Network Rail half-year results 2012/2013

Financial highlights of the last six months

- Revenue was £3,167m compared to £2,997m for the same period last year
- Operating profit was £1,226m compared to £1,227m
- Profit after taxation was £573m compared to £136m
- Capital expenditure – the amount invested in the railway over the period – was £2,064m compared to £2,071m
- Net borrowings were £28,043m compared to £27,200m at 31 March 2012

Patrick Butcher, Network Rail's group finance director said: "The railway continues to see strong traffic growth which provides us with the challenge of getting the balance right between capacity, reliability and efficiency. We have seen growth on the network of 5% a year for a decade and this is set to continue. That means we continue to become more efficient so we can continue to invest to meet this growth."

"This, combined with the traffic growth allow us to sustain high levels of capital investment, delivering £2.1bn of worth of capital work in the six months."

Investment

Investment in the railway continues, with a further £2.1bn outlay in the half year. The level of expenditure is the same as in the corresponding period last year, despite the suspension of work during the Olympics and the reduction in activity following the achievement of key milestones on the King's Cross and Thameslink projects.

There has been a significant ramping up of activity on the Reading Station area redevelopment project together with works on the East Coast main line and West Coast main line.

Milestones were also achieved on Southern platform lengthening and East London line works.

Revenues

Revenue in the period increased in line with expectations. The majority of Network Rail's turnover increases annually in line with the retail price index (RPI), in accordance with the regulatory settlement. The RPI increase for the period was 5.2%.

Borrowings

As anticipated, net borrowings have increased from £27,200m at the year end to £28,043m. The increase is primarily due to the funding of capital investment and to a lesser extent the increase in the valuation of RPI-linked bonds. £1.5bn was raised in the half year through the issue of six new bonds, denominated in US dollars and sterling. US dollar issues are immediately swapped to sterling so no currency risk is taken. During the first six months of the year £600m was raised under the commercial paper programme.

Assets

The value of the railway network increased to £45,342m from £43,112m at 31 March 2012. The increase reflects £2,064m of capital investment in the infrastructure, depreciation of £737m and an upwards revaluation of £903m, largely because of inflation.

Outlook

Mr Butcher concluded: "Network Rail continues to evolve. Last year we completed devolving authority to all ten of our routes and now we can make progress to moving to a group structure that reflects this. We have already set up our infrastructure projects division as a standalone business unit, launched Network Rail Consulting as our international business and we have plans to run our energy, telecoms and recycling operations each with their own profit and loss account. We believe this will generate greater efficiencies and unlock greater value to the business.

"Our daily focus remains on running safe, reliable and efficient railway service for passengers and freight users alike. Whilst train punctuality is at high, historical levels Network Rail recognises that on parts of network performance is not as good as it should be. As we have before, we will continue to take any appropriate action to improve services."

Contact information

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About Network Rail

Network Rail is the not for dividend owner and operator of Britain's railway infrastructure, which includes the tracks, signals, tunnels, bridges, viaducts, level crossings and stations - the largest of which we also manage. We aim to provide a safe, reliable and efficient rail infrastructure for freight and passenger trains to use.
www.networkrailmediacentre.co.uk Twitter: @networkrailPR

Financial highlights

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Variance £m	Variance %
Revenue	**3,167**	2,997	170	6%
Net operating costs excluding depreciation and amortisation	**(1,240)**	(1,117)	(123)	(11%)
Net operating costs	**(1,941)**	(1,770)	(171)	(10%)
Operating profit	**1,226**	1,227	(1)	-
Profit after tax	**573**	136	437	321%
Net cash from operating activities	**1,430**	1,537	(107)	(7%)
Capital expenditure	**2,064**	2,071	(7)	-

	Unaudited 30 September 2012 £m	Unaudited 30 September 2011 £m	Variance £m
Net borrowings	**28,043**	25,609	2,434
Net assets	**9,745**	8,665	1,080
Property, plant and equipment – the railway network	**45,342**	42,112	3,230
Investment property	**876**	879	(3)

Commentary

Summary

The railway continues to see strong traffic growth which provides us with the challenge of getting the balance right between capacity, reliability and efficiency. We have seen growth on the network of 5% a year for a decade and this is set to continue. That means we continue to become more efficient so we can continue to invest to meet this growth.

