FirstGroup Winter trading update and update on portfolio rationalisation 11 March 2020 transcript

Matthew Gregory (FirstGroup Chief Executive) – Thank you. Good morning, everyone and thank you for joining us on the call today. I'm joined by Ryan (Mangold), by Rachael (Borthwick), Faisal (Tabbah) and Nick (Chevis), as well as our Chairman, David Martin.

We've got a couple of topics to update you on today: the launch of our disposal process for the North American contract businesses, as well as an update on trading since our half year end.

Portfolio

Let me start with our North American contract businesses. As you know, we previously set out the fact that we had appointed advisers to formally explore all options in respect of First Student and First Transit, including a potential sale. Today, I can confirm that we've completed this review and we have concluded that a sale of the two contract businesses is the best way to unlock material value for all shareholders.

First Student and First Transit are well invested and leaders in their markets. They benefit from substantial scale and a best-in-class operating track record as well as unparalleled customer satisfaction and safety records. It is no surprise to us that since our announcement we've seen significant interest in these businesses.

As a result, we've been working extremely hard, in parallel with assessing all options, to prepare the business for a sale process. This preparation has been intense and has involved expert third party consultants and advisers who have helped to design the optimal carve-out structure to be implemented and put together the detailed materials and reports appropriate for a transaction of this scale. As a result, our M&A advisers are fully prepared, and the sale process has commenced.

The process will be brought to a conclusion as fast as is practicable and appropriate to maximise value for shareholders, and given a normal process and the fact that this sale would require shareholder approval, we expect it will complete during the second half of 2020.

Alongside the decision to launch the US sale process, we're also confirming today that the First Bus and First Rail businesses will form the core of the ongoing Group, and as such I can confirm that there are no plans to pursue a separation or sale of the Bus division.

We have a market-leading position in both of these businesses, with Rail having been strengthened by the addition of the West Coast Partnership and we continue to capture the benefits of our margin improvement programmes in our Bus business. Public transport has a leading part to play in transitioning to a carbon neutral society, and with our leading position in low-emission vehicles and deep local authority relationships, we have a strong platform for the future. We're also encouraged by recent government announcements supporting significant investment in bus and confirming HS2, demonstrating how important these vital public services are to our communities, customers and stakeholders.

Trading

So having updated on the portfolio rationalisation, let me give you an update on trading. At a headline level, the trading since the half year has been consistent with our expectations. Revenue is growing in all divisions other than our Greyhound business, and on a year-to-date basis revenue is up 7.5%, reflecting the recent inclusion of Avanti West Coast since

December. So, a continuing story of the Group's ability to generate growth. Let's go into the divisions in more detail.

First Student continues to see strong commercial performance with 4% revenue growth in the period, driven by last year's good retention rates and above inflation pricing. New business wins have been positive again this year, and we are winning more contracts from our major competitors than they are winning from us, which is as a result of our first-class customer satisfaction scores and safety record. We are pleased to see that our acquisition strategy continues to gather pace, with three acquisitions made this year. The most recent was a 544 bus and van acquisition in Canada that completed at the end of February. The pressure from driver shortages and wage inflation continues, but the business is in a strong position to deliver continued revenue growth and cash flow for the full year.

First Transit is delivering revenue growth of 6% through pricing and contract wins. We continue to lead the market in autonomous vehicle trials as well as moving ahead with our transportation network company (TNC) partnerships and on our Mobility As A Service (MaaS) offering. We previously noted driver shortages and insurance costs being a drag on margins along with a couple of legacy claims, but cost efficiency programmes are moving forward to improve H2 margins.

Turning to the **Greyhound** business, as we discussed at the half year, the reduced flow of immigration volume into the south of the country, as well as ultra-low-cost airline and other bus competition has impacted revenue and we saw a revenue decline of 9% in the period. Significant work is being done to reduce mileage and labour costs in the short term, as well as seeking new commercial initiatives to stimulate demand.

