5. Embed disciplined financial and risk management

Improving cash flow

The group's capital allocation and contract review processes have been strengthened to ensure that all investment opportunities compete for capital in a single 'pool' and are evaluated against a stringent set of economic and risk criteria.

2014 highlights

£526m
Cash generated from operating businesses in 2014

£553m
Total cash generated from continuing operations in 2014

£1bn
revolving credit bank facility refinanced in January 2015

c.200
contracts across the group reviewed by the CFO on a quarterly basis

2015 priorities

- Improve cash generation

Achievements

Operating cash flow

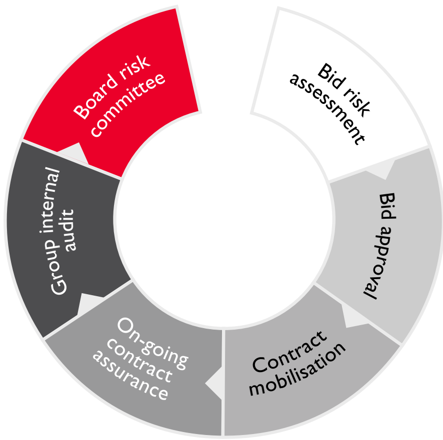
In 2014, we made a material change to the cash measure used in budgets, monthly reviews, long-term business and incentive plans, to deliver free cash flow after working capital. Our performance management cycle around cash flow has also changed. Our debtors sales outstanding (DSO), based on revenue for the last 90 days of 2014 was 48 days and there are many businesses where there are opportunities for improvement. We have moved the monitoring of cash and cash collections from monthly to weekly, and moved the collections agenda beyond finance by engaging the business in cash collections. We also need to be more disciplined about commercial terms for receivables, drive better terms from our supply chain through the new procurement processes and to reduce the time from event to billing. On average across the group we bill in 13 days, and as with DSO, there is considerable variation in the timeliness of billing across the group.

We are developing a programme across the global finance and commercial communities to systematically look at both the order to cash cycle, and the procure to pay cycle and analyse the systemic root causes that affect cash flow and then drive improvement, based on this root cause analysis.

Contracts, risk management and delivery assurance

We now have enhanced contract management processes in place across the group. There are clear reserved powers for the approval of contracts at group executive committee and board level to approve bidding for major, complex contracts and all material contracts with low profitability are subject to review at regional, group or board level, as appropriate, 29 contracts went through this process in 2014. For more detail please see the risk management section on page 42.

Contract risk management and governance model



We have also introduced a 360-degree model for ongoing contract assurance ("Contract 360"). As the name implies, this brings together a review of the financial, commercial, legal, delivery and reputational risks in taking on work for a customer and means that there is a holistic view of contract risk, both before we commit and during the contract life cycle. Then, during contract execution, amongst other things, we review the progress on delivery commitments made and we monitor customer satisfaction as well as commercial and financial performance. Contract 360 is well developed and embedded in our UK business and will be progressively implemented across all regions in 2015.

In terms of the broader contract portfolio, every quarter the finance organisation reviews the financial performance of all the major contracts, and the CFO performs a top-level review of the top 200 contracts across the group each quarter, equivalent to around a third of group revenue. These contract disciplines give us early sight of emerging contract issues, and the Contract 360 review process enables us to develop the appropriate commercial and legal strategy and ensures that the accounting is sound.

Capability building

These contract management changes would not be possible without capable people and effective processes, in finance, risk management and control. In Audit and Risk, we have appointed a Head of Global Risk and Audit. In finance, we have four new regional CFOs and a new group Financial Controller. Together with their teams they have significantly improved our internal financial reporting. We have a much more rigorous monthly and quarterly close process, monthly reviews through group finance that focus on quality of earnings, as well as enhanced processes around balance sheet integrity and control.

Regional Risk and Audit Committees

We also introduced regional risk and audit committees across the group, and these bring together the ongoing risk management agenda in the region, compliance matters, issues arising from internal and external audit, and an ongoing review of any issues requiring judgement. They are chaired by the Regional CEO and include representatives from group as well as Regional Finance, and are also attended by our external auditor.

The Regional Risk and Audit Committees are now a core part of the governance processes within the group. Together with the other changes discussed above, they provide an enduring platform in risk management and controls and have resulted in significant strengthening of the stewardship in the group.

Capital discipline

We believe our new approach to capital discipline is working; one single capital pool; a minimum 10% post-tax internal rate of return on all investments; a group wide investment committee that oversees both revenue and capital investments; and rebalancing capital away from acquisitions to organic capital investment. The more rigorous process around capital discipline was reflected in £138m capital expenditure (2013: £178m) down 22% from 2013. The lower spend is also a deferral of spend into 2015 as we bring some capital investment under the global IT, shared service and other programmes.

Restructuring

In 2013, we invested £63m to reduce costs, mainly in the UK and Europe. New areas of opportunity identified in 2014 accounted for a further £29 million charge. These programmes were essential in strengthening our competitive position, principally in the UK and in Europe. In the UK cash solutions business, we have reduced our branch footprint by 20% and headcount by around 10%. In Europe, we have consolidated our regional HQ in Amsterdam, consolidated our operations in the Netherlands and Belgium, and across the group funded some modest de-layering of duplicated or overlapping management and supervision.

Balance sheet

The board remains committed to maintaining a strong balance sheet with the long-term net debt to EBITDA ratio of less than 2.5 times. At the end of 2014, the net debt/EBITDA was 2.8x – a little higher than our long term aim mainly because of the payment relating to the UK electronic monitoring contract settlement. The group's revolving credit bank facility was successfully refinanced in January 2015 with improved pricing, terms and conditions achieved. The new facility is a five-year £1 billion committed facility provided by a consortium of leading international banks. Our unutilised but committed facilities at the year end were £998m. We continue to be soundly financed and have good access to capital markets as demonstrated by the recent renewal of the revolving credit facility.