Matthew Gregory
Chief Financial Officer

"In the year we strengthened our balance sheet by delivering strong free cash generation, supplemented by the start of franchise inflows relating to SWR, and by refinancing part of our bond portfolio at lower rates.

Summary of the year

Reported Group revenue in the year increased by 13.2% including the new SWR franchise from 20 August 2017, the 53rd week in the Road divisions and the translation of our US Dollar-based businesses into pounds Sterling at stronger rates than the prior year. Adjusting for these factors, Group revenue increased by 1.0% with growth in First Rail, First Transit and First Bus partly offset by small reductions in Greyhound and First Student revenues.

Group adjusted operating profit in constant currency decreased by 10.4% excluding the contribution from the new SWR franchise and the 53rd week in the Road divisions, with growth in First Bus and First Rail more than offset by reductions in the other divisions. Group adjusted operating profit margin in constant currency decreased by 90bps to 5.0%, reflecting a 50bps reduction for the Road divisions and the expected rebasing of the Rail margin. In reported currency, adjusted operating profit decreased by 6.5% to £317.0m (2017: £339.0m).

Net finance costs before bond 'make whole' costs decreased to £120.0m (2017: £132.0m), resulting in adjusted profit before tax of £197.0m (2017: £207.0m), a decrease of 4.8%. Adjusted profit attributable to ordinary shareholders was £147.7m (2017: £149.4m), with the lower adjusted profit partly offset by a lower effective tax rate. Adjusted EPS decreased by 0.8% to 12.3p (2017: 12.4p). In constant currency, adjusted EPS increased by 3.4%. EBITDA increased by 0.6% to £690.6m (2017: £686.6m).

Statutory operating loss of £196.2m (2017: profit of £283.6m) and statutory loss before tax of £326.9m (2017: profit of £152.6m), principally reflected Greyhound goodwill and other asset impairments, the onerous contract provision for the TPE rail franchise, non-recurrence of the gain on disposal of a Greyhound terminal in prior year, adverse developments in aged North American insurance claims, bond 'make whole' costs relating to redemption of the September 2018 bond, and higher intangible asset amortisation and restructuring and reorganisation costs than prior year. Statutory EPS was (24.6)p (2017: 9.3p) in the year.

Net cash inflow (before First Rail start of franchise cash flows) was £110.5m (2017: £147.2m including proceeds from sale of a Greyhound terminal). This cash inflow, combined principally with First Rail start of franchise cash flows of £88.5m and movements in debt due to foreign exchange, resulted in a decrease in net debt of £219.6m (2017: £120.3m). As at 31 March 2018, the net debt: EBITDA ratio was 1.5 times (2017: 1.9 times). Adjusting for cash ring-fenced in the First Rail division, net debt: EBITDA improved to 2.1 times (2017: 2.3 times).

Liquidity within the Group has remained strong; as at the year end there was £766.4m (2017: £941.1m) of headroom on committed facilities and free cash, being £603.0m (2017: £800.0m) of committed headroom and £163.4m (2017: £141.1m) of free cash. In February 2018 the Group placed $275m in long term US private placement notes with a weighted average fixed coupon of 4.25%. The notes were placed in two tranches, with $100m due in March 2025 and $175m due in March 2028, attracting interest costs of 4.17% and 4.29% respectively. In March the Group redeemed the £300m 8.125% coupon bond due September 2018 in full using the proceeds from the new notes, other cash on hand and our committed bank facility. These refinancing activities incurred a 'make whole' cost of £10.7m in the current financial year and will result in interest savings of an estimated £14m per year from the next financial year.

Our average debt maturity increased to 4.1 years (2017: 3.6 years) following the refinancing activities in the year. During the year, gross capital investment of £439.5m (2017: £365.6m) was invested in our business, with Road divisions' capital expenditure broadly flat and Rail increasing significantly as expected. ROCE increased to 9.5% (2017: 7.9% at constant exchange rates and 7.3% as reported).

Finance costs and investment income

Net finance costs before adjustments were £120.0m (2017: £132.0m) with the decrease principally reflecting lower level of net debt and lower interest rates.

Profit before tax

Adjusted profit before tax as set out in note 4 to the financial statements was £197.0m (2017: £207.0m), with the decrease due principally to lower adjusted operating profit partly offset by lower net finance costs. An overall charge of £523.9m (2017: £54.4m) for adjustments including other intangible asset amortisation charges of £70.9m (2017: £60.2m) resulted in statutory loss before tax of £326.9m (2017: profit of £152.6m).