With regard to our Greyhound sale process, negotiations with respect to the sale of the business are ongoing, and we will update the market as appropriate when they conclude.

Moving on to **First Bus**. Performance has been better in this period than in the first half, with revenue growing at 2%. Revenue per mile has also increased from the fare and network optimisation work that we've been engaged in. The environment has been challenged from poor weather and in particular the two recent storms, but margins have improved in the period versus H1 as cost efficiency measures start to come through, and we expect more of this to come in the next financial year.

I think it's worth saying that we're very encouraged by the level of discourse that we're seeing around buses at present. The £5bn funding package announced by the Government supports our belief that buses have a vital part to play in achieving the country's environmental, economic and social ambitions. As a leading player in this market, we’re very well placed to benefit from many of the measures announced in a number of different cities and regions.

Moving on to **First Rail**, like-for-like revenue growth was 4%. As ever, there were a number of moving parts in this division. We saw a very successful mobilisation of the Avanti franchise in December – and we’re delighted to welcome the new team to FirstGroup – and we welcomed the Government's announcement that the HS2 programme will proceed. Great Western Railway (GWR) is performing strongly with the successful introduction of their once in a generation timetable change and we continue to make good progress with our constructive discussions with the Department for Transport (DfT) for an extension to our contract post-31 March 2020. TransPennine Express (TPE) experienced difficult operating conditions due to the impact of delayed new fleet deliveries, network issues, as well as flooding, which affected our performance and our revenues, and we're working hard to bring service levels back to more acceptable levels. South West Rail (SWR) performance continues to be challenged as a result of network rail infrastructure problems and ongoing industrial unrest, and, as you know, network rail issues account for more than 70% of the delays on this line, significantly higher than on other railways. We continue our negotiations with the DfT to resolve our contractual issues. And finally, we were pleased to see that the most recent National Rail Passenger Survey showed an improvement in overall satisfaction on all of our controlled Train Operating Companies (TOCs).

So, let's talk a little bit about the **outlook**. Firstly, we should cover the final month of trading before our March year-end and these numbers that we're talking about go to the end of February. As it stands today, we're not seeing a significant impact on revenues from COVID-19 in our businesses, but we recognise that this is a fast developing situation. Absent of any deterioration of travel volumes before the end of March, or changes in Government guidance and policy as a result of COVID-19, we expect to be largely in line with our previous projections. However, it's important to note though that March is a very significant trading period for the Group and the COVID-19 position is developing quickly.

More broadly, we continue to monitor and assess the situation and are developing our plans to manage a number of scenarios. Overall, like a lot of businesses you'll have spoken to, particularly in this sector, we can't predict how this is going to play out, particularly when you look at what's happening to Italy for example at present. It is worth noting though that we do have a different profile to other operators. For example, we're not entirely dependent on direct fare-paying passengers for all of our revenue. We do have a broad geographic spread across 40 states in the USA and many regions in the UK. We've got more than 1,000 contracted customers in the US. We know that some shutdown days can be made up in our largest business, Student, but we don't know how this plays out in the event of a widespread shutdown. And, for example, in Transit, we are seeing some university campuses dictating closure in April after spring break. And also in the UK, we do have some level of revenue protection in some of our rail contracts.

But what we do know is that our businesses have good long-term prospects and have a vital part to play in both the US and UK economies, and the environmental agenda. Children will still need to be transported to school and people will still need to travel for work, business and leisure once this particular issue has been dealt with.

So, let me wrap up and summarise before opening up to questions. We've launched the sale process for First Student and Transit, and we believe that this is the best way to unlock and maximise the value in the Group for all shareholders; First Bus and Rail will form the core of the remaining Group in a market with a very positive long-term environment for public transportation; and overall trading was in line with expectations and we're delivering on our divisional strategies.

So, thank you very much for listening and with that let me open up for questions.

