

Financial background to National Express Group plc and the Greater Anglia franchise

1. This appendix describes the financial background of NEG and its operating subsidiaries. There is also a brief discussion of the operating performance of the Greater Anglia franchise.

NEG

Overview

2. NEG is a UK-based transport company with rail, coach and bus operations across the UK and bus operations in North America and Australia. NEG is the largest train operating group by passenger revenue and the largest operator of scheduled coach services in the UK. Turnover for the year ended December 2003 was £2,566.1 million, operating profit was £134.6 million¹ and profit after interest and tax was £43.0 million. 82 per cent of turnover and 70 per cent of operating profit was derived in the UK. More specifically, UK trains accounted for 66 per cent of turnover and 24 per cent of operating profit. For UK coach, these figures were 7 per cent and 11 per cent respectively. (See paragraph 8 for note on cost classification.)
3. For the six months ended June 2004 NEG reported turnover of £1,266.7 million, operating profit of £61.9 million and profit before interest and tax of £25.9 million. The proportion derived from the UK and in particular UK trains and UK coach are not materially different to those given in Paragraph 2. The results for the six months ended June 2004 include those for the Greater Anglia franchise since it began operating on 1 April 2004.
4. At August 2004 NEG operated nine passenger TOCs: Greater Anglia, c2c, Central Trains, Gatwick Express, Midland Mainline, ScotRail (until October 2004), Silverlink, the remainder of WAGN (principally Great Northern), and Wessex Trains.
5. NEG provides Britain's only scheduled national coach network and serves more than 1,200 destinations. In addition, it also provides coach services to British airports and European coach travel.
6. Table 1 shows the breakdown of group turnover, operating profit and operating margin, by NEG business segment, for the two years ended December 2003.

¹Before goodwill amortization, exceptional items and associated losses.

TABLE 1 **NEG: financial performance by division—two years ended December 2003**

	<i>Turnover</i>			<i>Operating profit</i>			<i>Operating margin</i>	
	2002 £m	2003 £m	2003 % of total	2002 £m	2003 £m	2003 % of total	2002 %	2003 %
UK bus	208.7	211.9	8.3	49.8	47.2	35.1	23.9	22.3
UK trains	1,553.2	1,702.4	66.3	33.9	32.0	23.8	2.2	1.9
UK coach	184.5	186.6	7.3	12.2	15.0	11.1	6.6	8.0
UK operations	1,946.4	2,100.9	81.9	95.9	94.2	70.0	4.9	4.5
North American bus	408.0	400.1	15.6	32.6	37.0	27.5	8.0	9.2
Australian bus	58.0	65.1	2.5	2.3	3.4	2.5	4.0	5.2
Continuing operations	2,412.4	2,566.1	100.0	130.8	134.6	100.0	5.4	5.2
Discontinued operations*	159.9	-	-	0.1	-	-	0.1	-
Total	2,572.3	2,566.1	100.0	130.9	134.6	100.0	5.1	5.2
Other items†				-196.4	-55.1			
Profit before interest and tax				-65.5	79.5		-2.5	3.1

Source: NEG Annual Report and Accounts 2003 (audited).

*Australian trains.

†Comprises goodwill amortization (2002: £45.2 million; 2003: £45.7 million), goodwill impairment (£13.5 million; nil), exceptional items (£5.0 million; £5.3 million), share of operating losses of associate (£6.6 million; 4.1 million) and loss on closure of business (£126.1 million; nil).

7. Table 2 shows the breakdown for group turnover, operating profit and operating margin, by NEG business segment, for the six months ended June 2004 and the corresponding period for 2003.

TABLE 2 **NEG: financial performance by division—six months to June 2004 (with comparatives)**

	<i>Turnover</i>			<i>Operating profit</i>			<i>Operating margin</i>	
	2003 £m	2004 £m	2004 % of total	2003 £m	2004 £m	2004 % of total	2003 %	2004 %
UK bus	103.8	115.1	9.1	22.1	21.1	34.1	21.3	18.3
UK trains	823.6	838.6	66.2	9.0	15.7	25.4	1.1	1.9
UK coach	85.3	87.8	6.9	2.9	4.2	6.8	3.4	4.8
UK operations	1,012.7	1,041.5	82.2	34.0	41.0	66.2	3.4	3.9
North American bus	216.3	191.8	15.1	24.5	23.8	38.4	11.3	12.4
Australian bus	29.8	33.4	2.6	1.7	1.2	1.9	5.7	3.6
Central functions	-	-	-	-3.6	-4.1	-6.6	N/A	N/A
Total	1,258.8	1,266.7	100.0	56.6	61.9	100.0	4.5	4.9
Other items*				-26.1	-36.0			
Profit before interest and tax				30.5	25.9		2.4	2.0

Source: NEG Interim Results 2004 (unaudited).

