



Rolls-Royce

2016 Half Year Results

John Dawson

Director, Investor Relations



Rolls-Royce

Agenda for today



Rolls-Royce

Introductions

John Dawson

Highlights

Warren East

Financial review

David Smith

Transformation and business outlook

Warren East



Safety

Safe
Harbour

Mobile
phones



Warren East

Chief Executive



Rolls-Royce

Goals for 2016



Rolls-Royce

With a focus on pace and simplicity...

Strengthen our focus on engineering and operational excellence and leveraging our installed base

Deliver a strong start to our transformation programme

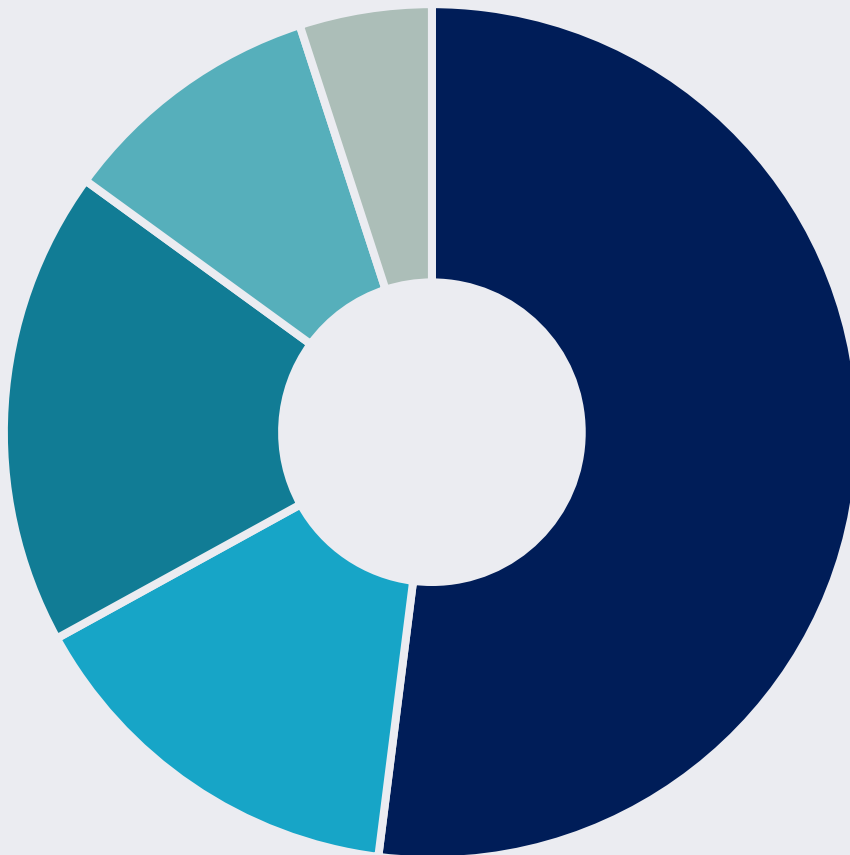
Start rebuilding trust and confidence in our long-term growth prospects

Group

First half 2016 highlights



Rolls-Royce



FIRST HALF BROADLY IN LINE WITH EXPECTATIONS

- Ahead on profit and cash but driven by timing

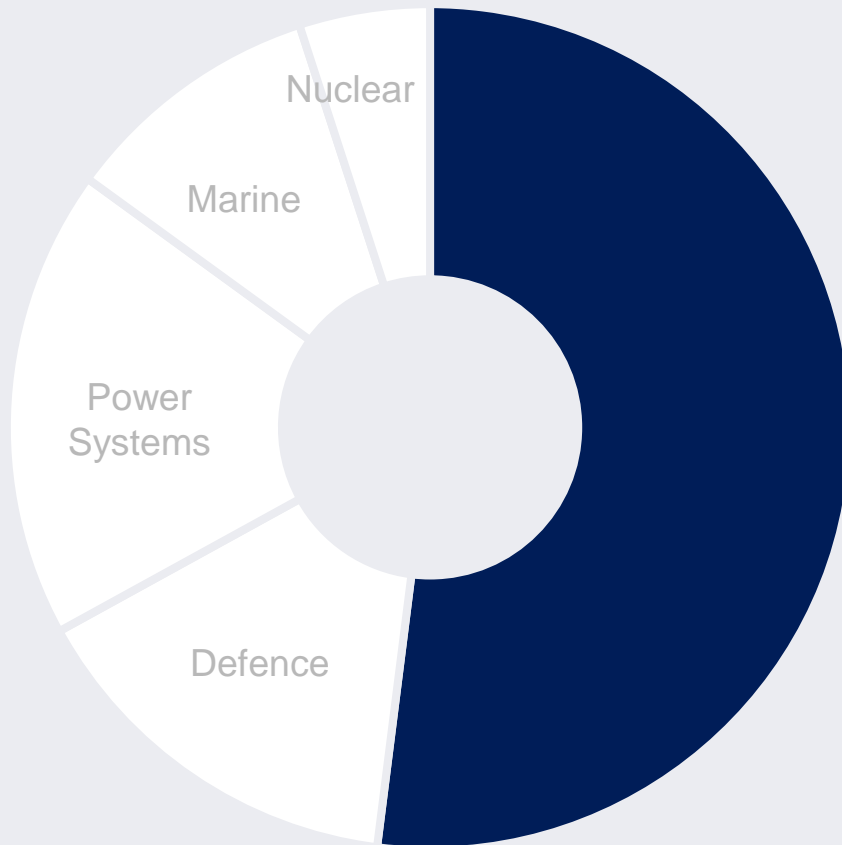
ON TRACK TO MEET FULL YEAR EXPECTATIONS

- Continued mixed market conditions

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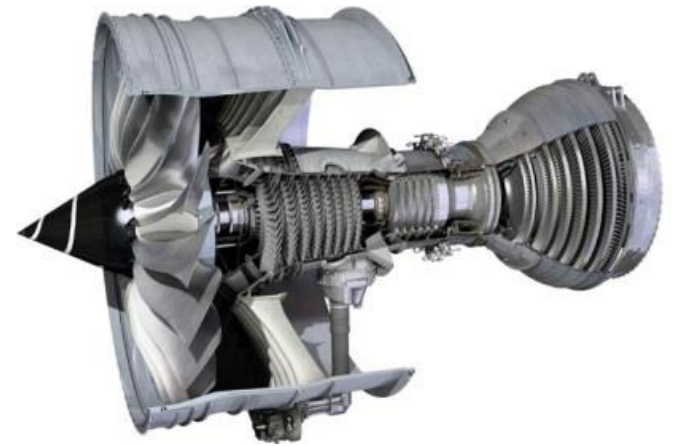
Start rebuilding trust and confidence in our long-term growth prospects