Sathish Sivakumar (Citi) – I have two questions. On COVID-19, if you could just briefly explain how the contracting works in the Student and Transit businesses. Is there any fixed element and a variable element which is linked to your revenue per mile or number of passenger volumes?

Secondly on the sale process, could you give us an update on Greyhound, because based on the last update, there was supposed to be an update on the Greyhound sale process. So could you let us know what is actually delaying an outcome in the Greyhound sale? Thank you.

Matthew Gregory – Sure, OK. Well thanks for that question. So, on the COVID-19 question, we do have more than 1,300 contracts in the US with individual customers and clearly each of those contracts is different. I think I would characterise it this way: So, in Student, if a school is closed down for a day or two for deep cleaning, something like that, then the treatment will be very similar to how we deal with weather shutdowns. So, each school has a budget for make-up days if there are shutdowns and we would expect that for a small number of days they would be able to make that up later in the year. As I said, it's very similar to how we deal with weather.

What's not clear is how the environment works in the case of significant shutdowns of a whole state, whole towns, for a 14 day period – like the shutdowns that we're seeing over here in Europe. Now we haven't seen that yet, but as I said, it's a very fast developing situation, we are very geographically spread, but that's one of those where we don't know how that's going to play out, how many extra days will be added, reactions from parents, all of these kind of things. So, smaller shutdowns, we think we know how that works, but a broader shutdown, like you see in Italy for example, is uncharted water for us.

In Transit, we've got a number of businesses in Transit, again, we've got a good spread of business. We have our fixed route business and we have our shuttle business, particularly, and really, they're generally being paid for providing the service, and it's irrespective of the passenger volumes. Again, as I said earlier in the call, we're seeing a couple of big universities saying they want to shut down after the spring break and we negotiate and discuss with the universities what would happen in that situation. The one area where there is a bit more direct relation to volume is the Paratransit business, which is around a third of our Transit business, where we are paid by trip for Paratransit. So again, we need to see how that plays out in the US over time.

As we all know, it's a very difficult thing for us to assess – for any business to really assess – and we're monitoring it and working through various scenarios for all of our businesses.

Coming back to the Greyhound situation; we've said there's a sale process underway. We said back in November that we were in discussions with prospective purchasers. Our negotiations are ongoing, and we are in very active negotiations, very detailed negotiations, on that sale. Clearly, as you know, with all of these M&A processes, at the point that we have concluded the sale, we will update the market accordingly.

Sathish Sivakumar – So, just to follow up on the Greyhound sale, is there a scenario where maybe a First Transit and First Student sale gets done before Greyhound? And secondly, I actually have a third question on the recent drop in crude prices: what are the benefits that you expect to see on your fuel cost?

Matthew Gregory – We are in very advanced negotiations on Greyhound, so we will update the market at the point that is concluded. The Student and Transit sale: we've done a huge amount of work for that and we are launching that process now. So, we are getting out in the market and telling the world – and we had a lot of interest in it – telling the world what a great set of assets these are. So, I think what I would say is these are very, very different businesses. The Student and Transit businesses are contractual businesses, very different dynamics to the Greyhound business, and we'll treat both of those accordingly.

On the oil price side: clearly, we've said many times in the past that the oil price, particularly in America where Americans are very keen to get into their cars: it does have an impact on the Greyhound business, so we know that there can be an impact on the business there. In terms of the hedging, we do hedging in all of our businesses for fuel, so we will see a different impact in each of our businesses. Is there anything you want to add on that, Ryan, in terms of the fuel price?

Ryan Mangold (FirstGroup CFO) – No, that's correct. The only business that we don't hedge fuel on is Greyhound because of the natural hedge we've got against revenues. But for all the other businesses, we do hedge the expected consumption of oil.

Alex Patterson (Peel Hunt) – Morning, everybody, and thank you on a very clear statement. I've got a handful of questions for you. Shall I list them all off or should I give them one at a time?

Matthew Gregory – Morning, Alex. Why don't you list them all off and then we'll work out in which order is best to answer them.

