

Press Release

27 February 2008

International success builds on UK strengths

Serco Group plc – 2007 Preliminary Results

	2007	2006	
Revenue	£2,811m	£2,548m	up 10.3%
Adjusted profit before tax	£123.2m	£105.0m	up 17.3%
Profit before tax	£114.6m	£107.4m	up 6.7%
Adjusted earnings per share	18.57p	15.92p	up 16.6%
Earnings per share	16.98p	16.62p	up 2.2%
Dividend per share	4.25p	3.60p	up 18.1%
Group free cash flow	£97.6m	£85.4m	up 14.3%

Success across our markets

- Signed £3.6bn of contracts and appointed preferred bidder for a further £1.0bn
- Record level of international awards including Dubai Metro (preferred bidder, £400m), US Postal Service (\$260m), LOGCAP IV (\$225m) and Borallon Correctional Centre (Aus\$100m)
- Significant progress in other new markets, including Glasgow City Council strategic partnership (preferred bidder, £265m) in local authority market and e-Borders (£200m) in homeland security
- Excellent progress in existing markets, including Marine Services (£750m) in UK defence, Forth Valley (£450m) in UK integrated facilities management and Yarl's Wood (£85m) in UK home affairs
- Maintained rebid win rate at more than 90% and continued to win one in two new bids

Strong margin and cash performance

- Adjusted PBT margin up from 4.1% to 4.4%
- Group free cash flow increased by 14.3% to £97.6m
- Strong balance sheet with Group recourse net debt reduced to £137.9m

Broad pipeline supports excellent visibility

- Order book at new record of £14.7bn at 31 December 2007
- Contracts valued at an additional £1.0bn at preferred bidder stage
- Visibility of 91% of planned revenue for 2008, 76% for 2009 and 63% for 2010
- £27bn of further opportunities identified

Growing markets and higher margins underpin positive outlook

- UK and international markets continue to generate increasing opportunities
- Confident of double-digit revenue growth for the foreseeable future
- Guidance for Adjusted PBT margin of 30 basis point increase for both 2008 and 2009

Christopher Hyman, Chief Executive of Serco Group plc, said: "2007 was an excellent year. We were awarded significant contracts in existing markets and used skills developed in the UK to build positions in markets such as Australian home affairs and Middle Eastern transport. We also reaped the benefits of the capabilities we have acquired in recent years, winning record levels of work in the US, securing the prestigious e-Borders programme in the UK and one of the first local authority strategic partnerships. At the same time, we further increased our margins. This success underpins our optimism for 2008 and beyond."

Note: Adjusted profit before tax and Adjusted earnings per share shown above are before amortisation of acquired intangibles and the £11.4m gain on sale of PFI investments in 2006 as shown on the face of the Group's income statement. Group free cash flow is from subsidiaries and joint venture dividends and is reconciled in Section 3 of the Finance Review.

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Richard Hollins, Head of Investor Relations

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Presentation

A presentation for investors and analysts will be held at JP Morgan Cazenove, 20 Moorgate, London EC2R 6DA at 9.30 am today.

A preliminary results interview with Christopher Hyman, Chief Executive, will be available at 7.00 am at www.serco.com or www.cantos.com.

Overview

2007 was an excellent year for Serco. We won important contracts in existing markets, continued to build our positions in new markets and were awarded record levels of international business. These contributed to another year of strong financial performance.

We grew revenue by 10.3% to £2,811m, Adjusted profit before tax (Adjusted PBT) rose by 17.3% to £123.2m and Adjusted earnings per share grew 16.6% to 18.57p. The Adjusted PBT margin increased from 4.1% to 4.4%, benefiting from our management of the contract portfolio and continued efficiency improvements. Profit before tax rose by 6.7% to £114.6m and earnings per share were 2.2% higher at 16.98p. Profit before tax and earnings per share in 2006 included the benefit of the one-off gain on sale of our PFI investments.

Our cash performance continued to be strong, with Group free cash flow increasing by 14.3% to £97.6m. This contributed to a reduction in Group recourse net debt of £34m to £137.9m. The strength of our balance sheet was further enhanced by the decline in our net pension liabilities.

Serco's policy is to increase the total dividend each year broadly in line with the increase in underlying earnings. The Board has proposed a final dividend of 3.02p per share, representing an increase on the 2006 final dividend of 18.4% and bringing the total dividend for the year to 4.25p, growth of 18.1%. The final dividend will be paid on 21 May to shareholders on the register on 7 March 2008.