■ CIVIL AEROSPACE

- Key engineering programmes

Trent 1000 TEN receives EASA certification

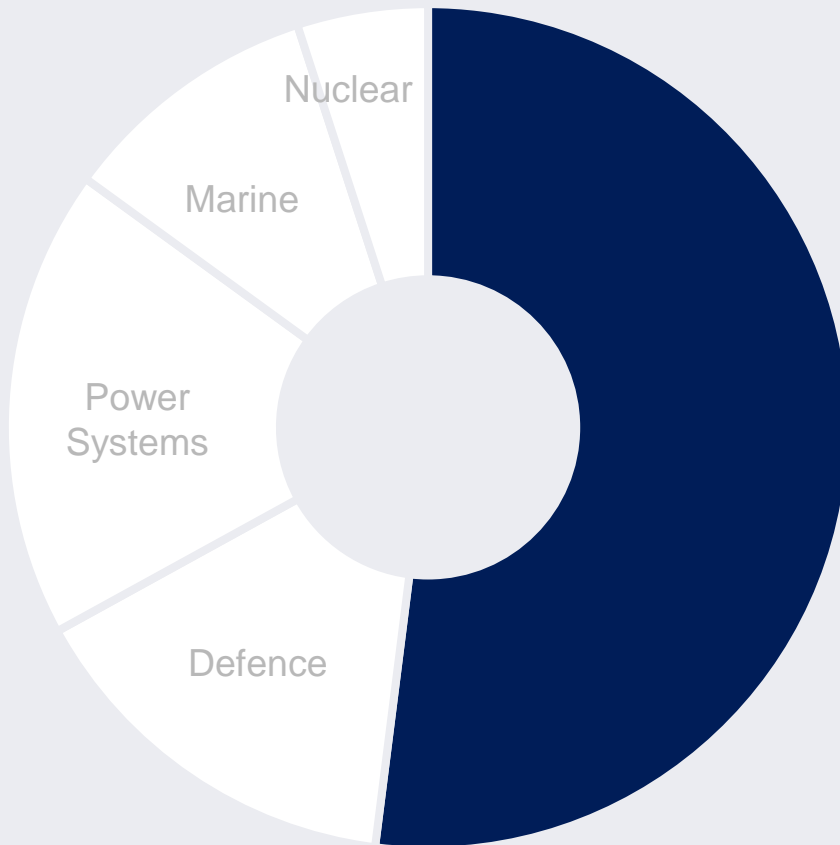


Civil Aerospace

First half 2016 highlights



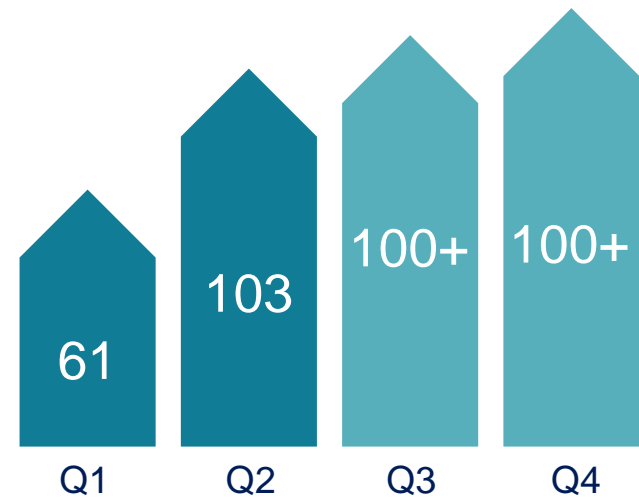
Rolls-Royce



■ CIVIL AEROSPACE

- Key engineering programmes
- Manufacturing ramp up

of large engines delivered



Strengthen our focus on engineering and operational excellence and leveraging our cost base

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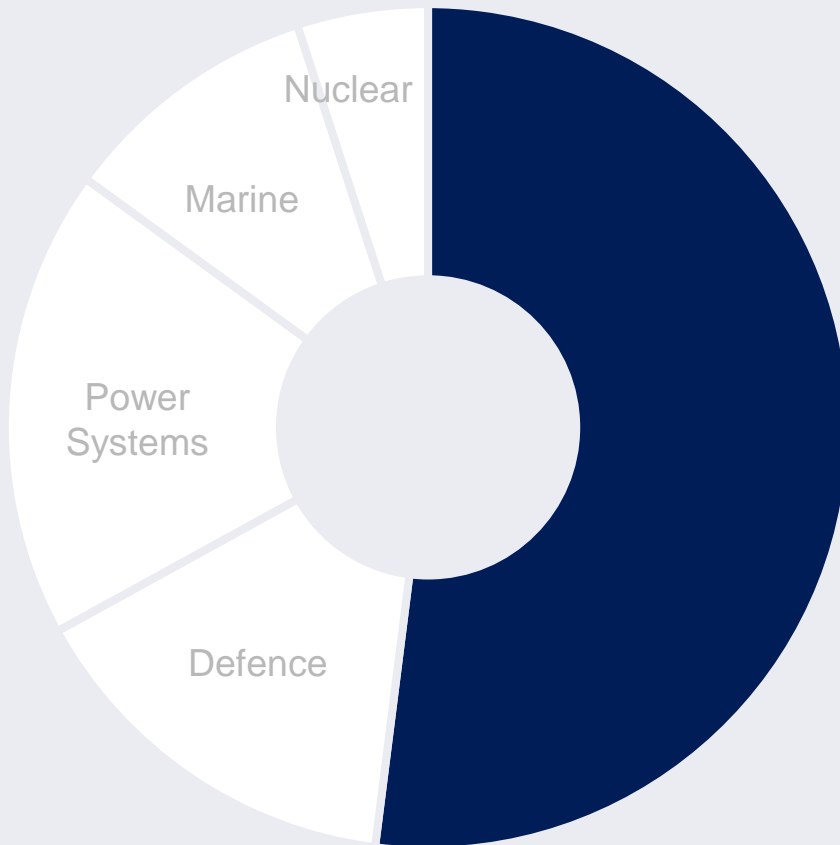
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Civil Aerospace

First half 2016 highlights

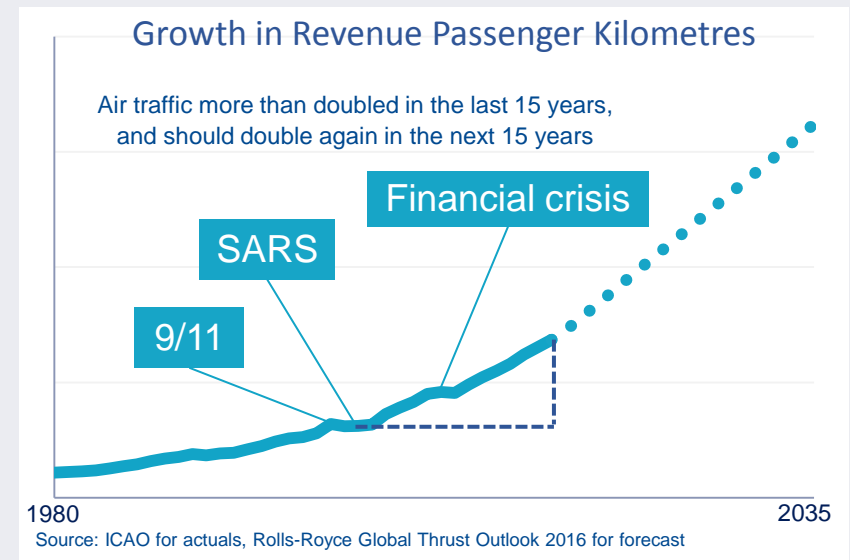


Rolls-Royce



CIVIL AEROSPACE

- Key engineering programmes
- Manufacturing ramp up
- Long-term demand remains positive



Strengthen our focus on engineering and operational excellence and leveraging our cost base

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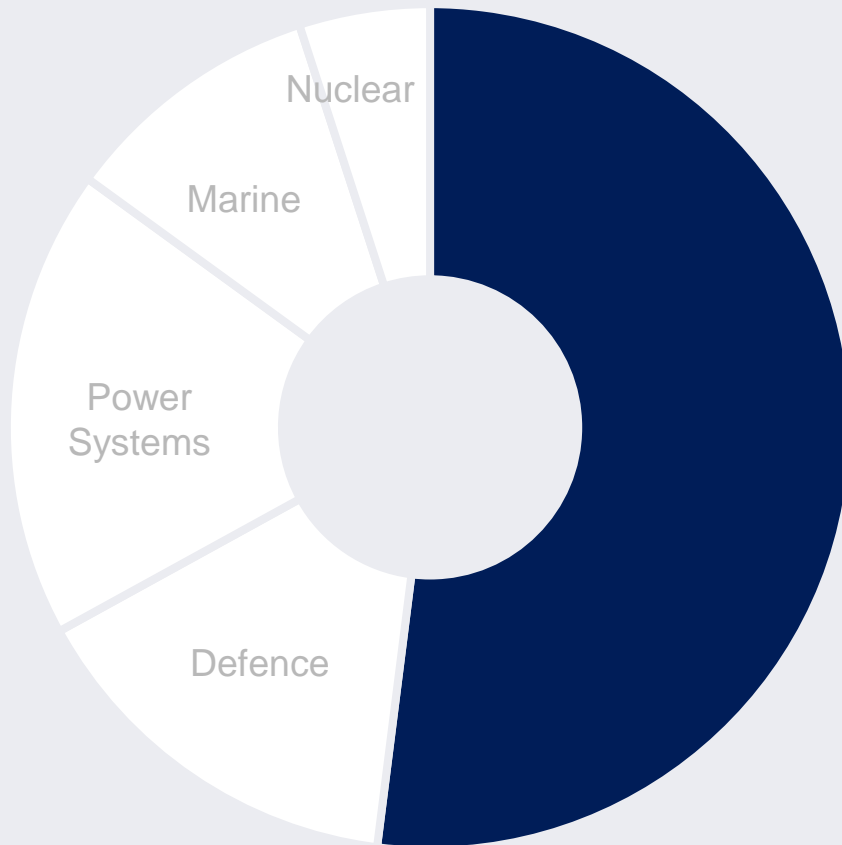
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Civil Aerospace

