UK and Germany

Alex Jensen

CEO: UK and Germany

Our National Express business in the UK and Ireland had five areas of activity through the year, scheduled coach, bus services in the West Midlands, corporate and private hire, and services in Ireland. In Germany, we operate 5 Rhein-Ruhr Express routes as well as the RE7 and RB48 of the Rhine Munster Express.

Urban bus

Long distance coach

Rail

Revenue (£m)
+9.2%

£869.9m

(2022: £796.8m)

Adjusted Operating Profit (£m)
-45.1%

£23.7m

(2022: £43.2m)

Statutory Operating Profit/(Loss) (£m)
-1,059.2%

£(98.8)m

(2022 restated: £10.3m)

Adjusted Operating Profit Margin (%)
-2.7%

2.7%

(2022: 5.4%)

In the UK Bus sector, Mobico is the market leader in the West Midlands – the largest UK urban bus market outside London. UK Coach is the largest operator of scheduled coach services in the UK, and also serves the fragmented, corporate shuttle, private hire and accessible transport markets.

In Germany, Mobico is the second-largest rail operator in North Rhine-Westphalia and one of the top five operators in Germany.

Results

Good constant currency growth with Divisional revenues up 8.4% on a constant currency basis (9.2% on a reported basis) but a decline in Adjusted Operating Profit of £19.5m (45.1%). In UK Bus, revenues were down 1.7% vs 2022. In UK Coach, revenues were up 30.5% vs 2022. In Germany, revenues were down 3.2% vs 2022 (5.1% at constant currency), although this mainly reflects lower "pass-through" costs in our contracts.

Highlights

In July 2023, the UK Bus and Coach businesses were combined into a 'one-UK' structure to drive efficiencies and best practice across the division. In September 2023, Alex Jensen was appointed as the new Divisional CEO, together with a new CFO. As with the North American division, new leadership was deemed necessary to bring sharper commercial focus to the business. The immediate focus has been in three areas: (i) driving performance through tighter operational control, optimising networks and driving volumes and yields; (ii) transforming the business models to improve the risk and reward balance and rebase costs; and (iii) building organisational capability and discipline, including around capital and cost allocation.

Although both UK businesses have delivered good passenger and revenue results, they share a common challenge in their respective cost bases which have risen sharply since 2019 on a unit-cost basis relative to unit-revenues (i.e. when looked at on a per passenger or per mile basis). Work is underway, at pace, to determine the optimum cost structure.

UK Coach

- Strong growth in UK Coach core scheduled coach revenue resulting from good passenger recovery (+25.4%) and yields (+3.7%) vs 2022; including an estimated £15m profit benefit from rail strikes
- National Express's UK scheduled coach network growth in 2023 has significantly outpaced our main competitors, with 6.4m seats added over the year
- 15% of first-time users on a rail strike day have since used National Express again.

UK Bus

- UK Bus was significantly impacted by the drivers' strike in Q1 and associated wage settlements which added £23.3m of incremental cost. The cost of the strike itself (from lost revenue net of saved variable costs) was £2.4
- Significant funding from West Midlands Combined Authority to protect the bus network of £47.0m (FY 2022: £50.7m). While this funding is important, it is not sufficient to cover the cost increases or deliver an attractive return, and the team is working to reset this in January 2025 when the current funding deal ends
- 12.5% fare increase implemented from July 2023, lagging but assisting in mitigating cost increases (the pay award was effective 1 January 2023)
- Customer complaints reduced by 28% year on year reflecting an increased focus on lost mileage, punctuality, driver recruitment & retention and customer response
- Reduced the driver vacancy gap from 11% to 6%.

German Rail

- Lifetime profitability of contracts adversely impacted by industry-wide disruption in the train driver market, lower labour productivity, volatility in energy costs and energy cost recovery indices, and persistent levels of inflation
- Increased onerous contract provision for RRX Lots 2&3 to £118.3m (FY 22 restated: £46.9m)
- Active discussions with PTA to renegotiate contracts and minimize disruption to passengers.