Network Rail continues to make progress in becoming more efficient. This, combined with the traffic growth allow us to sustain high levels of capital investment, delivering £2.1bn of worth of capital work in the six months.

Investment

Investment in the railway continues, with a further £2.1bn outlay in the half year. The level of expenditure is the same as in the corresponding period last year, despite the suspension of work during the Olympics and the reduction in activity following the achievement of key milestones on the King's Cross and Thameslink projects. There has been a significant ramping up of activity on the Reading Station Area Redevelopment project together with works on the East Coast Mainline and West Coast Mainline.

Milestones were also achieved on Southern Platform Lengthening and East London Line works.

Revenues

Revenue in the period increased in line with expectations. The majority of Network Rail's turnover increases annually in line with the Retail Price Index (RPI), in accordance with the regulatory settlement. The RPI increase for the period was 5.2%.

Borrowings

As anticipated, net borrowings have increased from £27,200m at the year end to £28,043m. The increase is primarily due to the funding of capital investment and to a lesser extent the increase in the valuation of RPI-linked bonds. £1.5bn was raised in the half year through the issue of six new bonds, denominated in US dollars and sterling. US dollar issues are immediately swapped to sterling so no currency risk is taken. During the first six months of the year £600m was raised under the Commercial Paper programme.

Assets

The value of the railway network increased to £45,342m from £43,112m at 31 March 2012. The increase reflects £2,064m of capital investment in the infrastructure, depreciation of £737m and an upwards revaluation of £903m, largely because of inflation.

Risks and Uncertainties

The principal risks and uncertainties affecting the business activities of the Group were set out on page 39 of the Annual Report and Accounts for the year ended 31 March 2012, a copy of which is available on the Group's website www.networkrail.co.uk

The Group's key risks and uncertainties are summarised under the headings of:

- Safety;
- Performance;
- External environment;
- Network enhancement;
- Finance; and
- People.

In the view of the Board the key risks and uncertainties for the remaining six months of the financial year continue to be those set out in the above section of the 31 March 2012 Annual Report and Accounts. In particular it should be noted that the autumn and winter seasons provide additional performance risks, due to increases in weather-related and track adhesion-related delays. The critical accounting judgements and key sources of uncertainties relating to these interim financial statements are set out on pages 15 and 16.

Outlook

Network Rail continues to evolve. Last year we completed devolving authority to all ten of our routes and now we can make progress to moving to a group structure that reflects this. We have already set up our infrastructure projects division as a standalone business unit, launched Network Rail Consulting as our international business and we have plans to run our energy, telecoms and recycling operations each with their own profit and loss account. We believe this will generate greater efficiencies and unlock greater value to the business.

Our daily focus remains on running safe, reliable and efficient railway service for passengers and freight users alike. Whilst train punctuality is at high, historical levels Network Rail recognises that on parts of network performance is not as good as it should be. As we have before, we will continue to take any appropriate action to improve services.

Patrick Butcher
Finance Director
21 November 2012

Statement of directors' responsibilities

The directors confirm that this condensed consolidated interim financial information has been prepared in accordance with IAS 34 as adopted by the European Union and that the interim management report includes a fair review of the information, namely:

- an indication of important events that have occurred during the first six months and their impact on the condensed consolidated interim financial information and a description of the principal risks and uncertainties for the remaining six months of the financial year; and

- material related party transactions in the first six months of the financial year and any material changes in the related party transactions described in the last Annual Report.

The directors of Network Rail Infrastructure Limited are listed in the Network Rail Infrastructure Limited Annual Report and Accounts for the year ended 31 March 2012. Since that report there have been four changes to the Board composition in that Peter Henderson, Richard Haythornthwaite and Stephen Russell resigned as directors on 19 July 2012 and Michael O'Higgins was appointed a non-executive director on 21 November 2012. A list of current directors is available on the Group's website: www.networkrail.co.uk.