First half 2016 highlights



Rolls-Royce



■ CIVIL AEROSPACE

- Key engineering programmes
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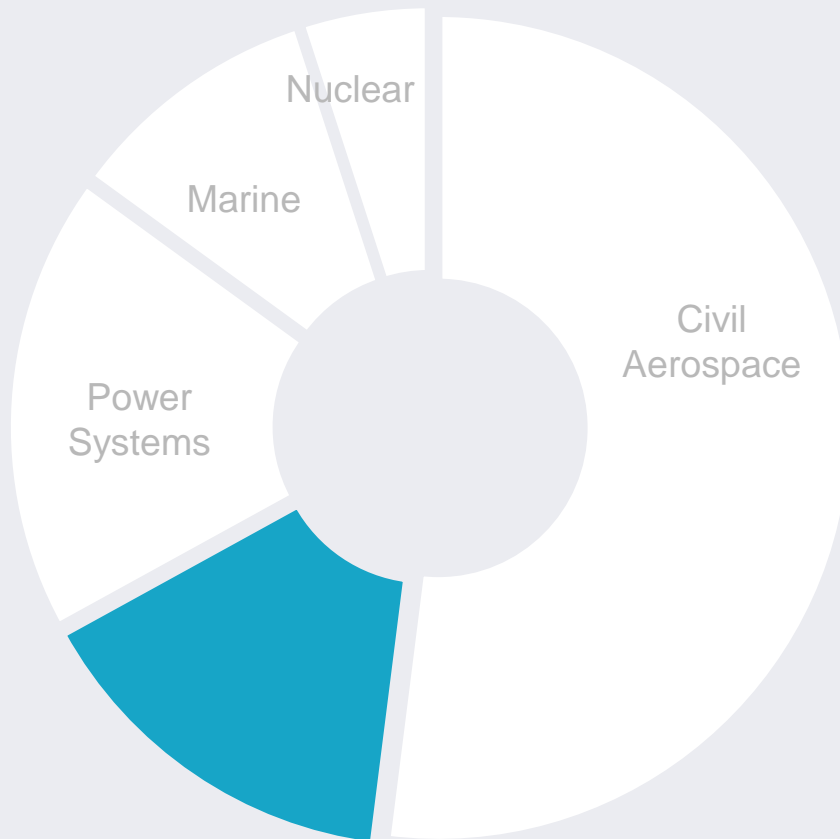
- Significant demands on engineering resources

Defence

First half 2016 highlights



Rolls-Royce

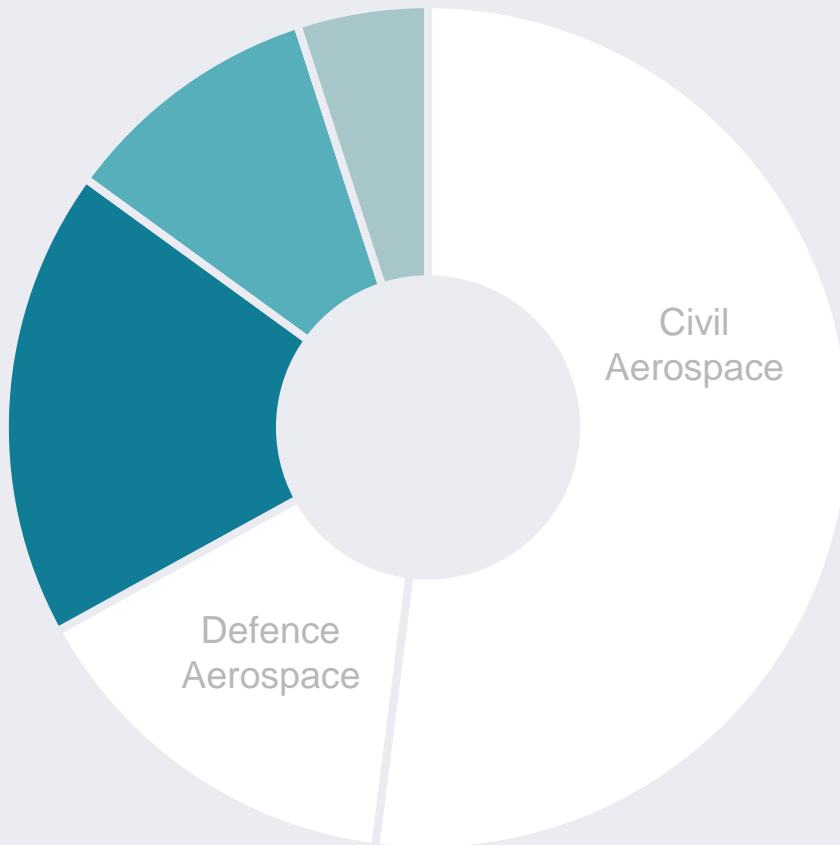


DEFENCE AEROSPACE

- Steady first half
- OE volumes remain good
- Positive outlook for the second half

Long term...

- Aftermarket services key to future success
- Making good progress capturing value from installed base with new services
- R&D investments focused on next generation of transport & patrol and combat platforms



POWER SYSTEMS

- R&D investment on new higher volume, common core engine platforms

MARINE

- Good progress delivering restructuring plans – key to future profitability
- Creating a more balanced business with good growth opportunities

NUCLEAR

- Focus on delivery performance to underpin strong position on new submarine platforms

Transformation well under way

Organisational hardware

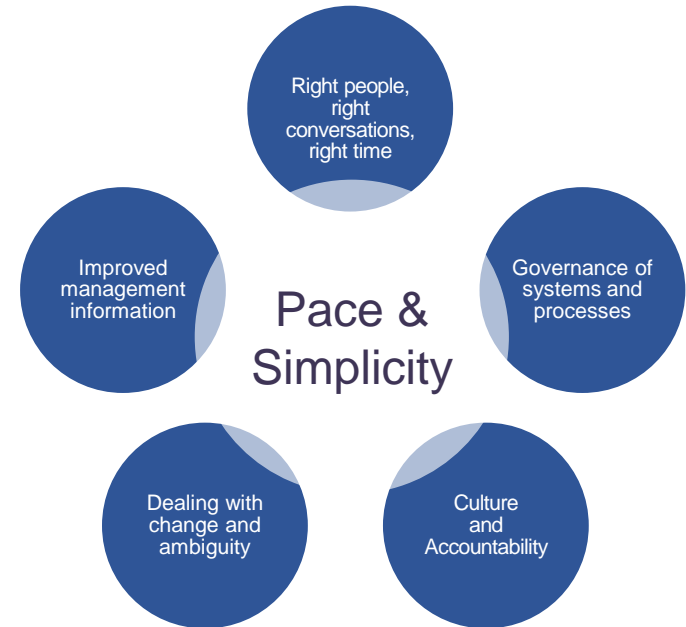
Primarily fixed costs

Senior level

Corporate and divisional



Organisational software



On track toward delivering top end of expectations

On track to deliver £150-200m annualised cost savings by end-2017



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£m	2016	2017	2018
Nov 2015 Transformation Programme			
Initial phase	c. 50	c. 50	0
Next steps		20-40	30-60
Incremental benefits	c. 50	c.70-90	30-60
Cumulative savings	c. 50	c.120-140	150-200

Strengthen our focus on engineering and operational excellence and leveraging our intellectual capital

Deliver a strong start to our transformation programme

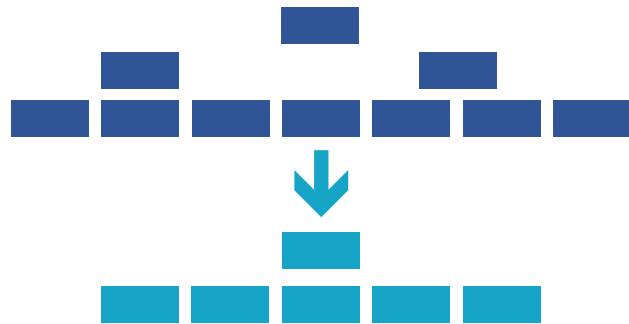
Start rebuilding trust and confidence in our long-term growth prospects

Notes: Costs of delivering the November 2015 transformation programme are expected to be largely taken as an exceptional charge. The charge in 2016 is expected to be towards the low end of the announced £75-100m range. Further exceptional costs may be taken in 2017.

