



Q4/full year Fiscal 2019 results conference call transcript

Attendance List: Ken Gregor
Ben Birgbauer

Title of Meeting: Q4 and full year Fiscal 2019 Results Call

Hosted By: Ken Gregor

Coordinator Ladies and gentlemen, good day and welcome to the Jaguar Land Rover fiscal 2019 quarter four and full year earnings conference call. We have with us today Mr. Ken Gregor, Chief Financial Officer, Jaguar Land Rover; and Mr. Ben Birgbauer, who is Treasurer at Jaguar Land Rover.

As a reminder, all participant lines will be in listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Please note this conference is being recorded. I will now hand the conference over to Mr. Ken Gregor. Thank you and over to you, sir.

K. Gregor Thank you and good afternoon, good morning to everyone and thank you for taking the time to join us on our Q4 and Full Year Results call. As normal, I'll run through the material. I'll try not to read every word on the slide and skip past a few in order to give us time for some Q&A at the end and mostly try to hit the highlights and I'll refer to the slide numbers, imagining that many of you will have had the chance to read them.

So, just starting off, slide 3—really just excited that we have a strong product pipeline that gives us every possibility of rejuvenating our sales performance. The I-PACE has won many awards around the world for our first battery electric vehicle, which we're really proud of. Really excited we have a new XE, a refresh that gives us the chance to drive some momentum there, and an all-new Evoque, which was incredibly important vehicle for us in the first iteration, rolling out sales across the world and we'll see a new Defender, produced in Slovakia, later this year. So a lot coming in our product pipeline.

Turning to slide 4, Q4, we have a profit of £269 million before exceptional items, so good that we returned to profitability in Q4. That was an EBIT margin of 3%, on the back of retail sales of 159,000 units.

Obviously, because of the losses that we've previously announced in the first nine months of the year, the full year remains a loss, now £358 million before exceptional items and obviously, as we know we have the exceptional items of the impairment in Q3 and we have a further exceptional item of £149 million of restructuring costs in Q4.

China joint venture on slide 5, tough year because as I'll talk about and as we talked about in the last call, many of our challenges stem from the performance of the business in China. Basically we saw break-even results for the JV in the full year last year with a loss in Q4.

Turning to the volumes, slide 6, and these are the full-year volumes overall. We finished at 578,000 units, down about 6% on the prior year. Actually, within that, some real bright spots. The US up 8%. The UK up 8%. Overseas up 2%. Europe, although down 5%, still our second biggest region with really healthy volume. So actually, some balance of some quite positive performance in some regions, but China at 99,000 units, down 34% compared to the prior year, is really what's driving the full year down 6%.

By product, on slide 7, a positive story here is our new products continue to provide growth, E-PACE, I-PACE, Velar, the '18 model year refresh of Range Rover and Range Rover Sport, all moving us forward. However, some product ageing on other vehicles and the impact of the challenging market conditions in China and the run out of the Range Rover Evoque impacting the Range Rover Evoque and Discovery Sport.

Slide 8 has a bridge full year to full year. You can see the impact of the volume reduction – the wholesale volume reduction – results which also included reducing dealer stock, and hence the wholesale volume is down 68,000 units, which is bigger than the reduction in retail volume year to year. And we saw higher variable marketing expenses during the year in more competitive market conditions, including the impact of the price compensation in quarter one of last year associated with the duty price change in China.

On the contribution cost side, net headwinds here, but some positives in TVM (Total Value Management) material cost reductions £200 million, helping to partially offset raw material costs, model year cost increases, higher warranty accruals, and some other factors. And on the structural cost side, depreciation & amortization continuing to grow during the full year, partially offset by fixed marketing and other admin and selling savings coming through on the back of project Charge, where we're really pushing to drive cost reductions across all areas of the business.

FX was net positive for the full year, mainly due to the roll off of hedge losses versus this time last year. But all of that taking us to a loss of £358 million.

Slide 9 describes the mostly positive story between quarter 3 and quarter 4, returning to profitability, stronger volume, material cost reductions, structural cost reductions, and helped by some tailwinds on the foreign exchange side, all of that moving us back into profit in Q4, which as we were expecting, but it's also good that we achieved it.

