CEO's review

Our results for 2023 are below the expectations we set ourselves at the beginning of the year. I am encouraged, however, at the progress we have continued to make in transforming the business with decisive action to bring in new leadership in North America School Bus and the UK & Germany; focus on pricing and delivery of our restructuring programs.

Ignacio Garat, Group CEO

Overview

2023 was a challenging year for Mobico Group. Profitability was affected by significant cost inflation (especially wage costs) and significantly reduced Covid subsidies. Structural issues in Germany (labour scarcity and energy price volatility), reduced expectations around the profitability of the UK private hire business, lower than expected growth in UK Bus passenger numbers, and higher driver recruitment costs in North America School Bus have also created a drag to our recovery in profitability. Decisive action has however been taken on pricing and restructuring which is expected to provide significant future benefits. This alongside good top line growth will help drive our recovery.

Mobico Group Revenue grew 12.2% on a reported basis and 10.9% on a constant currency basis. This reflects: (i) strong underlying growth in those businesses where revenue is driven by passenger demand and trip volumes; and (ii) continued recovery in North America School Bus through pricing and route recovery.

Adjusted Operating Profit decreased 14.5% and Group Adjusted Operating Margin decreased to 5.4% (FY 22: 7.0%), as the benefits of volume growth (+£88m), pricing improvements (+£114m) and the in-year impact of our Accelerate 1.0 restructuring initiative (+£15m) were not sufficient to offset:

- the impact of cost increases (£130m) of which approximately 55% was driver wage inflation, and 30% fuel and insurance costs,
- the lagged benefit from price rises in UK Bus and North America School Bus,
- a reduction in Covid subsidies of £105m (see strategic review section for more detail),
- the impact of lower expectations for energy subsidy recovery, higher costs, and the revised indices from the German Federal Statistical Office on profitability of our German rail contracts

Decisive action has been taken across the Group with the successful Accelerate program: Accelerate 1.0 delivered £15m in year savings (at least £30m on an annualised basis) and we have now launched Accelerate 2.0 (with a target of at least £20m annualised). Moreover, specific additional actions have been taken to i) recover cost increases in German Rail through ongoing contract renegotiation, ii) drive a recovery to profitability in National Express Transport Solutions (NXTS), and iii) further improve driver recruitment and training processes in North America School Bus.

Read more about our business model on pages 12 to 13

Read more about our Evolve strategy on pages 10 to 11

Read more about our leadership on pages 82 to 87

ALSA continued to trade well with growth across all lines of business, delivering Adjusted Operating Profit up 31.7% as a result of strong revenue growth of 21.1%, with especially strong trading in Long Haul, where the business acted quickly to capture the benefits of government backed travel initiatives (multi-voucher travel and 'young-summer' discounts). The profit impact of pricing increases and volume growth amounted to £111m, more than offsetting cost increases of £68m.

North America grew revenues by 6.4% as routes were re-instated in North America School Bus, with pricing recovery on expiring contracts also contributing positively. Adjusted Operating Profit was down £41.3m (60.4%) mainly as a result of a reduction in Covid funding of £44m (principally Covid-related CERTS funding) and the impact of wage costs and investment in the recruitment process. However, pricing recovery delivered an increased contribution in the second half of the year. Transit and Shuttle delivered 14 new contract wins worth approximately £54m in annualised revenue, at a ROCE of 31%.

In the UK and Germany, revenues grew 9.2%, representing strong trading in UK Coach, and with UK Bus patronage reaching 98% of pre-Covid levels. However, the fall in Adjusted Operating Profit was principally as a result of the January 2023 16.2% pay settlement in UK Bus which was effective from January (the primary driver of a £23m increase in driver costs, with price rises only effective from July), a reduction in Covid funding of £30m, and lower profitability in Germany.

In Germany lower expectations for energy subsidy recovery as a result of volatility in energy markets, higher costs associated with industry-wide driver shortages and the impact of the revised indices from the German Federal Statistical Office, reduced the profitability of our contracts:

- For the contracts not covered by the onerous contract provision (RME and RRX 1) profits reduced by £17m compared to prior year (to £0.2m). Of this reduction, approximately £10m was due to a reduction in the IFRS15 contract asset (primarily reflecting lower expectations of future profitability) and £6m of in-year impact of higher penalties associated with driver scarcity and higher net energy costs.
- The onerous contract provision associated with RRX Lots 2/3 increased from £47m (restated, as of 31 December 2022) to £118m as of 31 December 2023. This liability will unwind over the remaining life of the contract through to 2033.

