

FirstGroup plc half-yearly results for the six months ended 30 September 2010

TIM O'TOOLE: Good morning; thank you for joining us especially given what some of you might have had to go through to get here this morning, but we're glad you could join us for our review of the first half results; that is the six months leading up to 30 September 2010.

My name's Tim O'Toole. This is my first opportunity to address you as Chief Executive and I'm pleased to do it in a context of where we've been able to show further progress notwithstanding some tough conditions. We've been able to deliver overall results consistent with our expectations and we've also been able to deliver a cash generation beyond our targets and I think this last goal is largely due to the leadership of Jeff Carr and his team. One of the things that give me confidence in taking on this role is the opportunity to work with executives of this calibre. In that regard, before I go forward, I should say, as a matter of first importance, that I acknowledge and salute really the role and the contribution that Sir Moir Lockhead has delivered to the Group, to the industry as a whole over the last 21 years. It's truly a pleasure and a privilege to follow him; lucky for me he put together a top management team so I join with them and together we're going to try to fill Sir Moir's shoes.

In addition to the team, the other thing that gives me confidence is really the breadth of this enterprise. We have a diverse portfolio of businesses and where we see softening in one, we're able to lean on the strength of another to still deliver on our promises and meet our expectations as we've done this year.

The other thing that I'm finding encouraging is that over the first four months in this assignment, I've travelled to all of our operating properties and I've been kind of on this extended busman's holiday and the thing I've learned is, number one, we've literally thousands of people out there who are working very hard everyday to do the best they can for their passengers and our customers. The other thing I've seen is that there's plenty of room for improvement still. We are far from a perfect transportation enterprise with standardised processes; we're far from it in many cases.

So this is the up side for us. It's up side in greater efficiencies in the future but it is also the thing, I think, that as we get better and better, leads us to topline growth which has to be a focus of this company. Of course, those are just impressions and anecdotes. They aren't reduced to hard targets and goals and today, we're getting together to review the actual results, so let me turn to an overview.

There has been steady progress in a challenging environment. As you see, we've delivered on our expectations and we've returned earnings growth with EPS up some 16.7% so far this year and, as I said, we've increased cash generation so much so that we're able to raise our target for the year from £150 million to £180 million. I really believe that this performance provides an important insight into the strength of this company because, to be fair, if you think about it, we've taken this company through some of the toughest times - and we still are in some of our business segments - toughest times we've seen in many, many years and notwithstanding that, we have still delivered on our cash targets. Indeed, by the end of this year, this fiscal year, we'll have our net debt to EBITDA ratio down 2.5 times and not many people would have supposed that. When we drive through that target, we're moving straight on to two times and we're going to get there a lot faster than most people suppose. So I think that to the extent that a concern about this company has been this balance sheet, I really think that concern is on its way to being dispelled.

I think another drag on the perception of possibilities for this company, of course, was the spectre of the Comprehensive Spending Review and I join with my peers in saying that we're enormously relieved that the Government has shown that they actually get it, that transport has to be protected because it is one of the key enablers to turning this economy back to growth. You've seen the commitment to construction in heavy rail; you've

also seen that the threatened tax increases on fuel for buses has been much, much less than forecast and indeed, as a result, we've seen no impact from the Comprehensive Spending Review on our results in the near term. We feel we have plenty of time to adjust to the more modest increase in fuel taxes come 2012.

I really do think the Secretary of State and the Ministers of Transport deserve a lot of credit for obviously making the case for which I believe our passengers and we are going to benefit. So all in all, with the removal of these major concerns with our delivery so far this year, and overall basis for the Group, the strong cash generation gives us more than enough support for the Board's determination to increase dividends by no less than 7% going forward.

So, all in all, a steady performance, I think, and I'll turn it over to Jeff who will review the financial highlights and then I'll come back and give you a review of businesses sector by sector. So; Jeff.

JEFF CARR:

Thank you very much, Tim, and good morning, ladies and gentlemen. I'll just start by taking a quick look at the summary of the financial performance in the period. Total revenues increased by 4% in the period to just over £3 billion. At constant exchange rates, revenue growth is a little bit more modest at about 1.3% due to the strengthening of the slightly stronger dollar

this year than we had last year. EBITDA margins advanced slightly which is encouraging in this environment, up from 10.7% last year to 10.8% with improved margins at UK Bus, Greyhound and Transit, partly offsetting a tougher margin environment at First Student and operating profits, as you can see, and that's adjusted operating profits before non-recurring and amortisation charges, was up 3.5% to £170.6 million.

It's pleasing to see our overall cost of financing coming down and interest costs, as you can see, were down 4% to £92.9 million as we continue to benefit or really start to benefit from the lower levels of debt. That means that our profit before tax grew strongly; up 14.3% to £77.7 million.

Now, one of the key features of these results is the significant improvement in the statutory profit before tax; up 187%, you can see there, from £28.6 million to £82 million. The key issue there being the elimination of any restructuring costs that we had last year and any restructuring charges this year, and we did have some smaller amounts that have just been taken through normal operating costs and a one-off credit in the period of £22.5 million. The credit related to the settlement of an old Network Rail claim going back actually to the previous First Great Western franchise from several years ago.

Tax for the period was £19.1 million and that's based on a full year tax rate, estimated full year tax rate of 25% which I think is consistent with what we've been talking about.

