow number in 2013.

The second question, and I guess it builds partly on this launch pricing point, but just you clearly have good visibility about the launch pricing effects, but on XWB, as those volumes rise in 2015 and 2016, just how that plays out and how we should think about the headwinds that may or may not create?

And maybe the final one is just your comfort level on Trent 500 TotalCare net debtors. Trent 500 is 12% of your installed base. We've got 10% of the aircraft on the ground. You're offering, understandably, an improved package for the airlines of overhaul one, overhaul the other three. I'm just wondering how that plays out in terms of your view on whatever the TCP net debtor is on Trent 500. Thank you.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Mark is delighted to have one last question. Mark, the deposits?

Mark Morris - ***Rolls-Royce Holdings PLC - CFO***

Well, on deposit flows it won't surprise you the bulk of that has really come from Civil and the massive growth in the order inflow, order intake and order book. At the same time, of course, Defence has been running down as the production delivery phase has been coming through, but one's more than offset the other. I don't think we reveal the net difference between the two, but that's what's been driving it, Ben.

On launch pricing on XWB we're not going to get staked out in the sun program by program. In giving you the guidance from 2014, and what I'll call a bit of finger painting for 2015, we factored that in into our thought process.

And, again, ditto on Trent 500 net debtor. It's a small contribution to the overall net debtors. As you know, the Trent 500, as a four-engined aircraft, is not doing as well given the high fuel price environment. Again, that's factored into our calculations, but I'm not going to break it out specifically. But, again, it's reflected in the total rise in net TotalCare debtor that I gave you for 2014.

John Rishton - ***Rolls-Royce Holdings PLC - CEO***

Thank you. And, as you see, if we have one extra question the answers tend to get a bit -- less answers I think is the way I would describe it, less specific maybe.

Thank you very much for joining us this morning. It's very good to see you all again today. If I leave you with just a couple of thoughts, first of all, cost, cash, concentration and customer, really, really important for us and the business.

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That's where our focus is. That's where my focus is. That's where the Board's focus is, to make sure that we can do as Sandy was suggesting. Really important that we get the customer elements right and we're making good progress on that, but we still got way to go. 2014 pause growth, not a change in direction. Growth comes back in 2015.

Thanks very much for your time this morning.