Financial review

Chris Davies
Group Chief Financial Officer

"Decisive action taken to reduce costs and conserve cash."

In summary

- Strong start to the year with double-digit revenue growth before Covid-19
- Decisive action taken to reduce costs and conserve cash
- £187 million EBITDA; towards the top of guidance
- After separately disclosed items, a statutory loss after tax of £327 million
- H2 free cash flow positive and net debt reduced to £942 million
- £1.5 billion of equity and additional borrowing facilities raised
- £1.9 billion in cash, undrawn committed facilities and undrawn CCFF available
- Improving trajectory into 2021 with strong Q4 revenue, EBITDA and cash flow

Summary income statement

	Underlying result[1] 2020 £m	**Separately disclosed items[1] 2020 £m**	**Total 2020 £m**	Underlying result 2019 £m	Separately disclosed items 2019 £m	Total 2019 £m
Revenue	**1,955.9**	**–**	**1,955.9**	2,744.4	–	2,744.4
Operating costs	**(2,006.7)**	**(330.6)**	**(2,337.3)**	(2,449.1)	(53.0)	(2,502.1)
Operating (loss)/profit	**(50.8)**	**(330.6)**	**(381.4)**	295.3	(53.0)	242.3
Share of results from associates	**(2.1)**	**–**	**(2.1)**	0.4	–	0.4
Net finance costs	**(53.2)**	**(8.0)**	**(61.2)**	(55.7)	–	(55.7)
(Loss)/profit before tax	**(106.1)**	**(338.6)**	**(444.7)**	240.0	(53.0)	187.0
Tax	**29.3**	**88.7**	**118.0**	(55.2)	16.5	(38.7)
(Loss)/profit for the year	**(76.8)**	**(249.9)**	**(326.7)**	184.8	(36.5)	148.3

1 To supplement IFRS reporting, we also present our results on an Underlying basis which shows the performance of the business before separately disclosed items, comprising amortisation of intangibles for acquired businesses and, for 2020, certain costs arising as a direct consequence of the pandemic. Treatment as a separately disclosed item provides users of the accounts with additional useful information to assess the year-on-year trading performance of the Group. Further explanation in relation to these measures, together with cross-references to reconciliations to statutory equivalents where relevant, can be found on pages 243-244.

In a year shaped by the travel restrictions imposed to slow the spread of Covid-19, Group revenue was £1,955.9 million (2019: 2,744.4m), a decrease of £788.5 million (29%). After a strong start to the year, with Group revenue up 17% in January and February, extensive lockdowns were imposed by governments in each country in which we operate.

During this extraordinary period, we were well supported by customers and governments and for the Group overall this meant that despite passenger numbers declining by nearly 80% during Q2, the revenue decline was mitigated to around 50%. As lockdowns were lifted in the summer, revenue started to recover steadily. After a 50% year-on-year drop in revenue in Q2, this improved to a 37% reduction in Q3 and a 32% reduction in Q4.

In the UK, the Group recognised £84.7 million from the Covid-19 Bus Services Support Grant (CBSSG), and the Scottish equivalent, in return for maintaining bus services at around 100% of pre-pandemic levels with social distancing provisions in place. In addition, the Group recognised £15.3 million and £15.6 million for Covid-19 government compensation in ALSA and German Rail respectively. Had these various revenue-related grants not been available the Group would have operated a significantly lower level of services in order to further reduce costs. There was no revenue support provided by the Government for UK coach.

As set out in the table below, the Group recorded positive EBITDA in every quarter. The greatest year-on-year decline of EBITDA in 2020 was in Q2 during the peak of the restrictions on travel. Q3 is typically the Group's smallest quarter for profit because of the school holidays in North America. Q4 recovered strongly and contributed nearly 50% of the full year EBITDA.

Quarterly summary	Revenue year-on-year	EBITDA £m
Q1 (January to March)	+7%	69.5
Q2 (April to June)	-50%	18.8
Q3 (July to September)	-37%	5.4
Q4 (October to December)	-32%	92.9
Full year 2020	-29%	186.6

The Group recorded an Underlying Operating Loss for the year of £50.8 million (2019: £295.3m profit). The year-on-year reduction of £346.1 million reflected the net of £788.5 million lower revenue partially offset by £442.4 million lower underlying operating costs. After £330.6 million (2019: £53.0m) of separately disclosed items, the statutory operating loss was £381.4 million (2019: £242.3m profit).