Slide 10 talks to the substantial positive cash flow that we saw in Q4. Q4's cash flow was £1.4 billion inflow, helped by a very significant contribution of working capital, £1.3 billion, a big chunk of that being

normal seasonal rewind of payables. Also driven by a good reduction in inventory levels, partly seasonal, partly as a result of the extra actions we've been taking via project Charge to reduce the inventory levels within the business, given to drive cash flow. So all of that driving that £1.3 billion and what's also nice to see is working capital overall for FY19 because we've been driving that resulting in £400 million positive working capital for the full year.

But, sadly, in the full year, given the cash outflow that we'd had in the first nine months, the full year then coming to a £1.3 billion cash outflow.

Investment spending was £3.8 billion. We had initially guided the full year to spend £4.5 billion. When we launched project Charge, we said we wanted to be no more than £4 billion and we actually managed to come in at £3.8 billion, so overall a £700 million reduction in investment spending compared to what we were originally planning, which was good and really helped offset some of the challenges on the profitability side that we experienced last year and helping to mitigate the impact on the cash flow, really coming through a real focus on efficiency, a focus on timing of spend, moving things out where we didn't necessarily need to do some things. We stopped a number of smaller projects and non-core, non-product projects, but we maintained the investment in our core product portfolio and our core vehicle plans because those remain the lifeblood for the future. So we fought very hard this year to maintain that investment in those products, at the same time as reducing versus what we were planning.

Slide 12, still healthy liquidity, £5.7 billion, taking into account that cash inflow in quarter four and the undrawn revolving credit facility that we have around us and still a reasonably well spread maturity profile obviously coming in front of us.

Slide 13 talks to financing, so we thought we'd include. Perhaps we'll ask Ben to talk to it just quickly.

B. Birgbauer

Sure, Ken. This just shows that, as Ken said, we did end up with £3.8 billion of cash and £1.9 of an undrawn revolving credit facility, so total liquidity of £5.7 billion and that actually was 15.6% of revenue, so it is around the target we generally guided to. We did actually issue £1.2 billion of new debt last year, between the bond we issued and the syndicated loan that we completed, and that largely did cover the negative cash flow that we had last year, but didn't cover the \$700 million bond maturity.

Looking ahead, we just laid out what our thinking is on funding plans going forward. So we did actually complete a new \$700 million receivable facility at the end of March, but we didn't actually draw on it. It replaced a prior facility we had, which had about \$150 million drawn on it at the end of the quarter, so that's why we're showing the improvement in funding from that will be £425 million of incremental funding.

There is a little note here that also the accounting treatment is going to change. It has true sale treatment on the receivables. So the original \$150 million of funding we had at March, plus the incremental funding going forward, will be off-balance-sheet and not counted as debt, but it was accounted as debt at the end of March.

Then we're just saying that we're looking at other things to fund the business, so one of them is export credit agency funding and we're in discussions with a couple of agencies. One of those discussions is more advanced, although we're still in negotiations, so nothing to say in terms of anything being completed on this front yet, but we are working on it.

We are looking at some finance leases, probably small amounts, let's say, £100 million to £300 million maybe of finance leases that we're looking at doing, for facilities that are suitable for that. We will continue to look at the bond market and potentially coming back to the bond market at some point. Our bonds are trading significantly better than they were earlier in the year and we'll need to continue to take a pulse on whether that might enable a bond issue this year.

We did just note that in terms of maturities, we have a fairly light maturity schedule, one \$500 million facility in November and then another \$500 million bond in March that are maturing to cover.

And that's it.

K. Gregor

Thank you, Ben. Just turning to strategy and outlook, slide 15. I guess slide 15 just alludes to obvious challenges around various geographies, whether it's the US incentives and tariff risks, whether it's the UK with Brexit uncertainty unfortunately continuing, or whether it's China, where we see continued macro headwinds.

At the same time, there are positive factors: strong SUV demand in the US. Actually in the UK we've been outperforming the industry. And in China, the premium demand has held up overall, although as I'll talk about, there are some challenges there. So a challenging external environment, I think is the case.

Against that environment, we're really focused on our turnaround and transformation plan, underpinned by strong product pipeline, underpinned by project Charge to reduce cost, improve profits and cash flow, and in the longer term we have project Accelerate to help drive our robust long-term business structure and address some of the underlying issues that we need to focus on.

Slide 18 gives a sense of the continuing, developing product portfolio, with the addition of the Defender. Slide 19 showcases the I-PACE. European car of the year is something we're really proud of. Jaguar's never won that award before, so that's really quite something. And the sales development's starting to grow. I think that's something we're really looking forward to, seeing how that develops over the next 12 months.