Independent review report

to Network Rail Infrastructure Limited

Introduction

We have been engaged by the company to review the condensed consolidated set of financial statements in the half-yearly financial report for the six months ended 30 September 2012, which comprises the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity , the consolidated balance sheet, the consolidated cash flow statement and related notes. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed consolidated set of financial statements.

Directors' responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

As disclosed in note 1, the annual financial statements of the group are prepared in accordance with IFRSs as adopted by the European Union. The condensed consolidated set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting", as adopted by the European Union.

The maintenance and integrity of the Network Rail website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Our responsibility

Our responsibility is to express to the company a conclusion on the condensed consolidated set of financial statements in the half-yearly financial report based on our review. This report, including the conclusion, has been prepared for and only for the company for the purpose of the Disclosure and Transparency Rules of the Financial Services Authority and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed consolidated set of financial statements in the half-yearly financial report for the six months ended 30 September 2012 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

PricewaterhouseCoopers LLP
Chartered Accountants
London

21 November 2012

Consolidated income statement

		Unaudited six months ended 30 September 2012			Unaudited six months ended 30 September 2011		
	Notes	Results pre debt and derivative revaluations £m	Debt and derivative revaluations £m	Total £m	Results pre debt and derivative revaluations £m	Results post debt and derivative revaluations £m	Audited year ended 31 March 2012 £m
Revenue	2	**3,167**	**-**	**3,167**	2,997	2,997	6,004
Net operating costs	3	**(1,941)**	**-**	**(1,941)**	(1,770)	(1,770)	(3,667)
Operating profit		**1,226**	**-**	**1,226**	1,227	1,227	2,337
Property revaluation movements and profits on disposal		**20**	**-**	**20**	8	8	19
Total profit from operations		**1,246**	**-**	**1,246**	1,235	1,235	2,356
Investment revenue	4	**14**	**-**	**14**	9	9	51
Other gains and losses	4	**-**	**66**	**66**	-	(418)	(567)
Finance costs	4	**(693)**	**-**	**(693)**	(753)	(753)	(1,369)
Profit before tax		**567**	**66**	**633**	491	73	471
Tax	5	**(44)**	**(16)**	**(60)**	(46)	63	283
Profit after tax for the period		**523**	**50**	**573**	445	136	754

Consolidated statement of comprehensive income

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Profit for the period	**573**	136	754
Gain on revaluation of the railway network	**903**	1,145	313
(Losses)/gains on movement in fair value of hedging derivatives	**(15)**	7	(93)
Reclassification of balances in the hedging reserve to the income statement	**46**	(20)	67
Actuarial losses on defined benefit pension schemes	**(143)**	(37)	(245)
Tax relating to components of other comprehensive income	**(133)**	(255)	29
Other comprehensive income for the period	**658**	840	71
Total comprehensive income for the period attributable to equity shareholders	**1,231**	976	825

Consolidated statement of changes in equity

	Share capital £m	Share Premium £m	Revaluation Reserve £m	Other Reserve £m	Hedging Reserve £m	Retained Earnings £m	Total £m
At 1 April 2012	**160**	**85**	**3,764**	**1,458**	**(241)**	**3,288**	**8,514**
Profit for the period	**-**	**-**	**-**	**-**	**-**	**573**	**573**
Impact of change in tax rate	**-**	**-**	**57**	**-**	**3**	**(15)**	**45**
Revaluation of the railway network	**-**	**-**	**903**	**-**	**-**	**-**	**903**
Transfer of deemed cost depreciation from revaluation reserve	**-**	**-**	**(29)**	**-**	**-**	**29**	**-**
Increase in deferred tax liability on the railway network	**-**	**-**	**(201)**	**-**	**-**	**(7)**	**(208)**
Actuarial losses on defined benefit pension schemes	**-**	**-**	**-**	**-**	**-**	**(143)**	**(143)**
Deferred tax on actuarial gains	**-**	**-**	**-**	**-**	**-**	**33**	**33**
Decrease in fair value of hedging derivatives	**-**	**-**	**-**	**-**	**(15)**	**-**	**(15)**
Deferred tax on all hedging reserve movements/retained earnings	**-**	**-**	**-**	**-**	**(3)**	**-**	**(3)**
Reclassification of balances in the hedging reserve to the income statement	**-**	**-**	**-**	**-**	**46**	**-**	**46**
Balance at 30 September 2012 (Unaudited)	**160**	**85**	**4,494**	**1,458**	**(210)**	**3,758**	**9,745**