Operating costs were originally budgeted to grow proportionately with budgeted double-digit revenue growth, but immediately as the impact of the pandemic took hold in late March, we took action to reduce operating costs by c.£100 million per month relative to budgeted levels throughout the second quarter. All variable costs were reduced in line with service reductions and all discretionary expenditure was stopped. For several months in the year the Board and senior management agreed to pay sacrifices, and salary deferral schemes were in place across the Group.

Significant numbers of employees were temporarily laid off or furloughed utilising government income protection schemes. At peak, we had furloughed or temporarily laid off 40,000 staff from a global workforce of c.55,000. The furlough arrangements in place differ by country. In the UK, the Government provides companies with funding to pay employees that would otherwise be laid off. In Spain, companies agree temporary lay-off numbers with the Government which then provides enhanced benefits directly to the impacted employees with employers partially compensated for continued social security payments. In North America, the Government put in place a package to provide funding to employers who continued to provide benefits to employees who were temporarily laid off. The table below outlines the cost support recognised in the year.

Government Covid-related cost support	£m
UK – Covid Job Retention Scheme	27.1
ALSA – job retention schemes in Morocco, Spain and Switzerland	9.3
North America – employee retention credits in US (and equivalent in Canada)	18.5
Total	**54.9**

As well as scaling back variable costs as revenue fluctuated during the year, we also undertook a review of the fixed cost base, identifying up to £100 million of annualised savings which will be fully realised in 2021.

The majority of these savings were in payroll costs, driven by headcount reductions in managerial, administrative and customer service roles and through efficiency savings from process improvements. Other cost savings have been derived from property rationalisation, travel costs and professional fees, along with process improvements driving efficiencies in areas like repairs and maintenance.

Underlying net finance costs decreased by £2.5 million to £53.2 million (2019: £55.7m) reflecting the net of higher interest costs in the first half caused by the partial double-carry of Sterling bonds offset in the second half by the impact of lower net debt.

After finance costs and a loss of £2.1 million from the share of results from associates (2019: £0.4m profit), the Group recorded an Underlying Loss Before Tax of £106.1 million (2019: £240.0m profit).

The Underlying tax credit was £29.3 million (2019: £55.2m charge) representing an Underlying effective tax rate of 27.6% (2019: 23.0%). The statutory tax credit was £118.0 million (2019: £38.7m charge), an effective tax rate of 26.5% (2019: 20.7%). Tax losses in most jurisdictions have been recognised as deferred tax assets with forecasts of future profits supporting their utilisation.

The statutory loss for the year, after the separately disclosed items explained below, was £326.7 million (£148.3m profit).

Separately disclosed items

£338.6 million (2019: £53.0m) of separately disclosed items were recorded as a net cost before tax in the Income Statement, of which £126.9 million (2019: £7.2m) represented cash outflows in the year.

Separately disclosed items	**Income Statement 2020 £m**	Income Statement 2019 £m	**Cash 2020 £m**	Cash 2019 £m
Intangible amortisation for acquired businesses	**(52.6)**	(53.0)	**–**	–
Directly attributable gains and losses resulting from the Covid-19 pandemic	**(262.5)**	–	**(109.6)**	–
Restructuring costs	**(14.0)**	(8.8)	**(10.8)**	(7.2)
Other separately disclosed items	**(1.5)**	8.8	**–**	–
Separately disclosed operating items	**(330.6)**	(53.0)	**(120.4)**	(7.2)
Interest charges directly resulting from the Covid-19 pandemic	**(8.0)**	–	**(6.5)**	–
Total (before tax)	**(338.6)**	(53.0)	**(126.9)**	(7.2)

Consistent with previous years, £52.6 million (2019: £53.0m) of amortisation of intangible assets arising upon consolidation of acquired businesses is included in separately disclosed items.