Organisational hardware changes already yielding 'software' benefits



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↓ 20%
reduction in management
population



50%+ reduction in senior
leadership group



Stronger individual
accountability



Significant simplification of
'committee' structures and related
time burden on management



More efficient financial
reporting

Goals for 2016



Rolls-Royce

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Deliver a strong start to our transformation programme



Start rebuilding trust and confidence in our long-term growth prospects

David Smith

Chief Financial Officer



Rolls-Royce

Results summary



Rolls-Royce

Underlying Revenue

£6.1bn

↓ 5%

Gross Margin

£1,033m

↓ 26%

Underlying PBT

£104m

↓ 80%

Operating margin

2.6%

↓ 500 bps

Free cash flow

£(399)m

H1 2015: £(576)m

'Dividend' per share

4.6p

H1 2015: 9.27p

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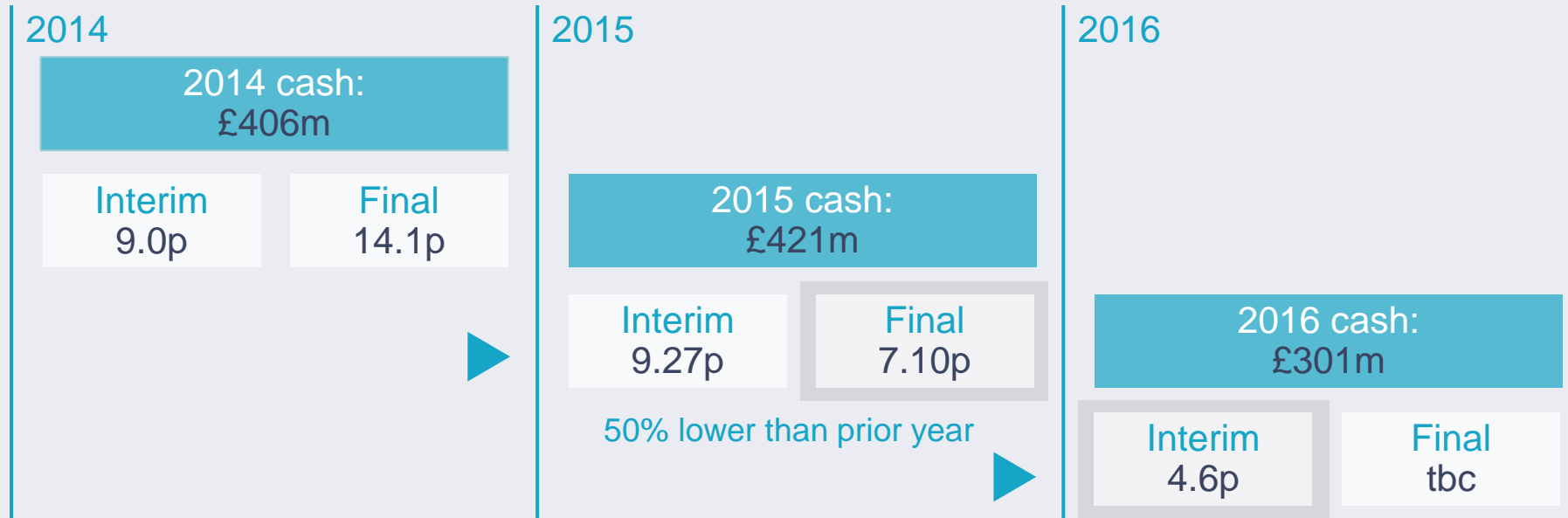
* Percentage change at constant FX

Shareholder payment halved

in line with February policy



Rolls-Royce



“We recognise the importance of a healthy ‘dividend’ to our shareholders. Subject to short-term cash needs, we intend to review the payment so that it will be rebuilt over time to an appropriate level. This reflects the Board’s long-standing confidence in the strong future cash generation of the business.”

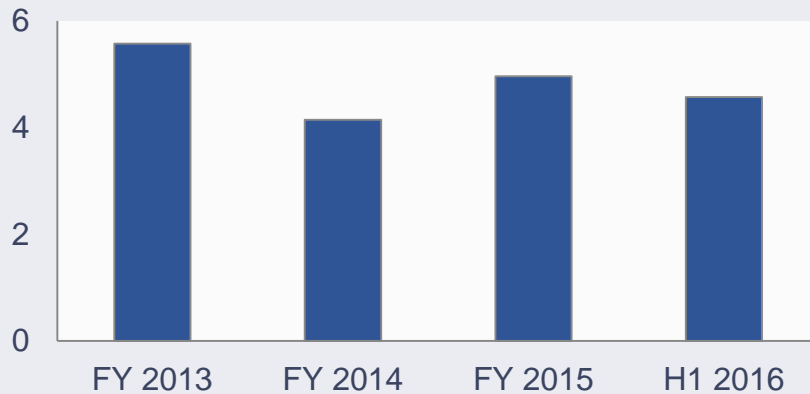
Balance sheet



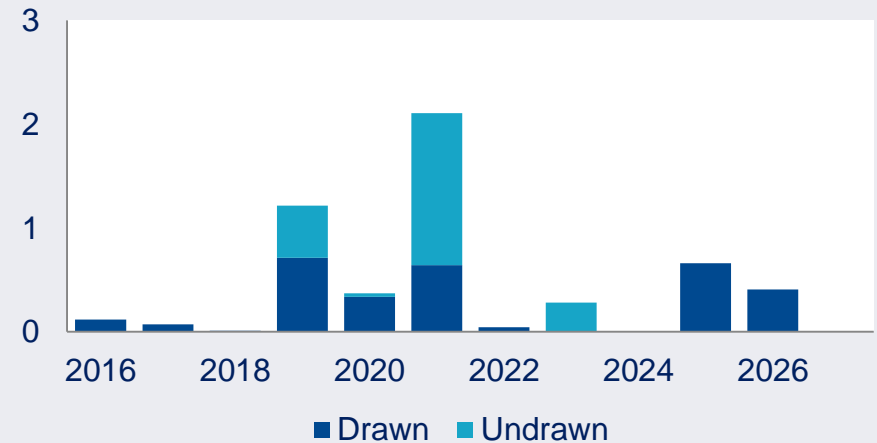
Strong liquidity position – total liquidity ~£4.5 billion

Revolving credit facilities increased by £0.5 billion in H1 2016

Total Liquidity (£ billion)



Debt Maturities (£ billion)



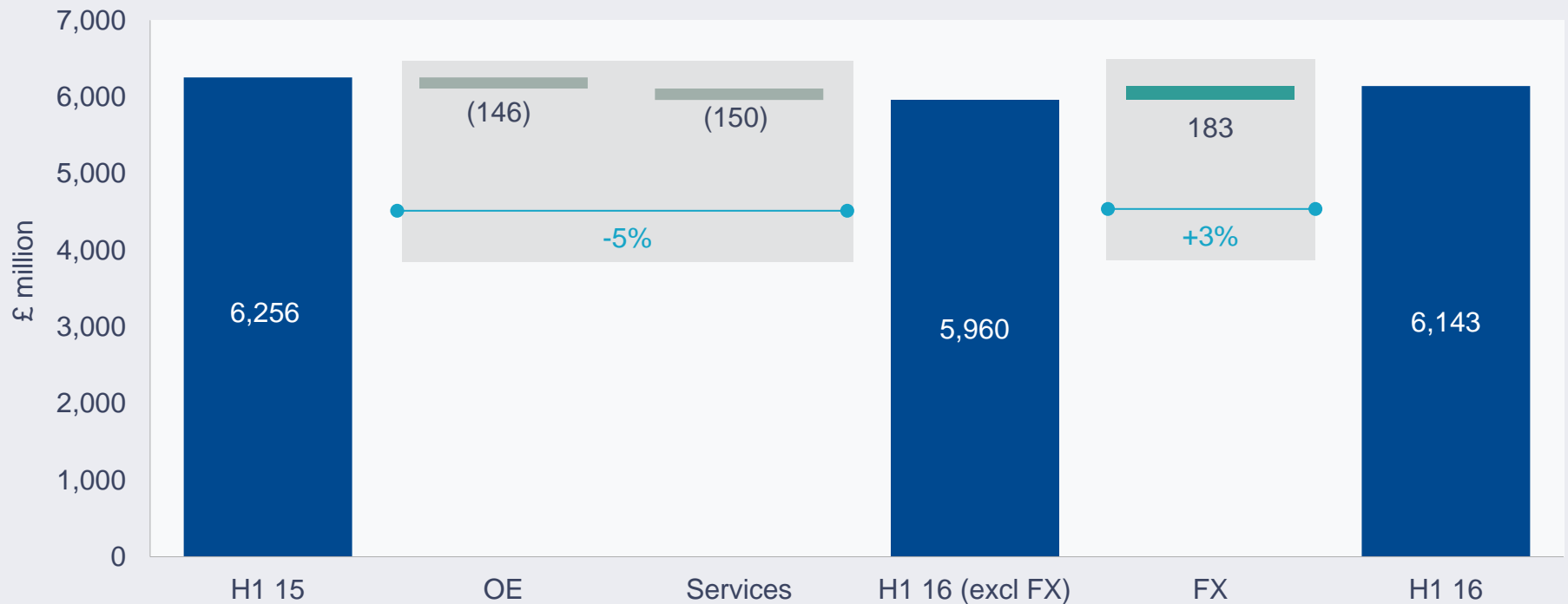
'A' credit rating and liquidity provide confidence and flexibility for customers and suppliers.