The all-new Range Rover Evoque is on sale, as I said before. That was such an important vehicle for us when we launched it originally in 2011 and this all-new vehicle moves it forward in refinement, in ride and handling, in interior comfort and luxury. In many, many ways, it's a super replacement, all-new replacement vehicle, and brings with it plug-in hybrid and improved CO₂ technology options as well. That's rolling out across markets around the world from now, so we're really looking forward to seeing the sales development of that vehicle also.

And then of course, actually, something we're really excited about, having finished production of the old Defender 2015. It's been a bit of a wait, but we're truly excited to be revealing the all-new Land Rover Defender later this year. And, as I say, production will start in Slovakia. So, looking forward to that.

And it doesn't stop, on slide 22 we have refreshes and replacement models planned across the model range and a couple of all-new vehicles we haven't talked about yet. So, lots to look forward to in our product pipeline and electrification plans, which are critical for our future and hence why we fight for every penny to continue making those important investments in those vehicles and technologies.

Turning to a couple of the market focus areas, we thought we'd give an update on China, as well as a little bit of a deeper dive on the US. On China, slide 24 talks to the premium market. Still growing in China, but at a slower rate and the overall car industry actually reducing over the last four quarters. Within segments, some of the larger vehicle segments slowing a bit more than the smaller vehicle segments, which still grow. And those factors are definitely having an impact on our business.

Incentive levels, which is the lower left-hand chart on slide 24, appear to have stabilized, but perhaps a bit early to say whether they start to recover from there.

Our own market perspectives – on our own metrics on slide 25, most showing a positive development, perhaps a stabilization. I think it's fair to say, I think we feel very much more to do on driving retailer profitability to continue to improve that. It's good to have retailers who are making money. Then obviously, they're far more supportive of our business in China. Part of that is continuing to drive down the inventory level. We've made some progress, but more to do. So we're on track for that. Some stabilization of the metrics and some more to do.

Turning to the US. I guess we wanted to highlight the US; it's actually a really large—it's our largest region in terms of the last year's volumes. It's a stable premium market and the shift to SUVs and trucks, which are highlighted on the lower left-hand part of slide 26, is a favourable factor for our business and helps drive profitable business for us in the US, providing good contribution towards our fixed costs with 17 million units overall in the industry being pretty stable over the last five years.

Slide 27 shows the volume development growing from 71,000 units to 126,000 units over the last five years, so we really managed to grow our market share in the US, with our new product introductions. You can see the balance between Jaguar and Land Rover in the right-hand top bar. And you can see some of our market shares shown there.

In terms of slide 28, talks to the pricing situation in the US. It's definitely a very competitive market from an incentive point of view and what you see on these slides is industry—on the lower left-hand chart—industry incentive levels generally rising over time. You can see our Land Rover incentive levels rising over time, but still significantly lower than the average of the industry. And you can see that we've managed to reduce the level of the incentives on the Jaguar side of the business.

So, a competitive market with rising incentive levels, but overall because of our strong Land Rover business, a bit lower than the average. And the other parts of slide 28 alluding to positive EBITDA from the US markets at a rate that's only a little bit lower than the average of the entire Jaguar Land Rover business.

Slide 29—we've been working with our retailers to really roll out what we call our ARCH dealer network identity and infrastructure and you can see there are a range of facilities across the US that really state-of-the-art, really nicely branded, showcasing both brands really well, with advanced service facilities. We're doing that hand-in-hand with our retailers who are overall profitable in the US, which is a good and healthy situation to have. And it's underpinned by good financial services arrangements that we have in place also with the retail finance partnership with Chase, which we've now had for over ten years, which is great.

Slide 31 talks to project Charge being on track in terms of its delivery. Investment, as I already said, we underspent by more than we were planning for FY19. On working capital, we're being a bit conservative in terms of what we're calling. We're calling full year working capital benefits £0.4b, but actually, second half, we drove £800 million of inventory reduction in the second half of FY19, contributing to the really strong cash flow in Q4, so we're pleased about that.

Cost savings take a little bit longer to come through the income statement. Maybe £150 million in FY19, but more to come in FY20 on material costs and certainly more to come on the employment cost reduction, given that the majority of the workforce reduction was completed at the end of March, so then we start to see the savings thereafter. So we'll keep working through that.