A focused action plan – working with our Passenger Transport Authorities (PTA's) – to recover the profitability of these contracts is underway.[1]

Balance Sheet, debt maturity and interest costs

The Group's covenant gearing ratio at 31 December 2023 was 3.0x, increased from 2.8x last year-end compared to a covenant test gearing limit of less than 3.5x. Free Cash Flow of £163.7m was slightly ahead of prior year (FY 22: £160.5m). However, cash outflows in respect of Adjusting Items of £71m (including cash costs of restructuring programmes and cash outflows relating to German onerous contracts) and dividend payments to equity shareholders of £41m (FY 22: £nil) resulted in covenant net debt broadly flat on prior year at £987.1m (FY 22: £985.8m) alongside slightly lower covenant EBITDA.

As of 31 December 2023, the Group had £2.0bn of cash and committed facilities. During the year, debt maturity and liquidity were improved with the £527m RCF (the majority of which would have matured in 2025) being replaced by a £600m RCF facility to 2028. We also refinanced the 2023 £400m bond with a €500m Eurobond issue maturing in 2031. Both the RCF and Eurobond were secured at competitive rates. As rates stand today, the anticipated net interest charge in FY 24 will be in the region of £85m to £90m (£75m in 2023). Approximately 80% of our debt is fixed, with the 20% that is swapped to floating rate due to revert to fixed in 2025.

Mobico has made clear its objective to reduce gearing. However, the lower than previously expected profits generated in 2023, increased costs associated with restructuring, and the German onerous contract cash costs means the timeline of that plan has been extended with the target range of 1.5x-2.0x now expected to be reached in 2027. The Group announced in October that it would look to accelerate the deleveraging (and reduce future capital intensity) with the potential disposal of NASB. Preparations for a potential sale continue to progress well and a sale at an appropriate valuation would accelerate the deleveraging timetable.

Dividend

On 12 October, the Board announced the suspension of the 2023 final dividend when it became clear that covenant gearing would not decrease in the year and in the light of the weaker than expected macro-economic environment and trading performance.

The Board will continue to monitor business performance and prospects and the associated pace of reduction in covenant gearing and will reinstate the dividend when it considers that sufficient progress is being made, targeting a 2x coverage ratio (EPS to DPS) once reinstated.

Outlook

Based on current market conditions Adjusted Operating Profit for FY 24 is expected to be within the range of £185m to £205m. Similarly to FY 23, we expect a greater bias to the second half of the year, given the phasing of cost reduction programmes and the timing of price increases.

Strategic commentary

2023 has been a year in which important underlying progress has been made in the context of an evolving market, where Mobico has:

- Adapted to the reality of a post-pandemic world and addressing notable external headwinds;
- Acted decisively to adjust the business model to be 'fit-for-the-future': addressing new patterns of demand, evolving requirements of the cost base, changing methods of delivery, and to capture new opportunities; and
- Positioned to capture future growth opportunities

[1] Opening balance restated £46.9m plus charge of £99m less utilisation to give closing position of £118m.

Adapted to external headwinds

2023 has been a year of continued progress in the face of notable external headwinds and an evolving market, including:

i. Reduced government funding

In 2023, we have offset a significant headwind from the £105.4m year-on-year reduction in Covid funding (FY 23: £26.3m; FY 22 £131.7m) with underlying improvements in trading.

Covid support	FY 23	FY 22
Revenue	**13.4**	56.7
Cost support	**12.9**	75.0
Total	**26.3**	**131.7**

It is a reality of many public transport systems that, if operated purely on a commercial basis, they would likely involve fewer routes and higher fares. It is therefore important to note that government support for transport services remains strong, and we continue to see evidence that governments around the world are increasingly aligned with our agenda and interested in driving the modal shift from cars to public transport.

ii. Markets undergoing continued evolution, both structural and cyclical

In ALSA, our Long Haul business grew significantly, despite the impact of high speed rail competition on some key corridors.

Elsewhere, five-day-a-week commuter travel has fallen as a result of increased hybrid working. This particularly impacted NXTS where the Private Hire and UK Holiday markets have also been slower to return to pre-pandemic levels of activity. The impact of lower commuter activity resulted in the decision to close two of our depots, with residual operations consolidated into a smaller depot footprint.

The impact of lower commuter activity on our Shuttle business in North America has been less pronounced as we are paid on a per-vehicle (rather than per-passenger) basis.