The directly attributable gains and losses resulting from the Covid-19 pandemic are comprised as follows:

Directly attributable gains and losses resulting from the Covid-19 pandemic	Income Statement 2020 £m	Cash 2020 £m
One-off costs, cancellation charges and compensation payments	(46.4)	(28.1)
Discontinuation of fuel trades	(17.3)	(14.6)
Onerous contract provisions and associated impairment	(133.4)	(66.9)
Impairments and associated charges	(99.3)	–
Re-measurement of the WeDriveU put liability	33.9	–
Total	**(262.5)**	**(109.6)**

One-off costs, cancellation charges and compensation payments include items such as compensation payments to third party operators and provision for Covid-related claims. The imposition of travel restrictions reduced operated mileage and hence trades were placed to reduce hedged fuel volumes in line with updated mileage and the original trades were recycled to the income statement, giving rise to a £17.3 million charge.

Onerous contract provisions were recognised in relation to contracts that, due to the impact of Covid-related restrictions, are now evaluated as loss-making for the rest of the relatively short remaining term prior to renewal and hence where there is no ability to recover to a profitable position. Where there were assets dedicated to onerous contracts, these assets were impaired where applicable. Further impairments and associated charges were recorded where there were dedicated assets, other than those related to onerous contracts, associated with contracts that have been terminated or not renewed due to the impacts of the pandemic or where subsequent strategic restructuring has changed the Group's usage of such assets.

The put liability resulting from the acquisition of WeDriveU is required to be re-measured at each reporting date. Whilst in the medium term we remain confident in the prospects and growth potential of the shuttle business, we have adjusted short-term projections for the business disruption due to the pandemic which impacts the two remaining years of the exercise period.

A further £8.0 million of interest charges directly resulting from the Covid-19 pandemic were recorded for items including arrangement fees on new Covid-19-related facilities, fees to amend covenants, and interest costs on the short-term financing under the Bank of England Covid Corporate Financing Facility (CCFF) programme that was drawn and repaid during the year.

In addition £14.0 million (2019: £8.8m) of restructuring costs were incurred as well as £1.5 million (2019: £8.8m credit) of other items principally comprising, in both the current and prior year, losses/gains on disposal of subsidiaries.

Segmental performance

	Underlying Operating (Loss)/ Profit 2020 £m	Separately disclosed items 2020 £m	Segment result 2020 £m	Underlying Operating Profit 2019 £m	Separately disclosed items 2019 £m	Segment result 2019 £m
ALSA	**6.7**	**(100.2)**	**(93.5)**	109.5	(15.7)	93.8
North America	**12.4**	**(188.4)**	**(176.0)**	123.0	(35.0)	88.0
UK	**(49.0)**	**(50.4)**	**(99.4)**	85.0	(0.9)	84.1
German Rail	**(4.9)**	**(19.1)**	**(24.0)**	5.0	(1.4)	3.6
Central functions	**(16.0)**	**27.5**	**11.5**	(27.2)	–	(27.2)
Operating (loss)/ profit	**(50.8)**	**(330.6)**	**(381.4)**	295.3	(53.0)	242.3

ALSA recorded an Underlying Operating Profit of £6.7 million (2019: £109.5m) despite a 33% reduction in revenue. Separately disclosed items totalled £100.2 million (2019: £15.7m) and comprised £17.1 million (2019: £15.7m) of amortisation of intangible assets arising from acquired businesses; £55.4 million of onerous contract provisions and associated impairments of assets; £10.8 million of impairments of vehicles and intangible assets; £3.9 million of restructuring costs, reflecting actions to reduce the cost base going forwards and £13.0 million of other Covid-related expenses including incremental health and safety costs and discontinuation of fuel hedges. After separately disclosed items, ALSA recorded a loss of £93.5 million (2019: £93.8m profit).

In North America an Underlying Operating Profit for the year of £12.4 million (2019: £123.0m) was achieved. Separately disclosed items totalled £188.4 million (2019: £35.0m) and comprised £32.7 million (2019: £35.0m) of amortisation of intangible assets arising from acquired businesses; £50.0 million of onerous contract provisions and associated impairments of assets; £79.1 million of impairments of intangible assets and property, plant and equipment; £4.4 million restructuring costs; and £22.2 million of other Covid-related expenses such as incremental health and safety costs and discontinuation of fuel hedges.

During the year the Group undertook a review of its transit businesses and contracts, which culminated in a decision to exit, dispose or close down certain operations that were deemed no longer strategically core and/or which were low margin businesses that had been severely impacted by the pandemic and were projected to consume cash over the medium term. Furthermore the Group reviewed its portfolio of school buses, resulting in an impairment of the most aged and least energy efficient vehicles. Together, these two activities principally drove the £79.1 million of impairments of assets referred to above.