Success depends on our ability to meet – and often exceed – the expectations of our customers. Serco's delivery of excellent service was once again reflected in our contract win rates. During 2007, we maintained our win rates at more than 90% for rebids and one in two for new bids. In total, we signed £3.6bn of contracts and were appointed preferred bidder for contracts valued at around £1.0bn.

Among the significant wins in existing markets, we signed a contract with the UK Ministry of Defence (MoD) to provide marine services to the Royal Navy. The contract is valued at around £750m over 15 years, a sizeable increase on our previous contract. We signed a £450m, 30-year contract to provide services to the new NHS Forth Valley Acute Hospital, which includes a number of technological innovations. The contract will begin in 2010. We also commenced work at Yarl's Wood Immigration Removal Centre under an eight-year, £85m contract with the UK Home Office. We were, however, disappointed by the cancellation of the Leicester Pathway PFI project for which we had been appointed preferred bidder in 2004.

We made inroads into new, high-value markets during the year, reaping the benefits of the technology capabilities we acquired in 2005 and our ability to bring together the skills of different divisions to create a compelling offering for our customers. Trusted Borders, a consortium of which Serco is a key member, was awarded a ten-year contract by the UK Home Office to develop and implement the e-Borders project. The contract is valued at around £200m to Serco. Glasgow City Council approved the creation of a strategic

partnership with Serco, to provide property and information and communication technology services. The partnership is valued at £265m to Serco over ten years and also positions us to support the Council on other transformational work.

We also won a record level of work in international markets, in particular in the United States. We renewed and significantly increased our contract with the US Postal Service to provide engineering, technical, project management and IT services. Over ten years it has a potential value of \$260m. The US Army selected Serco for the \$225m LOGCAP IV contract to provide cost analysis, logistics planning and supply chain consulting services worldwide. In addition, the Space and Naval Warfare Systems Center awarded us two contracts to assist with anti-terrorism systems. The first has a potential value of \$64m over five years. The second contract has a potential value of \$115m over five and a half years.

In the United Arab Emirates, we were appointed preferred bidder to operate and maintain the Dubai Metro. The contract is valued at more than £400m over 12.5 years, with passenger operations due to commence in autumn 2009. In Australia, the Queensland Department of Corrective Services appointed us to run Borallon Correctional Centre, under a contract valued at around Aus\$100m over five years. The Victoria Department of Justice selected us for a four-year safety camera contract valued at Aus\$90m.

A key strength of our business model is the visibility of future revenues. At 31 December 2007 we had visibility of 91% of planned revenue for 2008, 76% for 2009 and 63% for 2010. Our order book stood at a record £14.7bn and we were preferred bidder on contracts valued at £1.0bn. In addition, we have identified a pipeline of further opportunities across our markets estimated at £27bn.

Our actions to increase margins will deliver further improvements in the next few years. We continue to manage our contract portfolio by not renewing contracts and exiting businesses which do not fit our business model. We have introduced a range of measures to improve our operating efficiency, such as the roll-out of our new SAP system and the introduction of strategic sourcing of goods and services. Going forward, winning higher-value work will increasingly contribute to our margins. As a consequence of these actions, we expect our Adjusted PBT margin to increase by 30 basis points in both 2008 and 2009.

Serco has made a positive start to 2008. Although we were disappointed that the Oman Ministry of Defence no longer wishes to proceed with its project to develop a military training college, we were delighted to announce in February the signing of the £265m Glasgow City Council strategic partnership and a significant environmental services contract with the London Borough of Hammersmith and Fulham, valued at around £140m over 14 years.

Operating Review

Civil Government

Civil Government is our largest segment and includes home affairs, information technology and business process outsourcing, integrated facilities management, consulting and much of our work in the private sector. 2007 saw an increasing requirement for technological content in these markets, as customers looked to procure more sophisticated services. Segmental revenue increased by 8.8% to £952m, representing 34% of Group revenue (2006: 34%).

Home Affairs

We had two notable successes with the UK Home Office. Trusted Borders, a consortium of which Serco is a key member, signed a contract to develop and implement the nation's e-Borders project, an advanced border control and management programme. Serco is responsible for infrastructure and service management. The contract is valued at around £200m to Serco over ten years. We also won a contract to manage and operate Yarl's Wood Immigration Removal Centre. The contract began in April 2007 for an initial three years, with optional extensions for up to eight years. Over the full eight years, the contract is valued at around £85m.

