DRIVING AN EFFICIENT RAILWAY: NETWORK RAIL'S FULL YEAR RESULTS 2010/11

9 June 2011

Network Rail continued to make steady progress in reducing its costs and remains on target to achieve the challenging efficiency savings set out for its current funding period – control period 4 (CP4) which runs from 2009-2014. In real terms, it has reduced the costs of running the railway by £400m in the year and around £600m since the start of CP4.

Group finance director, Patrick Butcher, said: "The findings of the government-commissioned McNulty value for money review show that there are clear opportunities for the whole industry to make further savings in the costs of running the railway. The message is clear: the rail industry simply has to become more affordable for the users of the railway network and for tax payers."

Network Rail has taken a number of significant steps during the year in pursuit of delivery beyond our regulatory targets and to position the company for the longer term ambition set out in the McNulty review.

Financial highlights

- Revenue was £5,712m (2009/10: £5,668m)
- Operating profits were £2,028m (2009/10: £1,981m)
- Profit after tax was £313m (2009/10: £284m)
- Capital expenditure was £3,997m (2009/10 : £3,920m)
- Net debt at year end was £25,049m (2009/10: £23,838m)
- Gearing ratio (debt to regulated asset base) was 63.4% (2009/10: 63.9%)

Efficiencies

- Operating costs, excluding depreciation reduced to £2,467m from £2,546m
- Staff costs fell to £1,734m from £1,746m. Staff numbers fell to 35,606 from 37,153 although average salaries rose by 1.5%.
- Operating and maintenance costs per train mile in real terms have fallen by 77p to £7.61 during the last year – down from £11.64 seven years ago
- An example of how efficiency has been improved is that better use of high-output plant has reduced the cost of track renewal by 6.5%
- The maintenance division was restructured, saving over £100m pa

Performance results

- In 2010/11 90.9% of passenger trains ran on time down on the 2009/10 figure of 91.5%
- The drop in performance was mainly as a result of the severe winter weather

Projects

There has been further progress in the number and scope of vital enhancement projects Network Rail is managing, to add capacity to the railway and drive economic growth. Some highlights include:

- Airdrie to Bathgate – a new line built in Scotland, opened in December 2010
- A new station building was opened at Newport
- The programme of work for the London 2012 Olympics is largely completed. This includes new lines, new stations and better facilities on the North London Line and East London Line, in addition to works to support the transport links being developed in the Stratford area
- The new concourse building at King's Cross is nearing completion and will open in October 2011
- Construction is well advanced on the Thameslink programme – major milestones completed included the track switch at Blackfriars and the installation of the Borough High Street viaduct
- Major milestones have been completed on the Reading project including the Caversham Road bridge replacement
- The Birmingham Gateway project is making good progress – a deal was signed to build a new John Lewis store at the site – this brings £100m of third-party funding
- Preparatory work on electrification schemes in the north west and on the Western route has started

Mr Butcher concluded: "This is a moment of great potential for the rail industry, where real reform for the benefit of user and taxpayer is a genuine possibility. Network Rail has been in the vanguard of change over the past year and will continue to drive for rapid, safe evolution. Examples of our initiatives include moving decision making closer to our customers, partnering with key industry players and setting up the potential for greater competition as a stimulus to further improvements in performance. There can be no turning back for reform – the key question we face is how to deliver at an ever increasing pace."

Financial highlights
For the year ended 31 March 2011

	2011 £m	2010 £m
Revenue	5,712	5,668
Operating profit	2,028	1,981
Profit before tax	438	395
Profit after tax	313	284
Net cash from operating activities	2,486	2,234
Net debt	(25,049)	(23,838)
Net assets	7,689	6,555
Railway network fixed assets	39,577	36,629
Investment property	778	764
Capital expenditure	3,997	3,920

Income statement
For the year ended 31 March 2011

	Note	Results pre debt and derivative revaluations 2011 Group £m	Debt and derivative revaluations 2011 Group £m	2011 Group £m	2010 Group £m
Revenue	2	5,712	-	5,712	5,668
Net operating costs	3	(3,684)	-	(3,684)	(3,687)
Operating profit		2,028	-	**2,028**	**1,981**
Revaluation movements and profits on disposal of properties		11	-	11	62
Total profits from operations	4	**2,039**	-	**2,039**	**2,043**
Investment revenue		83	-	83	26
Other gains and losses		-	(183)	(183)	(477)
Finance costs		(1,501)	-	(1,501)	(1,197)
Profit before tax		**621**	(183)	**438**	**395**
Tax	5	(176)	51	(125)	(111)
Profit for the year attributable to equity shareholders		**445**	**(132)**	**313**	**284**

All amounts in the current and prior years relate to continuing operations.