So overall, as Tim's mentioned, adjusted EPS was up 16.7% which we think is a good performance on the right track.

Before we look at each of the businesses in turn, I've just shown here a summary of the bridge from last year to this year's operating profit split out by the key divisions. As we've highlighted, Student margins being under pressure; operating profit is down year on year by just over £10 million but this has been more than offset by good profit increases at Transit, Greyhound and, you can see, UK Bus. UK Rail's profit is basically flat year on year which is an excellent performance considering the increase in premium costs that we'd flagged as we went into this year. In the period, that's about an extra £50 million in terms of premium charges.

Group costs were up slightly; £3.6 million, mainly due to a low share based payment cost last year and a more normalised amount in the current period.

So moving on to start with Student in terms of the businesses and looking at each of the businesses in turn. I'm going to do Student, Transit and Greyhound in dollars just to take away the

foreign exchange and then UK Bus and Rail back in pounds/sterling.

Student revenues, as you can see, were down 0.9%; just under 1% and the small decline resulting from, as Tim mentioned, some route consolidations which we've seen in a number of contracts which probably accounted for about half of the decline and also the fact the charter revenue continues to be down year on year and it's down about 5% in this period versus last year. In the first half, it represented about 10% of our sales, so again, that's about half a percentage point of decline. EBITDA was \$157 million, again down a little bit from last year, \$11 million, due to the revenue reductions that I've just described and also limited pricing opportunities in an environment where the school boards remain under significant budget pressure.

Operating profit, therefore, at \$40 million for the period is down just over \$15 million versus last year which reflects higher depreciation charges in the period as we continue to invest in the fleet. As previously stated, we expect these margin pressures to continue into the second half of the financial year.

The story of Transit is somewhat different with strong revenue growth and good margin development. Revenues were up 5.5% to just under \$600 million and the growth really coming from shuttle and paratransit. In fact, our shuttle business is up just

under 25% compared to last year and paratransit revenues grew strongly also; up 6% as a result of partly new contract wins and partly expansion of existing business.

The fixed route business which represents more traditional Metro transit services grew at a more modest 1.5% which again, is in line with our expectations. As I mentioned, as well as the good topline growth, you can see good margin development there with operating profit up to \$39.6 million, or 6.6% as a percentage of net revenue.

Looking at Greyhound, we continue to make good progress at Greyhound and total revenues were up 4% which include our parcel and food service businesses. Like-for-like, passenger revenues were up 1.9% and we made good margin development based on lower fuel costs and also the fact we continue to look to streamline our fixed cost structures. For example, total selling costs continue to decline as we expand Internet sales and eliminate commissions and we also continue to look to reduce our terminal overhead costs. Additionally, we made good progress in Canada in our profit recovery plan for the Canadian business. However, Canadian margins continue to remain below acceptable levels and there's still a lot more work that needs to be done there.

In UK Bus, revenues were actually down 2.6% mainly due to the fact that we continue to manage mileage as we look to protect margins and total mileage driven in the period was down 6% when compared to last year. Passenger revenue on a like-for-like basis has been relatively stable for some time now and it was at 1.3% for the period. I'd expect this trend to continue for the balance of the year, probably coming in at between 1% to 2% growth. Margin improvements, as you can see, margins were up to 9.7%, operating profit up to £55 million as you benefit from lower fuel costs and the effect of the mileage reductions.

Moving on to UK Rail, as I've mentioned, despite the significant increase in premiums which were up about £50 million, we're pleased to see that operating profit is broadly in line with last year; £48.4 million. The premium increases mainly relate to First Great Western with some smaller increases at First Capital Connect. The stronger operating profit reflected good continued cost improvements and a strengthening of the topline performance. Just looking at the topline development in a little bit more detail; passenger revenues across all the train operating companies showed good progress in the period. Obviously there was little pricing in this period and most of this growth is related to volume gains. First Great Western was up 5.4% and First TransPennine continued to perform solidly, up 5.7%.

Looking forward, the trends remain encouraging and prospects for the second half are promising.

Let me move on to cash flow which, as you know, is one of the key priorities for the Group. Overall, we're very pleased with the performance in the first half. As you can see from the chart, a net cash outflow in the first half improved from £93.4 million last year to just under £15.7 million. It would have been good to have got to zero or positive but we were short a little bit.

Now, what's pleasing is that's been achieved while we've been increasing our capital expenditure levels and continue to fund a dividend growth policy and you can see the key drivers of the improvement have been strong operating cash and good working capital performance relative to last year. As Tim's mentioned, the strongly cash generative nature of our business means we're able to increase our full year target from £150 million of net cash to £180 million and when we include the disposal proceeds from GB Railfreight, that means that our total cash available to reduce debt for the year will be over £200 million.

Just looking at the cash flow in a little bit more detail and starting with the operating cash flow, you can see there £61 million improvement. The key factor driving the operating cash flow, we had so many with EBITDA improvement but obviously as a

reversal on the non-recurring items that we discussed earlier which obviously has an impact on cash.

I think most important is we look at the cash generated by operations line and this is really the true test of the strength of the cash generative nature of the business. You can see that increased from £164 million last year to just under £300 million in the current period. That's an increase of 80% and the key driver of that being the working capital change where we had an outflow of over £100 million last year and we normally have outflows in working capital in the first half of the year and inflows in the second half of the year, but the outflow this year was only £16 million given there's a difference of just about £89 million.