After separately disclosed items, North America recorded a loss of £176.0 million (2019: £88.0m profit).

The UK Underlying Operating Loss of £49.0 million (2019: £85.0m profit) was driven by an operating loss in UK coach, where revenue declined 67%, partially offset by a small operating profit in UK bus reflecting strong pre-pandemic trading and profits on disposal of property. Separately disclosed items in the UK totalled £50.4 million (2019: £0.9m) and comprised £0.5 million (2019: £0.9m) of amortisation of intangible assets arising from acquired businesses; £12.7 million of support payments to third party coach operators; £11.2 million of onerous contract provisions and associated impairments of assets; £5.1 million of restructuring costs; £9.3 million of impairment of vehicles and £11.4 million of other Covid-19 related expenses such as incremental health and safety costs, contractual penalties and discontinuation of fuel hedges. After separately disclosed items, the UK business recorded a loss of £99.4 million (2019: £84.1m profit).

German Rail's Underlying Operating Loss of £4.9 million (2019: £5.0m profit) reflected an adjustment to the phasing of subsidies due to the re-assessment of the Rhine-Münster Express contract life revenues and profitability in light of the pandemic. Excluding this adjustment German Rail recorded a small underlying operating profit, reflecting the net of a loss of passenger revenue in the RME contract offset by compensation provided by the Government and transport authorities. The £19.1 million (2019: £1.4m) of separately disclosed items comprised £2.3 million (2019: £1.4m) of intangible amortisation and £16.8 million of asset impairments arising from an onerous contract assessment in respect of RRX. Over its remaining life, the RRX contract was assessed to generate positive EBITDA but to be loss-making after taking account of the amortisation of contract mobilisation costs, resulting in the impairment of these assets. After separately disclosed items, German Rail recorded a loss of £24.0 million (2019: £3.6m profit).

Central functions Underlying costs of £16.0 million (2019: £27.2m) were £11.2 million lower than the previous year reflecting cost savings and lower charges in respect of bonuses and long-term share-based incentive schemes. Separately disclosed items totalled a £27.5 million profit (2019: £ nil) comprising a £33.9 million credit in respect of revaluing the WeDriveU put liability, partly offset by incremental costs attributable to the pandemic and restructuring.

Cash management

Funds flow	2020 £m	2019 Re-presented £m
Underlying Operating (Loss)/Profit	**(50.8)**	295.3
Depreciation and other non-cash items	**237.4**	214.8
EBITDA	**186.6**	510.1
Net maintenance capital expenditure	**(215.9)**	(211.4)
Working capital movement	**(78.3)**	(42.0)
Pension contributions above normal charge	**(7.4)**	(7.6)
Operating cash flow	**(115.0)**	249.1
Net interest paid	**(56.0)**	(45.4)
Tax paid	**(7.7)**	(25.0)
Free cash flow	**(178.7)**	178.7
Growth capital expenditure	**(35.3)**	(24.7)
Net inflow from discontinued operations	**–**	(1.2)
Acquisitions (net of cash acquired)	**(52.4)**	(166.4)
Disposal of subsidiaries (net of cash disposed)	**4.4**	21.7
Separately disclosed items	**(126.9)**	(7.2)
Proceeds from equity instruments	**725.6**	–
Dividends	**–**	(78.3)
Other, including foreign exchange	**(54.3)**	18.6
Net funds flow	**282.4**	(58.8)
Net debt	**(941.6)**	(1,224.0)

Note: 2019 is re-presented for the transfer of £17.5 million out of net debt in respect of vehicle leases entered into in 2019 to fulfil contracts that have been deemed to be in scope of IFRIC 12. The effect of this re-presentation is to reduce 2019 net growth capital expenditure and closing net debt by £17.5 million compared with the previously reported figures.

The Group generated EBITDA of £186.6 million in the year (2019: £510.1m).