Statement of other comprehensive income
For the year ended 31 March 2011

	2011 Group £m	2010 Group £m
Profit for the year	313	284
Gains/(losses) on revaluation of the railway network	222	(1,033)
Losses on cash flow hedges	(251)	(179)
Recycling of balances in hedging reserve to the income statement	5	4
Exchange differences on cash flow hedges recycled from the hedging reserve	360	154
	114	**(21)**
Actuarial gains/(losses) on defined benefit pension schemes	545	(292)
Tax relating to components of other comprehensive income	(60)	376
Other comprehensive income/(loss) for the year	**821**	**(970)**
Total comprehensive income/(loss) for the year attributable to equity shareholder	**1,134**	**(686)**

Statement of changes in equity

For the year ended 31 March 2011

Group	Share capital £m	Share Premium £m	Revaluation Reserve £m	Other Reserve* £m	Hedging Reserve £m	Retained Earnings £m	Total £m
Balance at 1 April 2009	**160**	**85**	**4,298**	**1,458**	**(318)**	**1,558**	**7,241**
Profit for the year	-	-	-	-	-	284	284
Other comprehensive income							
Revaluation of the railway network	-	-	(1,033)	-	-	-	(1,033)
Transfer of deemed cost depreciation from revaluation reserve	-	-	(147)	-	-	147	-
Decrease/(increase) in deferred tax liability on the railway network	-	-	330	-	-	(41)	289
Actuarial losses on defined benefit pension schemes	-	-	-	-	-	(292)	(292)
Deferred tax on actuarial losses	-	-	-	-	-	82	82
Decrease in fair value of hedging derivatives	-	-	-	-	(179)	-	(179)
Exchange differences on cash flow hedges recycled from the hedging reserve	-	-	-	-	154	-	154
Deferred tax on all hedging reserve movements/retained earnings	-	-	-	-	5	-	5
Recycling of balances in hedging reserve to the income statement	-	-	-	-	4	-	4
Total comprehensive (loss)/income	-	-	(850)	-	(16)	180	(686)
Balance at 31 March 2010	**160**	**85**	**3,448**	**1,458**	**(334)**	**1,738**	**6,555**
Profit for the year	-	-	-	-	-	313	313
Other comprehensive income							
Impact of change in tax rate			103	-	(10)	(18)	75
Revaluation of the railway network	-	-	222	-	-	-	222
Transfer of deemed cost depreciation from revaluation reserve	-	-	(158)	-	-	158	-
Increase in deferred tax liability on the railway network	-	-	(17)	-	-	(41)	(58)
Actuarial gains on defined benefit pension schemes	-	-	-	-	-	545	545
Deferred tax on actuarial gains	-	-	-	-	-	(142)	(142)
Decrease in fair value of hedging derivatives	-	-	-	-	(251)	-	(251)
Exchange differences on cash flow hedges recycled from the hedging reserve	-	-	-	-	360	-	360
Deferred tax on all hedging reserve movements/retained earnings	-	-	-	-	65	-	65
Recycling of balances in hedging reserve to the income statement	-	-	-	-	5	-	5
Total comprehensive income	-	-	150	-	169	815	1,134
Balance at 31 March 2011	**160**	**85**	**3,598**	**1,458**	**(165)**	**2,553**	**7,689**

*Other reserves of £1,458m (2010: £1,458m) include the vesting reserve on privatisation.

Balance sheet

At 31 March 2011

	Note	2011 Group £m	2010 Group £m
Assets			
Non-current assets			
Intangible assets		71	72
Property, plant and equipment - the railway network	6	39,577	36,629
Investment property		778	764
Loan to immediate parent company		397	391
Derivative financial instruments		576	702
Finance lease receivables		6	8
Interest in joint venture		5	5
Total non-current financial assets		**984**	**1,106**
		41,410	**38,571**
Current assets			
Inventories		108	132
Finance lease receivables		1	2
Trade and other receivables		905	720
Derivative financial instruments		-	6
Current tax assets		104	297
Cash and cash equivalents		771	2,321
		1,889	**3,478**
Total assets		**43,299**	**42,049**
Current liabilities			
Trade and other payables		(2,823)	(3,043)
Current tax liabilities		(7)	-
Bank loans and overdrafts		(2,314)	(2,223)
Derivative financial instruments		(373)	(210)
Short-term provisions		(17)	(57)
		(5,534)	**(5,533)**
Net current liabilities		**(3,645)**	**(2,055)**
Non-current liabilities			
Bank loans		(23,345)	(23,380)
Derivative financial instruments		(574)	(507)
Other payables		(2,293)	(1,887)
Retirement benefit obligation		(485)	(985)
Deferred tax liabilities		(3,377)	(3,200)
Obligations under finance leases		(2)	(2)
		(30,076)	**(29,961)**
Total liabilities		**(35,610)**	**(35,494)**
Net assets		**7,689**	**6,555**
Equity			
Share capital		160	160
Share premium account		85	85
Revaluation reserve		3,598	3,448
Other reserve		1,458	1,458
Hedging reserve		(165)	(334)
Retained earnings		2,553	1,738
Total shareholder's funds and equity attributable to equity holders of the parent company		**7,689**	**6,555**