Acted to become fit-for-future

Throughout 2023 the Group has already taken decisive action to address these challenges, but also to create a business that is fit-for-future and well positioned to capitalise on future opportunities. This required change including:

- a sharper commercial focus of divisional leadership,
- driving further cultural alignment across the Group, and
- refining our business model.

i. Important leadership changes

In order to drive strong operational focus, the Group changed the leadership of two of the businesses: North America School Bus, with immediate impact (delivering one of the most successful school-year start-ups for several years); and the UK & Germany Division, to bring a sharper commercial focus and a fresh perspective on the operating model.

ii. Working with government partners to access continued funding

Throughout the year we continued to work with governments (regional and national) to access funding and create sustainable, long-term partnerships. Some notable successes in the year included:

- **ALSA:** integrating multi-voucher ticketing into our booking platform, gaining a significant competitive edge
- **North America:** accessed funding to purchase 143 fully electric school buses through the EPA Clean School Bus Program
- **UK:** funding package secured to the end of 2024 to allow the UK Bus business to maintain network coverage, with price rises implemented from 1 July 2023.
- **Germany:** secured funding to compensate for the impact of the €49 ticket on passenger revenues in our RME contracts (with the funding secured until the end of 2024 when the initiative is due to expire)

iii.Action to address structural changes

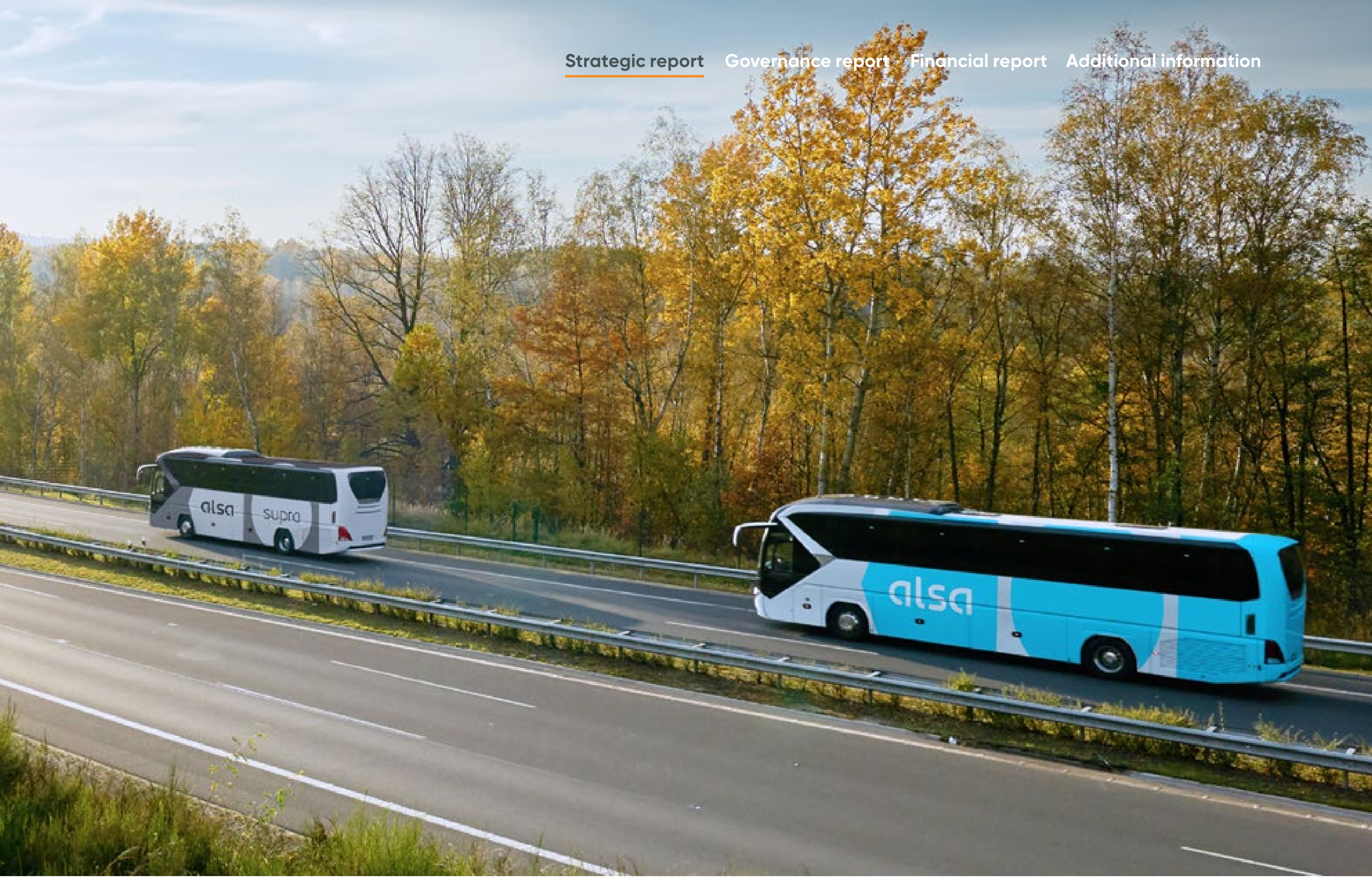
Across the Group we took action to combat structural change;