The majority of the £215.9 million maintenance capital investment was in respect of fleet replacement in ALSA and North America. The ratio of maintenance capital expenditure to depreciation of 0.9 (2019: 1.0) was a slight reduction year-on-year reflecting actions taken to reduce capital expenditure following the onset of the pandemic. Given the long payment terms on fleet purchases these actions are anticipated to take greater effect on the maintenance capital expenditure ratio in 2021. Additions of property, plant and equipment in 2020 for both maintenance and growth purposes combined totalled £209.9 million (2019: £311.5m), a year-on-year reduction of £101.6 million. At the year end there was £289.6 million (2019: £263.3m) owing to vehicle suppliers, with the year-on-year increase reflecting growth capital additions in respect of new contracts such as Casablanca; the maintenance capital component has reduced, reflecting the capital reduction actions during the year.

The Group recorded a working capital outflow of £78.3 million for the year (2019: £42.0m outflow), the net of a £139.6 million outflow in the first half and a £61.3 million inflow in the second half.

Over the year as a whole, strong cash collection was more than offset by a decrease in payables, reflecting the cost saving measures implemented (the benefit of which is recorded in EBITDA), and a change in the mix of revenue away from cash-upfront passenger revenue to subsidies and compensation paid in arrears. The diversified nature of the Group's revenue streams and the predominantly government-backed or blue-chip profile of the customer base helps mitigate the potential credit risk impact of the pandemic on receivables, but we continue to keep it under close review. Consistent with previous periods the Group makes use of non-recourse factoring arrangements on receivables and advance payments. The usage of these arrangements was broadly unchanged on the previous year; the total draw down at the year end was £111.6 million (2019: £107.1m).

Net interest paid increased by £10.6 million to £56.0 million (2019: £45.4m), reflecting the final interest payment on the 2020 bond maturing in June (payable annually in arrears) whilst at the same time making interest payments on the new borrowings. This was partly offset by the benefit of lower draw down on the revolving credit facilities (RCFs), reflecting the strong liquidity position during the year.

The net impact of the factors outlined above was a free cash outflow of £178.7 million in the year (2019: £178.7m inflow), comprising an outflow of £193.0 million in the first half and an inflow of £14.3 million in the second half.

Growth capital expenditure of £35.3 million included vehicles to service new contracts in ALSA and North America, and infrastructure and other costs incurred with the mobilisation of new contracts in German Rail and ALSA. We made one acquisition early in the year, prior to the pandemic, of a coach company in the UK for upfront consideration of £25.3 million (net cash payments of £9.6 million plus the absorption of £15.7 million of borrowings) with up to a further £7.5 million of deferred payments. Subsequently we paused our acquisition strategy in order to conserve cash and protect liquidity within the business. In addition, deferred consideration paid in the period for acquisitions made in previous years was £27.3 million in respect of a number of acquisitions made in prior years, including Monroe School Transportation and Cook-Dupage Transportation.
In December, the Group sold its Dundee bus business to a Group with more scale in Scotland. The cash inflow of £4.4 million from disposals reflects the net of the proceeds from the sale of the Dundee business, plus the final settlement in respect of the sale of Ecolane in 2019.

A cash outflow of £126.9 million was recorded in respect of the items excluded from Underlying results as explained above. The Group received £725.6 million from a combination of the share placing in May 2020, delivering £230.1 million, and the hybrid issue in November 2020, which raised £495.5 million net of costs.
Other cash outflows of £54.3 million principally reflect the significant movement in the closing rate of Sterling against the Euro from 31 December 2019 to 31 December 2020, which increased the value of debt denominated in Euros.

Net funds inflow for the period of £282.4 million (2019: £58.8m outflow) resulted in net debt of £941.6 million (2019: £1,224.0m).

Reconciliation to statutory cash flow statement

Statutory cash generated from operations for the year was an outflow of £96.7 million (2019: £356.2m inflow) as shown in the Group Statement of Cash Flows and expanded further in note 13. Free cash flow for the year was an outflow of £178.7 million. A reconciliation of free cash flow to net cash flow from operating activities is set out on page 244.
The principal differences are that the free cash flow includes net maintenance capital expenditure (£215.9 million outflow) but excludes the cash outflow in respect of separately disclosed items.