Working capital will remain a priority and as we make progress in the current period, I'm still confident that there's room for improvement going forward.

Looking at the uses of cash you can see capital expenditure, as I've mentioned, was up by around about 40% to £147 million in the period and for the full year, we expect capital expenditure to be around £300 million which I think is pretty much where we previously guided people to but that's up almost 50% from last year.

Moving on just very briefly, we can see an increase in cash from the interest and tax charges of £29.4 million; the largest element to this being interest costs related to the timing of bond payments and this was a one-off which we'll see a bit of a catch-up in the second half and some offset for that in the second half of the year.

Finally, with the proceeds from the sale of GB Railfreight, you can see the net change in cash of £77.7 million.

Let me just wrap up with some quick comments on leverage.

The strength and diversity of our business means we continue to make good progress reducing our leverage. At the half year, as we've mentioned, net debt to EBITDA was 2.8 times and we're confident of reaching 2.5 times by the end of the current financial year. In respect of refinancing, we have two revolver facilities; one for \$1.5 billion and one for just over £500 million. These are both due in February 2012 and I expect that this refinancing will be complete well before the end of the current financial year.

You can see we have significant headroom at the moment relative to the committed facilities, so we'll probably refinance at a slightly lower level than the current facilities.

So, thank you, ladies and gentlemen. I'll now pass back to Tim.

TIM O'TOOLE:

Thanks, Jeff. I'm now going to run through the businesses.

What I'm going to try to do is just kind of give you some flavour of how I see these businesses. The current situation is loaded with some impressions but also maybe some hints at our aspirations for the future.

Following the same order that Jeff followed, we start with First Student. First Student plainly faces the toughest trading conditions. You know the story. It's this cutback in property tax receipts, sales tax receipts in some states put enormous pressure on the school boards. As a result, we've seen cutbacks because the school boards have consolidated routes. They've cut back their charter business so there are fewer trips for the athletic teams, fewer trips to the museums in the middle of the day for the school children and that has hit us and it hit us in a year where we had an abnormally high number of contract expirations, so it has been a tough situation. Notwithstanding this environment, I remain very bullish about this business and one of the reasons is, and since I've spent time with these teams, they aren't just sitting back taking these blows. They're taking the business forward and they're making sure that they improve the technology and improve the offer that we're presenting to the marketplace so that as this market stabilises, we are going to be in a position to further extend our leadership in this business.

So, for example, you've heard of our FOCUS projects where we're putting this GPS-based system in our buses. The important thing is that this is no longer an IT project. It's now in over half of our buses. By the end of the next school year, it'll be in all of our buses and this is really is a differentiator for us in the marketplace I believe because it isn't just that this tracks the buses; it also generates the driver's payroll and it creates the reports for the school districts themselves. Why this matters? You're somebody who runs a school district. You're subject to all these pressures; parents calling, complaining etc, and a standard one is the mother who calls up and screams that her child's bus is 20 minutes late everyday. "I'm going to the school board. I'm going to make your life miserable." With our system, the administrator can call up the reports and say, of course; "I can see quite plainly it was three minutes late yesterday, it was on time the next three days" etc. We make their jobs dramatically easier and it's because we have this system that I actually believe it will differentiate us. Some other companies will talk about they're supplying the GPS system but every one I've seen, these off the shelf systems, they don't have this integrity. They're most important in terms of the accuracy because they don't drive the driver's payroll but the other thing is they don't generate the management report; they actually solve the problem.

Another thing this team's trying to do in these difficult circumstances is cast themselves as a solution to these

budgetary problems. One of the things we're trying to sell is give us more of the work up the chain of the delivery of this work and we can save you more money. So, for example, in St Louis, Missouri, we've gone to the school district and convinced them to allow us to do the dispatching, the routing; something we do in other districts, in addition to providing the transport services. They did that; we were able to save them 20% more on their budget. There's a similar project that was successful in Rochester, New York, where we saved a little over 10%. So the only reason I'm raising these examples is because I do want to depict that this is a team that's determined to raise its profile, its own professionalism because as this business comes back, I do believe we will extend our leadership.

If you step back and look at this business, we have a strong business with very strong margins compared to other companies. We are many times the size of even our next closest competitor. We're in 42 states, we're in 8 provinces in Canada, so we can't escape the fact that when the market, as a whole, faces these kinds of pressures, we're going to feel them but we also feel we have a view over this business, we're convinced, as a result of that that First Student will remain, over the long term, a source of growth for FirstGroup.

We turn to a slightly happier story of First Transit where we have seen this very steady and strong revenue growth. This is a

business you just have to love. It just keeps growing, just quietly, dependably moves forward. You can see its book of business is already over \$1 billion. This is, in many ways, our most entrepreneurial business. These people run shuttles, they run fixed routes, they run paratransits or run call centres; basically they will go wherever and do whatever. A government or a company who wants to improve their efficiency in their transportation provision or they want to see innovation, they come to First Transit.

This business has been able to resist the budgetary pressures. I know people worry whether you're going to see them in this business, but it's been able to resist them more successively than First Student largely because they have sold themselves as a solution and also because they have a lot of clients that aren't subject to that problem. We have two very prominent examples this year; big success stories; one, a conversion in California and another major private provision of service in Canada.