Alex Patterson – Perfect. OK. Firstly, just obviously we've seen a very big move in discount rates, and you mentioned the sensitivity of the insurance provisions to that. Would you be able to give a slight quantification of that? How much the relevant discount rates have moved and what that does to the provisions – and what that may do to what you need to do.

And on the other side, obviously you've got a lot of owned fleet in the UK and North America; it's about 45,000 student buses. Would you look at a sale and leaseback of that fleet to perhaps alleviate any downside from the insurance provisions?

Secondly, you mentioned the university campus shutdowns. Were you saying that you might get compensation for that or if not, can you give us a rough indication of what the impact would be?

Just on Student and Transit, what kind of bidders are showing interest in that? Are they infrastructure funds, private equity, or are they other operators? I don't know if you can give any colour there.

Just on First Bus, you're saying you're not pursuing a sales process – is that because you don't think the UK market will consolidate much further or rather that you just don't want to be part of that at this point in time?

And finally, just, hopefully you can get a very good price on the sale of Student and Transit. Could you just indicate what you would do with the disposal proceeds, please?

Matthew Gregory – Sure, there's a lot there. Thank you for that, Alex. Let me go through the more strategic comments and I'll let Ryan talk about the discount rate point first. So, why don't you start, Ryan, with the discount rate point?

Ryan Mangold – Alex, that's a really good question. The provision that we've got for insurance on the balance sheet for our North American, or particularly USA, operations is a long term provision that we build up over time. It's carried on the balance sheet and from an actuarial point of view, we've got to assess that based on a discount rate – and a discount rate that is moved materially as a consequence of federal intervention in the US. Currently the ten-year treasuries are sitting at about 0.69%, earlier this week they were down about 0.48%. As at the half year, the discount rate that was applied was 1.6%. So, it's awfully volatile. To put it into context for this fiscal year to the half year, the impact on the discount rates decline from full year 2019 to the half-year 2020 was approximately $10 million from going down to 1.6%. So, depending on where it actually lands at the end of the fiscal year for us on 31 March, that will determine how much of an impact that discount rate would have. The order of magnitude – it's roughly about where we are standing today – roughly about £15 million in total impact to our earnings, of which half is taken at the half year already.

This other point that you had in terms of sale and leaseback in order to be able to hand over the insurance costs to perhaps the lessor or to another provider; I think that would be quite difficult to achieve, because at the end of the day, all of our lease contracts that we currently have got in place – we've got a few of them in the business – the responsibility for insurance and maintenance actually sits with the lessee, not the lessor.

Alex Patterson – I didn't mean the insurance liabilities would move, I just meant that the value of your borrowing costs, if you were to sale and lease back would come down, because yields have declined so much.

Ryan Mangold – Yes, and for all of our acquisitions that we do make as part of our contractual commitments, for example, in Student, we do look to see what's the most efficient and effective way to finance those acquisitions, either through leases or through outright purchases, because there's a lot more into it than just simply a purchase, there are warranties, there's discount availability, there's extended credit terms, etc, that goes into our calculation and thinking on how we actually finance acquisitions.

Matthew Gregory – And I'm sure, Alex, those kind of questions will come up in the sale process: these are things that people I'm sure we'll be thinking very long and hard about, as to how best to finance the fleet. So, yeah, possibly some opportunities there.

Let me cover off the university campus piece. What I was trying to do there was just give you some examples. So we've got contracts to run for buses in Stanford and in Princeton, for example. The contracts themselves are probably worth about $10-12 million each on an annual basis. Interestingly, we've had very mixed messages. We've had one of them say, well, maybe we don't come back after spring break. One of them said, yeah, we're definitely going to do that, but then recoiled immediately because all the students are suddenly saying, "Well, hang on, we're paying you to provide services so you're going to impact my studies". So, there's a lot of moving parts and things are moving very rapidly, so I wouldn't want to try and say this is an example of how it's all going to work, but what we're trying to say is that we've not seen significant impact in the numbers up to the end of February, but this is moving on a daily basis.