Dividend

The Group's capital allocation policy aims to achieve a balance between reinvesting in the business for future growth and returns, reducing net debt to within our revised target range of 1.5x to 2.0x EBITDA and paying a growing dividend to shareholders. As previously guided, in light of the exceptional economic circumstances and conditions attaching to our amended covenants, the Group will not be paying a dividend in respect of 2020. Looking ahead, the Board recognises the importance of the shareholder returns and will reinstate the dividend when economic conditions permit and it is appropriate to do so. Such a decision will be based upon the Group's prevailing and expected free cash flow generation as well as gearing returning to within pre-amendment covenant levels.

Treasury management

The Group maintains a disciplined approach to its financing and is committed to an investment grade credit rating. Both Moody's and Fitch twice reaffirmed their investment grade ratings during the year whilst revising the rating outlook to negative from stable in line with their views on the transport sector as a whole (Baa2/negative) and (BBB/negative).

In light of the impact of the pandemic on EBITDA generation, the Group has renegotiated its covenants. The gearing covenant has been waived by the lenders throughout 2020 and 2021, and will next apply as at 30 June 2022. The interest cover covenant has been amended to 1.5x and 2.5x for the 30 June 2021 and 31 December 2021 test periods respectively. In return for these waivers and amendments to the covenants the Group has agreed to a quarterly £250 million minimum liquidity test and a bi-annual £1.6 billion maximum net debt test during the waiver period. In addition the Group has agreed to pay no dividend during the period of the amendments if gearing exceeds 3.5x or interest cover is below 3.5x. At 31 December 2020, the gearing ratio was 5.1x (31 December 2019: 2.4x) on a reported basis and 6.4x on a covenant basis (the principal difference being that the impact of IFRS 16 is removed in the covenant basis). Interest cover at the end of the year was 2.7x (31 December 2019: 9.6x); this compares to an amended covenant of 1.5x. All covenants are on a pre-IFRS 16 basis.

At 31 December 2020, the Group had £2.8 billion of debt capital, committed facilities and Bank of England CCFF. Excluding the specific short-term Covid-related facilities, the average maturity is 5.2 years. At 31 December 2020, the Group's RCFs were undrawn and the Group had available a total of £1.9 billion in cash, undrawn committed facilities and the undrawn CCFF. The CCFF is available until 21 March 2021 to be drawn for 12 months. However, given the other committed funding facilities available to the Group and the ample liquidity headroom projected, including in downside scenarios, the Directors do not intend to draw upon it and will instead allow it to lapse.

The table below sets out the composition of these facilities.

Funding facilities	Facility £m	Utilised at 31 December 2020 £m	Headroom at 31 December 2020 £m	Maturity year
Core RCFs	495	–	495	2025
Short-term Covid-related RCFs	287	–	287	2021
2023 bond	400	400	–	2023
2028 bond	247	247	–	2028
Private placement	406	406	–	2027–2032
Private placement	71	71	–	2021
Leases	311	311	–	various
	2,217	1,436	781	
CCFF	600	–	600	2021
	2,817	1,436	1,381	
Cash and cash equivalents		(521)	521	
Total		**915**	**1,902**	

In the first half of the year the Group received the proceeds of the delayed draw US private placements, comprising £406 million of funding (translated at closing exchange rates) in a mixture of Sterling, Euro and US Dollar. To secure additional liquidity through the Covid-19 crisis, the Group obtained funding of up to £600 million under the Bank of England CCFF, of which £300 million was initially drawn in April and repaid in December. In addition, £287 million of additional short-term RCFs were secured. During the first half of the year, a £225 million Sterling bond and €250 million floating rate note matured and £100 million of term loans were repaid. In December a $100m term loan was repaid.

The Group also raised £726 million through equity or equity-like instruments: firstly through a share placing in May that raised £230 million, and secondly through the issuance of a hybrid instrument in November that raised £496 million. The hybrid instrument has been recorded within equity because the contractual terms allow the Group to defer coupon payments and the repayment of the principal amount indefinitely. The instrument has a coupon of 4.25%, which is payable annually. The coupon payments are treated the same as an equity dividend distribution, but will be deducted from earnings for the purposes of calculating earnings per share.

To ensure sufficient availability of liquidity, the Board requires the Group to maintain a minimum of £300 million in cash and undrawn committed facilities at all times. This does not include factoring facilities which allow the without-recourse sale of receivables. These arrangements provide the Group with more economic alternatives to early payment discounts for the management of working capital, and as such are not included in (or required for) liquidity forecasts.