In southern California, for years we've run paratransit for the city of San Diego but also for this catchment area to the north, around Oceanside, called North County Transit District. Last year, the big change was North County Transit District turned over its entire fixed route operation to us which is quite a coup because I'm telling you, you will not see a better engineering plant than this place, a better fleet. We took over all their

employees; we're able to deliver them substantial budgetary savings and, at the same time, we provide ourselves with a very handsome margin. The neat thing about this story is it's been such a success that these people actually volunteered to appear in videos that we can use as a sales promotion tool to show it to their counterparts around the country, that this is something that people need to be considering to help solve their budget crisis.

The other example is we got landed a big contract with Fluor to move the oil workers into the oil sands fields in Alberta, Canada. A big contract, very attractive and I think it's an example of the interesting new businesses First Transit's been able to open up.

As Jeff mentioned, the shuttle business has been a great one for us. We run shuttles at airports. You get on a bus to go to a rental car company at an airport, you're probably on one of ours. We run a lot of shuttle businesses that have been growing on college campuses. These are big businesses. University of Texas, I think we run about a 185 bus fleet that's in service at one time. These are big businesses that have been quite successful; it's very encouraging.

I told you I went around to our properties and one message I got consistently when I went state to state to state is when I'd meet with clients, they, on their own, kept volunteering that the First Transit people, the professionals, are really at the top level of

professionalism in the business. They really emphasised, when they have a project where there's got to be delivery, the quality has to be there, really First Transit are the people they think about. There are some people who will try to bid under us but the clients recognise if you don't go with us, you do risk quality, and I think we have two examples of how that kind of reputation can reverberate and give you more business with the same client. These are kind of reciprocal situations. Reno, Nevada; we always ran their fixed route network. They recently just gave us the paratransit. Durham, North Carolina, the exact opposite occurred. We always have run their paratransit; they've turned over the fixed route to us. That only happens if you're doing a good job. As I said, this is a business that is very easy to like. Modest capital appetite and yet it is delivering this kind of steady growth for us.

At Greyhound, as Jeff mentioned, they're in the midst of a very nice turnaround. You know the story. When we took them over, this is a business that I don't think had bought a bus for about seven or eight years, had a sprawling network of neglected terminals and fleet and it had a small fraction of the passengers that used to use it. So management recognised, you know, you're going to do something about this. You've got to address it all; you've got to hit the network, you've got to hit the terminals, you've got to hit the fleet. So they really have gone a very long way to accomplishing that. They've stripped out the mileage in

their network condensing down to just the high volume lanes, so the milk runs and the branch lines are gone now. In the terminals, similarly, they're just cascading down to the least cost solution in the terminals, so with the big terminals, if you don't have sufficient transfer of passengers between buses, you get out of them to smaller facilities. Even at the smaller facilities, if you can, you get out of them and you go to these intermodal facilities a lot of municipalities are providing or you even go to third parties with agency situations and ultimately, you go to kerbside pickup. The point is you're just driving to the lowest least cost solution. Last year, we got out of 89 facilities; this year in the first half, we've got out of about 57 facilities and we're just going to keep up this process.

Then we come to the fleet. With this fleet, it was so neglected; it's pretty hard to put a commercial product out there, it was breaking down on the road. But they knew we weren't going to allow them to go on some capital spending spree with new buses. So instead, they put together a very economical and sensible refurbishment programme. We've authorised the refurbishment of some 250 buses. These are rebuilt engines, new transmissions. This is actually a much more reliable product. This year, we'll do 150 of those buses. This production line in Indiana has been such a success and the quality of the products has been so good, we'll probably just allow this line to keep running because it's really giving Greyhound this new look and its

ability to compete. What's so exciting about this is it's doing this while it's remaining cash generative to us, so it's giving them the time to transform their business model but a very low risk to the Group as a whole. So it's quite encouraging that even in the face of very tough circumstances, they're able to do this.

I did spend quite a bit of time with this team in Dallas and one of the things I found quite encouraging is though they're absolute zealots about their company and their product, they don't live in a museum. They understand that they're going to have to follow bold change if they're going to have a way forward and I think there's plenty of evidence. You can see that these people are doing just that. If you look at the BoltBus product, which I know you know about, highly successful in very competitive Northeast markets up against Megabus and the Chinese buses and all the rest of it. Now, they're taking that business model, Internet based, no cash, no terminals, kerbside pickup, and they're marrying it with their brand, so we're going to be unveiling our Greyhound Express in Chicago starting in December and it's going to be very interesting to see how this further shapes the transformation of the Greyhound business model.

Greyhound still faces a really tough market when you consider who their clientele is and who's been hurt the worst in this recession but, the fact of the matter is, they're remaining cash generative and they're keeping up the momentum, so it really is quite encouraging.

Turn then to UK Bus; you've heard the numbers Jeff reported. This has been a very steady performer. As they ran into the tougher economy through the beginning of this year, they maintained that very tight grip on the network, reducing mileage in response to any reductions in demand. This has been a very prudent strategy. It's the strategy that actually allows you to see the kind of dependable performance but now that things are loosening up, I do think we have to push ourselves. I do think we have to be sure we're not leaving any growth on the table. We have to be sure that we've got this optimum combination of frequency, price and cost discipline. So I think we have to experiment a bit more and push ourselves and this experiment can only happen at the local level and it can only be successful at the local level if you've really good relationships with the local authorities, the PTEs and the like. Where we have those relationships, we've been able to create growth. We have to just make sure we're taking advantage of all the opportunities that are available in this business and make sure that we're getting all we can out of this business.