Tax

The tax charge, on adjusted profit before tax, for the year was £44.2m (2017: £53.8m) representing an effective tax rate of 22.4% (2017: 26.0%). This reduction is primarily due to the US corporate income tax rate reducing from 35% to 21% under the US Tax Cuts and Jobs Act which was signed into law on 22 December 2017. This change also resulted in the remeasurement of brought forward deferred tax balances giving rise to a one-off tax credit in the income statement of £24.6m (and a one-time tax debit through Other Comprehensive Income of £21.8m). There was also a tax credit of £55.6m (2017: £17.3m) relating to intangible asset amortisation charges and other adjustments of £523.9m (2017: £54.4m). The total tax credit was £36.0m (2017: charge £36.5m) representing an effective tax rate on the statutory loss before tax of 11.0% (2017: 23.9%). This rate is lower than the effective tax rate on adjusted profits primarily because no tax credit arises on the impairment of Greyhound goodwill. The Group's effective tax rate is sensitive to the geographic mix of profits including tax rates in the US and Canada (including state taxes) that are higher than in the UK and to changes in tax law and rates in the jurisdictions in which it operates.

The actual tax paid during the year was £12.2m (2017: £10.2m) and differs from the tax credit of £36.0m primarily because no cash benefit arises in respect of the one-off tax credit for the US tax reform and the tax credit on the TPE onerous contract provision.

EPS

Adjusted EPS decreased 0.8% to 12.3p (2017: 12.4p) and basic EPS decreased to (24.6)p (2017: 9.3p).

Shares in issue

As at 31 March 2018 there were 1,203.1m shares in issue (2017: 1,207.3m), excluding treasury shares and own shares held in trust for employees, which increased in the year to 7.7m (2017: 0.4m) reflecting a new policy to spread the purchase of own shares for employee share schemes across the year. The weighted average number of shares in issue for the purpose of basic EPS calculations (excluding treasury shares and own shares held in trust for employees) was 1,205.1m (2017: 1,204.8m).

Reconciliation to non-GAAP measures and performance

Note 4 to the financial statements sets out the reconciliations of operating (loss)/profit and (loss)/profit before tax to their adjusted equivalents. The adjusting items are as follows:

Greyhound goodwill and other asset impairment

Recognising the difficult trading conditions experienced by Greyhound in 2017/18, the strategic plans for the business and estimates of future cash flows generated by the Greyhound division were revised. The calculated value in use of the division resulted in a £277.3m shortfall to the carrying value of assets (2017: £360.4m surplus).

Following their review of these cash flow estimates, the Directors concluded that there should be an impairment charge of £277.3m on the Greyhound cash generating unit (CGU). This is reflected in the financial statements as an impairment in full of the carrying value of Greyhound goodwill of £260.6m, as well as impairment charges of £12.3m on Greyhound's property, plant and equipment, £2.5m on the brand and trade name and £1.9m on software.

TPE onerous contract provision

Management have prepared updated financial forecasts for this franchise until the initial end date of 31 March 2023. The updated forecasts are based on a number of assumptions, most significantly passenger revenue growth. These are based on economic and other exogenous factors as well as changes in timetables, capacity and rolling stock. Although we are already achieving industry-leading revenue growth, our forecasts suggest that we will fall short of the growth requirements in the original franchise bid. Based on these forecasts the Group considers it has an onerous contract, the value of which is estimated to be £106.3m. Accordingly this amount has been charged to the income statement.

Other intangible asset amortisation charges

The amortisation charge for the year was £70.9m (2017: £60.2m). The increase primarily reflects a higher charge in the North American divisions due to an incremental £7.5m in software intangible amortisation.

North America insurance reserves

There have been adverse developments on a small number of aged insurance claims in North America which mainly relate to the 2014/15 and 2015/16 financial years. In aggregate, the adverse developments on these claims give rise to a cost representing a significant proportion of the respective divisional results and accordingly management consider that including such amounts in operating profit would distort year-on-year comparisons for the North American divisions. The impact of these adverse developments was a charge of £32.7m comprising First Student £13.4m, First Transit £15.8m and Greyhound £3.5m.