UK Coach

UK Coach delivered strong passenger growth of 25% in 2023 from a network that grew by 29%. Yields increased by 3.7%, and occupancy was marginally down at 69.7% as airports built back up.

National Express coaches provided significant support to customers during the repeated rail strikes through the year, which generated an estimated 615,000 additional passengers, and £17m revenue. Excluding strike impacts in 2022 and 2023, estimated underlying passenger growth in 2023 was 24%.

Overall, the growth in active online customers registered with National Express was circa 43%. This includes new customers who switched to our service, due to the disruption caused by continued rail strikes in 2023 and who we have subsequently retained.

In October, a review of the loss-making NXTS business resulted in a decision to close two depots (Gillingham and Sydenham) which have been impacted by a reduction in daily commuter traffic as a result of the working-from-home trend. The rest of the NXTS business has a significant dependence on the UK private hire and charter market which has been slow to recover post Covid. All potential options are being considered, including further rationalisation and rightsizing.

UK Bus

In FY 23 commercial passenger numbers were up 8.2% and exited the year at 98% of 2019 levels on a smaller network (at the end of 2023, the network was operating at 89% of 2019 mileage levels).

The drivers' strike in Q1 2023 resulted in a wage settlement of 16.2%, backdated to 1 January 2023 with the total cost of driver pay awards being £23.3m. The net cost of the strike itself, including lost revenue and other business interruption costs, but after savings, was £2.4m. While this is unwelcome, settlements that are above inflation are unsustainable and we have taken the action necessary to maintain the business on a sustainable and strong footing. In response to the pay increase, National Express increased ticket prices in July 2023 by circa 12.5%, with the average day ticket increasing from £4.00 to £4.50.

During the year, we continued to receive government funding support to deliver customer growth and to maintain those parts of the bus network that are not commercially viable (£47.0m of funding was received in FY 23, compared with £50.7m in FY 22). This contribution reduces to £38.7m in FY 24, after which time the current agreement ends. The reduction mainly reflects the end of specific support received for the fare freeze in FY 23 (£3m) and a £5m reduction in support received under the Bus Recovery Grant. Discussions are underway to secure further funding, and alternative network cuts (removal of non-profitable routes) have already been identified which would act to bridge any remaining funding gap.

Contract wins, renewals and mobilisations

Late in the year, the UK Coach business successfully retained its Luton Airport contract after a competitive process, extending a very effective and collaborative partnership exemplified by the response to the major fire at the airport parking facilities in October 2023. This new contract (five-year plus two-year extension option) continues a successful partnership that has run since 2013 serving circa 1.5 million passengers per year.

Our Ireland operations, operating as Dublin Express, continue to grow and expand. In January 2024, we successfully retained the contract in a competitive tender process to operate Airport to City services from the premium departure slots until 2027. We see further growth in this buoyant market both in terms of ongoing airport growth and expansion of Dublin Express' reach, starting with launch of an additional service to southern Dublin in H1 2024. Overall passenger numbers grew from 1.2m in FY 22 to 1.7m in FY 23 (+48%). This growth was driven by ongoing recovery in Dublin Airport air passenger numbers, further embedding of the Dublin Express brand in the Irish market and a focus on partnerships, such as our exclusive ticket sales arrangement with national rail operator, Irish Rail. To meet this demand, we increased our overall seat capacity between Dublin and Dublin Airport by 94% over the course of the year.

In parallel, we launched the Dublin to Belfast route on 18 July 2023. Comprising 16 round trips per day, this route has already gained a significant foothold in the market and was profitable after just three months. We have now carried 150k passengers and believe that this will grow to over 0.5m passengers per annum over the next two years.

We continue to build our reputation for quality and reliability, enjoying an NPS on Belfast routes of over 70 (and over 40 on high frequency Airport-Dublin routes), demonstrating the quality of service being delivered hand in hand with the significant growth over the period.