	Share capital £m	Share Premium £m	Revaluation Reserve £m	Other Reserve £m	Hedging Reserve £m	Retained Earnings £m	Total £m
At 1 April 2011	160	85	3,598	1,458	(165)	2,553	7,689
Profit for the period	-	-	-	-	-	136	136
Impact of change in tax rate	-	-	53	-	(9)	(3)	41
Revaluation of the railway network	-	-	1,145	-	-	-	1,145
Transfer of deemed cost depreciation from revaluation reserve	-	-	(81)	-	-	81	-
Increase in deferred tax liability on the railway network	-	-	(287)	-	-	(20)	(307)
Actuarial losses on defined benefit pension schemes	-	-	-	-	-	(37)	(37)
Deferred tax on actuarial gains	-	-	-	-	-	9	9
Increase in fair value of hedging derivatives	-	-	-	-	7	-	7
Deferred tax on all hedging reserve movements/retained earnings	-	-	-	-	2	-	2
Reclassification of balances in the hedging reserve to the income statement	-	-	-	-	(20)	-	(20)
Balance at 30 September 2011 (Unaudited)	160	85	4,428	1,458	(185)	2,719	8,665

Consolidated statement of changes in equity (continued)

	Share capital £m	Share Premium £m	Revaluation Reserve £m	Other Reserve £m	Hedging Reserve £m	Retained Earnings £m	Total £m
At 1 April 2011	160	85	3,598	1,458	(165)	2,553	7,689
Profit for the period	-	-	-	-	-	754	754
Impact of change in tax rate	-	-	107	-	(49)	(12)	46
Revaluation of the railway network	-	-	313	-	-	-	313
Transfer of deemed cost depreciation from revaluation reserve	-	-	(235)	-	-	235	-
Increase in deferred tax liability on the railway network	-	-	(19)	-	-	(56)	(75)
Actuarial losses on defined benefit pension schemes	-	-	-	-	-	(245)	(245)
Deferred tax on actuarial gains	-	-	-	-	-	59	59
Decrease in fair value of hedging derivatives	-	-	-	-	(93)	-	(93)
Deferred tax on all hedging reserve movements/retained earnings	-	-	-	-	(1)	-	(1)
Reclassification of balances in the hedging reserve to the income statement	-	-	-	-	67	-	67
Balance at 31 March 2012 (Audited)	160	85	3,764	1,458	(241)	3,288	8,514

Consolidated balance sheet

	Note	**Unaudited 30 September 2012 £m**	Unaudited 30 September 2011 £m	Audited 31 March 2012 £m
Assets				
Non-current assets				
Intangible assets		**70**	71	70
Property, plant and equipment – the railway network	6	**45,342**	42,112	43,112
Investment property		**876**	879	878
Loan to immediate parent company		**408**	400	405
Derivative financial instruments		**585**	736	672
Finance lease receivables		**4**	5	5
Interest in joint venture		**8**	6	6
		47,293	44,209	45,148
Current assets				
Inventories		**161**	134	125
Finance lease receivables		**1**	1	1
Trade and other receivables		**744**	681	670
Current tax assets		**3**	-	3
Derivative financial instruments		**129**	5	1
Cash and cash equivalents	7	**2,686**	1,630	1,886
		3,724	2,451	2,686
Total assets		**51,017**	46,660	47,834
Current liabilities				
Trade and other payables		**(2,496)**	(3,058)	(2,704)
Current tax liabilities		**-**	(10)	-
Borrowings	7	**(2,587)**	(2,217)	(1,156)
Derivative financial instruments		**(321)**	(657)	(411)
Provisions		**(7)**	(14)	(12)
Obligations under finance leases		**-**	(2)	(1)
		(5,411)	(5,958)	(4,284)
Net current liabilities		**(1,687)**	(3,507)	(1,598)
Non-current liabilities				
Borrowings	7	**(28,142)**	(25,020)	(27,929)
Derivative financial instruments		**(843)**	(718)	(797)
Other payables		**(2,793)**	(2,192)	(2,579)
Retirement benefit obligation		**(820)**	(537)	(661)
Deferred tax liabilities		**(3,263)**	(3,570)	(3,070)
		(35,861)	(32,037)	(35,036)
Total liabilities		**(41,272)**	(37,995)	(39,320)
Net assets		**9,745**	8,665	8,514