In London, again we're just continuing to focus on operational performance. We're quite pleased with our performance on the west side of the city. We've still work to do in the east although we're still a player there and I'm pleased that we have landed a number of new routes. Most prominently, TfL just awarded us

this route 25; the major move between Essex to Oxford Circus, so we're still there, we're still pushing. Now we're starting to even turn our attention to the Olympics 2012 because, as you know, we're the major bus provider for that which will be a great moment I think for the company as well as the country.

I think when you step back from this business and look at it, FirstGroup comes from the buses. We're the largest bus company in the UK. When you combine it with our Transit operation in the US, surely we're the leading bus company but it isn't just about size. It's also about being at the forefront of development so that you know you're going to be there in the future. Something that people don't realise is how far advanced we are in the technical end of things. We're the only company in the world opening up a hydrogen fuel cell depot and bus service here in East London as well as in Connecticut. We're the only company that's been asked to operate this fast charge, electric bus in California that the US DoT has made such a fuss over. These are largely science projects on someone else's dime but the fact of the matter is we're the ones who are gathering the institutional expertise, so however the markets go in the future, we intend to be there. It's about staying in the forefront of operations and engineering and market growth as we're doing in First Transit. We just have to make sure with this business that we do all that but we also get all the growth that's available in our traditional business.

Finally, UK Rail; rail has really been the star of the first half of this year; very strong earnings. The thing is, we're now starting to see even better sales of tickets, the advance purchase of first class is finally returning, the flexible standard fares are returning, so that's all good news. Hopefully, the market will keep in that direction.

As you would expect of any good rail business, really focused on operating performance, so First Great Western, First ScotRail, First TransPennine Express, all above 91% PPM and First Capital Connect above 90% which is above its target. It's been there for the first half, so that's all quite positive stuff. We are the largest in rail as we are in bus and we're trying to make sure we leverage that size and that expertise across the business. We have an example that's going forward right now. First ScotRail which was, of course, named Transport Operator of the Year again, had a very successful ticket promotion for the over 55s on their network. We're now going to take this nationwide on our network and we hope to see that turn out quite well.

As you might imagine, rail is very dear to me. I was lucky enough to join the leading rail company in the UK and you can rest assured that I hope to do everything I can to retain that description in the years ahead for this business.

Let me sum up with an overall outlook. As I said, I think we're in a good position right now; steady performance. Earnings up; EPS is up over 16%. Strong cash generation, as you've heard, but I think the bottom line is this is a company that's very solid but it's also got a lot of opportunities for improvement. I hope I've conveyed my excitement about the opportunity to join the Group. This is a company that is astride the UK and the US in the transport business and it's in places, both of which I've run transport companies, so I really think it's a tailor fit for me and I'm very excited about this opportunity.

With that, we'll be happy to take any questions. Thank you.

JOE SPOONER: Good morning; Joe Spooner, from RBS. Just a number of questions; firstly of the increased cash generation target. You obviously have the Network Rail settlement of £22 million. Does that largely explain the increase that you're talking about there and scope for further improvement as the year progresses?

Secondly, on the fuel benefit. I think the benefit for the full year worked out at about £100 million. How much of that was delivered in the first half?

Then Tim, there's a couple of points that you made. I think you said that two times net debt to EBITDA would be achieved faster than people expected. Can you maybe flesh out the thoughts that you're thinking on that front? Secondly, you said that the 7% DPS target will be no less than 7%; just thinking maybe there's scope to increase the growth that you're talking about on that front.

JEFF CARR: The cash; obviously the settlement with Network Rail was a big part of improving that but also I think just generally, we're very pleased with the way it's going. We're being relatively cautious about the guidance. I think moving up to £180 million; we feel comfortable with. When you add on the benefits from GB

Railfreight, that means we're over £200 million for the full year in terms of free cash, that's post dividend and post capital expenditure. We're comfortable with that guidance but that was one of the key reasons obviously we were able to increase that.

Obviously we've been working on that for some time, so it was always in our thoughts that there'd be some sort of settlement.

In terms of the fuel, I believe the numbers are closer to £90 million for the full year once you take into account foreign exchange fluctuations and we're just less than half of that in this period, so probably just under £40 million and we explained at the time, last year, how that would be broken out by division but also the fact that some of that gets offset by things like pension increases that we've got going through the organisation and various other areas. The £40 million is mostly in UK Bus, Greyhound, a little bit in Student and Transit and some in rail as well, so it's spread over those with UK Bus and Greyhound getting the lion share.

In terms of the two times, Tim can answer this if you want.

TIM O'TOOLE: As far as the two times, as you can imagine, I've been in the position for three days and Jeff has his arms right here holding me back! No, I'm not prepared to put a date on it but it will not be in the long term. As far as whether there is room for increases

beyond the 7%, we've made the 7% commitment and that's where we are right now, but I will tell you that I do think a steady dividend and upside in dividend is critical especially in these kinds of businesses. If there's one thing I've learned in running transport businesses, the risk is always that people will squander capital and the only way you can maintain a discipline and a credibility with your shareholders; it's really the only way you can have this firm communication with them is this kind of really dependable with an upper looking dividend policy. So I'm firmly committed to that kind of profile going forward.