Group revenue

H1 2016 v H1 2015



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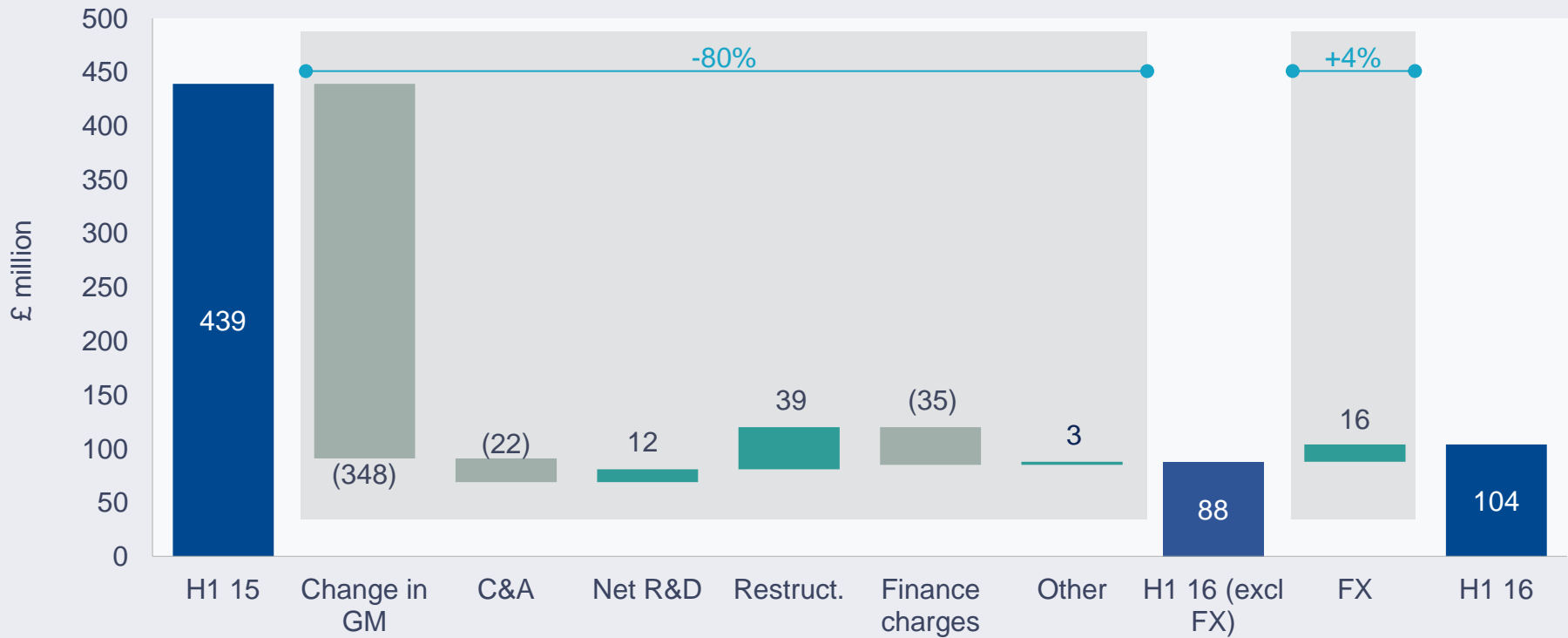
Start rebuilding trust and confidence in our long-term growth prospects

Group profit before tax

H1 2016 v H1 2015



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Group profit to free cash flow

H1 2016



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* Payments to defined benefit post-retirement schemes in excess of PBT charge

Foreign exchange

Transactional



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- \$35 billion GBP:USD hedge book provides ~6 years' cover
- Hedge book average rate is £/\$1.57

- Modest in-year benefits

Objectives of FX hedging policy

- Reduce volatility caused by FX movements
- Set maximum and minimum levels of FX cover
- Manage changes in forecast exposures

Foreign exchange

Other effects



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Translation benefit for full year*



~£600m benefit to revenue
~£60m benefit to PBT

Civil long-term planning rate change



added £2.1bn to order book
added £35m to Civil profit

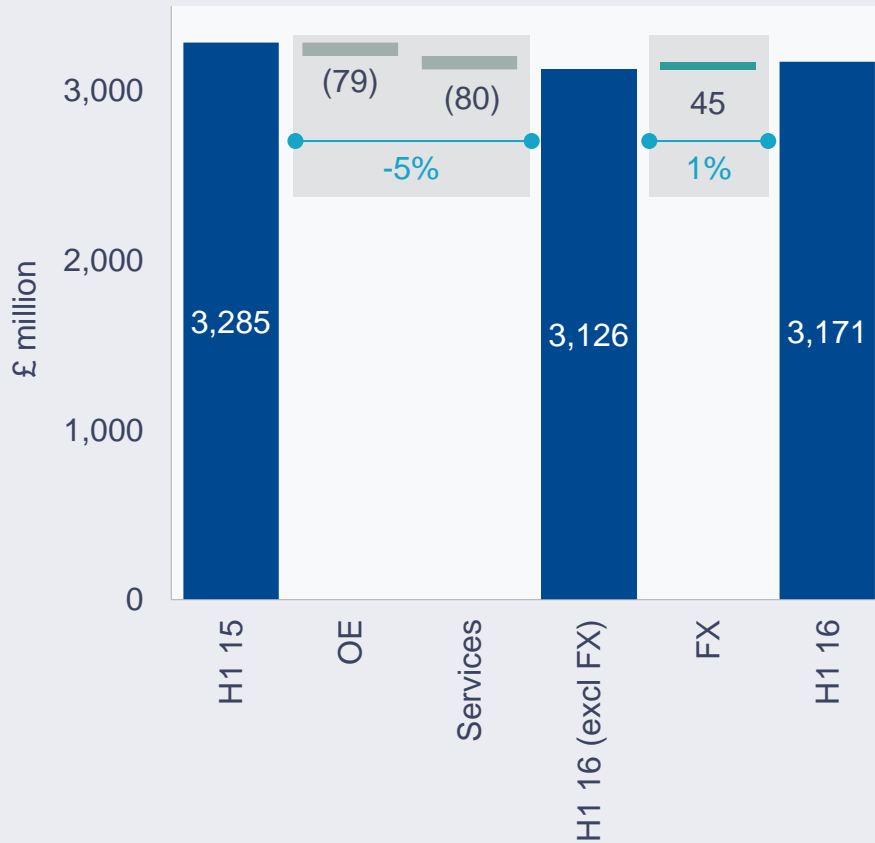
Mark-to-market impact on hedge book



reduced reported PBT by £2.2bn

Civil Aerospace

Revenue



- Reduced Trent 700 linked engines
- Weaker business jet volumes
- Increased volumes of Trent 900/1000/XWB
- Double digit flying hour growth on our in-production Trent fleet
- Reduced aftermarket revenues from legacy fleet & regional

Civil Aerospace

Original equipment revenue mix



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	H1 2015		Change at constant FX	yr-on-yr change	FX	H1 2016	
	£m	of whole	£m		£m	£m	of whole
OE	1,516	46%	(79)	(5)%	24	1,461	46%
Large Engine: linked and other	637	19%	19	3%	1	657	21%
Large Engine: unlinked installed	298	9%	13	4%	1	312	10%
Business Aviation	413	13%	(75)	(18)%	22	359	11%
V2500	168	5%	(36)	(21)%	0	133	4%