We continued to build our presence in the Australian home affairs market, winning contracts to manage and operate Borallon Correctional Centre and to provide safety camera services. Borallon, near Brisbane, accommodates 500 male prisoners. This contract with the Queensland Department of Corrective Services is valued at around Aus\$100 million over five years, with the potential for a further five-year extension. The safety camera contract is with the Victoria Department of Justice. The four-year contract is valued at Aus\$90m, with the potential for a three-year extension.

IT and BPO Services

In UK local government, Glasgow City Council approved the creation of a partnership with Serco, to transform the Council's land, property and information and communications technology (ICT) services. The partnership will be worth £265m to Serco over ten years, and will also position us to support the Council on transformational projects to improve the Council's efficiency and service delivery. The partnership is the first of its kind in Scotland and is expected to save the Council more than £70m. We also secured a £30m, ten-year partnership with Ealing Council, to provide ICT support, and Southwark Council selected Serco to provide and support its ICT infrastructure in a five-year deal valued at £26m.

Severn Trent – one of the world's largest private water companies – awarded Serco a five-year IT infrastructure framework contract valued at around £40m. We will provide programme and project management, consulting, technical delivery, IT engineering and technology refresh services.

We continued to enhance our position as the leader in the UK business support market, winning a contract with the South West Regional Development Agency to provide the Business Link service for Cornwall, Devon and Somerset. The contract is for 28 months and is valued at around £15m.

The US Postal Service Engineering Organization appointed Serco to provide engineering, technical, project management and IT services. The two-year contract has four two-year options and over the full ten years has a potential value of \$260m, a sizeable increase over our previous contract. The latest contract broadens our role to include management services focused on enhancing efficiencies, quality assurance services and testing of mail processing equipment.

Integrated Facilities Management

Our integrated facilities management business had several notable successes. We signed a £450m, 30-year contract to provide support to the new NHS Forth Valley Acute Hospital, drawing on our healthcare experience to influence the hospital's design and thereby enhance infection control. Innovations include segregation of patient, visitor and goods traffic as well as the introduction of proven robotic technology to support the movement of goods around the hospital site. The contract will begin in 2010.

We signed contracts to provide operational management to the United Arab Emirates University in Al Ain (£70m over ten years) and to deliver property management and support services to State Street Bank (£50m over five years). Mid Suffolk and Babergh District Councils awarded us a contract in a groundbreaking shared services partnership for waste and recycling services. The contract is for up to 21 years and is valued at around £80m. Mid Sussex District Council also appointed us to provide refuse, recycling and street cleaning services. The contract is for up to 21 years and is valued at around £74m.

Consulting

We developed our consulting business with the acquisition of Cornwell Management Consultants plc, adding new capabilities in information and knowledge management, while increasing our capacity in project and programme management and enterprise architecture. We also acquired ER Consultants Limited as part of our building of capability in the area of sustainable change. ER brings experience and skills in leadership development and organisation design and development. These are key issues for many organisations and the acquisition enhances our ability to help our current customers and also to target new blue chip customers in the commercial sector.

Our consulting expertise resulted in our selection for a number of important frameworks in 2007. We were one of ten firms chosen to provide consultancy to UK government departments looking to undertake transformational projects as part of the four-year, £1.5bn Catalist framework. Serco was one of only two suppliers included in all five categories of the Metropolitan Police's four-year, £200m Development Services Framework. We were one of ten suppliers selected for the MoD's four-year, £100m "Catalogue" framework, the main route for the MoD to acquire consultancy services. We also qualified as one of only four providers

of project and programme management resources to the Department for Environment, Food and Rural Affairs. The potential value of the framework to the qualified suppliers is £80m over four years.

Defence

Revenue in Defence increased by 11.8% to £721m, representing 26% of Group revenue (2006: 25%). 2007 was a year of strong organic growth in defence, supplemented by demand for our value-added services.

United Kingdom

We had a highly-successful year in winning new business in the UK defence market, primarily in support of the Royal Navy and Royal Air Force.

The key win in the UK was a contract with the MoD to deliver marine services to the Royal Navy. The MoD selected our joint venture with Denholm Shipping and Infrastructure Investors (I²) for a 15-year private finance initiative (PFI) contract valued at around £1bn, of which Serco's operating contract represents £750m. This is a sizeable increase on our previous operating contract, under which we have provided marine services to the Royal Navy since 1996.