We don't have any specific projects or anything to announce. We will keep looking at everything in the portfolio plainly because we want to make sure that what we have is generating returns for you.

JEFF CARR:

I think just to follow up on that, the reason I highlighted the cash generated from the operations line on the cash flow, which improved to just under £300 million up 80% from last year, is to highlight the fact that most of the performance is coming from the operations; it's coming from our day to day business, working capital, EBITDA and I think that's what we're relying on to get the two times. If anything comes above and beyond that in disposals, that would just accelerate the process and I think we're not talking several years; we're talking in the next 12 to 24 months; that's the timeframe, and if we get to 2.5 times which I'm

confident we will by the end of this year, then clearly you can see the trajectory from 3 times in March 2010 to 2.5 times in March 2011. It'll be a challenge to keep that trajectory going but certainly within 24 months, we'll be there.

DOUGLAS MCNEILL: Douglas McNeill, Charles Stanley. On the capex side for you, Jeff, £300 million I think you said; can you give us a sense for what proportion of that relates to the FOCUS programme? What I'm driving at is to what extent the US school bus business is becoming more capital intensive or is it not costing much? A related point; if the refurb programme at Greyhound is enabling you to avoid a capex spree at the moment, does that mean there will have to be a capex spree at some future point there?

JEFF CARR: No. I think the capex that we've discussed, FOCUS is a relatively small amount of capex. I think this year, we'll be spending something in the order of \$10 million, \$15 million; something in that order of magnitude but it's a relatively small amount. At Student, we continue to spend; we've upped our capital this year. Most of the increase in the first half was split between Student and UK Bus. That's mostly maintenance capital, so that's replacement of existing services as we look to keep the average fleet age at a healthy level and we have kept both of those fleets at relatively healthy levels. So there's no real need to step up in terms of Student.

Greyhound; it's been a process, since we've owned Greyhound, we have bought few new buses and this year, we'll be buying, I think, it's something like 50 new buses. The refurbishment is just a cost effective way of extending the life and we've been on the refurbished buses; they actually look and feel like new.

TIM O'TOOLE: You couldn't tell the difference between a new bus and our refurbished bus. It's going to give us between five and seven additional years.

JEFF CARR: The \$90,000 per refurb relative to just under \$400,000 for a new bus, so I think there isn't a capex bubble there for Greyhound. What we're doing is we're investing wisely to refresh the fleet over a period of time and we're doing a similar thing in IT for Greyhound. There needs to be a refresh going on and we're being very cautious about how much capital we commit to it but as their EBITDA grows, we'll give them a little bit more. We'll let the dog off the leash a little bit more each time their EBITDA increases.

DAMIAN BREWER: Damian Brewer, Royal Bank of Canada. I've got a couple of questions; firstly, just on the US and North American GB bus operations. As you look beyond this year, what becomes, for you, normal in terms of operating margin within the business? Do you think this will, for example, save money to your customers, is

most of that savings passed back to the customer or are you taking some share of that?

Just a second question; both the North American business and UK, where are you on labour settlements, labour turnover? Is there inflation there or is it relative to this issue?

TIM O'TOOLE: As far as the US Student and the margins, obviously one of the things that lead to the results that you've seen is that we've been protecting our margin. As the market leader, we feel we have to do that and we are encountering some extreme behaviours in some of the smaller companies who literally undersign a contract at any price just to have the cash flow to survive another year and we can't allow that to really drive our business. So we have seen some surrender in our overall margin as a result of things like charter business going away because obviously that's pure gravy to us when you've got the assets there already but overall, we're trying to maintain the discipline and it's really to protect the margin a point or two below where it's been in the past is the most shrinkage we hope to see.

It's hard to make real bold predictions in Student because we're still facing this turmoil and we just have to manage through it.

JEFF CARR: In terms of labour settlements; in general terms, in the US, certainly the settlements are coming in around about 2% to 3%, 2,5%; that sort of level is what we've been seeing which is a bit

more than what we've been getting on the topline in terms of pricing.

TIM O'TOOLE: We haven't had a whole lot of settlements recently; that's why.

JEFF CARR: We can; I mean, it depends; contract by contract. In terms of FOCUS, what that does is drive efficiency in terms of labour and that's something that we can share. Generally, the sort of examples that we quoted would be examples where most of that gets passed on to the authority. Obviously we're keen to work with school districts to make sure that we can help them bring their costs down and that helps the relationship going forward. If we can partner with them and help solve their problems, then that's good for the longer term.

TIM O'TOOLE: The evolution of FOCUS is that ultimately, you know, right now, we're a source of information but ultimately in the next stage, the tool passes on to them and they're going to have direct access to it, so there'll be transparency in the information. So, okay, you give up some power you have but, on the other hand, then you're knitted into their operation; they really don't want to do without you, so we see that is where you have to head to a transparent relationship where we're both committed to each other long term.

GEOFF VAN KLAVEREN: Geoff van Klaveren from Deutsche Bank. Tim, looking at First Student, the impression I have is despite the downturn, the market's still as fragmented as ever. Is there any evidence of small operators exiting and just thinking of FOCUS, does that give you a real sort of competitive advantage when you bid for contracts? My second question, just for Jeff, on the pension deficit, would you expect the change from RPI to CPI to have any sort of beneficial impact on your deficit?