Let me just come back to then the points around the transactional side of things. So, who's been interested? Well, a lot of people from a lot of different areas have been interested. So, we've had interest from private equity firms, we've had interest from strategics, we've had interest from infrastructure funds, we have had a very broad range of interest and a lot of people coming forward to us. So, I think this is the benefit of going through a process. We open it up to the market and everybody can make their interest known, and we know that these are very strong assets, well invested, market-leading, long-term fundamental growth prospects. We know – irrespective of anything that's happening with COVID-19 – we know that children have got to go to school next year, so these are good businesses that a lot of people want to get involved in, but they very rarely come onto the market at this kind of size, so as you can imagine a lot of interest there.

In terms of First Bus piece – when we've been thinking about the portfolio, the key issues for us is we've got five market leading businesses; we've said many times that there are no synergies, but we said that there were many friction costs that we had to deal with and we had to work out the best way of dealing with that. David [Martin] came into the business, with a fresh pair of eyes – he's got a huge amount of experience in this sector. We've worked very closely together, David and I, on this project and with Rothchild who have been doing this piece of work, and we have concluded that the best way to unlock and maximise shareholder value is through the sale of these two businesses, and that is the primary announcement that we're making.

We're therefore saying that then the core of this business is going to be our UK bus and rail business. And as I said earlier, there's a lot of very positive discourse around infrastructure in the UK, there's some very good announcements coming out of the government: £5 billion of funding for bus, you've got HS2 is going to proceed. So again, this is all about unlocking the value, we think that's the best way of unlocking the value and we just wanted to be clear to people that the core of the business is in good shape and in markets where there's some good potential.

And then finally, I think the last question I think was just around the use of funds. Clearly our objective is to maximise returns to shareholders. We're getting a little bit ahead of ourselves – we're starting the process now; we're expecting to maximise value, we're expecting there to be a lot of interest in these assets and we are working through plans now to determine how best to deal with the proceeds that will come out of that, but clearly I think everyone is in agreement, I think all of our shareholders are in agreement, that we need to maximise value and we want to maximise returns to shareholders, taking into account some of the legacy issues we've got to deal with.

Alex Patterson – Brilliant. Well, thank you very much indeed. That's very clear.

Stephanie D'Ath (RBC) – Hi, good morning. My first question is on the contract business divestment. Could you please share with us your expectations maybe worse and best case in terms of the timing, would you expect to conclude the divestment by the end of fiscal 2021; and in terms of how much you expect to get from that business? You might not want to comment on that for competitive reasons, but maybe can you then share where consensus valuation is and how comfortable you are at reaching that?

Secondly, on your operating expenses: could you please remind us how much is fixed versus variable in UK Bus and in UK Rail in the event of strong traffic decline as a result of the virus? How quickly can you adjust your operating expenses and to which extent are they fixed and non-adjustable? Thank you.

Matthew Gregory – Sure, well let me deal with that first question. I think the UK businesses – we have a very high percentage of fixed costs within the UK business. We are contracted to provide bus schedules – we're contracted to provide rail schedules. Rail: we know that we have a huge amount of infrastructure that we're paying for; Network Rail fees, all of that. And in the bus business; there's a large percentage of cost going into the drivers and that is what we need to run the service. So a high proportion of fixed costs, but clearly we are looking at a number of different angles and a number of different scenarios around this to deal with what is a very one-off situation here, about how we can adjust schedules, we're talking to Government as we speak as an industry (or rather as both industries) about how we can be more flexible in the way that we deal with our cost base, for example.

Coming back to the divestment. We have done a huge amount of work on this in the last three to four months since we have announced that we're doing this review of strategic options. Because we got a lot of interest immediately, we've done a lot of work up front with third-party advisers and contractors, so we're really ready to go on this, and the process has started. Now we know that these auction processes take a number of months to go through. We know that this will be a Class I transaction, so there will be a shareholder approval process, which is why we're saying we think the second half of calendar 2020 is when we would expect to conclude this transaction. We're working very hard and fast on getting this done quickly, but also making sure we maximise value for shareholders.