Statement of cash flows

For the year ended 31 March 2011

	Note	2011 Group £m	2010 Group £m
Net cash generated from operating activities	7	**2,486**	**2,234**
Investing activities			
Interest received		77	24
Purchases of property, plant and equipment - the railway network		(3,759)	(3,939)
Proceeds on disposal of investment property		12	1
Capital grants received		186	339
Capital element of finance leases' receipts		2	2
Net cash used in investing activities		**(3,482)**	**(3,573)**
Financing activities			
Repayments of borrowings		(1,926)	(1,416)
New loans raised		1,782	4,053
Collateral repaid to counterparties		(395)	(508)
Losses on derivatives not hedge accounted		(15)	(192)
Net cash generated from financing activities		**(554)**	**1,937**
Net increase/ (decrease) in cash and cash equivalents		**(1,550)**	**598**
Cash and cash equivalents at beginning of the year		2,321	1,723
Cash and cash equivalents at end of the year		**771**	**2,321**

Notes to the financial statements

For the year ended 31 March 2011

1. General information

The financial information set out in this preliminary announcement does not constitute the Group's statutory accounts for the years ended 31 March 2011 or 31 March 2010 but is derived from those accounts. Whilst the financial information has been prepared in accordance with International Financial Reporting Standards (IFRSs) and IFRS Interpretations Committee updates as adopted by the European Union, this announcement itself does not contain sufficient information to comply with IFRSs. Statutory accounts for the year ended 31 March 2010 have been delivered to the Registrar of Companies and those for the year ended 31 March 2011 will be delivered following the Group's annual general meeting. The auditors have reported on those accounts; their reports were unqualified. The preliminary announcement has been prepared on the basis of the accounting policies as stated in the previous year's financial statements as no new Standards, Amendments or Interpretations that became effective in the financial year had an impact on the Group's results. The preliminary announcement was approved by the board on 8 June 2011.

Going concern

The Group has considerable financial resources together with long term contracts with a number of customers and suppliers. As a consequence, the Directors believe that the Group is well placed to manage its business risks.

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

2. Revenue

	2011 Group £m	2010 Group £m
Franchised track access and grant income	5,408	5,387
Freight revenue	43	52
Property rental income	244	206
Other income	17	23
	5,712	**5,668**

The net effect of the performance regimes on the results of the Group was net loss of £14m (2010: net income £42m).

3. Net operating costs

	2011 Group £m	2010 Group £m
Employee costs	1,734	1,746
Own costs capitalised	(623)	(680)
Other external charges (including infrastructure maintenance costs)	1,601	1,730
Other operating income	(245)	(250)
Net operating costs before depreciation	**2,467**	2,546
Depreciation and other amounts written off non-current assets	1,271	1,193
Capital grants amortised	(54)	(52)
Net operating costs	**3,684**	**3,687**

4. Profit from operations

Profit from operations is stated after charging/(crediting):

	2011 Group £m	2010 Group £m
Research and development costs expensed	1	1
Depreciation and other amounts written off property, plant & equipment	1,271	1,193
Amortisation of intangible fixed assets	1	1
Amortisation of capital grants	(54)	(52)
Profit on sale of properties	(12)	-
Decrease/(increase) in the fair value of investment properties	1	(62)
Write downs of inventories recognised as an expense	10	7
Cost of inventories recognised as an expense	176	179
Employee costs	1,734	1,746
Amounts payable to auditors		
Fees payable to the Company's auditors for the audit of the Company's annual accounts	0.27	0.37
Fees payable to the Company's auditors for other services to the Group		
- The audit of the Company's subsidiaries pursuant to legislation	0.03	0.04
Total audit fees	0.30	0.41
Other services pursuant to legislation		
- Regulatory accounts audit and interim review	0.08	0.12
- Other	0.02	0.02
Total non-audit fees	0.10	0.14
Total amounts payable to auditors	0.40	0.55

5. Tax

	2011 Group £m	2010 Group £m
Current tax:		
UK Corporation tax at 28% (2010: 28%):		
Corporation tax charge	(19)	(1)
Less advance corporation tax (ACT) set-off	13	-
Corporation tax liability	**(6)**	**(1)**
Prior year (charge)/credit	4	8
Group relief payable to Network Rail Holdco Limited	(6)	(3)
Total current tax	**(8)**	**4**
Deferred tax:		
Deferred tax at 26% (2010: 28%)		
Current year charge	(131)	(120)
Effect of rate (charge)/credit	163	-
Prior year (charge)/credit	(149)	5
Total deferred tax	**(117)**	**(115)**
Total tax	**(125)**	**(111)**

The adjustment of £149m in respect of prior years relates to reassessments of provision for deductions in capital allowances.