Restructuring and reorganisation costs

There was a charge of £26.0m (2017: £16.8m) in the year for restructuring, impairment of assets and reorganisation costs relating to the business turnarounds in First Bus (£20.6m)

Revenue and adjusted operating profit

Revenue and adjusted operating profit by division is set out below. For more information on divisional operating performance see the business review on pages 12 to 22:

	Year to 31 March 2018			Year to 31 March 2017		
	Revenue £m	**Operating profit[1] £m**	**Operating margin[1] %**	Revenue £m	Operating profit[1] £m	Operating margin[1] %
First Student	**1,771.1**	**156.5**	**8.8**	1,780.3	171.1	9.6
First Transit	**1,072.7**	**58.2**	**5.4**	1,042.0	73.3	7.0
Greyhound	**690.2**	**25.5**	**3.7**	684.7	42.6	6.2
First Bus	**879.4**	**50.2**	**5.7**	861.7	37.0	4.3
Group items[2]	**16.2**	**(31.2)**		15.8	(38.8)	
Road divisions	**4,429.6**	**259.2**	**5.9**	4,384.5	285.2	6.5
First Rail	**1,968.8**	**57.8**	**2.9**	1,268.8	53.8	4.2
Total Group	**6,398.4**	**317.0**	**5.0**	5,653.3	339.0	6.0
North America in US Dollars	**$m**	**$m**	**%**	$m	$m	%
First Student	**2,350.6**	**210.4**	**9.0**	2,323.3	222.0	9.6
First Transit	**1,420.4**	**77.8**	**5.5**	1,358.9	95.2	7.0
Greyhound	**912.7**	**32.8**	**3.6**	894.0	55.2	6.2
Total North America	**4,683.7**	**321.0**	**6.9**	4,576.2	372.4	8.1

1 Adjusted.

2 Tramlink operations, central management and other items.

and costs related to contract losses and impairment of assets in First Transit (£5.4m).

Bond 'make whole' costs

The early redemption of the £300m bond in March this year resulted in a one-off £10.7m 'make whole' interest charge.

Capital expenditure

Cash capital expenditure was £425.6m (2017: £404.3m), of which £299.4m (2017: £323.9m) was in the Road divisions. It comprised First Student £186.0m (2017: £198.7m), First Transit £19.0m (2017: £17.8m), Greyhound £46.6m (2017: £30.1m), First Bus £42.8m (2017: £74.4m), First Rail £126.2m (2017: £80.4m) and Group items £5.0m (2017: £2.9m). First Rail capital expenditure is typically matched by franchise receipts or other funding. In addition, during the year we entered into operating leases for passenger carrying vehicles with capital values in First Bus of £6.0m (2017: First Transit £8.0m), and we expect our use of operating leases to increase going forward.

Gross capital investment was £439.5m (2017: £365.6m) and comprised First Student £205.1m (2017: £165.9m), First Transit £28.5m (2017: £25.8m), Greyhound £44.4m (2017: £31.7m), First Bus £26.9m (2017: £63.9m), First Rail £129.6m (2017: £75.4m) and Group items £5.0m (2017: £2.9m). The balance between cash capital expenditure and gross capital investment represents creditor movements in the year.

Cash flow

The net cash inflow (before First Rail start of franchise cash flows) was £110.5m (2017: £147.2m) with the reduction driven by lower proceeds from the disposal of property, plant and equipment primarily due to the sale of a Greyhound terminal last year and higher interest payments as a result of the early bond redemption partly offset by the timing of certain working capital flows. Net cash flow including the First Rail start of franchise cash flows of £88.5m (2017: £nil) was £199.0m (2017: £147.2m) and this, combined with movements in debt due to foreign exchange, resulted in a decrease in net debt of £219.6m (2017: £120.3m) as detailed below.

Balance sheet

Net assets have decreased by £585.3m since the start of the year. The principal reasons for this are the unfavourable translation reserve movements of £324.9m and the retained loss for the year of £290.9m partly offset by favourable after tax hedging reserve movements of £34.4m.

Goodwill

The carrying value (net assets including goodwill but excluding intercompany balances) of each CGU was tested for impairment during the year by reference to their projected value in use and following their review of these projections, the Directors concluded that there should be an impairment charge of £277.3m on the Greyhound CGU. This is reflected in the financial statements as an impairment in full of the carrying value of Greyhound goodwill of £260.6m (note 11), as well as impairment charges of £12.3m on Greyhound's property, plant and equipment (note 13), £2.5m on the brand and trade name and £1.9m on software (note 12). Apart from Greyhound, there continues to be sufficient headroom in all other CGUs.