*Comprises goodwill amortization (2003: £22.4 million; 2004: £26.4 million), exceptional items (nil; £5.3 million) and share of operating losses of associate (£3.7 million; £4.3 million).

Note: N/A = not applicable.

8. As of 1 January 2004, NEG changed its segmental analysis classification. In particular, bidding costs for franchises are now shown within the UK trains figures (previously within exceptional items), and central functions are shown separately (previously allocated across divisions). In 2003, these costs were £5.3 million and £8.1 million respectively, and unfortunately 2002 comparatives are not publicly available. Therefore Tables 1 and 2 are prepared on slightly different cost classifications. If the 2003 results shown in Table 1 were re-analysed on the basis of the new classification, the operating margin on UK bus would be 22.4 per cent (an increase of 0.1pp compared with the previous basis), UK trains would be 2.0 per cent (an increase of 0.1pp) and UK coach would be 8.6 per cent (an increase of 0.6pp). In total this would increase the operating margin on all UK activities to £97.0 million or 4.6 per cent (an increase of £2.8 million or 0.1pp).

Trains

9. Tables 1 and 2 show that NEG's UK trains operations have been the least profitable division, with operating margins of 1.9 per cent for the year ended December 2003, compared with 8.0 per cent for UK coach operations, and 22.3 per cent for the UK bus operations.
10. Tables 3 and 4 show the breakdown of the UK trains turnover and operating profits by the various business segments.

TABLE 3 NEG UK Trains financial performance—two years ended December 2003

	Turnover			Operating profit			Operating margin	
	2002 £m	2003 £m	2003 % of total	2002 £m	2003 £m	2003 % of total	2002 %	2003 %
London and South-East	535.7	555.9	32.7	21.0	20.0	62.5	3.9	3.6
Long distance/Intercity	156.1	207.0	12.2	8.2	12.4	38.8	5.3	6.0
Regional services	861.4	939.5	55.2	4.7	-0.4	-1.3	0.5	0.0
Franchise bid costs	-	-	-	-	-	-	N/A	N/A
Total UK trains	1,553.2	1,702.4	100.0	33.9	32.0	100.0	2.2	1.9

Source: NEG Annual Report and Accounts 2003 (audited).

Note: N/A = not applicable.

TABLE 4 NEG UK Trains financial performance—six months to June 2004 (with comparatives)

	Turnover			Operating profit			Operating margin	
	2003 £m	2004 £m	2004 % of total	2003 £m	2004 £m	2004 % of total	2003 %	2004 %
London and South-East	274.6	348.6	41.6	8.8	5.9	37.6	3.2	1.7
Long distance/Intercity	93.1	106.3	12.7	5.9	6.0	38.2	6.3	5.6
Regional services	455.9	383.7	45.8	-4.5	5.1	32.5	-1.0	1.3
Franchise bid costs	-	-	-	-1.2	-1.3	-8.3	N/A	N/A
Total UK trains	823.6	838.6	100.0	9.0	15.7	100.0	1.1	1.9

Source: NEG Interim Results 2004 (unaudited).

London and the South-East, which includes, among others, the Greater Anglia franchise (since 1 April 2004), the c2c franchise, and the WAGN franchise (in whole, or its remainder since 1 April 2004), achieved an operating margin of 3.6 per cent for the year ended December 2003, as shown in Table 5. This was less profitable than

the Long Distance Intercity (6.0 per cent) but more profitable than the Regional Services (approximately at breakeven). For the six months ended June 2004, London and South-East profitability, in monetary and percentage terms, has fallen significantly when compared with the corresponding period for 2003. We understand that this is primarily due to the seasonality of the Greater Anglia franchise and the reduction of subsidy receipts.

TABLE 5 WAGN and c2c financial performance—two years ended December 2003

	Turnover			Operating profit			Operating margin	
	2002 £m	2003 £m	2003 % of total	2002 £m	2003 £m	2003 % of total	2002 %	2003 %
WAGN*	248.6	253.1	45.5	18.7	17.1	85.5	7.5	6.8
c2c†	93.6	99.3	17.9	-3.9	0.6	3.0	-4.2	0.6
Other	193.5	203.5	36.6	6.2	2.3	11.5	3.2	1.1
London and South East‡	535.7	555.9	100.0	21.0	20.0	100.0	3.9	3.6

Sources: Audited financial statements year ended December 2003.

*West Anglia Great Northern Railway Ltd.

†c2c Rail Ltd.

‡NEG.