Deferred tax is calculated at a rate of 26% (2010: 28%). The 26% rate is also used for the reconciliation above as the tax charge is substantively deferred tax.

UK corporation tax is calculated at a rate of 28% (2010: 28%).

6. Property, plant and equipment – the railway network

	Group £m
Valuation	
At 1 April 2009	34,925
Additions	3,920
Depreciation charge for the year	(1,193)
Transfers from investment property	10
Revaluation in the year	(1,033)
At 1 April 2010	**36,629**
Additions	**3,997**
Depreciation charge for the year	**(1,271)**
Revaluation in the year	**222**
At 31 March 2011	**39,577**

Given the interdependency of the assets comprising the railway network, the Group has concluded that the railway network is a single class of asset. The railway network is carried at its fair value, which is measured as the estimated future cash flows that are expected to be generated in perpetuity, discounted at the Group's pre-tax rate of return, as set by independent rail regulator, the Office of Rail Regulation (ORR) in its Access Charges Review. This rate reflects the risks and opportunities that exist in the regulated market for railway infrastructure assets and equates to the cost of capital for this market.

Because there is no active market in railway infrastructure assets, the Group has derived the fair value of the railway network using an income approach. The income approach assesses the discounted future cash flows that are generated by the railway network. This valuation is carried out annually and revaluation gains and losses are reflected in other comprehensive income.

The depreciation charge for the year is calculated using the average carrying value for the year and the estimated weighted average remaining useful economic life of the railway network. The weighted average remaining economic life of the railway network was calculated using the engineering assessment of serviceable economic lives of the major categories of asset that comprise the railway network. The estimated remaining weighted average useful economic life of the network is currently 30 years (2010: 30 years).

As at 31 March 2011 the comparable valuation of the railway network according to the historical cost convention is £35,015m (2010: £32,157m).

At 31 March 2011, the Group had entered into contractual commitments in respect of capital expenditure amounting to £1,501m (2010: £1,436m).

7. Notes to the statement of cash flows

	2011 Group £m	2010 Group £m
Operating profit from operations	2,028	1,981
Adjustments for:		
Depreciation of the railway network	1,271	1,193
Amortisation of capital grants	(54)	(52)
Amortisation of intangible assets	1	1
(Decrease)/increase in provisions	(39)	48
Operating cash flows before movements in working capital	**3,207**	**3,171**
Decrease/(increase) in inventories	24	(44)
Decrease in receivables	52	67
Increase/(decrease) in payables	139	(29)
Cash generated from operations	**3,422**	**3,165**
Income taxes paid	-	(20)
Interest paid	(936)	(911)
Net cash generated from operating activities	**2,486**	**2,234**

Cash and cash equivalents

Cash and cash equivalents (which are represented as a single class of assets on the face of the Balance sheet) comprise cash at bank, collateral held from counterparties and money market deposit investments, all of which are on call with the exception of £21m of short term deposits with an average term of one day (2010: one day) from the Balance sheet date. In 2010/11 cash and money market deposits had an average maturity of one day (2010: six days) from the Balance sheet date.

8. Analysis of changes in net debt

	At 1 April 2010 £m	Cash flows £m	Non cash movements £m	Capital accretion £m	Amortisation of discount £m	Fair value through profit and loss and fair value hedging movements £m	Foreign exchange movements £m	At 31 March 2011 £m
Cash and cash equivalents*	1,767	(1,155)	-	-	-	-	-	612
Borrowings due within one year	(2,223)	1,860	(2,360)	-	-	65	344	(2,314)
Borrowings due after one year	(23,380)	(1,716)	2,360	(657)	-	32	16	(23,345)
Obligations under finance leases	(2)	-	-	-	-	-	-	(2)
	(23,838)	**(1,011)**	**-**	**(657)**	**-**	**97**	**360**	**(25,049)**

	At 1 April 2009 £m	Cash flows £m	Non cash movements £m	Capital accretion £m	Amortisation of discount £m	Fair value through profit and loss and fair value hedging movements £m	Foreign exchange movements £m	At 31 March 2010 £m
Cash and cash equivalents	661	1,106	-	-	-	-	-	1,767
Borrowings due within one year	(1,773)	1,189	(1,970)	(2)	(2)	231	104	(2,223)
Borrowings due after one year	(21,192)	(3,826)	1,970	(345)	(7)	(30)	50	(23,380)
Obligations under finance leases	(3)	1	-	-	-	-	-	(2)
	(22,307)	**(1,530)**	**-**	**(347)**	**(9)**	**201**	**154**	**(23,838)**

* Excludes collateral of £159m (2010: £554m).