TIM O'TOOLE: On the first one with regard to the small operators; if you think about how this story has played out and the discontinuous nature of the Student market, you can go through this bidding season and then you endorse something and this is really the first full year where it's hitting us and hitting all the small operators. So we are looking to see whether there are opportunities going forward with them because we want to make sure that we take advantage of any opportunities in the marketplace. We'll just have to wait and see how that plays out.

I do believe long term, FOCUS will be a differentiator especially for them because they're just not going to be able to offer a product like that. On the other side, you have to be realistic because we're not looking to run around and pick up 50 bus operations in the middle of nowhere. There have to be other sides that it really makes sense where we can bring the scale

and really generate savings, so we'll see how this school year plays out.

JEFF CARR: In terms of pensions, we have a slide on page 32 in the appendices which shows we've actually taken about a £70 million benefit from the change from RPI to CPI and that effects the rail plans and the Local Government plans in bus and the £70 million has gone through equity but it's been more than offset by a change in discount rates and effectively, what we're looking at with discount rates down to just about 5% is the gap between discount rates and inflation has really narrowed which means the overall deficit has remained at about £350 million; so the £70 million basically got wiped out because of the discount rate. All in all, there's a lot more that we can do and are working on to manage that in the longer term.

OLIVER NEAL Ollie Neal, Goldman Sachs. Two questions. In First Student, would you expect similar levels of margin erosion in the second half to that which you saw in the first half? Secondly, would it be possible to comment on recent revenue trends in Greyhound?

JEFF CARR: I'll talk about Student margins. Yes, I think the margins will be slightly worse than we've previously been talking about. We've previously been guiding people to about a 50 basis point margin decline; I think we're now looking at something more like 100 basis points. Now, that difference is \$10 million to \$15 million

difference in terms of the EBIT, so it's a manageable level. The key driver for that is the fact that charter revenue continues to decline. We can, to some degree, offset that by our records but we have seen, in the start of the new school year, a continuation of that trend which is a bit disappointing.

TIM O'TOOLE: So far as Greyhound revenues; overall like-for-like revenues up about 1.9% but there's a lot of mix in there. One of the things is the performance in Canada is masking some of the progress they're making in the US. They have not yet – because of regulatory issues – stripped out the mileage in Canada that they have in the US and that's the next step. We've got to get there because right now, it's a drag on their overall operation. You have these very different markets that Greyhound's in, in the United States. The Mexican market's been down some and that, in the past, has been a source of a lot of growth. Culturally, in Mexico and in the border, it's all about buses; that's the major form of transport and Greyhound has suffered some reductions in the Northeast, not Bolt; it's done very well but Greyhound itself but, overall, about a 1.9% increase.

JEFF CARR: I think that's what we're seeing continuing through the second half; something in that order of magnitude.

TIM BARRET: Tim Barrett; JP Morgan Cazenove. Two quick things. Firstly, in terms of US Student, do you feel that any of that charter

reduction is structural in terms of it not coming back or is it purely a cyclical impact that you're planning on? Just also, is there anything to add on rail from the Government's spending review? Thanks.

TIM O'TOOLE: As far as the cyclicality of charter, yes, we think it is cyclical but, more importantly, we think it's incumbent upon us to up our game because in too much of our operation, the way charter works is you're a person sitting there and answer a phone. "Oh, you want a bus; fine" and now, what we're going through is putting resource out there to actually drive charter because we don't have to just do the museum run; we can also do the local bowling club and a lot of other things. So we're putting in targets and centre targets for our local managers to get them to turn their attention actively so that we can drive the charter market rather than just wait for the school districts to hand it to us.

As far as rail, we hear rumours of further announcements but we wait to hear from the Government first.

Rail pricing? We don't have anything to say beyond the Government announcement of RPI plus three in 2012 is going forward and RPI plus one now.

GERALD KHOO: Gerald Khoo of Arbuthnot Securities. A couple of questions. Firstly, you talked about having, in school bus, an abnormally high number of renewals or contracts coming up for renewal this year. What does that profile look like compared to last year?

What does that profile look like going into the New Year?

Secondly, in Greyhound, you talked exiting what sounds like a rather large number of properties. Have you been able to release any capital out of the loss of that or are they just leased properties and should we expect that as being an opportunity as that process seems to continue?

TIM O'TOOLE: As far as contract renewals, this past year, the total was something like 20% above normal and this year, it's more at normal levels, so we see a little less vulnerability than we faced last year.

As far as Greyhound, yes, some of them are leased properties, some of them are owned and we do release them as the opportunity presents itself but I don't want to get ahead of ourselves and offer some big numbers.

JEFF CARR: It sounds a lot but actually, relative to the total size of just under 800, it's a relatively small amount; maybe about 15% over the last year and a half. We have seen some value come through in terms of cash from some of those but they've been relatively small properties to date. We talked about some bigger properties in the pipeline. We talked about that in the past. There are still some exciting opportunities and I think there will still be some opportunities to unlock some of the potential for the bigger properties but we don't want to do that until the timing's right,

until the property market can give us full value for those. As you know, it's been a pretty tough market for the last year or so.

JOEL COPP BARTON: Hi; it's Joel Copp Barton here from Nomura. Just on UK Bus properties; is seasonality this year kind of going to be similar to what it has been previously? Secondly, just on charter revenues; I think that used to be about 7-8% of overall revenues in school bus. Can you just tell us where we are now?