Consolidated balance sheet (continued)

	Unaudited 30 September 2012 £m	Unaudited 30 September 2011 £m	Audited 31 March 2012 £m
Equity			
Share capital	**160**	160	160
Share premium	**85**	85	85
Revaluation reserve	**4,494**	4,428	3,764
Other reserve	**1,458**	1,458	1,458
Hedging reserve	**(210)**	(185)	(241)
Retained earnings	**3,758**	2,719	3,288
Total equity	**9,745**	8,665	8,514

This interim financial report was approved by the Board of Directors on 21 November 2012.
It was signed on its behalf by:

Patrick Butcher (Director)

Consolidated cash flow statement

	Note	**Unaudited six months ended 30 September 2012 £m**	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Cash flows from operating activities				
Cash generated from operations	8	**1,763**	1,803	3,661
Interest paid		**(333)**	(267)	(970)
Taxation received		**-**	1	-
Net cash generated from operating activities		**1,430**	1,537	2,691
Investing activities				
Interest received		**8**	6	40
Purchases of property, plant and equipment		**(2,159)**	(2,112)	(4,521)
Proceeds on disposal of property		**24**	4	29
Capital grants received		**64**	309	400
Capital element of finance lease receipts		**1**	2	1
Investment in joint ventures		**(2)**	-	-
Net cash from investing activities		**(2,064)**	(1,791)	(4,051)
Financing activities				
Repayment of borrowings		**(362)**	(546)	(2,545)
Repayment of obligations under finance leases		**(1)**	-	(1)
New loans raised		**1,870**	1,685	5,489
Collateral received from/(repaid to) counterparties		**5**	(26)	(78)
Cash flow on settlement of derivatives		**(78)**	-	(390)
Net cash from financing activities		**1,434**	1,113	2,475
Net increase in cash and cash equivalents		**800**	859	1,115
Cash and cash equivalents at beginning of the period		**1,886**	771	771
Cash and cash equivalents at the end of the period		**2,686**	1,630	1,886

Notes to the interim financial statements

Six months ended 30 September 2012

1. General information

This condensed consolidated interim financial information does not comprise statutory financial statements within the meaning of Section 434 of the Companies Act 2006. Statutory financial statements for the year ended 31 March 2012 were approved by the Board of Directors on 6 June 2012 and delivered to the Registrar of Companies. The auditors' report on these financial statements was unqualified, did not contain an emphasis of matter paragraph and did not contain a statement under Section 498 of the Companies Act 2006.

The condensed consolidated interim financial statements are prepared in accordance with the Disclosure and Transparency Rules of the United Kingdom Financial Services Authority and International Accounting Standard 34, 'Interim Financial Reporting' as adopted by the European Union.

This condensed consolidated interim financial information has been reviewed, not audited. The condensed consolidated interim financial information should be read in conjunction with the Annual Report and Accounts for the year ended 31 March 2012, which have been prepared in accordance with IFRSs as adopted by the European Union. A copy of this document is available on the Group's website: www.networkrail.co.uk

Accounting policies

Except for the changes noted below, the accounting policies applied are consistent with those described in the annual financial statements for the year ended 31 March 2012.

The following new and revised Standards and Interpretations have been adopted in these financial statements. Their adoption has not had any significant impact on the amounts reported in these financial statements but may affect the accounting for future transactions or arrangements.