Funding and risk management

Liquidity within the Group has remained strong. At the year end there was £766.4m (2017: £941.1m) of headroom on committed facilities and free cash, being £603.0m (2017: £800.0m) of committed headroom and £163.4m (2017: £141.1m) of free cash. Largely due to the seasonality of First Student, committed headroom typically reduces during the financial year up to October and increases thereafter. Treasury policy requires a minimum of £150m of committed headroom at all times. Our average debt maturity was 4.1 years (2017: 3.6 years). The Group does not enter into speculative financial transactions and uses only authorised financial instruments for certain risk management purposes.

Fuel price risk

We use a progressive forward hedging programme to manage commodity risk. In 2017/18 in the UK, 89% of our 'at risk' crude requirements (1.9m barrels p.a.) were hedged at an average rate of $60 per barrel. We have hedged 82% of our 'at risk' UK crude requirements for the year to 31 March 2019 at $58 per barrel and 57% of our requirements for the year to 31 March 2020 at $63 per barrel.

Cash flow

	2018 £m	2017 £m
EBITDA	**690.6**	686.6
Other non-cash income statement charges/(credits)	**17.2**	(6.2)
Working capital excluding First Rail start of franchise cash flows	**36.9**	23.9
Movement in other provisions	**(10.5)**	(30.6)
Pension payments in excess of income statement charge	**(47.9)**	(37.6)
Cash generated by operations excluding First Rail start of franchise cash flows	**686.3**	636.1
Capital expenditure and acquisitions	**(425.6)**	(404.3)
Proceeds from disposal of property, plant and equipment	**11.4**	43.0
Interest and tax	**(137.6)**	(116.3)
Acquisition of non-controlling interest	**(13.8)**	–
Dividends paid to non-controlling minority shareholders	**(1.1)**	(11.9)
Other	**(9.1)**	0.6
Net cash inflow before First Rail start of franchise cash flows	**110.5**	147.2
First Rail start of franchise cash flows	**88.5**	–
Net cash inflow after First Rail start of franchise cash flows	**199.0**	147.2
Foreign exchange movements	**23.2**	(26.5)
Other non-cash movements	**(2.6)**	(0.4)
Movement in net debt in the year	**219.6**	120.3

In North America 63% of 2017/18 'at risk' crude oil volumes (1.4m barrels p.a.) were hedged at an average rate of $56 per barrel. We have hedged 53% of the volumes for the year to 31 March 2019 at $55 per barrel and 28% of our volumes for the year to 31 March 2020 at $53 per barrel.

Interest rate risk

We seek to reduce our exposure by using a combination of fixed rate debt and interest rate derivatives to achieve an overall fixed rate position over the medium term of at least 50% of net debt.

Foreign currency risk

'Certain' and 'highly probable' foreign currency transaction exposures including fuel purchases for the UK divisions may be hedged at the time the exposure arises for up to two years at specified levels, or longer if there is a very high degree of certainty. The Group does not hedge the translation of earnings into the Group reporting currency (pounds Sterling), but accepts that reported Group earnings will fluctuate as exchange rates against pounds Sterling fluctuate for the currencies in which the Group does business. During the year, the net cash generated in each currency may be converted by Group Treasury into pounds Sterling by way of spot transactions in order to keep the currency composition of net debt broadly constant.

Pensions

In the year we successfully consolidated assets in three UK local government pension schemes into one and on 1 April 2018 both of the main UK defined benefit schemes were closed to defined benefit accrual. We have updated our pension assumptions as at 31 March 2018 for the defined benefit schemes in the UK and North America. The net pension deficit of £358.5m at the beginning of the year has decreased to £273.7m at the end of the year principally due to better asset returns together with favourable foreign exchange movements. The main factors that influence the balance sheet position for pensions and the sensitivities to their movement at 31 March 2018 are set out below:

	Movement	Impact
Discount rate	**+0.1%**	Reduce deficit by £30.0m
Inflation	**+0.1%**	Increase deficit by £25.0m

Seasonality

First Student generates less revenue and profit in the first half of the financial year than in the second half of the year as the school summer holidays fall into the first half. Greyhound operating profit is typically higher in the first half of the year due to demand being stronger in the summer months.