- **ALSA:** investment in innovative marketing and service delivery to optimise our proposition against High Speed Rail (HSR) helped to mitigate the impact of significant, discounted capacity on our major corridors.
- **North America:** in our Transit business we had already exited a number of loss making businesses where we deemed no recovery was possible through contract negotiation. In the remaining portfolio we have renegotiated a number of contracts to rebalance the fixed and variable components of income, and in 2023 we also retained two key contracts (Framingham and Tucson) with significant rate increases to restore profitability in the light of reduced volumes. An action plan is also in place to address remaining under-performance in six Customer Service Centres (CSCs) in Transit & Shuttle. The diversification strategy, taking Shuttle into new sectors and geographies, has delivered important gains for the business.
- **UK:** in response to the structural impact of increased home-working on our NXTS commuter businesses (Clarkes and Kings Ferry) we took action to close two depots and instigated a review of options across the remaining NXTS business, which is exposed to Private Hire demand.

iv.Combating the impact of inflation

2022 and H1 of 2023 saw a significant peak in inflation, particularly driver-related costs, which increased 2023 costs by £130m compared with prior year (which includes the impact of the full-year effect of the School Bus pay increase).

Recovering the impact of inflation has been a key priority for the Group and with significant progress having been made (typically with a lag between cost inflation and price rises). However, when inflation is high and persistent there is a need to act further which is why we have taken action on pricing and on the unit costs in the business.



During the year, we continued to make good progress on pricing:

- In School Bus we achieved price increases of 13% on the portfolio of contracts up for renewal at the beginning of School Year 2023/2024. This represented about 40% of our contracts, and comes on the back of the 10% rise achieved on a further 40% of the contracts in the prior year (noting, however, that there will be a lag before the price increases are annualised);
- In UK Bus we agreed a price rise of 12.5%, effective from July 2023; and
- In our Long-Haul Coach businesses we achieved full-year yield increases of 3.7% in the UK and 7.5% in ALSA.

However, recognising that there was a need to do more we have continued to address our cost base. We announced our Group-wide restructuring, cost and efficiency programme (Accelerate 1.0) in Q1 of 2023 with the stated aim of achieving £25m of annualised savings. That programme has delivered £15m of savings in FY 23 and is expected to deliver annualised savings in excess of £30m in FY 24. In Q4 2023 we announced a second cost and efficiency initiative (Accelerate 2.0) with a stated aim of unlocking a further £20m of annualised benefits (£10m targeted in FY 24). This programme is focused on fundamental organisational design, so that we have business models (and unit costs) that position the Group to be fit-for-the-future.

v. Solving driver shortages

Industry-wide driver shortages have been particularly acute in North America School Bus, UK Bus and, more recently, Germany.

In North America School Bus, there was a c.15 % driver shortage at the beginning of School Year 22/23 (i.e. September 2022). By December of 2023, we had reduced this to c.2%. This was achieved by overhauling recruitment processes, with a record net number of 990 drivers hired in the year (compared to 884 in FY 22 and a loss of 569 in FY 21). Although we did incur higher than expected recruitment costs in the second half of 2023 this represented necessary investment. As the pressure has eased, those costs are now significantly lower.

In UK Bus, we exited 2022 with a driver shortage of 11%. As a result of actions taken, this had reduced to 6% by the end of 2023. Actions taken include an overhaul of the candidate attraction process, standardised medical and interview procedures, updated onboarding processes, and improving the time taken to make offers to candidates. This resulted in an increase in offers (from application) from 14% to 17%, a reduction in onboarding “no shows” from 20% to 15% and a significant reduction in the time taken to gain the PCV licence.

In Germany, we have a plan that is well underway to reduce the driver gap including increasing drivers trained from 39 in 2022 to 70 trained in 2023, with this higher level continuing through 2024. We are also working with the PTAs to significantly increase capacity in Government sponsored courses.