Amendments to IAS 12	*Income Taxes*

At the date of authorisation of these financial statements, the following Standards and Interpretations, which have not been applied in these financial statements, were in issue but not yet effective (and in some cases had not been adopted by the EU):

IFRS 9	*Financial Instruments*
IFRS 10	*Consolidated Financial Statements*
IFRS 11	*Joint Arrangements*
IFRS 12	*Disclosure of Interests in Other Entities*
IFRS 13	*Fair Value Measurement*
IAS 27 (revised 2011)	*Separate Financial Statements*
IAS 28 (revised 2011)	*Investments in Associates and Joint Ventures*
Amendments to IAS 1	*Presentation of Financial Statements*
Amendments to IAS19	*Employee benefits*
Amendments to IAS 32	*Financial Instruments: Presentation*
Amendments to IFRS 7	*Financial Instruments: Disclosures*
Annual Improvements to IFRSs: 2009-2011 Cycle	

The Group has yet to assess the full impact of these accounting standards.

Going concern

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 interim financial statements.

Business segments

No segmental analysis is provided because the Group operates one class of business, that of managing the national rail infrastructure and undertakes that class of business in one geographical segment, Great Britain.

Critical accounting judgements and key sources of uncertainty

The principal risks managed by Network Rail are unchanged from those set out in the 31 March 2012 Network Rail Limited Annual Report and Accounts. This can be found in the Directors' report on page 39 and in Note 28 Funding and Financial Risk Management on pages 93-99. The key accounting judgements and sources of uncertainty at the half year are set out below.

(i) Property, plant and equipment – the railway network: the estimate of the fair value of the railway network is based on an income approach using the regulatory asset base, which equates to the discounted future cash flow associated with the network, adjusted for the net present value of any variances from the Office of Rail Regulation's determination included in the Group's Business Plan. The methodology of the valuation and critical judgements therein are discussed in detail in Note 12 to Network Rail Infrastructure Limited Annual Report and Accounts 2012 on pages 78-80 and remain largely unchanged. The additional critical judgement at interim is to forecast the inflation to be applied to the regulatory asset base. Inflation is applied using the November 2012 Retail Prices Index (published in December 2012). This is estimated at 2.65% and for every 10 basis points variance from that forecast the regulatory asset base, on which the valuation is based, will vary by £40m.

(ii) Investment property: Jones Lang LaSalle provided independent valuations of 15 one-off individual properties. The balance of the estate was valued under the Beacon method by splitting the portfolio into homogeneous classes of property and areas. Jones Lang LaSalle independently assessed the appropriate yield to be adopted within each of these classes and areas. This enabled the directors to estimate market values by applying the provided yields to the net rental income from these properties, in accordance with a standard UK investment property valuation. The method of calculation is the same as set out in Note 13 in Network Rail Infrastructure Limited Annual Report and Accounts 2012. Victoria Place Shopping Centre, purchased in September 2011 for £92m, has been stated at cost. The directors believe the cost reflects its fair value at 30 September 2012.

(iii) Retirement benefit obligations: the Group recognises and discloses its retirement benefit obligation in accordance with the measurement and presentational requirement of IAS 19 'Employee Benefits'. The calculations include a number of judgements and estimations in respect of the expected rate of return on assets, the discount rate, inflation assumptions, the rate of increase in salaries and life expectancy amongst others. Changes in these assumptions can have a significant effect on the value of the retirement benefit obligation. The key assumptions made are set out in Note 29 in Network Rail Infrastructure Limited Annual Report and Accounts 2012. The key changes at interim are that the discount rate has reduced to 4.5% from 5.2% and the RPI assumption has decreased from 3.2% to 2.5%. Changes of twenty five basis points in the combined effect of the discount rate and inflation assumption affects the defined benefit obligation by approximately £220m and the retirement benefit obligation by around £132m. The total contribution rate payable under the Railway Pension Scheme (RPS) and the Career Average Revalued Earnings (CARE) scheme is normally split in the proportion 60:40 between the Group and the members, respectively.

(iv) Provisions: provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date and are discounted to present value where the effect is material.

(v) Hedge Accounting: Network Rail's hedging strategy aims to achieve a known fixed rate on current and future debt issuances. A key judgement is in relation to the highly probable future issuances. At 30 September 2012 Network Rail has deferred derivatives with a market value of £140m in equity to use against highly probable and expected future issuances. Interest rate swaps with a market value of around £42m are due to start before 31 March 2013.