And to that point, you're right, I'm not going to talk about value. There's no point in me bidding against myself for this business, but what we do know is these are extremely valuable assets and I think everyone that we talk to, all of our shareholders that we consult with, all agree that these are valuable assets, they've got long term fundamentals, they've got well invested asset bases, they've got good contracts spread across the entire country. So we think these are very, very valuable assets; so again, that's why we're seeing this high level of interest in the process that we've launched today.

[Donna XIM] – Hi, I just quickly want to ask what are your plans in terms of refinancing the upcoming 2021 maturity and for the rest of the debt as well, what are your plans? And maybe you can give us some colour on what are you planning to do with the pension deficit? And in terms of the sale announcement: on the investment grade rating, do you think you'd be able to still keep the rating?

Ryan Mangold – Okay, thanks Donna. For the refinancing of the £350 million bond that matures in April 2021, we're currently in the process of putting in financial capacity to be able to deal with that. Bearing in mind we've just announced the potential sale of our North American business, and so the entire capital structure for 'RemainCo' would need to be looked at in the context of all of the fixed financing streams that we've currently got in and so we will update the market in due course with that.

With regards to the pension deficit, I presume you're asking specifically on UK Bus in terms of the implications of a transaction or are you asking a question about the ongoing funding for UK pensions?

Donna – The ongoing funding for UK pensions. Would some of the proceeds from the sale be used to close the deficit?

Ryan Mangold – Yeah, so the UK Bus pensioners are clearly a key stakeholder in our business, and they'll have a keen interest on anything as significant as this from a strategic change, from the business perspective and we've engaged very positively with the pension trustee as part of separating the portfolio. As indicated in our November update for the half-year, we've got a framework in place that we think is a good framework to be applied both by the trustee and the company, with the aim of trying to get the Bus pension fund on to a 'low dependency' basis, and we think that's ultimately where we're going to get to. As I say, we're only going to start engaging more positively with the trustee as the transaction evolves because one of the key points that they will have from their perspective is what is the 'RemainCo' covenant look like, which is what we will engage with them on going forwards.

At the moment, we are finalising the April 2019 valuation with the trustee and agreeing with them what the deficit repairs would be; but to the extent that we pay any deficit repairs off the April 2019 valuation, that clearly would be taken into account in determining how much we need to contribute as part of the sales process for selling Student and Transit.

Following the sale process, will we remain as investment grade? That's clearly a fairly important measure for us and so to have a well-capitalised balance sheet would be generally the intention and we will embark on that once we're a bit more advanced with the process.

Donna – Thank you for your answers. Maybe just a little bit on what would be the plans for the rest of the debt? Would it be restructured? Would it be separated once the sale has been announced? Maybe part would be passed on to anyone who's buying the business, or would you still keep all of this? Or would you pay down? Any idea on it?

Matthew Gregory – The key thing is that we're announcing the commencement of the process today, which I think is very positive news. There's work to be done; we're getting a little bit ahead of ourselves, in terms of how we're going to deal with the proceeds. But I think our key issue, and I think David would probably agree at this point as well: the primary objective here is to maximise value and maximise returns to the shareholders. But we have to work through all of this. There's a lot of issues that we've got to work through: the debt structure, the pensions. There's a lot of issues we're working through.

Gerald Khoo (Liberum) – Morning, everyone. Gerald Khoo from Liberum here. You talked about March being a significant trading period for the Group. I'm just wondering whether you could give an indication as to whether you can quantify that? Obviously relative to say one twelfth being the average, how much more important is it?

Secondly, with regard to the Greyhound sale process: what alternatives have you considered to a sale? Obviously, that process is now getting on for nearly a year, what alternatives have you considered, or would you contemplate?