At 31 December 2020, the Group had foreign currency debt and swaps held as net investment hedges. These help mitigate volatility in the foreign currency translation of our overseas net assets. The Group also hedges its exposure to interest rate movements to maintain an appropriate balance between fixed and floating interest rates on borrowings. It has therefore entered into a series of swaps that have the effect of converting fixed rate debt to floating rate debt or vice versa. The net effect of these transactions was that, at 31 December 2020, the proportion of Group debt at floating rates was 7% (2019: 24%).

Group tax policy

We adopt a prudent approach to our tax affairs, aligned to business transactions and economic activity. We have a constructive and good working relationship with the tax authorities in the countries in which we operate and there are no outstanding tax audits in any of our main three markets of the UK, Spain and the USA. The Group's tax strategy is published on the Group website in accordance with UK tax law.

Pensions

The Group's principal defined benefit pension schemes are all in the UK. The combined deficit under IAS 19 at 31 December 2020 was £135.1 million (Dec 2019: £90.0m), with the increase being principally driven by a reduction in discount rates. The two principal plans are the UK Group scheme, which is closed to new accrual, and the West Midlands Bus plan, which remains open to accrual for existing active members only. The deficit repayments will be around £7 million per annum, rising with inflation, until 2026. The IAS 19 valuations for the principal schemes at 31 December 2020 were as follows:

- WM Bus: £141.6 million deficit (2019: £99.1m deficit); and
- UK Group scheme: £12.3 million surplus (2019: £14.2m surplus).

Fuel costs

Fuel cost represents approximately 7% of revenue. Clearly it is more complex than in previous years to forecast volume in the current environment, but based on 'base case' modelling, the Group is 99% hedged for 2021 at an average price of 38.3p per litre; around 60% hedged for 2022 at an average price of 30.2p; and around 25% hedged for 2023 at an average price of 29.9p. During the year, hedge accounting was discontinued for a number of fuel derivatives where volumes were in excess of actual or expected consumption due to the pandemic. As a result, accumulated fair value movements were recycled from other comprehensive income to the Income Statement. The resulting impact was an Income Statement charge of £17.3 million in the year which has been treated as a separately disclosed item.

Brexit

Given the diversified nature of our business model and the fact that we no longer run scheduled operations between the UK and the Continent, we do not believe that the recently agreed UK-EU trade agreement presents any direct material risk to our business. The main risks to the Group relate to suppliers of parts and vehicles, as we purchase some vehicles from European manufacturers for UK operations, and cross-border data sharing. We have active mitigation plans in place for these issues.

Going concern

The Board continues to believe that the Group's prospects are positive. We are diversified geographically, by mode of transport and by contract type, and no single contract contributes more than 3% to revenue. Furthermore, a large proportion of the Group's contracts have some form of protection from volatility in passenger numbers. The Group is well positioned to benefit from the future trends in transportation. Public transport is key to increasing social mobility as well as being fundamental to addressing the challenges of congestion and poor air quality.

The Financial Statements have been prepared on a going concern basis as the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for a period of 12 months from the date of approval of the Financial Statements. Details of the Board's assessment of the Group's 'base case', 'reasonable worse case', and 'reverse stress tests' are detailed in note 2 to the Financial Statements on pages 149 to 151.

Outlook

With the continuing uncertainty of the impact of Covid-19 across the countries in which we operate, it remains difficult to forecast financial performance with any level of certainty. The going concern analysis outlined in note 2 to the Financial Statements on pages 149 to 151 provides a range of potential scenarios. In our base case we anticipate the macro situation to be similar in the first half of 2021 to the second half of 2020, with varying levels of lockdowns and travel restrictions remaining in place. Accordingly we anticipate performance in the first half of 2021 to be similar to that achieved in the second half of 2020. Our base case scenario assumes that vaccines will reduce infection rates by the summer, with a consequent lifting of travel restrictions allowing a steady recovery in revenue in the second half such that by December 2021 Group revenue recovers to levels similar to December 2019. Under this scenario we anticipate robust positive free cash flow in 2021 as EBITDA improves through the year and the capital expenditure reduction actions taken in 2020 take effect on the maintenance capital outflows.

Chris Davies

Group Chief Financial Officer

18 March 2021