Foreign exchange

The most significant exchange rates to pounds Sterling for the Group are as follows:

	Year to 31 March 2018		Year to 31 March 2017	
	Closing rate	**Effective rate**	Closing rate	Effective rate
US Dollar	**1.40**	**1.34**	1.25	1.29
Canadian Dollar	**1.81**	**1.75**	1.67	1.74

Contingent liabilities

Investigations into the Croydon tram incident are ongoing and it is uncertain when they will be concluded. The tram network is operated by Tram Operations Limited (TOL), a subsidiary of the Company, under a contract with a TfL subsidiary. TOL provides the drivers and management to operate the tram services, whereas the infrastructure and trams are owned and maintained by a TfL subsidiary. No proceedings have been commenced and, as such, it is not possible to assess whether any financial penalties or related costs could be incurred.

Net debt

The Group's net debt at 31 March 2018 was £1,070.3m (2017: £1,289.9m) and comprised:

			31 March 2018	31 March 2017
Analysis of net debt	**Fixed £m**	**Variable £m**	**Total £m**	Total £m
Sterling bond (2018)	**–**	**–**	**–**	298.8
Sterling bond (2019)	**–**	**249.9**	**249.9**	249.8
Sterling bond (2021)	**–**	**348.3**	**348.3**	348.3
Sterling bond (2022)	**321.6**	**–**	**321.6**	321.1
Sterling bond (2024)	**199.8**	**–**	**199.8**	199.6
Sterling bank loans	**–**	**197.0**	**197.0**	–
HP contracts and finance leases	**104.7**	**–**	**104.7**	183.7
Senior unsecured loan notes	**195.2**	**–**	**195.2**	80.0
Loan notes	**8.7**	**0.8**	**9.5**	9.5
Gross debt excluding accrued interest	**830.0**	**796.0**	**1,626.0**	1,690.8
Cash			**(163.4)**	(141.1)
First Rail ring-fenced cash and deposits			**(391.5)**	(255.8)
Other ring-fenced cash and deposits			**(0.8)**	(4.0)
Net debt excluding accrued interest			**1,070.3**	1,289.9

Under the terms of the First Rail franchise agreements, cash can only be distributed by the TOCs either up to the lower amount of their retained profits or the amount determined by prescribed liquidity ratios. The ring-fenced cash represents that which is not available for distribution or the amount required to satisfy the liquidity ratio at the balance sheet date.

Viability statement

In accordance with provision C.2.2 of the UK Corporate Governance Code 2016, the Directors have assessed the viability of the Group over a three-year period, taking into account the Group's current position and the potential impact of the principal risks set out on page 36 onwards. Based on this assessment, the Directors confirm that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to 31 March 2021.

Whilst the Directors have no reason to believe the Group will not be viable over a longer period, the period over which the Directors consider it possible to form a reasonable expectation as to the Group's longer term is the three year period to 31 March 2021. This period reflects the Group's corporate planning processes and is considered appropriate for a fast-moving competitive environment such as passenger transport.

The Group's corporate planning processes include completion of a strategic review, preparation of a medium term business plan and a quarterly re-forecast of current year business performance. The plans and projections prepared as part of these corporate planning processes consider the Group's cash flows, committed funding and liquidity positions, forecast future funding requirements, banking covenants and other key financial ratios, including those relevant to maintaining the Group's existing investment grade status. It also considers the ability of the Group to deploy capital. A key assumption underpinning these corporate planning processes is that debt and asset-backed financing markets will be sufficiently available to the Group.

In making their assessment, the Directors took account of the potential financial and operational impacts, in severe but plausible scenarios, of the principal risks which might threaten the Group's viability during the three-year period to 31 March 2021 and the likely degree of effectiveness of current and available mitigating actions that could be taken to avoid or reduce the impact or occurrence of such risks. The scenarios considered were: 1) weak economy, adverse operating environment and forfeit of rail franchises; 2) low growth economy, heightened terrorism and increased environmental pressures; and 3) weak economy and credit market shock.

The Board confirms that in making this statement it carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity.

Going concern statement

The Group has established a strong balanced portfolio of businesses with approximately 50% of Group revenues secured under medium term contracts with government agencies and other large organisations in the UK and North America.

The Group has a diversified funding structure with average debt duration at 31 March 2018 of 4.1 years (2017: 3.6 years) and which is largely represented by medium term unsecured bank facilities and long term unsecured bond debt. The Group has an £800m committed revolving banking facility of which £603m (2017: £800m) was undrawn at the year end. This facility has a maturity of July 2021.

The Directors have carried out a detailed review of the Group's budget for the year to 31 March 2019 and medium term plans, with due regard for the risks and uncertainties to which the Group is exposed, the uncertain economic climate and the impact that this could have on trading performance. Based on this review, the Directors believe that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, the financial statements have been prepared on a going concern basis.