Slide 32, I think we continue with project Charge. That's for sure. Keep focusing on product investment, basically on track, of course. On track in FY20 to spend less than £4 billion again, thereby delivering on the second £500 million of the investment reduction plans that we targeted. On working capital, £100 million to £200 million of further working capital improvement through lower inventories being targeted. Circa £400 million of labour and salary cost reductions from the 6,000-odd people

that we reduced over the last six months on an annualized basis, and further cost and efficiency reviews across all areas of the income statements, including on the material cost side, we're very much pushing TVM approach, supply negotiations, and cost benchmarking and feature and specification changes to drive cost down.

And with that focus moving towards also project Accelerate on slide 33, focusing on launching our products on-time, improving our quality, deliver competitive material cost, and at both our dealers and from ourselves to really enhance our sales performance and experience for our customers.

And that really brings to slide 34, the end of my pitch. Provides some updated guidance here to how we see the outlook going forward. EBIT margin for FY20 in the 3% to 4% range, positive PBT, investment spending around £4 billion, negative cash flow and also to say we do expect also to see negative cash flow in FY21.

Some factors around that, in FY21, we have some important model changeovers happening and that will make it a year of transition, a year of change, with a solid chunk of investment spending in those new models and some volume interruption caused by the model run out and model run in and model ageing. All of that's normal. It will just provide challenge through FY21 and into FY22 as we move forward. So, expecting that and planning for it.

And back into FY20, we expect to see a loss in Q1, so I thought it's important to point out that some of the further de-stocking that we've been doing has continued into quarter one to reduce inventory levels and reduce our production levels. And we also have an extra week of plant shutdown for potential hard Brexit protection, in addition to normal production sales seasonality in Q1. So, we'd also expect to see negative cash flow in Q1 with some of the normal seasonal working capital movement. So, just wanted to point that out. We'd expect to see profit in the subsequent quarters and improving cash flow also.

With all of that, I want to say thank you. Just one more note—you might have picked up on it or might not. But this will be my final investor presentation and results conference. After 11 years as CFO, which is a good chunk of time, it's definitely from my point of view, time for me to go and take on a new challenge elsewhere and really thank you for all your support and for the Jaguar Land Rover business over this time. I love the business and we have two really strong brands and lots of positive plans for the future and our new products.

We announced yesterday that I would be stepping down as CFO after 22 years with the business and we announced that my successor will be a chap called Adrian Mardell, who's worked in the business for 29 years. He's been in the past Deputy CFO. He's presently our Chief Transformation Officer – I really welcome him and wish him all the best. He'll be able to hit the ground running when he starts, which we will hand over at the beginning of June.

With that, I think we pause there and have the opportunity to do a few questions.

Coordinator Thank you very much. We will now begin the question and answer session. Please stand by for your first question.

First question is from Phil Baggely from BAML. Please go ahead.

P. Baggely Hi, everyone. Thanks for the presentation. My question is, I wanted to ask, just on project Charge, about the savings from the headcount reductions. I see £400 million from 6,000 people. I thought that was quite a lot per head, even if I account for employee national insurance and so on. Can you give us a little bit more detail around that, please?

K. Gregor Yes. In terms of the overall mix, it—sorry, just hang on a second—it kind of averages out circa £65,000 per head, per person, on average across the entire 6,000 people. There were about 1,500 production employees there, and our production employees when you include shift premia, overtime, and employer's and employee national insurance and pension contributions, that certainly perhaps gives a higher cost per person than you might otherwise appreciate.

Through the 4,500 of staff reductions, those occurred at all levels across the grade hierarchy, including in our senior leadership team, so when you take into account all of that, it mixes out with a fairly – not far off, actually, our average cost per person, to be perfectly honest with you, but that's roughly how you get to £400 million. And I'm talking about a full year annualised figure here.

P. Baggely Sure. I appreciate that. I guess we'll see half or so, I guess in 2020. And then, how else do you think about the bridge from FY19 EBIT margin minus 0.7%, I think, to the 3% lower bound of the guidance? If those cost saves are about 100, 150 basis points or so on a reported basis, what would the bridge be? What would the balance be?

K. Gregor I'm not quite following you there.

P. Baggely If there's in 2019, I think, the EBIT margin was negative 70 basis points and then guidance for 2020 is 3% to 4% EBIT margin. If those cost saves in terms of headcount we saw—

K. Gregor I'm back with you again. I wasn't sure if you were asking about FY19 or FY20. As we look into FY20, there are a number of factors that we are going to build on. We definitely look to some not huge, but modest, profitable volume growth that should drive improved operating leverage in the year and that contributes improvements to EBIT margin.