Serco will manage, operate and maintain a fleet of around 110 vessels, providing services that enable the Royal Navy to put to sea. The joint venture will also bring over 30 new vessels into service during the early years of the contract, enhancing service flexibility and responsiveness and helping to meet the Royal Navy's demanding operational requirements. Serco chose I² in 2006 to become its strategic partner for financing and investment in PFIs. In this project, I² will provide all the subordinated debt and the largest proportion of the equity (49%). Serco retains 41% of the equity as well as day-to-day management of the joint venture, so as to implement the successful transition of the project over the first 18 months.

The MoD awarded us a contract to manage the maintenance, repair and operation of the UK Armed Forces' estate facilities in Gibraltar. The contract is valued at around £50m over five years, with a further two option years and the potential for additional work. We will also provide military logistics, workshops and marine services support to the naval base and other MoD operations.

The Naval Air Command appointed Serco preferred bidder for a partnering contract valued at around £7m per annum. We will provide aviation, engineering and aircraft support at two Royal Naval Air Stations, Yeovilton and Culdrose, improving the availability of aircraft and trained aircrew to the Fleet Air Arm at a time of considerable operational pressure. The work will build on the operational support we already provide to the Royal Navy's aircraft.

We were also awarded a contract to provide a range of services at RAF Lyneham, home to the UK's tactical Air Transport force of Hercules aircraft and one of the largest and busiest operational stations in the RAF. In addition to providing base support, facilities management and logistics services, Serco will support the No 1 Air Mobility Wing, Tactical Medical Wing and No 4 Force Protection Wing. This win will further strengthen

Serco's relationships with Air Command and key equipment manufacturers such as Rolls Royce. The contract is for four years with three option years and is valued at around £34m over the full seven years.

We were awarded the Apache helicopter Interim Support Arrangement contract by AgustaWestland, the prime contractor for Apache 'depth' maintenance at Wattisham in the UK. Depth maintenance involves stripping the aircraft down and reassembling with repaired or new parts as necessary. The contract is valued at around £15m to Serco over three years.

United States

Our North American defence business won a record level of new contracts against a continued backdrop of pressure on non-combat operations. The US Army awarded us a contract to provide cost analysis, logistics planning and supply chain consulting services, under the Logistics Civil Augmentation Program IV (LOGCAP IV). The indefinite delivery/indefinite quantity (IDIQ) contract has a one-year base period with four annual options, for a five-year total period and a potential value of \$225m.

The Space and Naval Warfare Systems Center (SPAWAR) awarded us two contracts to assist the Navy and other government agencies with anti-terrorism systems. Under the first contract we will evaluate, integrate and install advanced anti-terrorism systems at Navy ports around the world. The IDIQ contract has a total potential value of \$64m over five years. The second contract extends that relationship with SPAWAR to other government agencies. The contract is valued at around \$62m over three years, and could reach \$115m if all five of the six-month award options are exercised.

The US Navy selected us for the major portion of the "Sea Enterprise" contract. The IDIQ contract is to provide engineering and installation services for command, control, communication, computers, intelligence and reconnaissance systems at ship, shore and submarine locations on the West Coast of the United States. It has a one-year base period with four annual options, for a maximum term of five years and a potential value of around \$156m. A key objective is to reduce the costs of installations by improving productivity and achieving long-term efficiencies.

Transport

Transport revenues grew by 4.7% to £655m, representing 23% of Group revenue (2006: 25%). A key feature of the year was the use of our UK skills to secure international opportunities.

Light Rail

The Dubai Government Roads and Transport Authority (RTA) selected Serco as preferred bidder to operate and maintain the initial two lines of the new Dubai Metro, the first such system in the region and an important development for the city. The contract includes pre-launch consultancy and planning, with operations and maintenance running for five years from autumn 2009 and the potential for a further five-year extension. The contract is valued at more than £400m over this 12.5 year period.

Serco will run the operations control centre, maintain rolling stock, track and station facilities and provide train attendants and all station staff. The lines will cover 76 kilometres of track and are predicted to carry 200m passengers per year. Ultimately, the RTA intends to extend the Dubai Metro to more than 300 kilometres, making it the world's largest driverless metro system.