2. Revenue

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Franchised track access and grant income	**3,017**	2,861	5,706
Freight revenue	**29**	25	51
Property rental income	**109**	100	215
Other income	**12**	11	32
	3,167	2,997	6,004

The effect of the performance regimes on the results of the Group was a net income of £6m (six months to 30 September 2011: net income of £24m).

3. Net operating costs

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Employee costs*	**861**	851	1,679
Own costs capitalised	**(287)**	(278)	(684)
Other external charges (including infrastructure maintenance costs)	**782**	658	1,594
Other operating income	**(116)**	(114)	(242)
Net operating costs before depreciation	**1,240**	1,117	2,347
Depreciation and other amounts written off non-current assets	**737**	681	1,378
Capital grants amortised	**(36)**	(28)	(58)
Net operating costs	**1,941**	1,770	3,667

* The average number of employees (including executive directors) in the six months ended 30 September 2012 was 34,864 (six months ended 30 September 2011: 35,102). Annualised average cost per employee, including pension contributions and employer's NI, was £49,392 (six months ended 30 September 2011: £48,487).

Research and development expenditure in the six months was £250,000 (six months ended 30 September 2011: £1,080,000)

4. Investment revenue, finance costs and other gains and losses

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Investment revenue			
Interest receivable on investments and deposits	**14**	9	50
Interest receivable on finance leases	**-**	-	1
Total investment revenue	**14**	9	51
Finance costs			
Interest payable on borrowings	**(748)**	(810)	(1,492)
Expected return on assets less interest on liabilities in respect of defined benefit pension schemes	**(7)**	(1)	(3)
Total borrowing costs	**(755)**	(811)	(1,495)
Less: capitalised interest	**62**	58	126
Total finance costs	**(693)**	(753)	(1,369)

Other gains and losses			
Net ineffectiveness arising from cash flow hedge accounting	**-**	(123)	(124)
Fair value (loss)/gain on fair value hedges	**(62)**	38	(103)
Fair value gain/(loss) on carrying value of fair value hedged debt	**48**	(49)	77
Net increase in fair value of non-hedge accounted debt	**(12)**	(37)	(8)
Gain/(loss) on derivatives not hedge accounted	**92**	(247)	(409)
Total other gains and losses	**66**	(418)	(567)

5. Tax

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Current tax:			
Current tax on profits	**-**	-	(12)
Less advance corporation tax (ACT) set-off	**2**	-	5
Corporation tax credit/(liability)	**2**	-	(7)
Prior year credit	**-**	-	15
Group relief payable to Network Rail Holdco Limited	**(2)**	-	(3)
Total current tax	**-**	-	5
Deferred tax:			
Current year charge	**(148)**	(24)	(96)
Effect of rate change	**88**	87	168
Prior year credit	**-**	-	206
Total deferred tax	**(60)**	63	278
Total tax	**(60)**	63	283

The rate used for the purposes of deferred tax in these financial statements is 23% (2011: 25%) as this is the current rate and the rate at which the temporary differences are expected to reverse.

There are no current tax charges in the period as Network Rail Infrastructure Limited has significant brought forward losses.

In addition to the changes in rates of Corporation tax disclosed above a number of further changes to the UK Corporation tax system were announced in the March 2012 UK Budget Statement. These include a further reduction to the main rate which is proposed to reduce the rate to 22% from 1 April 2014. These further changes had not been substantively enacted at the balance sheet date and, therefore, are not included in these financial statements.

The proposed reduction of the main rate of corporation tax to 22% from 1 April 2014 is expected to be enacted separately. The overall effect of this further change, if it applied to the deferred tax balance at the balance sheet date, would be to further reduce the deferred tax liability by an additional £142m.

6. Property, plant and equipment – the railway network

	Group £m
Valuation	
At 1 April 2011	39,577
Additions	4,600
Depreciation charge for the year	(1,378)
Revaluation in the year	313
At 31 March 2012	**43,112**
Additions	2,064
Depreciation charge for the period	(737)
Revaluation in the period	903
At 30 September 2012	**45,342**

Given the interdependency of the assets comprising the railway network, the Group has concluded that the railway network is a single cash generating unit and that its fair value is the estimated future cash flows that will be generated in perpetuity, discounted at the regulatory cost of capital, as set by the Office of Rail Regulation (ORR) in its Periodic Review.