We look to the cost reductions to drive lower employment cost as a percentage of revenue, lower material cost as a percentage of revenue, through the TVM actions and product mix impacts. We will see also some hedges roll off. Obviously, that all depends on foreign exchange rates, but we see a continuation of the hedge losses related to the pre-Brexit hedges that we have in place, continuing to roll off in FY20, subject to what happens with exchange rates.

All of those things contributing to improvement in EBIT margin.

P. Baggely

Great. Thanks.

Coordinator

Thank you for that. Your next question comes from Rodolphe Ranouil of Pictet. Please go ahead.

R. Ranouil

Yes, hi. Good afternoon. My question has to do with the roll out of the plug-in hybrid in China. The reason why it is of importance has to do with the cost of the model. I was wondering when do you expect this to be in full swing and what the competitive picture looks like? And sadly, your successor is not on the call, but I still will ask the question—has there been discussions internally around the setting up of a bona fide or independent investor relations function?

K. Gregor

I'll maybe ask Ben to give his thoughts on investor relations.

B. Birgbauer

I think at this point now that is covered out of treasury and I think that we don't have direct equity investors. I'd honestly say that the amount of questions we get in between things like bond conferences or calls like this is actually not enough to warrant a separate function. The reality is that I cover it, my deputy Ed Bolton covers it and Jon Knuppel covers it, who is our Financing Manager and basically that seems to be enough at this point.

We can have a discussion around whether or not you're getting as much as you need as an investor. As you know, we do go to probably 10 to 12 bond conferences a year, so we're well represented there and we're always available to take questions, so I think probably the question would be, in asking the question, you must be thinking maybe we're not getting you something that you need and maybe we need to have a discussion around that.

R. Ranouil

I don't think that's necessarily the case as much as I was thinking that in those days where you're having a big restructuring to implement and refinancing activities to carry out, an independent function would certainly help, in my view, just to – not necessarily from availability purposes -- but more in terms of thinking organisationally for the firm, really.

B. Birgbauer

I think it does come down a bit to if we had a—there's no doubt if we had our own equity outstanding, the requirements would be greater and we'd have more staffing for it, whether it would be investor relations out of treasury or something separate, I'm not sure. All I can say is we keep trying to improve our investor relations coverage.

I think if you compared our results presentations now compared to, let's say, three, four years ago, the level of disclosure I think is quite a bit greater. I think part of that is driven by the nature of the business and our weaker performance in the last year. Nevertheless, I think it has changed quite a bit. And we have also added investor days. I don't know if you're going to our investor day on the 5th of June, but we are quite focused on investors and getting the right information to you. If

you or other investors don't feel you're getting all the right information, I guess we need that feedback and we'll try to adapt what we're doing.

K. Gregor

Yes. Absolutely. Thanks for the question. It's good to reflect on that, but certainly 5th of June investor day is a good opportunity for that, and as Ben says, feedback we're certainly happy to take and we'll reflect on it.

I don't know that I have China PHEV volume figures at my fingertips right now, other than to say that the market development is, to be honest it's consumer-led, and I think will take a bit of time for consumer appetite in China to continue to grow around plug-in hybrids. We'll obviously need to work to make sure—they're an important part of the compliance for China, so we're working very much to balance the production that we need and the demand that we need in order to help drive in future years the sales mix that we need.

But I think that's something perhaps to come back on. That's something perhaps to come back in future calls, but we'll certainly be watching that development with interest. We'll have the Range Rover, Range Rover Sport and the Evoque all with plug-in hybrid options during the course of this year, so that starts for us to cover the marketplace with what we need from that point of view.

R. Ranouil

Okay. Thank you very much. Very interesting.

Coordinator

Thank you for that. Your next question is from Christophe Boulanger from Barclays. Please go ahead.

C. Boulanger

Hello. Good afternoon. I will have two questions. The first one is on your funding plan. I can see on your slide 13 that you mentioned different ways to fund yourself going into this coming fiscal year, including new bond issuance. Could you please clarify in terms of bond issuance whether you intention to do unsecured bond issuance or will you be open to do secured bond issuance? That's the first question.

And the second question is on your project Charge plan. Looking at your working capital, it looks like you have achieved already 80% of the target and leaving around £0.1 billion to achieve. It looks like at least £0.1 billion. Can you please share with us what is the potential additional working capital squeeze that you could be achieving going into the next two years? Is it really £0.5 billion or can you go to £1 billion, for instance?