11. The WAGN franchise includes West Anglia, Stansted Express and Great Northern. The former two are now part of the Greater Anglia franchise and their performance is analysed in Table 7. In 2003, WAGN received a subsidy from the SRA of £12.5 million,² or 4.9 per cent of total turnover.
12. We understand that c2c revenue includes approximately £1.2 million in respect of the Southend Central to London Fenchurch Street route. In 2003, c2c received a subsidy from the SRA of £20.1 million, or 20.2 per cent of total turnover.

Coaches

13. UK Coaches comprises National Express, Eurolines and Airlinks. Based on the draft financial statements for the year ended December 2003, National Express Limited earned revenue of £128.8 million (2002: £121.9 million) and an operating profit³ of £9.7 million (2002: £7.5 million) at a margin of 7.5 per cent (2002: 6.1 per cent).
14. Table 6 sets out the turnover and operating profit of selected routes discussed within this report. Excluding the Norwich–Heathrow–Gatwick service (route 727), the remaining nine routes earned turnover of £[REDACTED] million and a contribution of £[REDACTED] million (or [REDACTED] per cent).

²Net of amounts paid pursuant to the adjustment of clause 18.1 of the respective Franchise Agreement.

³After goodwill amortization.

TABLE 6 Selected route performance—year ended December 2003

Route	Origin/destination		Turnover		Contribution	
			£'000	£'000	£'000	%
481	Ipswich	London	()	✂	
484	Clacton	London				
490	Norwich	London				
308	Great Yarmouth	Birmingham				
350	Liverpool	Clacton-on-Sea				
497	Great Yarmouth	London				
727	Norwich	Heathrow/Gatwick				
305	Liverpool	Southend-on-Sea				
495	Cromer	London				
496	Cromer	London				

Source: NEG submission.

Greater Anglia Franchise

15. The creation of the Greater Anglia franchise has brought together previously separate franchises: Anglia, Great Eastern (both of which expired on 31 March 2004), and the West Anglia and Stansted Express elements of the WAGN franchise. There are no historical consolidated results. Table 7 sets out a pro-forma analysis of the Greater Anglia franchise.

TABLE 7 Pro-forma Greater Anglia franchise financial performance—two years ended March 2003

	Turnover			Operating profit			Operating margin	
	2002 £m	2003 £m	2003 % of total	2002 £m	2003 £m	2003 % of total	2002 %	2003 %
Anglia*	65.3	68.5	19.3	-1.1	-0.1	-0.6	-1.7	-0.1
Great Eastern†	179.8	187.7	53.0	23.2	19.7	111.3	12.9	10.5
	245.1	256.2	72.3	22.1	19.6	110.7	9.0	7.7
Stansted Express‡ West Anglia‡	(✂				
Total								

Sources: *Anglia Railways Trains Services Ltd, audited financial statements year ended March 2003.

†Great Eastern Railway Ltd, audited financial statements, year ended March 2003.

‡WAGN, unaudited management accounts, years ended December 2002 and 2003.

*Ultimate parent company: GB Railways Group plc.

†Ultimate parent company: FirstGroup plc.

‡Previously part of the WAGN franchise operated by NEG. The results are for the two years ended December 2003.

16. Based on 2003 results, the pro-forma analysis suggests that the Greater Anglia franchise will earn turnover of £[✂] million and operating profit of £[✂] million at an operating margin of [✂] per cent. The operating margin for the Greater Anglia franchise is less than that of the WAGN as a whole ([✂] per cent), but greater than that of the UK Trains division of NEG ([✂] per cent), its London and South-East segment ([✂] per cent) and c2c ([✂] per cent).

17. Using the pro-forma performance for 2003 set out in Table 7, it can be seen that by winning the Greater Anglia franchise, NEG will earn an additional £256.2 million turnover and £19.6 million operating profit at an operating margin of 7.7 per cent.

18. The pro-forma analysis in Table 7 does not take into account any synergies or additional costs that may arise from the integration of the franchises. Also, it includes the historical subsidies from and premiums to the SRA. In 2003, Anglia paid a premium of £5.9 million, Great Eastern paid a premium of £5.0 million, Stansted Express paid a premium of £[~~5~~] million whilst West Anglia received a subsidy of £[~~5~~] million. In January 2004 the SRA stated that in respect of the Greater Anglia franchise, 'future value of total franchise premium receipts to the Authority is in excess of £0.5 billion in present value terms after taking into account of adjustments for the change to CP3 (Controlled Period 3) performance rates of approximately £0.1 billion. Further adjustments will take place to take account of the finalized track access elements of CP3 on which the Regulator is still consulting'. We understand that the finalized access elements of CP3 results in a subsidy payable to NEG.
19. We understand that the Great Eastern revenue includes approximately £2.2 million in respect of the Southend Victoria to London Liverpool Street.