Civil Aerospace

Aftermarket revenue mix

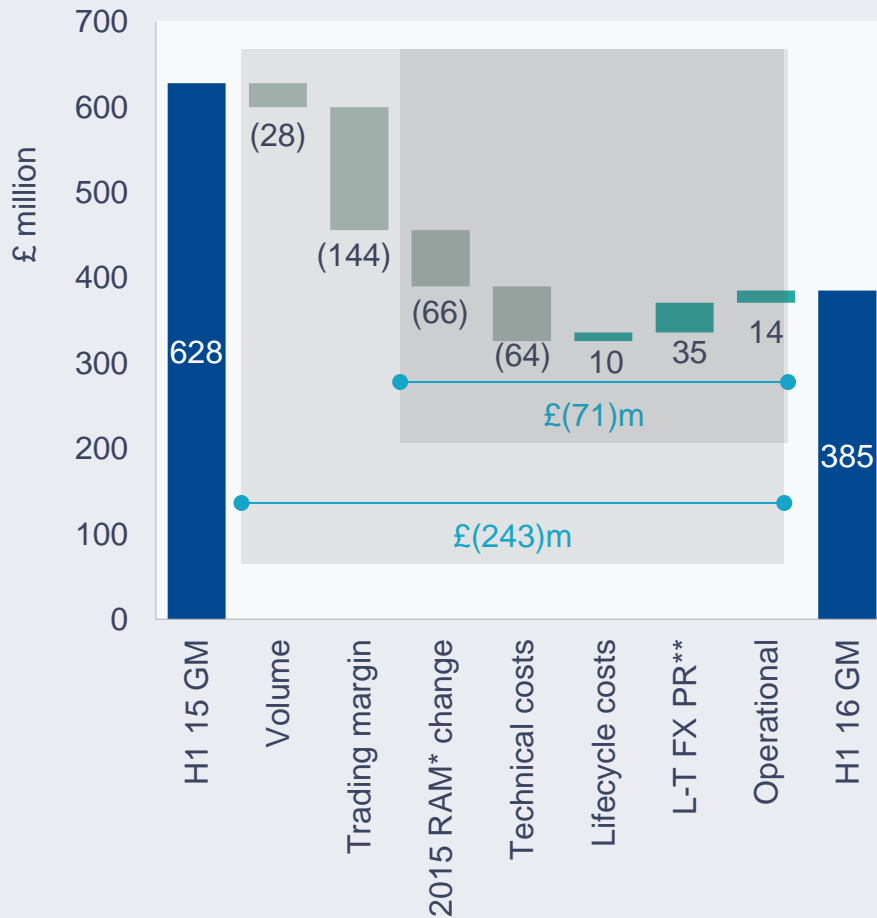


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	H1 2015		Change at constant FX		FX £m	H1 2016	
	£m	of whole	£m	yr-on-yr change		£m	of whole
AM	1,769	54%	(80)	(5)%	21	1,710	54%
Large Engine	1,094	33%	(66)	(6)%	3	1,031	33%
Business Aviation	219	7%	(2)	(1)%	10	227	7%
Regional	191	6%	(32)	(17)%	8	167	5%
V2500	265	8%	20	8%	0	285	9%

Civil Aerospace

Gross margin



- Reduced Trent 700 volumes and profitability
- Aftermarket headwinds on out-of-production legacy fleet
- Net £(23)m adjustments vs £48m in H1'15

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Deliver a strong start to our transformation programme

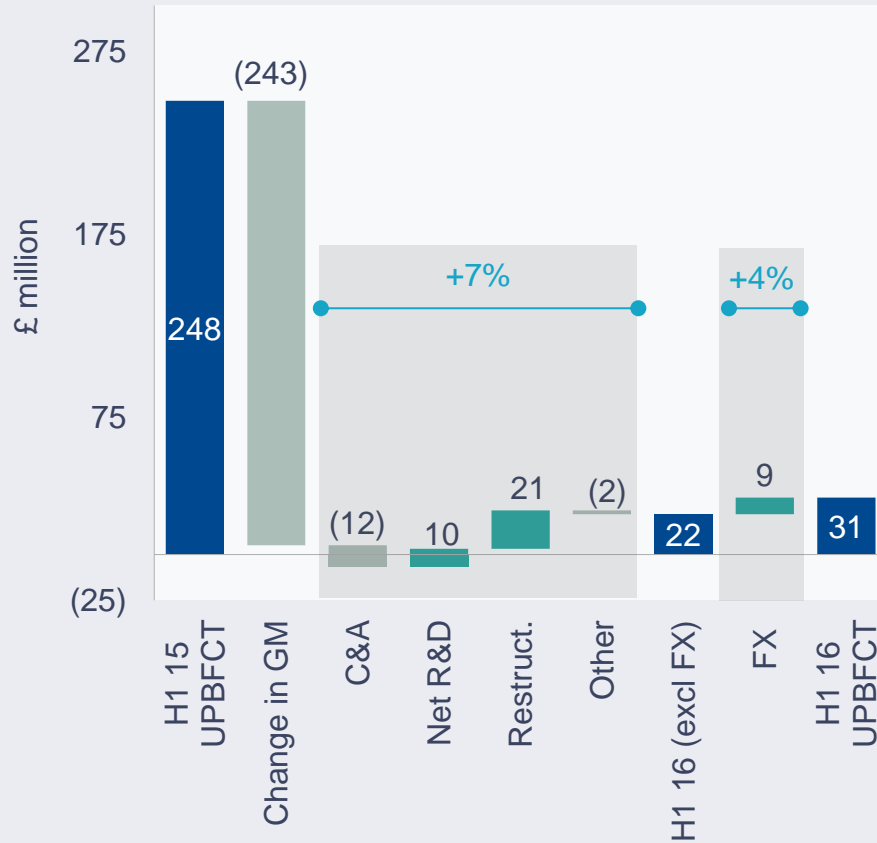
Start rebuilding trust and confidence in our long-term growth prospects

* Risk assessment methodology change

** Long-term FX planning rate change (USD)

Civil Aerospace

Profit



- Lower overall gross margins
- Higher C&A incentives accrual
- Lower R&D driven by capitalisation
- Lower restructuring charges
- H1-H2 phasing



- Continue to face headwinds in H2
- Expect a stronger performance overall in line with expectations
- Headwinds mitigated through increased deliveries, including profitable spare engines
- Positive results from our dedicated focus on improving lifecycle costs



Underlying revenues (1)%

- OE revenues +8%
- Services (6)%

Underlying profit lower

- Driven by gross margin
- Lower restructuring costs

Gross margin lower

- Adverse change in OE product mix
- TP400 programme

Outlook

- Supported by ↑ engine deliveries
- Additional actions underway to offset TP400 expenditure



Underlying revenues (3)%

- OE revenues (3)%
- Services (2)%

Underlying profit lower

- Driven by lower gross margin
- R&D reduced by 6%

Gross margin lower

- Adverse product mix
- Lower volumes

Outlook

- Order book resilience in key sectors
- H2 - cautious but positive outlook

Underlying revenues (25)%

- OE revenues (30)%
- Services (17)%

Underlying profit lower

- Driven by lower gross margin

Gross margin lower

- Lower volumes
- Partly offset by non-repeat of 2015 contract provision

Outlook

- Ongoing rationalisation
- Uncertain marketplace
- Further cancellation risks



Underlying revenues +14%

- OE revenues +27%
- Services +7%

Underlying profit lower

- R&D tax credit of £3m
- Indirect programme costs and performance incentives

Gross margin lower

- Adverse product mix
- Technical challenges

Outlook

- Focused on improving delivery performance

Technical factors for 2016



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Guidance at constant 2015 foreign exchange

	2015	2016 Guidance
Finance Charges	£94m*	£90m-£110m
Tax rate	24.5%	c.26%
Capital expenditure (Property, plant, and equipment)	£494m 4% of revenue	£500m-£550m
Net R&D spend	£831m 6% of revenue	~£900m
Free cash flow	£179m	£(100)m-£(300)m

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Start rebuilding trust and confidence in our long-term growth prospects

* 2015 excludes an underlying gain of £34m taken in 2015, on realised foreign exchange contracts settled to convert significant overseas dividends from group companies and is not expected to recur

Accounting under IFRS 15: background



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- 2 years to introduction: effective from 2018, with 2017 restated
- Introduces new accounting principles for revenue recognition
- Currently only tentative conclusions
- Consulting with other companies in the aerospace and defence sector
- Adoption of IFRS 15 does not change cash flow profiles

Likely key changes



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- No longer recognise contractual aftermarket rights (CARs)
- Linked accounting will no longer be applied
- Revenue will be recognised on an input basis

OE revenues and costs	➔	Recognise at time of sale
TotalCare services	➔	Higher margin over life of contract
Catch-up adjustments	➔	Expected to be smaller
Time and materials	➔	Largely unchanged