K. Gregor

It's a good question. Perhaps I'll just ask Ben to take the funding question. I'll come back on the working capital.

B. Birgbauer

I think the answer on the funding question is the same as we previously said on this particular question. We have had a lot of questions, I'd say in the last six months about whether we were thinking about secured funding instead of unsecured funding. I think we've been consistent in saying that we don't have any plans for secured funding at this point. In our view, we've worked very hard to achieve the capital structure

that we have with all unsecured debt and I think our view would be that we wish to continue with that capital structure.

Obviously, we have the flexibility to do something different, but it's not in our thought process at this time to do anything other than unsecured bonds.

C. Boulanger Maybe just to follow up on the funding, you do mention export credit agency funding and new finance lease. Do you have any idea in terms of potential size that you could be doing?

B. Birgbauer Well, I think I said earlier, finance leases—and the reason I gave the number was just so that you didn't think that we would be going crazy with secured financing, and I said that maybe it's £100 million to £300 million to just indicate that it was relatively modest what we had in mind. On export credit agency, I think I'm going to say that I don't want to give a size right now, but I think that that could easily be hundreds of millions of pounds. And I think that when there is something firmer to talk about than I'm able to talk about today, we can share that with you.

C. Boulanger Okay. Thank you.

K. Gregor And on the working capital, yes, we obviously really squeezed it during the course of the second half of FY19 and that's been part of the substantial positive cash flow. That substantial squeezing means that the possibility of doing that size again isn't there, but I certainly believe that £100 million to £200 million worth of working capital reduction is possible in FY20 and that's what we're targeting internally.

In addition to that, actually slide 13 does talk to the receivables financing facility, which although it's funding, will be seen as it comes through, given the treatment of it, the growth in that facility from what was roughly \$150 million that was drawn at the end of March through to potentially \$700 million by the end of March '20 will contribute circa £425 million of reduction in our receivables balance, is how you'll see it come through in terms of working capital.

But that's in addition to what I would believe is possible intrinsically, put aside funding of £100 million to £200 million during the course of the year.

C. Boulanger Okay. I don't know if I can squeeze one more question on investment. Saying you have achieved 70% of your plan and it looks like at least £0.3 billion. You achieved £3.8 billion of investment for this year? Does it imply that in fiscal year '20, you will be potentially doing more than £4 billion of investment?

K. Gregor We're targeting under £4 billion, so I think we could be in the region of £3.9 billion to £4 billion, something like that. That's our target and I think we feel reasonably confident of getting at that sort of level and therefore actually we'll overachieve a bit overall on the investment spending versus the target we set ourselves before.

C. Boulanger Okay. Thank you very much.

K. Gregor Thank you.

Coordinator Thank you. The next question comes from the line of Brian Studioso of CreditSights. Please go ahead.

B. Studioso Hi. Thanks for taking my call. I was just wondering if you could provide a little more detail on China. I know the retail, as you talked about maybe yesterday, about improved cash liquidity and enhancement measures. Could you maybe go into a little more detail on how much of that is better cash position from inventory drawdown versus support through cash coming from the parent, from JLR to CJLR?

And then, my second question is in terms of the dealer mix. I know in the last call you talked a lot about not really being in the right place in terms of tier one and tier two cities. I was wondering, how long do you see the progression playing out in order to get the dealers or the mix of dealers more towards those tier one and two cities? How many years are we talking about before we start seeing an impact? Thanks.

K. Gregor On the profitability side, you're right—it's a mix of factors, definitely from the dealers' point of view. We're working to reduce the inventory and that helps from a cash and liquidity point of view. So that's good as a one-time factor that eases the pressure a bit, but what we've also really been focused on is working with our dealers to agree a plan for this year that gets them, on average, profitable across China. That's really important for us.

We've made some progress in improving the level of profitability from a point where most of our dealers were losing money last year. But we do still have, as was shown on one of the charts, we do still have more to go to get the dealers solidly profitable across China and we're very focused on that this year.

Some of that clearly has required additional levels of what I call variable marketing, or incentive support, both from ourselves as JLR and from CJLR and you see that reflected in the weaker margin performance of JLR. We talked about it in the bridge. A chunk of the extra incentive spending that we saw in FY20 has come from China and the same is also true in CJLR, where the lower margin performance has come because of the extra variable marketing support we've had to put behind the products in China.

