

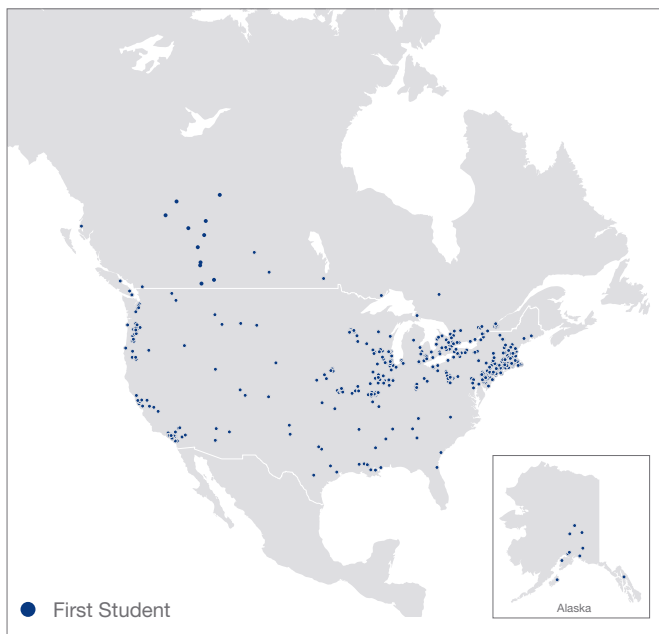


Market overview

First Student is the largest provider of student transportation in North America – over twice the size of the next largest competitor.

We must continue to deliver a service we can be proud of while ensuring we can do so for the long term, by earning sustainable returns.

Dennis Maple
President, First Student



Market review and trends

School buses provide home to school transportation for millions of students in the US and Canada. There are more than 15,000 school districts in North America, which deploy more than 500,000 school buses. The total North American market is estimated to be worth around \$24bn per annum, of which school districts directly operate approximately 63%, with 37% outsourced to private operators. Charter services are also operated, typically of limited duration and scope, either for school customers separate from scheduled school runs or for other customers such as church and community groups or businesses.

Long term demand for school transportation services is principally driven by the size of the school-age population; however other factors including the propensity of school boards to outsource and changes in the local criteria for service provision (such as the distance to school bands within which the service is offered) can play a part in the addressable market for private operators. In the last three years, the market has stabilised with some positive but limited organic growth, following a period when the economic downturn put pressure on customer budgets, which led to organic retraction, price pressure, and atypical levels of contract churn. While school board budget pressures have eased, high quality, high efficiency outsourced providers offer an increasingly attractive value proposition to potential customers.



Over 500 operating locations across US and Canada



Around 1,300 contracts, typically 3-5 year duration

Customers

School districts provide transportation for students depending on varying criteria determined at state level. Contracts typically specify either fixed or annually indexed pricing, meaning that private operators bear cost risk. These contracts are typically three to five years in duration, after which they are competitively retendered. School districts receive their funding from state and local sources, including property tax receipts, and their budgets for all expenditure, including transportation, tend to be linked to economic factors. In addition to school districts outsourcing student transportation for the first time (known as 'conversion'), growth is driven by additional routes for a given school due to population growth or other factors ('organic growth'), as well as inflation-related price indexation built into some contracts.

Competitors

The private outsourced market is highly fragmented with 14 operators running more than 1,000 buses. The largest four companies, including our business, account for just below half of the outsourced market. The next 45 largest contractors operate approximately 25,000 buses, and the remaining outsourced contracts are operated by several thousand companies, often termed 'mom and pop' operators. 'Share shift', or winning contracts previously managed by other outsourced providers, together with acquisitions, provide additional avenues of growth.

Market attractions

- Contracted revenue with public sector customers, typically low credit risk
- Typically high levels of contract retention
- Security and safety track record at least as important as price
- Established relationships with local communities a barrier to entry
- Fragmented competitive environment – long term consolidation opportunity.

Approximate share of outsourced market (around 37% of total market)



First Student	26%
National Express	11%
Student Transportation of America	6%
Illinois Central	2%
Other	55%

Strategy and performance

	2015	2014
Revenue	\$2,368.6m	\$2,339.3m
Operating profit	\$177.3m	\$152.8m
Operating margin	7.5%	6.5%
Number of employees	57,000	57,500

Financial performance

Revenue in our First Student division was \$2,368.6m or £1,478.8m (2014: \$2,339.3m or £1,467.4m), 1.3% higher on a US Dollar basis, benefiting from our successful pricing strategy during the 2014 bid season and modest organic growth. Operating profit was \$177.3m or £114.9m (2014: \$152.8m or £93.5m), resulting in a US Dollar margin of 7.5% (2014: 6.5%). The one percentage point improvement in margin reflects the benefits of our pricing strategy in respect of the approximately one third of the portfolio retendered in the 2014 bid season, recovery of operating days lost to the severe weather in the prior year, a benefit of \$19m in the year from our ongoing \$50m per annum cost efficiency programme, partially offset by continued pockets of driver shortage in parts of the business and cost inflation running slightly ahead of price indexation on the bulk of our contracts not yet rebid under our pricing strategy.

Our strengths

Clear market leader (bigger than next four competitors combined) – scale economies in vehicle and parts procurement, insurance, fleet management, technology development, etc.

Differentiated offering – technology, safety programme, strong customer relationships and satisfaction scores

Turnaround plan is progressing – disciplined contract portfolio management, capital discipline and cost efficiency plans are driving margins and returns

Repositioning business to sustainably deliver profitable growth and returns from market leadership in the long term.