During the year, we finished our contracts to operate the Manchester Metrolink and the Copenhagen Metro. We did not renew the contracts at rebid, as we continue to actively manage our contract portfolio.

Heavy Rail

Northern Rail, which we operate in a joint venture with NedRailways, carried nearly 79m passengers in 2007 and achieved a strong operational performance despite the severe floods in the summer. Northern Rail's success has led to it winning two prestigious national awards: Public Transport Operator of the Year at the National Transport Awards 2007 and the Example of Excellence in the Rural Action category at the 2007 Business in the Community awards. Our other joint venture with NedRailways – Merseyrail – was the best performing railway in the country in terms of reliability and punctuality, surpassing its previous best performance in 2005.

Great Southern Rail, our Australian rail operation, performed well in 2007, with good growth on both The Ghan and Indian Pacific services. The Overland service between Melbourne and Adelaide was re-launched in May 2007, since when its patronage has increased by more than 50%.

Traffic Management

In the UK, we successfully rebid our contract with Transport for London to maintain traffic signal control equipment and provide related services. The contract is for five years with the potential for a further two-year extension, and is valued at around £60m over the seven years. Serco will provide cover for all traffic control equipment including traffic signals, crossings, automatic number plate recognition cameras and traffic information signs. The services cover central London and the City, including important transport link points for the 2012 Olympics.

Serco operates the National Traffic Control Centre (NTCC) on behalf of the Highways Agency. We were pleased that the NTCC achieved final completion in May 2007, recognising the delivery of quality services and continuing innovation at this world-first facility. We have successfully rolled out the travel time variable messaging system, providing valuable real-time information for drivers.

In the US, the Georgia Department of Transportation appointed us to run the state's Traffic Management Center. This is Serco's first traffic management contract in North America. The contract is for up to four years and is valued at \$12m.

Science

Science revenues grew by 19.9% to £483m, representing 17% of Group revenue (2006: 16%). Technology and innovation are at the heart of our offering in this market.

Our joint venture with BNFL and Lockheed Martin to operate the UK's Atomic Weapons Establishment (AWE) continued to perform strongly. The infrastructure upgrade programme is progressing well, with the facility to house the Orion research project due to open on schedule in March 2008. This facility will cover both weapons research and civil science studies such as evolving stars and super dense matter. The construction of energy-efficient offices for up to 1,400 staff is also on time and on budget. As previously reported, BNFL is in the process of disposing of its shareholding in AWE and we hope this will be completed later this year.

Serco Technical and Assurance Services (Serco TAS) won several contracts in the nuclear market during the year. A consortium led by Serco TAS was awarded a £15m contract to provide specialist technical and engineering support to Magnox reactor sites over the next five years. A range of specialist nuclear technical services will be provided, including safety case management, systems engineering, analysis of safety-critical structures and systems and technical advice on waste management.

Serco TAS, in partnership with Golder Associates, was also awarded a £10m two-year contract to examine and develop plans to clean up contaminated land at Sellafield. The work will include assessment of the condition of the land and groundwater, mathematical modelling, development of a strategy for dealing with the contamination and identifying the technologies and actions needed for clean up.

The Nuclear Decommissioning Authority (NDA) appointed a consortium led by the Washington Division of the US company, URS, as preferred bidder to manage the UK's low-level radioactive waste repository at Drigg in West Cumbria. Serco TAS is an integrated sub-contractor and will provide regulatory, safety and environmental technical support to the consortium. The ten-year contract can be extended to up to 17 years.

Market Development

Serco's markets continue to expand rapidly, as local and national governments face budget deficits and ever-increasing pressure from citizens to improve public services. Governments increasingly recognise the benefits of opening up public service monopolies to competition and innovation. A review by the Serco Institute of 200 government and academic studies spanning 30 years, 12 countries and five sectors found that competition resulted in typical cost savings of 20%, with savings as high as 30-40% in some cases. Value for money in public services is driven by innovation and smarter ways of working. In the UK, the Government has launched a major study to help it understand the contribution of the public service industry and how the Government can support it, including the potential to export the UK's expertise in this area.

Turning to individual markets, we expect to see continued strong growth in home affairs. In the UK we are well established across all areas and we are expanding our footprint in Australia. Key drivers include the

threat of global terrorism, concern about immigration, perceptions of rising crime and the continued rise in prisoner numbers. These will increase governments' use of the private sector to provide capacity and to develop new capabilities to meet new threats.