The estimate of the fair value is based on the regulatory asset base (RAB) which is based on a discounted future cash flow calculation adjusted for the net present value of any variances from the ORR's determination included in the Group's business plan. This takes into account: the provisional ORR RAB balance; any regulatory out/under-performance derived by comparing future income and expenditure projections in the Group's business plan against the regulatory settlement; assets funded directly by third party contributions rather than RAB funded; and an adjustment to reflect that a subset of this valuation is disclosed separately as investment properties.

In arriving at its valuation of the railway network the Group considers what the value of the network would be to a conventionally funded third party, taking into account the expected terms of a regulatory settlement that would apply in those circumstances.

The depreciation charge for any 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 that comprise the railway network. The estimated remaining weighted average useful economic life of the network is currently 30 years (2011: 30 years).

7. Net borrowings

	Unaudited 30 September 2012 £m	Unaudited 30 September 2011 £m	Audited 31 March 2012 £m
Net borrowings by instrument			
Cash and cash equivalents*	**2,686**	1,630	1,886
Commercial paper	**(409)**	(149)	-
Bank loans	**(673)**	(1,242)	(966)
Bonds issued under the Debt Issuance Programme (less unamortised premium, discount and fees)	**(29,647)**	(25,846)	(28,119)
Finance leases	**-**	(2)	(1)
	(28,043)	(25,609)	(27,200)
Movements in net borrowings			
At the beginning of the period	**(27,200)**	(24,890)	(24,890)
Increase in cash and cash equivalents	**800**	859	1,115
Proceeds from borrowings	**(1,870)**	(1,685)	(5,489)
Repayment of borrowings	**362**	546	2,545
Capital accretion	**(207)**	(329)	(521)
Exchange differences	**27**	(22)	(30)
Fair value and other movements	**45**	(88)	70
At the end of the period	**(28,043)**	(25,609)	(27,200)
Net borrowings are reconciled to the consolidated balance sheet as set out below			
Cash and cash equivalents*	**2,686**	1,630	1,886
Borrowings included in current liabilities	**(2,587)**	(2,219)	(1,157)
Borrowings included in non-current liabilities	**(28,142)**	(25,020)	(27,929)
	(28,043)	(25,609)	(27,200)

*Includes collateral received from derivative counterparties of £86m (September 2011: £133m, March 2012: £81m)

8. Notes to the cash flow statement

	Unaudited six months ended 30 September 2012 £m	Unaudited six months ended 30 September 2011 £m	Audited year ended 31 March 2012 £m
Operating profit	**1,226**	1,227	2,337
Adjustments for:			
Depreciation of the railway network	**737**	681	1,378
Amortisation of capital grants	**(36)**	(28)	(58)
Amortisation of intangible assets	**-**	1	1
Movement in retirement benefit obligations	**9**	-	(72)
(Decrease)/increase in provisions	**(5)**	4	(5)
Operating cash flows before movements in working capital	**1,931**	1,885	3,581
Increase in inventories	**(36)**	(26)	(17)
(Increase)/decrease in receivables	**(72)**	53	47
(Decrease)/increase in payables	**(60)**	(109)	50
Cash generated from operations	**1,763**	1,803	3,661

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, commercial paper and money market deposits with a maturity of up to three months.

9. Contingent liabilities

Provision has been made for the directors' best estimate of the known claims, investigations and legal actions in progress.

10. Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

The Company's ultimate parent company and controlling entity is Network Rail Limited, a company limited by guarantee without shares. The Company's immediate parent company is Network Rail Holdco Limited.

Loans to parent company and subsidiaries:

	Unaudited 30 September 2012 £m	Unaudited 30 September 2011 £m	Audited 31 March 2012 £m
Network Rail Holdco Limited	**408**	400	405
Network Rail Development Limited	**8**	-	7
Network Rail (NDS-Plant) Limited	**7**	-	8

Amounts repayable by Network Rail Holdco Limited are non-current and bear interest at 2.85% (September 2011: 2.63%).