Focus on
First Student

New recruitment system offers benefits

First Student is at the initial stages of introducing a consolidated recruiting model allowing online application, which will replace the previous paper-based, decentralised driver recruiting process. The new system, which is based on a similar successful model developed by our UK divisions, allows a more consistent approach to recruitment across different locations and online application, saving time for our management teams. A pilot was launched at 53 locations in late 2014, and learnings from this pilot will help inform the phased roll out of this new system which will take place across the division over the next three months.



Prudent investment in our key assets

Focused and disciplined bidding

A key element of our turnaround plan in First Student is addressing contract portfolio pricing on new bids and renewals to ensure that we achieve appropriate returns on capital on our contract portfolio. As is typical, approximately one third of our bus portfolio was up for renewal in the 2014 bid season, and we were pleased to achieve average price increases on these contracts of approximately 4.5%. Our contract retention rate of 90% on those contracts up for bid was at the upper end of our range of expectations. As a result, the proportion of First Student's contract portfolio earning margins below 5% has reduced from 36% in 2014 to below 30% in the current year. The level of acceptance of our price increases, together with a third year of modest organic growth under existing contracts, suggests that market conditions are continuing to improve. We continue to compete effectively in the conversion market from in-house to privately operated services, which we believe offers significantly better value, though at present the number of new outsourcing opportunities continues to be limited. Together with some 'share shift' wins from competitors and a small tuck-in acquisition in New York, our overall bus fleet reduced by around 60 buses, remaining just over 49,000.

Continuous improvement in operating and financial performance

In addition to the pricing strategy, we made good progress on the next phase of our cost efficiency programme. We are rolling out a programme to address the recruitment challenges we have faced in some localised parts of our business, which includes an applicant tracking system developed in our UK divisions, and further savings continue to be driven by implementing and monitoring compliance with identified best practice operating procedures throughout our more than 500 locations. This programme has now delivered around \$120m in annual cost efficiencies including \$19m in 2014/15 as targeted, and we expect to deliver a further \$30m per annum in savings by the end of the 2016/17 financial year. Almost three quarters of our engineering locations have achieved silver or gold 'lean' certification. Key areas of opportunity going forward include further savings from lean engineering and maintenance procedures, employee productivity, procurement and more efficient use of fuel.

Prudent investment in our key assets

We continue to increase our use of technology to raise customer service levels, promote environmental benefits and differentiate our services. Our FOCUS GPS system (which links onboard data to back office systems) is now fitted throughout the bus fleet, and functions as a platform for additional improvements. For example, our DriveSMART initiative, which combines driver training with fuel use data from FOCUS, incrementally saved nearly \$6m in fuel costs in the year. We are also carrying out field trials this year on a system using FOCUS to give parents the ability to track bus location in real time, which will be ready for roll out in time for the 2016 bid season. Our MyFirstPass system continues to be deployed in selected locations, giving parents and schools timely information on student ridership through swipe card technology. We invested approximately \$280m in new buses, refurbishments and onboard technology in the year; our average fleet age remained constant at 7.5 years.



Fleet of approximately 49,000 yellow school buses



Six million students transported per day

We also continue to develop our more structured approach to charter business, which delivers very strong incremental returns on capital employed as it utilises the existing bus fleet in between the contracted services at the beginning and end of the school day. In the year we opened three regional charter centres, handling almost a third of all our non-school charter work, which grew by 7% in the year.

Responsible partnerships with our customers and communities

Our services form an integral part of the school experience for the millions of children in our care each day, and we take our responsibilities to them and to their parents, schools and communities very seriously. We are pleased to have achieved a sixth consecutive year of improved customer service scores, and we had a strong performance in our safety KPIs. Continuous improvement in our customer service and safety track record is deeply embedded in our values as an organisation, and is also a competitive advantage.

In addition to cost savings, the 2% improvement in fuel efficiency from our DriveSMART initiative reduces our environmental impact, and our alternative fuel fleet continues to grow, increasing by 250 buses in the year.

Future priorities

First Student is a leader in our marketplace, both in terms of our size and the quality and safety of the services we provide. Through the continuation of our turnaround plan, we will deliver our medium term target of double digit margins by ensuring that we continue to bid or renew contracts only at prices that reflect the quality of service we provide and the capital that we employ. In addition we continue to implement and monitor best practice policies and procedures in all key areas throughout our business to reduce cost. In the longer term, First Student's unique market position, value proposition and increasing operational efficiency will ensure we are increasingly well placed to grow through further share shift, tuck-in acquisitions and organic opportunities.

Outlook

During the 2015 bid season First Student is continuing to seek higher pricing with the resultant risk of some contract losses. With just over half of the negotiations completed so far, we are encouraged by our progress, with average price increases achieved to date of over 5%. We expect this improvement, together with additional cost efficiencies, to result in further margin improvement in 2015/16, despite an impact of approximately \$17m to operating profit as a result of fewer operating days due to the timing of Easter and Labor Day, which will reverse in our 2016/17 financial year.

First Student fleet footprint



New York/New Jersey/Pennsylvania	21%
New England	13%
Ontario	11%
Illinois	9%
California	7%
Other	39%

Focus on First Student

New campaign brings our value proposition to life

First Student have developed a new value proposition based on market insights and team expertise, and rooted in the Group's vision and values. The customer promise, including posters featuring employees, began to be rolled out at Employee Appreciation Days in May 2015.

5 Maintain responsible partnerships with our customers and communities