Balance Sheet

Restatement of Prior Year financials

- TotalCare debtor arising on concession deferral subject to transition adjustment
- CARs balance subject to transition adjustment
- TotalCare creditor adjusted to reflect profit and cash flow status of contracts as at 1 Jan 2017

TotalCare creditor

- Ongoing adjustments to recognise revenue/profits when taken at point of cost or service

P&L

OE gross margin

- Adjustment to concession deferral on new sales
- End of CARs on unlinked
- No amortisation of CARs

Services gross margin

- No amortisation of concession deferrals
- Revenue & profits recognised at point of cost/service event

Financial summary



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- Underlying performance in line with full year expectations
- Good progress mitigating key market-driven issues
- Strong cash performance

- In-year modest benefits from foreign exchange weakness

- Steady H1 order intake positions businesses well for remainder of year

Warren East

Chief Executive



Rolls-Royce

Goals for 2016



Rolls-Royce

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Many opportunities for improvement in each of our focus priorities



Rolls-Royce

Engineering excellence

- Focused on high performance power systems
- Leverage engineering excellence to build market share and long-life installed base

Operational excellence

- Manufacturing transformation to drive higher margins
- Sustainably lowering costs through continuous improvement

Leverage our installed base

- Performance critical assets provide the platform for value added services and systems
- Potential to leverage knowledge to drive additional value added for customers and build attractive margins

Many opportunities for improvement in each of our focus priorities



Rolls-Royce

Engineering excellence

Operational excellence

Leverage our installed base

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Opportunities for improvement in each of our focus priorities



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Engineering
excellence

Digital
Product
Definition

e.g. digital product definition

Optimisation of processes, methods, tools and organisation required to engineer our products

↑ 20%

improvement in time-to-market for new products from 2020

- Standardised digital definition...
 - enables efficient product development
 - simplifies processes and enables systems enhancement
 - leverages global engineering expertise & capacity

Opportunities for improvement in each of our focus priorities



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Operational excellence

Reduce lead times

e.g. Trent 1000 OE lead time improvement at Singapore

↑ 24%

improvement in lead-time with further ~17% planned

- Use of lean principles to eliminate waste
- Introduction of new technology to reduce cycle time
- Engagement of employees in the improvement challenge
- Learning being read across to Trent XWB, targeting 50% lead time reduction

Power Systems drive to maximise value from lean REMAN process



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Operational
excellence

Reduce
lead
times

e.g. Power System's REMAN operations lean flow line

↑ 35%

improvement in lead-time

- Restructured towards a lean flow line v 'box' or cellular approach
- Systems and supply chain developed to support just-in-time approach
- Lead time reduction of 35% - 40 day reduction to customer

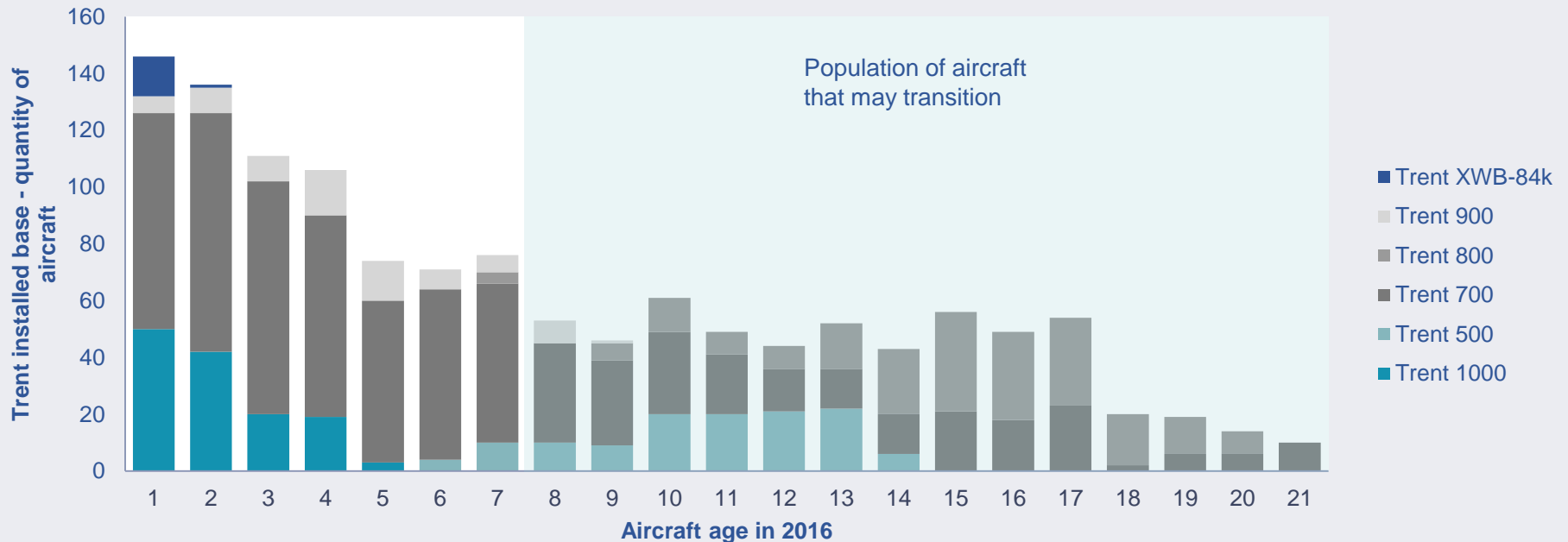
Maturing Trent fleet set to drive increasing number of aircraft transitions



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Leverage our installed base

Maximise value from time in service



Trent powered aircraft over 8 years old

230 in 2010

530 today

~900 in 2020

Strengthen our focus on engineering and operational excellence and leveraging our installed base

Deliver a strong start to our transformation programme

Start rebuilding trust and confidence in our long-term growth prospects

Dedicated resources to ensure an increased focus on aircraft transitions



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Leverage our installed base

Maximise value from time in service

↑ 160%

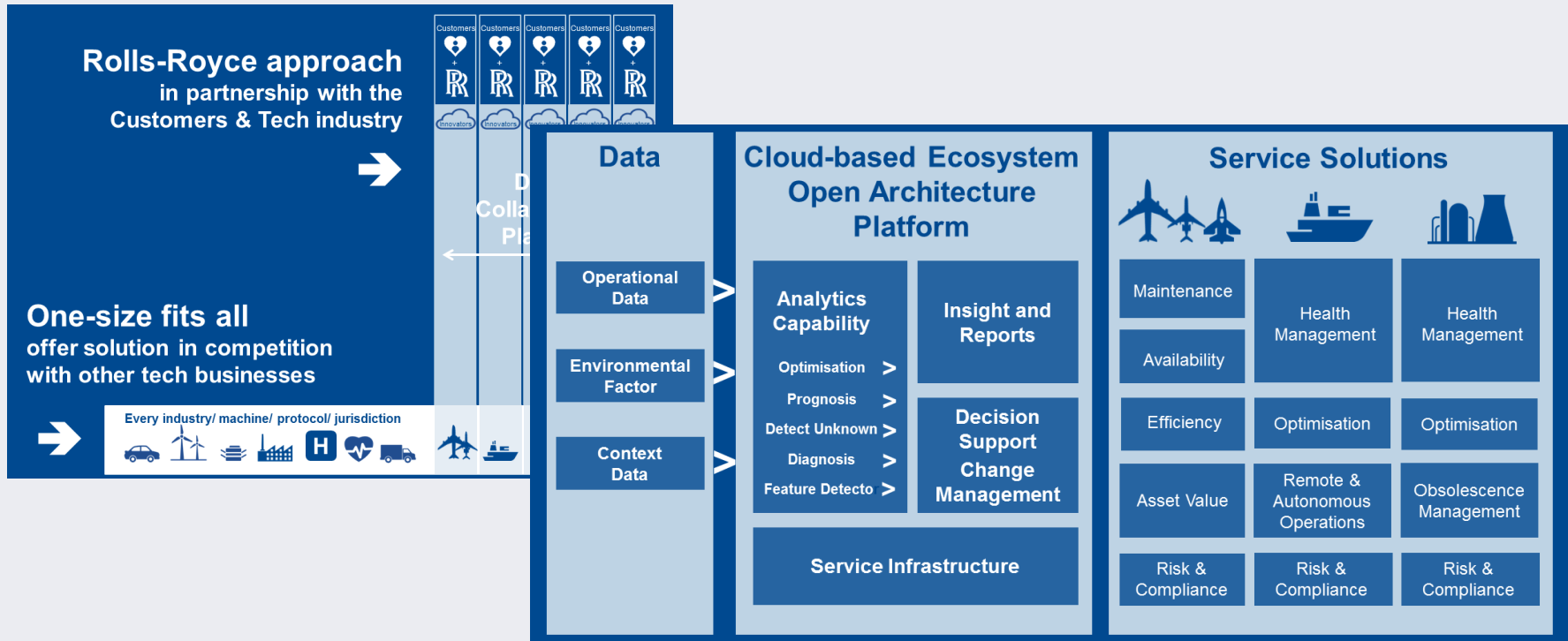
increase in successful Trent transitions compared to H1 2015