Some of that is needed in order to fund a good chunk of the discounts that the dealers are giving customers in China for—which, as we talked about, is a competitive industry feature. That's not just us. That's just the market in China. So we made progress, but more to do.

On the retailer mix, to be honest, the detail of that is perhaps something that I'm less well qualified to talk to. My instinct is it's clearly, given we're talking about physical infrastructure that's in place across China, that it will take perhaps a couple of years to get from where we are now

to where we would really, ideally like to be. That doesn't mean we're not doing anything, of course. It just means that it takes a bit of time to work it through. But that might be something to pick up on a further call with, at the point we get Qing back to follow up on a prior call to give us a bit more insight and perspective on this plan that I'm perhaps less able to give you here now.

B. Studioso Okay. Thanks. And so the support of the China dealers, that just will fall into the category of general support and incentives. There's no way we can get a breakout in terms of what the cash flow and implications are in terms of cash out as you try and turn the China operations around?

K. Gregor Not really, but mainly because the cost is funded via what I call variable marketing, and month by month rather than a big chunky one-time cash payment. Really what we have to work to achieve is a level of sustained profitability for the dealer month in, month out, and ultimately that has to come from the transaction price that the dealer's selling the car at in China, being adequately supported by the price that we sell the car to the dealer at, net of the discounts that we support.

B. Studioso Okay. Thank you.

Coordinator Thank you. Your next question comes from the line of James Maxwell from Janus Henderson. Please go ahead.

K. Gregor Hi, James.

J. Maxwell Hi, Ken and Ben. A few questions for me. Could you just come back on the minimum levels of cash that you need to run the business, how low you're happy to go there?

The second point, just with regards to your guidance for the next few years that you have there, what are your background assumptions just on the market and I think you thought you'd outgrow the premium market, but this assuming broadly stable sort of industry volumes. And to what extent are you concerned or prepared for maybe a weaker overall market?

And added to that, what do you think would be the risks for you if Trump decides to go ahead and start imposing tariffs on cars imported from Europe, which I guess whilst we're on this side of Brexit, that would impact you.

And then finally, if I may say, Ken, as you're moving on, but you're at a point where burning cash, ratings on a downward path, you're going to need funding going forward. I'm wondering what steps you're taking beyond the measures to just fix the business itself to actually try and arrest the decline in ratings and make sure that you have access to competitive finance going forward? And in that, I guess I'm talking about potential for capital injections into the business, whether that come from Tata Motors, or as has been talked about, potentially teaming up with somebody else.

- K. Gregor Okay. Thanks, James. Lots of questions in there. I'll maybe ask Ben to try and tackle the funding questions and if we miss one or two questions, obviously, come back to us.
- B. Birgbauer I'll probably start, James, the question is what's the minimum cash we'd be willing to entertain. I find it a hard question to answer honestly, just because we always want to have a significant cash buffer between what might be a minimum level. I think I'd come back to we've consistently said we would target 12% to 15% cash as percentage of revenue that we'd be wanting to have at the end of each year.
- That continues to be our target. That does have in it a healthy buffer. But I think what I'd say is—and part of it is, I think, your question at the end—but plan A for us as a business is to execute project Charge and the new products that we have coming to improve our profitability and margins in the business. That, combined with some funding that we think we can do, plan A would have us keeping the business within that target cash flow. It also would help manage the situation with the rating agencies. So that is our plan A. At this point now, I don't think we're—of course, we do contingency planning—but plan A is as described.
- J. Maxwell Okay. Then with regards to plan A as described, but maybe the question around your assumptions for the guidance on the overall market, what you think would be the impact of tariffs? Because I've had a look at it and it's interesting what the conversation about the comments that were made yesterday by I think by the head of your North American business. That looks like it's in pretty decent shape. Your UK business and that looks to be in pretty decent shape. The US business was also – the mix looked really good.
- So I just scratch my head, thinking that things over there are actually looking okay and yet the numbers are still obviously not working out the way we're thinking.
- K. Gregor Yes. Good thoughts, James. On the assumptions underpinning our volume, we're targeting single digits percentage volume growth this year. I think, let me put it that way. We're not assuming we're going to—we'd obviously like to grow faster. We have new products that could enable us to do that, but we're also taking into account relatively flatter industry projections and obviously, product aging as well as the impact of new products.
- The impact of tariffs undoubtedly is a worry. I think that's fair to say. We're optimistic that we won't see tariffs on cars between the US and Europe, but of course that's a risk. If it did, the potential impact is clearly quite significant. One could speculate, but with circa 20% of our volume on a £25 billion revenue business being in the US and then start to imagine percentages of those, one can scare oneself quite quickly about the potential impact.
- And if we did see that potential impact, we'd clearly have to then work on what steps we'd take to avoid that, whether we'd work on pricing

action, whether we further address the product mix in the market, whether we significantly reduce the volume of certain model lines in the market. We'd have to work on all those actions, so we know that.