On South Western, I think you made reference to ongoing talks about the contractual situation. Would default on the franchise pre-empt those talks or are they basically effectively one and the same thing in terms of the wider discussion?

And finally, you talked at length about the attractions of the North American contract businesses. Whilst I'm not challenging the decision to separate, what's the rationale for keeping the UK and selling the US as opposed to the other way around?

Matthew Gregory – So, thanks Gerald for that. I'll deal with these on process and then maybe we'll talk about the attractions, and perhaps David will have some comments on this as well, because he knows these markets extremely well.

On the trading, we're not going to get into exactly how much is March worth. If we get into the technicalities, March is a five-week month for us, from the way that we do our reporting, so that's why that's relevant to us, it's also a period where generally all the schools are in, all the universities are in, people are all working, so that's why it's a bigger month for us. But we're not going to get into how much it is to tell you exactly month by month what everything is – obviously, Easter has a big impact on that as well.

I think on Greyhound, what I would say is that we are in active negotiations. The guys here are heavily involved in genuine negotiations, discussions on the sale of that business. This is not just a theoretical "we're talking to a few people" type of thing – this is really right down to nuts and bolts, nitty gritty, and at the point that we've got something to say on that, then we will say it.

Obviously, we've looked at other options. We recognise there's a huge amount of property within that business, so this is why we are taking care to make sure we get the best deal we can for the business that we currently have. So, we've looked at a number of options there, but as soon as we have something to update, then we will do that.

On SWR, I think we've got a number of things going on at the moment in the rail division. We've got Great Western where we've had good discussions, good progress being made on that and we need to get that sorted out before the end of this month, that's the end of the current franchise. The SWR negotiations are ongoing, we need to make sure that we have reflected the fact that we've got huge amounts of infrastructure issues – we've got a railway where 70% of the issues are down to Network Rail, which is much higher than on other franchises, we've got industrial unrest there as well and we need to make sure we put ourselves on a better footing at a better balance of risk and reward on that franchise. So those are negotiations that are ongoing and at the point that we're able to conclude on those, we will update you.

I think coming onto the final point, which is the attractiveness: we believe that all of our businesses are market leading and we've talked about that before – we've just said that there are no synergies between them. Through the work we did last year, we've been able to really get under the skin of the pensions and really see what a solution could be there, and we've obviously had the rail business that has been bolstered by the West Coast Partnership, and we've done a huge amount of work to look at the options for the North American business and we have considered all those options.

But I think, from my perspective, I think all of our businesses have good long-term fundamentals: Student, Transit, absolutely, I talked about those before – but the UK bus business and the rail business is seeing a really high profile, a lot of discussion. David, I wonder whether in your time this has been – to me this seems like this is one of the most interested the government's been in bus for a long time and the attractions of that UK market?

David Martin (FirstGroup Chairman) – Honestly, I totally agree with you, Matthew. At the moment, in my experience, this is one of the most exciting times, with potentially real deliverables there and money standing behind it – both in pursuit of the sustainability agenda but also maybe the intention of replacing routes: not from the Beeching cuts but from local authorities who effectively are not prepared and cannot afford to actually support the social services in their networks, that really has driven the reduction in patronage. For the first time in my 30 years, I actually believe it's actually going to happen, and society needs it, environmentally we need it and we've got a business here that could actually deliver.

To come back to your direct question, Gerald: as you know I came in in September last year right after the announcement of the successful winning of the Avanti franchise. Everybody understands and knows that at the moment rail is a complete mystery and a mess, but it's not that much of a mess for FirstGroup. We've actually got Avanti, it's delivering, I'm quite happy with the contract there, I think there's a basis there to go forward with. We have Open Access, we have Hull Trains – which delivers more profit, that's for sure, than South Western Railway will – and we have a new Open Access on the East Coast, which is quite exciting actually and that will come into play I think at the back end of next year. So, suddenly we're starting to get a picture here… And of course, we are discussing a direct award of Great Western and maybe a switch to a management contract in South Western. So, we could find ourselves with a rail business that's actually pretty robust and will actually generate cash to give us that robustness going forward, alongside a UK bus business in an environment within the political agenda which is far stronger than I've ever seen before and it's a UK bus business that has seriously underperformed for years.