I suppose the last thing, just on London Bus, I've always thought that margins have been kind of a bit lower than what the sector averages have been. Is there anything from obviously having a good look at it that says this shouldn't go back to sector margins at some stage?

JEFF CARR: Just on the seasonality and the charter; yes, UK Bus is seasonal in terms of most of the profits that came through in the second half. The way the fuel hedges roll off, we have a little bit more benefit in terms of fuel in the second half relative to the first half but we've given pretty clear guidance in terms of total expectation, so we'd expect our second half profits to be a bit more advanced relative to last year than the first half was.

In terms of charter, it is still around about just under 8%; 7-8% of total. That number hasn't changed significantly. In the first half, it tends to be higher because you've got lower school revenues,

basically because of the summer holidays, so it's around about 10% in the first half and a bit lower in the second half. It was down, I think, last year just in the low double digits in terms of the declines. What we're seeing this year is a further 5% reduction in terms of charter. That's split between school charter and commercial charter and as Tim was saying, I think our challenge is to drive the commercial charter and reverse those trends and work harder with a better, a clearer sales and marketing offering.

TIM O'TOOLE: As far as bus margins go, it is an intriguing area, let me just say that. When you look at the available data, our margin is better than most of our competitors. It's not as good as another one. Some of these data are quite suspect and we don't want to conclude too much but, on the other hand, we don't want to be defensive and maybe there is more opportunity. If you push so much on revenue per mile, you're actually not exploiting the margin you could drive if you could increase your loads, and so I think we have to push ourselves and we have to test that thesis. If some people have some better techniques that work locally, I'm more than happy to embrace them and, as I said, we need to push ourselves in this business. It's a good steady business, so it's the perfect time to push harder on it.

DAMIAN BREWER: Damian Brewer, again. Just a question on rail. You've got three franchises with between them, 15 to 17 months or so left to run and given the Government has yet to decide what future

franchises even look like, how do you position yourselves into that environment?

TIM O'TOOLE: As you might imagine, we're positioning ourselves to be able to respond however the Government plays this, including working with the Government, putting in our feedback on how we think the best way forward is for the refranchising. Plainly, as you would expect, we're all for much longer franchises. We think to the extent you can get much longer time for these franchises, you've a better chance of building a business, working with your employees and getting them to identify your goals and all the rest of it. We are anxious not to get ahead of the Government and be certain we respond, in a public way, to what they bring forward.

Your question however hits the key point and that is they have an enormous amount of work in front of them and, therefore, if there are ways we can help them by moving these franchises forward in an efficient arrangement, we're all for fostering those further talks.

JEFF CARR: It's not just FirstGroup that has significant renewals; there's quite a backlog building up... the start of a bottleneck building up.

PAUL BUTLER: Paul Butler from Macquarie. Just two questions. Could you give us an idea of where the margin is in the Greyhound business in Canada relative to the US? If you could talk a little bit more in

detail about why the Canadian business has been so much worse than the US business and what the prospects are for turning it round. Secondly, I just wonder if you could give us a sense of where you think we might be in terms of the school budget issues; whether we're still on the way down or we've bottomed out or maybe there's some light at the end of the tunnel.

JEFF CARR:

Let's talk about Greyhound Canada. We said last year, Greyhound Canada lost pretty much close to Canadian \$20 million. If you back out, the US margins they were pretty good in a difficult year. The target really was to get them close to break even this year. I don't think we'll quite get there but I think we'll show significant improvement. Clearly, that's a one-year target. Our longer term target is they've got to return their cost of capital like all of our businesses.

The reason – one of the key reasons – Canada's a little bit different is it's a regulated market and because it's regulated, it's much more difficult to flex the capacity with demand, so we've been running a lot of buses through a lot of empty space with not many people on them. We've been in negotiations with each of the provinces to basically come to the party and work with us to make that service work. We were quite hopeful; there was a Federal working group that has been working on it and they've come up with recommendations. We were expecting the recommendations in September because the provinces and the

federal authorities do recognise there's an issue in Canada. Unfortunately, that study has been delayed. I think all those provinces have to agree the outputs and they're still discussing it, so until we see the outcome of that, I think that's going to be one of the key issues that determines our strategy going forward in Canada in terms of the volume, the level of service and subsidy. That's clearly one of the key issues in Canada. Obviously we can do a lot to manage our own costs which we need to do as well and I think we're determined to get Canada up to an acceptable level of return on capital.

TIM O'TOOLE: In terms of where we might be; we're either going to see subsidies or we need to exit.

JEFF CARR: If we exit, it'll be exiting specific provinces probably and keeping an east coast/west coast operation. Most of the subsidy requirement we need, and that's what it's all about at this stage, is in the central provinces.

TIM O'TOOLE: As you know, 80% of the population is within 200 miles of the border, so there is a profitable business there but what you can't be doing is running buses all up through Saskatchewan and that's what has to be changed.

As far as where we might be on school buses, as you might imagine, three days into the job, I'm not yet in a position to call

market changes. We just need to keep working this problem and the other thing about school buses, as I said, it's this discontinuous nature. We've got to go through next year's bidding season before anything really intelligent can be predicted for the future.

JEFF CARR: Any final questions? No, okay.

TIM O'TOOLE: Thank you very much for coming here and joining us this morning.