Focus on efficiency

Through the year, the UK Coach operated network has grown – with operated mileage in 2023 at 61.3m miles, 29% higher than in 2022 with seat utilisation at 70%, 6% above 2019 levels (64%). This growth has been added quickly but in an efficient and sustainable manner, without sacrificing punctuality or customer satisfaction. Absolute growth in the National Express network has significantly exceeded that of our two largest competitors combined.

During 2023, UK Bus placed a strong focus on driver recruitment and retention, investment in new more reliable fleet, and proactively working with local authorities to limit highway disruption. The launch of 'Project Clockwork' is designed to deliver a significant improvement in bus punctuality and further improvement in lost mileage by the end of 2024.

Disciplined capital allocation

During the year, the business undertook a commercial review of a project to bring 100 Hydrogen Fuel Cell ZEVs into UK Bus operations, as part of the ZEBRA (Zero Emission Bus Regional Areas) Government funding scheme. The review drew on insight gained in running a fleet of 20 buses in Birmingham in partnership with Birmingham City Council. Given what we learnt from this small trial, we made the decision to move away from the hydrogen element of the ZEBRA scheme. We are in discussions with TfWM and DfT about next steps. Hydrogen may become viable for longer distance Coach operations in the future, and that will be further evaluated as the technology evolves.

Germany

In Germany we face pressure on profitability of our contracts mainly as a result of three key structural issues: firstly, costs associated with industry-wide disruption in the train driver market and lower productivity; secondly, lower expectations for net energy cost recovery relating to volatility in energy costs and associated energy cost recovery indices (including the impact of the revised indices from the German Federal Statistical Office); and finally, persistent levels of inflation.

Driver scarcity

Driver scarcity in Germany is an industry-wide issue caused by an increasingly competitive market for driver recruitment. Supply of drivers has traditionally been dominated by Deutsche Bahn's own workforce planning (and where state-backed retirement benefits are very attractive to the older members of the workforce). It is estimated that 40% of drivers will retire by 2027. In context, a typical driver training program requires 12-18 months to complete. This scarcity has recently been compounded by three key structural issues:

i. Continuing pressure on labour productivity by the unions who are seeking a reduction in productive working hours of 8% (to 35 hours a week). As a result, the driver establishment in North RhineWestphalia (NRW) for all train operating companies (TOCs) has increased significantly and it is expected that there will be a recruiting requirement of nearly 1,000 new drivers in the region.

ii. In late Summer and Q4 of 2023, we saw higher than anticipated resignations as drivers left to join agencies (where they could be re-employed on significantly higher pay). This has been a significant and rapid change for the industry. When we mobilised the RRX Lot 1 emergency award in February 2022 only 20 agency drivers were employed representing 5% of our driver workforce. By January 2024, in contrast we were running with an agency driver quota of 12%.

iii. Significant network upgrade work with almost 1,000 construction projects planned for the NRW region. Major projects include RRX expansion and the remodelling of the Cologne junction and affects around 30 per cent of daily journeys in NRW, this results in longer journeys and a higher driver requirement.

As a result of the issues outlined above, at the end of FY 23 we had an overall driver gap of circa 9%, (after the utilisation of 41 agency drivers). While a driver gap of 5-10% can be managed in the short term (with higher penalties and overtime costs), this level of gap is not sustainable over the medium term, and management have put in place an action plan to address:

- Agreed mileage reductions with our PTAs to minimize disruption to passengers and associated penalties (although with a reduction in subsidy) over the next 12 months
- Increased the number of our own driver training courses from 39 in 2022 to 70 in 2023 and a similar number planned in 2024, in order that we recover the driver shortage by 2025/26
- Amended our workforce plans to take account of lower productivity

Energy subsidy

Energy subsidies are received to compensate operators for volatility in energy prices, and are calculated by reference to specific indices published by the German Federal Statistical Office, DeStatis. The way that indices relevant to our RME and RRX 2&3 contracts are compiled is not transparent.

However, historically the way in which these indices had behaved was relatively predictable: tending to increase as wholesale prices increased (and decrease as market prices fell) but in a less pronounced way. For example, energy prices for short-dated energy purchases peaked in August 2022 at over 500% of August 2021, the energy compensation index only increased 250%. During 2023 the index started to behave in a different way from this previous experience giving us a greater exposure.