And one of the rationales here is we know we can improve it, we will improve the margin in that business and we will continue to demonstrate additional value in that context. I'd like to just to reflect on this perception of why Bus is not better. I totally agree with what Matthew says. I've been working with the exec directors since I joined in reality, understanding the dynamics and legacy issues that sit within this business. Fundamentally, over the course of those weeks it became quite clear on the best way to deliver shareholder value… This is after long discussions with all our major shareholders – I have a very clear steer as to what shareholders are expecting, I've a very clear steer as to the impatience of our shareholders. And when we reflected on it the jewel in our crown, let's be honest, is our North American business. Clearly there's no synergies between the two [the UK and North American businesses]. That's been made quite apparent. And the more we looked at it and with appointed independent advisers, the more they looked at it, it became apparent that the way of realising maximum shareholder value was to unlock that value in our North American businesses.

Now some of you may say, but why is it taking so long to get to where we are today? I'm sure there's an unwritten question out there or maybe it's coming. The fact is, we actually came to this conclusion in November. We told the market in December. Since then we have been rigorously and robustly pursuing that sale process, to make sure that we get ourselves into a position where we can make it as informative and seamless to potential bidders, which I believe we're now in, that we're in the correct position to actually go forward with that disposal.

Now shareholders, as you know – you've seen they have views on where the value may be. We are all in violent agreement, is the only thing I can say. Everybody is on the same page in the one direction of maximising shareholder value and providing the ability to create substantial returns to shareholders in the short term, or within the second half of this year. That's our plan of action, we're extremely robust about it, and we're looking forward to moving forward.

Gerald Khoo – OK, thanks very much.

Erik Salz (JPMorgan) – Hi, good morning. Erik Salz, JPMorgan. Just a question on the strategy: I think last year there was a discussion about how to proceed with rail and waiting for the Williams review and see where the risk/reward model will end up. Now you're saying bus and rail will be the core of the business following the sale of the US contract businesses, but why is the conclusion now drawn that rail is a core part of the business while the Williams review is still not out there and the risk/reward model for the future is also unclear?

Matthew Gregory – Well we talked about some of that at the point of the West Coast Partnership. David has put forward just a second ago a very clear view on our existing franchises and how working through this, there is some real value to be generated from rail. The West Coast partnership, that franchise or partnership as they want to call it, was effectively blessed by Keith Williams and he was basically saying that this is the type of franchise that I want to have going forward. For us, it's about risk and reward: we think there's much better risk and reward mechanisms on the West Coast Partnership. As David said we're close to the Great Western award, working through discussions on that, we've got Open Access opportunities, so I think the position has changed significantly since last year. We will welcome the Williams review, and we're looking forward to that being published, but I think the key thing is that West Coast Partnership was effectively blessed by him [Keith Williams] as we took that one on.

Erik Salz – All right, if I may ask two follow-ups. So, the other part of the future strategy: it will be a UK-based business, so does it rule out businesses outside of the UK, and bus and rail being the core of the strategy: does it rule out other modes of transportation in the future?

Matthew Gregory – No, it doesn't rule it out –the announcement today is around the commencement of the sale of our North American contract businesses. As we've said, there's a huge amount of work gone into that, and we're running very hard at that process. At the same time, we're just being clear to people that if we're selling the US businesses, then the UK businesses of today will be the core of our business, but that doesn't rule out growth opportunities as we move forward, whether that is geographically, whether that's different modes of transport, as we move forward as a plc.

That's great. Well, thank you everybody for your time today and we will speak to you at our next update at the end of May. Thanks very much.