But, frankly, I think that our core assumption is that Donald Trump will, one way or another, agree position with the EU on automotive tariffs which will avoid tariffs. It's clearly a risk factor, which you guys can dimension also.

J. Maxwell Okay. Thank you. I'll leave it there.

K. Gregor Thanks, James.

Coordinator Thank you. Your next question comes from the line of Diomidis Ntountounakis of Chenavari. Please go ahead.

D. Ntountounakis Yes, hi. I think the first question is on the working capital. Can you, in the fourth quarter, in that number, can you perhaps explain a bit more how much of that was helped by wholesales being down, how much of that was your project Charge, and speak a bit more about the items, about what happens especially in the inventories and payables, which are the big numbers there.

K. Gregor Yes, part of what I'd say is if you look at our actual working profile for the last few years, you will see a profile which has a fair amount of seasonal volatility, which I suppose from one perspective I'd rather not have, but we do have it. And typically, it's being driven by the fact that about 80% of our volume plus – 85% – is sold to our retailers via our national sales companies, with those retailers having wholesale funding arrangements that mean that we collect cash from them very quickly, within a day or two, which means that proportionally, our receivables are quite low for a business this size.

So we collect cash when we build and sell cars. We collect cash quite fast. Against that, we pay our suppliers on 45- to 60-day terms, so we pay for production two months after we build it. What that means is, in a quarter like Q4, we have lots of production days. Lots of production days mean more production, means more wholesale, and therefore, because we collect the cash fast, we drive cash flow from revenue.

However, also in Q4, we are paying for the vehicles we built in October to December. Because we had lower production in October through December, which drives the payables to rebound quite significantly in Q4, which was something we were always expecting was going to happen. So a large part of that is a seasonal rebound in payables, which by the way will unwind a bit also in Q1 of the fiscal year, so that's why in guiding, we expect to see negative cash flow in Q1, because we'll be paying for the units we built in Q4 FY19, in Q1 FY20. And then we'll be building fewer units in Q1 because of the production shutdown.

So the payables movement is mostly a seasonal factor. The inventory movement, I'd say, is roughly half and half between Charge driving improvements over the second half of the year and between normal

seasonal patterns, which would see us correcting the growth of inventory that we had in the first half of the year and other actions we've taken to really push down to squeeze the pipeline during the second half of the year in order to really keep it as tight as we possibly can. Hence, you see in the full year, it's also a positive figure.

The receivables is mostly mechanical, because we collect cash from the balance of our sales. We collect on 60 to 90 day terms typically from many of our importers. So at the moment at least it's a balance that moves in the other direction typically, receivables. So if we grew sales in Q4, it turns negative, but in the full year, it's positive as we reduce sales actually, sadly, to our importer markets.

So there's a number of moving pieces there and it's actually quite difficult to say exactly which bit is seasonal and which bit is specifically related to project Charge, but definitely what you can rest assured is internally, we've been very, very focused on aligning production with supply and squeezing our pipeline of finished vehicle inventory and have it as lean as possible on a sustainable basis, also, I'd say—not artificially at the end of Q4, but just to keep it tight and align it to the volume level that we have.

Either way, whichever way it comes from, I'm really pleased because in the full year, we had a positive working capital movement driving cash flow and in the second half of the year, Q4 in particular, strong finish to the year, correcting and seeing the rebound on the seasonal factor for some of what happened in the year.

D. Ntountounakis Alright. That's great. Thank you.

K. Gregor Just to say once again thank you for your support. I know we go through challenging times here for Jaguar Land Rover.

At the end of the day, it's a positive to see a return to profitability in Q4, positive cash flow in Q4, and clearly lots to do, but we look to move forward with our product investment driving that long-term profitable growth, for our business via new products in the electrification technologies that are going to be critical for the future. And I thank you for your support for our business over the last year and to come in FY20.

Thank you.

Coordinator Thank you. On behalf of Jaguar Land Rover, that concludes this conference. Thank you for joining us. You may now disconnect your lines.

[END OF CALL]