As a result, we have revised our forecasts for long-term cost recovery under the contracts.

Revised Indices

In addition to the issues described above, in early March 2024 DeStatis republished values for the index used in our contracts, replacing previous data for the 38 months from January 2021 to February 2024. This revision required us to re-evaluate our forecasts for how the energy subsidy index will behave relative to our assumptions about the cost of energy.

Financial impact

Although we are involved in constructive ongoing dialogue with our PTAs to rebalance contracts for the structural issues that are outside of our control, the impact on our German operations prior to mitigation is as follows:

- Adjusted Operating Profit on our RME and RRX Lot-1 contracts reduced by £17m (compared to prior year) in 2023 to £0.2m. Of this change, approximately £10m is due to the IFRS15 contract asset, principally reflecting lower expectations of future profitability, with the balance of £6m representing the in-year impact of lower net energy costs, lower subsidy and the costs associated with driver shortages
- We expect that the RME and RRX Lot-1 contracts will generate future profits (through Adjusted Operating Profit) of approximately £20m over the remaining contract lives, but with a loss of approximately £5m in FY 24 as the driver issues are resolved, and we transition to operating RRX Lot-1 on a permanent basis (compared to an emergency award basis between February 2022 and December 2023)
- As a result of the issues described above, the onerous contract provision in respect of our RRX Lots2/3 contracts (which recognises all of the expected losses on that contract over its contract life) increases to £118.3m (FY 22 (restated): £46.9m), with an expected cash outflow of approximately £30m in FY 24, and an average cash outflow of £10m p.a. for the remainder of the contract lives.

Evolve outcomes

- **Safest:** UK FWI per Million Miles of 0.001 (FY 22: 0.002) reflecting the launch of an enhanced suite of 'Golden Safety Rules', expert coaching, and continued deployment of driver simulator in UK Bus. Germany had an FWI of 0.047 (FY 22: 0.000) as a result of a fatality of a track worker which is still under investigation.
- **Most satisfied customers:**
  - **UK Bus:** Passenger volume growth of 8.2%. Punctuality & reliability complaints, the biggest satisfaction driver for our customers, reduced by 48% year on year.
  - **Coach:** Passenger volume growth of 25%. Customer satisfaction for National Express (Coach) remains strong with an NPS of 36.8, flat on 2022, despite the impact of a significant number of rail strikes resulting in much busier services and increased traffic congestion.
  - **German rail:** Passenger volume growth of 13% stimulated by subsided fares in the form of the €49 ticket.
- **Employer of choice:** UK eNPS of -28, although disappointing, represents a significant improvement on prior year (+10 on FY 22), which was impacted by industrial relations issues and management change. In our drive to become Employer of Choice, we launched our National Express Inclusion Playbook for managers and colleagues, which is a toolkit for managers and their teams to navigate and nurture an inclusive culture.
- **Most reliable:**
  - OTP (On Time Performance) of 80.8% (FY 22: 85.6%) in UK Bus, and 86.9% (FY 22: 88.9%) in UK Coach: A key controllable driver of reliability for our customers is lost mileage (defined as the difference between our scheduled mileage and operated mileage, reflecting services which have not been delivered) across both our Bus and Coach operations. In a period of rail strikes, growing demand for our services and the impact of increased traffic and roadworks, this metric has improved by circa 35% in both businesses. Despite this OTP has declined as a result of increased congestion and driver shortages.
  - OTP of 60.9% (FY 22: 64.3%) in German Rail: with the fall due to significant network infrastructure upgrades and route diversions, compounded by the scarcity of drivers. As discussed above, we are working with the PTAs to minimize the impact of disruption to customers.
- **Environmental leader:** Our UK Bus business now has 159 electric buses in operation (79 as at December 2022) meaning that 10.1% of our operated network that is fully electric, with further ZEVs already on order that will take that proportion significantly higher. In Coventry we are leading the UK's first 'All Electric Bus City' project, which is on schedule to be completed by 2025.

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