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# Serco reports better than expected trading and positive outlook lead to increase in full year guidance

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*Full report from Serco*

## As a result of stronger than expected trading in the first four months of the year, along with a positive outlook for the balance of the year and favourable foreign exchange movements, Serco is today issuing an unscheduled trading update and revised guidance for 2022. Serco will publish results for the first half of 2022 on Thursday 4 August 2022. In the following statement, all numbers are quoted in constant currency unless otherwise indicated.

Increased Underlying Trading Profit expectation for 2022

We now expect Underlying Trading Profit (UTP) to be around £215m on a constant currency basis (2021: £229m), an increase of about £20m versus prior guidance.  In addition, at current exchange rates, we expect favourable translation movements to increase UTP by around £10m.  We therefore revise reported UTP guidance upwards by £30m to around £225m, approaching the level achieved in 2021.

First half

Trading in the first four months of the year has been stronger than we expected, with all regions performing above their budgets, and three of the four delivering higher profits than last year. Our work on the UK Test & Trace programme ended in April and, as a result, related revenues are likely to be about £220m lower than in the first half of 2021. However, we now expect to be able to largely replace this with other government work around the world, so Group revenues in the first half are likely to be at similar levels to last year, at a little over £2bn.

This would represent organic growth for the Group excluding UK Test & Trace of around 8%. Margins in the first half are likely to be stronger than we previously expected, at over 5%. Reported UTP is expected to be at similar levels to the prior year, notwithstanding a near £30m drag on first half profits from a combination of the Atomic Weapons Establishment contract, which ended in June 2021, and the wind down in UK Test & Trace. The pipeline of new opportunities remains strong.

Our North America business is expected to have a strong first half, helped by good organic growth in our Federal Civil sector and improved margins in Defence, which have been improved by the acquisition of WBB in April 2021. In Australia, we expect to see good profit growth in the first half, with revenues similar to 2021, but higher margins as a result of strong trading in Immigration, Facilities Management and Defence. We are also likely to report improved margins in the Middle East business, with profits at similar levels to last year despite a reduction of around 35% in revenues as a result of the loss of the Dubai Metro contract.

In the UK & Europe, despite a £220m reduction in Test & Trace revenues, we expect first half revenues to be only about 5% lower than the prior year, at around £1bn. This reflects strong growth in other work, including: Immigration-related revenues, which are likely to around £100m higher than the prior year; the DWP Restart programme; and smaller increases in Defence, Transport and Leisure. Margins are expected to be lower than 2021 as a result of the near £30m drag on UK&E profits from AWE and Test & Trace referenced above.

After distributing dividends of £20m to shareholders in the first half and spending in the region of £30m on share buybacks, we expect net debt at 30 June to be around £170m, compared to £178m at the start of the year. Our leverage is likely to be at similar levels to the 2021 year end, and well under 1x Net Debt to last 12 months' EBITDA.

Full year 2022

We now expect reported revenue of £4.3bn-£4.4bn in 2022 as a whole and reported Underlying Trading Profit of around £225m, significantly ahead of our expectations set out at the time of our full year results in February, and approaching the levels reported in 2021. Revenues in the second half are expected to be similar to the first half, with the year-on-year reduction of £260m of Test & Trace revenues being offset in large part by increases in Immigration and other programmes around the world. Overall, we expect organic revenue growth excluding UK Test & Trace to be about 6% in the second half. As in 2021, we expect second half margins to be lower than those in the first half due to seasonality and mix.

Serco is well protected against inflation. Although it is hard to forecast the precise impact on revenues and costs, the nature of our contractual arrangements with our customers means we do not expect costs to increase faster than revenues, although there will be timing differences between indexation and cost increases.

Our latest guidance for 2022 is:

| | 2021 | 2022 | |
|---|---|---|---|
| | Actual | Previous guidance | New guidance |
| Revenue | £4.4bn | £4.1bn-£4.2bn | £4.3bn-£4.4bn |
| Organic sales growth | 10% | ~(8)% | ~(5)% |
| Underlying Trading Profit | £229m | ~£195m | ~£225m |
| Net finance costs | £24m | ~£25m | ~£25m |
| Underlying effective tax rate | 24% | ~25% | ~25% |
| Free Cash Flow | £190m | ~£100m | ~£120m |
| Adjusted Net Debt | £178m | ~£220m | ~£200m |

NB: The guidance uses an average GBP:USD exchange rate of 1.26 in 2022 and GBP:AUD of 1.79. Net Debt guidance includes the £90m share buyback programme. We expect a weighted average number of shares in 2022 of 1,203m for basic EPS and 1,224m for diluted EPS.

Commenting on today's update, Rupert Soames, Serco Group Chief Executive, said:

"We have had a strong start to the year, and it is pleasing to be able to increase reported profit guidance to levels approaching last year's. To deliver this outcome, we are having to replace with other work some £500m of revenues and over £60m of contract profits from the ending of Test & Trace and of the AWE contract. We are able to do this because customers rely on us to deliver their critical programmes, and this has driven strong order intake over recent years on contracts that are now delivering revenues and profits. This is testimony to the effectiveness of our unique Business-to-Government platform, with its international footprint, its resilience, agility and efficiency, which allows us to respond rapidly to support the ever-changing priorities of the many governments we serve."