- Increase in Trent aircraft in transition inevitable driven by maturing fleet
- Dedicated team in place, evolving our services to meet customer needs
- 13 Trent powered aircraft successfully transitioned to new operators in H1 2016
- 28 additional Trent aircraft have next operators identified

Our Digital strategy harnesses best practice to add value to key customers



Rolls-Royce



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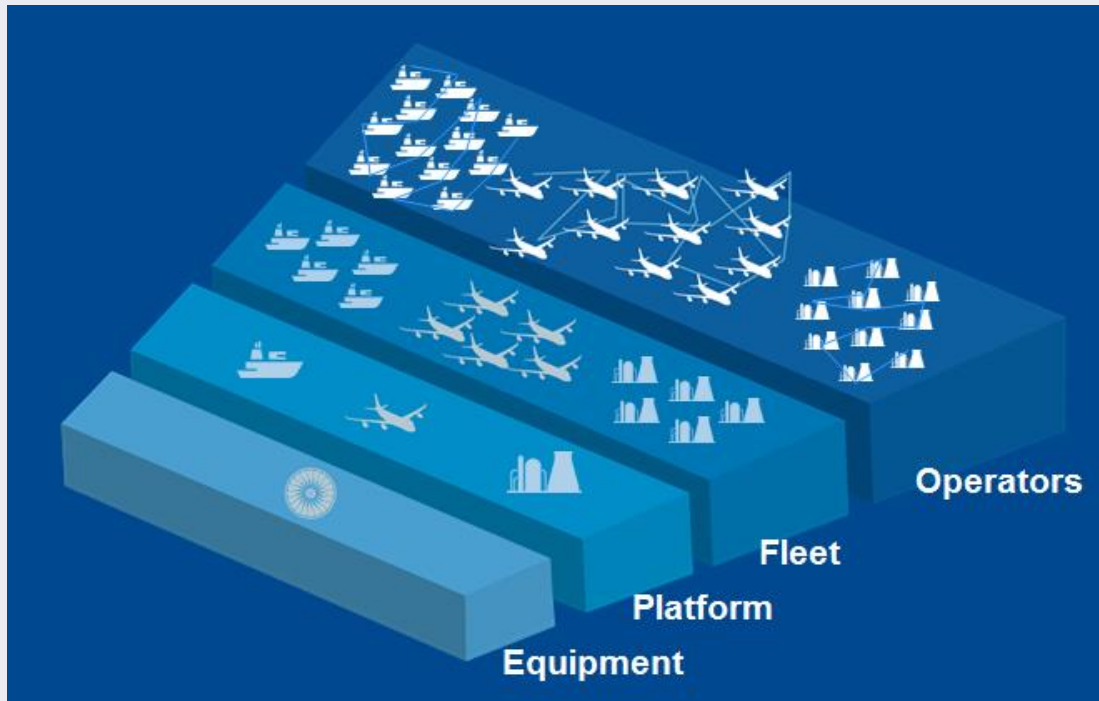
Singapore Airlines partnership



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Leverage our installed base

Digital



- Builds on leading Microsoft cloud and IoT platforms
- Drive benefits in fuel usage, route mgt and service support
- Applications in Marine fleet management as well as supporting Ship Intelligence projects

Acquisition of ITP is an opportunity to consolidate aftermarket value



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Leverage our installed base

Reduce margin leakage

> 10%

increase in Engine Flying Hour revenues retained from key Civil programmes from 2017 onwards

- Partner on TP400 and EJ200
- Leading RRSP on key Civil growth platforms, including Trent 1000, Trent 7000 and Trent XWB
- Strengthens position on several key aerospace platforms as they start to generate aftermarket cash flows

Legacy Issues



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Co-operating with
authorities including
UK & US

Significant actions to
improve ethics/ABC culture
& processes

Zero tolerance to
misconduct

Second half priorities



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Strengthen our focus on engineering and operational excellence and leveraging our installed base

Deliver a strong start to our transformation programme

Start rebuilding trust and confidence in our long-term growth prospects

- Deliver on customer commitments across all businesses
- Maintain progress on transformation
- Sustain the open conversation we started with investors and analysts
- Continue to focus on our three strategic priorities to drive value



Rolls-Royce

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Q&A

Warren East, Chief Executive
David Smith, Chief Financial Officer

...with a focus on pace and simplicity



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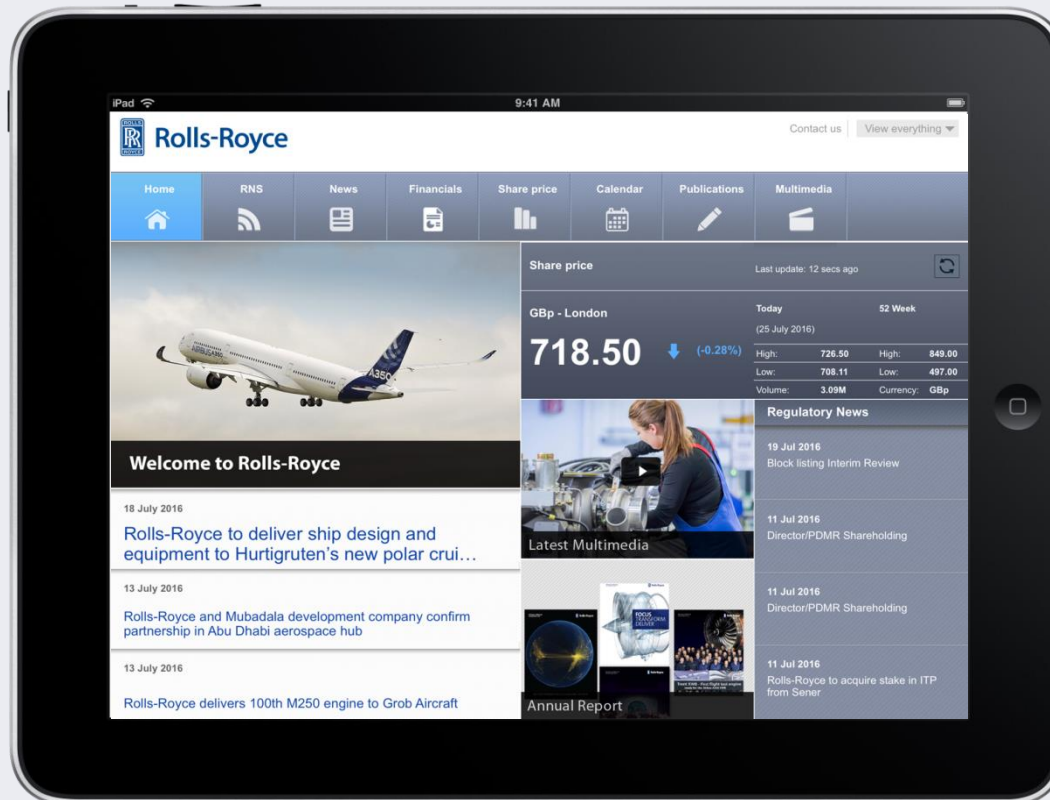
For more information: www.rolls-royce.com/investors

Investor iPad App



Rolls-Royce

Available as a free download from iTunes



Safe harbour statement



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This announcement contains certain forward-looking statements. These forward-looking statements can be identified by the fact that they do not relate only to historical or current facts. In particular, all statements that express forecasts, expectations and projections with respect to future matters, including trends in results of operations, margins, growth rates, overall market trends, the impact of interest or exchange rates, the availability of financing to the Company, anticipated cost savings or synergies and the completion of the Company's strategic transactions, are forward-looking statements. By their nature, these statements and forecasts involve risk and uncertainty because they relate to events and depend on circumstances that may or may not occur in the future. There are a number of factors that could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements and forecasts. The forward-looking statements reflect the knowledge and information available at the date of preparation of this announcement, and will not be updated during the year. Nothing in this announcement should be construed as a profit forecast. All figures are on an underlying basis unless otherwise stated. See note 2 of the Financial Review for definition.