Positioned to capture future growth opportunities

Opportunity pipeline remains attractive; conversion is strong; retention is high

Since it was launched in 2021, the Evolve strategy has been crucial in building a robust business model that will capture sustained future growth. For example, we have taken further action in the past year to put the Group on a firm foundation for the future including leadership changes and the launch of our Accelerate restructuring programmes. We have also reinforced Business Development and Sales functions across the Group. While doing so, Mobico’s conversion of opportunities has been strong with 43 new contracts won in the year, worth over £1bn in total contract value and c.£126m in annualised revenue, at average ROCE of c.23%. ROCE will improve as we continue to favour Asset-Light opportunities. The new contracts won provide the platform for delivering our revenue growth targets.

Revenue growth has been good and the pipeline of opportunities – both organic and through M&A – remains well populated. That pipeline currently represents c.£2.5bn of annualised revenue (as compared with the equivalent £2.5bn at 31 December 2022). In 2023, we also closed a number of small, but strategically important acquisitions.

Debt reduction remains a priority

The Group enjoys excellent liquidity and very clear sight of interest costs given that circa 80% of such costs are fixed with weighted interest costs on our bonds of 4.0%, and a margin of 0.55% above SONIA on our RCF. Nonetheless, it is clear that the Group's debt (which increased as a consequence of Covid) and gearing is an issue that needs to be addressed. Mobico remains confident that it can reduce leverage through Adjusted EBITDA growth over the medium term. However, reduced expectations about the rate of profit recovery and increased cash costs associated with restructuring and German onerous contracts in the near term have delayed plans for full recovery and debt reduction; we now expect to achieve the target covenant gearing range of 1.5x-2.0x in 2027.

In October 2023, we announced the potential sale of the North America School Bus business on which preparations are progressing well. If a sale at an appropriate valuation is concluded, the proceeds will make a significant contribution to debt-reduction ambitions.

Zero emissions vehicles as a catalyst for change

The Group is moving at pace to evaluate, adopt, and mobilise ZEVs in fleets across our businesses. Mobico has a crucial role to play in planning and facilitating the transition to ZEVs, while remaining vigilant regarding the risks of decarbonisation and the commercial viability of solutions. We have previously set out and now reconfirm zero emission fleet targets, to hit net zero by 2040 (based on Scope 1 and 2 emissions). We continue to make excellent progress on our ZEV transition plan and remain on track to secure (operating and on-order) 1,500 ZEVs by the end of 2024 and 14,500 by 2030.

Updated long-term financial ambitions

In 2021, Mobico published financial ambitions as part of the launch of its Evolve strategy. In light of recent performance and the current trading environment, these have now been updated as follows:

- FY 27 revenue of at least £3.8bn (£1bn above FY 22)
- Sequential growth in Adjusted Operating Profit with FY 27 Adjusted Operating Profit of approximately £300m (circa £100m above FY 22)
- Cumulative Free Cash Flow (after growth capex and M&A) for FY 23 to FY 27 of around £300m
- Covenant net debt/covenant EBITDA of between 1.5x to 2.0x by FY 27
- Paying a dividend targeting 2.0x cover (once re-instated)

* NB our definition of Free Cash Flow (now after growth capex and M&A) has been changed to reflect the ongoing discipline in the re-investment of cash flow to drive growth in revenue and profitability. Cumulative Free Cash Flow (prior to growth capex and M&A) and which previously had been guided to be £1.25bn between FY 23 and FY 27 would now be over £1bn).

Ignacio Garat

Ignacio Garat
Group CEO

21 April 2024

Case study

Key Luton Airport Coach contract retention reflects values of Evolve

Winning new contracts is important. Retaining them? Even more so. Delivering the Evolve strategy is about providing the best experience, delivering the safest and most reliable service, and being the most efficient and highest quality provider that we can be. So, when we believe we have delivered against our own exacting expectations, it is particularly rewarding to have customers renew their partnerships with us – and especially when those decisions rely on such qualitative, as well as financial, criteria.

One such instance has been the retention of two key lots for Luton Airport, one of London's fastest growing hubs, where Mobico has been successful in retaining contracts to deliver coach operations. One for the core London–Luton Airport lot, and the other, a regional services lot, that integrates Luton Airport as a stop on our intercity network. National Express already ran frequent coach services between Central London and London Luton Airport – 24 hours a day, seven days a week – with four departures an hour during the daytime.

When the contract was up for tender, a competitive submission was made to deliver the airport and National Express' shared vision of providing a green, affordable transport option for customers travelling to and from the airport and giving a seamless customer experience. In December 2023, National Express was re-awarded the five contract.

As if emphasising that truly committed service is a continuous process, when a recent, significant fire destroyed a car park, the National Express Luton team went above and beyond to support passengers through the night and ensure people could get to where they needed to go safely.