Health and 'welfare to work' offer major future growth areas for Serco. The UK's National Health Service needs to deliver efficiency savings and meet stretching targets and Serco can play a critical supporting role. We plan to offer better value-for-money clinical services to the primary sector and to provide fully-managed healthcare solutions that deliver the information and support needed by clinicians and patients. The UK Government is also increasingly looking to the private sector to help the jobless move back into employment. We are well positioned to play a role in this important new market.

UK local authorities face major challenges, creating opportunities for Serco. The Government's 2007 Comprehensive Spending Review requires councils to deliver 3% annual efficiency savings, a degree of financial pressure new to many council leaders and chief executives. They will look to service providers for innovative and cost-effective solutions. In addition, local government reorganisation is creating a number of unitary authorities with greater responsibilities. This inevitably involves back-office consolidation, in particular in IT-based services. Serco is well placed to help. Finally, local authorities are being given a greater remit to shape their area and deliver local priorities, notably through agencies such as the police, health and highways. Serco's track record in reducing crime and in improving the environment, school performance and transport gives us a pivotal role, with our broad understanding of the local agenda placing us in a unique position in the market.

In defence, the public debate in the UK about the level of funding to equip and support the armed forces has intensified throughout the year. Our core business lies in helping government achieve greater value for money, and it is on that basis that we have continued to work with the MoD as it refreshes its Defence Industrial Strategy.

Our track record in the provision of operational support services to the front line commands and our independence from equipment manufacturers, position us well to deliver significant growth. This will be achieved by using our role as an integrator of people, infrastructure, training and technology to help the MoD deliver through-life capability management, and by leveraging our extensive capabilities in operational support and training into new overseas markets.

We have a significant position in the US defence market, and have broadened our offerings, which should serve us well as that sector continues to evolve to an imminent post-Iraq era. In particular, there is a continuing demand for our services to military personnel and their families, where we have a solid track record. We are well-positioned to provide logistics services as the military and other government agencies face greater pressures to reduce costs, and for advanced port security and other anti-terrorism/force protection applications, an area where we see continued emphasis in the near future.

In transport, we continue to monitor opportunities to address congestion and improve traffic efficiency. We have built strong links with customers in the UK and around the world to further this. In the United Arab Emirates there are substantial opportunities to grow our presence in the transport market with the development of the Dubai Metro. This system will be expanded over time and we anticipate a growing pipeline of opportunities with the rapid expansion of Dubai and further transport innovation across the Emirates, in particular Abu Dhabi. Our reputation for service delivery and working closely with clients is bringing a substantial range of opportunities across both light rail and traffic control systems that fit within our strategy.

We have engaged with the UK Government on future options for its trading funds and agencies. These options include the Government-Owned, Contractor-Operated (GOCO) model, of which our successful operations at AWE and the National Physical Laboratory are examples. GOCO is an attractive operating model where it is strategically important to retain a public stake in an organisation, and we will continue to work with government to examine its full potential while exploring other contractual mechanisms.

In the UK NDA market, our primary focus is on producing a competitive bid for Sellafield. SBB Nuclear, the consortium of Serco, Bechtel and The Babcock & Wilcox Company, is one of four invited by the NDA to submit final tenders. Tender responses are scheduled to be returned to the NDA in the spring of 2008, with the announcement of the winning bidder planned for the summer of 2008. SBB Nuclear is a unique and highly effective team, with a proven track record of safely and securely delivering high performance at AWE and at nuclear sites in the US, through partnership with employees and local communities. Together our consortium has experience of successful transition at 26 major sites in the UK and US. We look forward to continuing to work with the NDA and the stakeholders at Sellafield through the concluding stages of the competition process. There are also a number of other opportunities, including the decommissioning of the Magnox reactors, Dounreay and other smaller sites. We will continue to review the attractiveness of these opportunities as the market develops.

We continue to study the potential for our service-led model to be introduced into a number of new markets. While many of these markets are at an early stage, China, India and South Africa look likely to present opportunities in the medium term.

People

Serco's success depends on the quality, skills and dedication of our people. The best recognition of this is in the long-term relationships we build with our customers, the growth in existing contracts as our customers give us more work and in the number of customers who want Serco back when our contracts expire.

The quality of our employees is also reflected in the numerous awards and commendations that Serco receives. Among these, for the fourth year in a row, we were voted the UK's most admired support services company in Management Today's 'Britain's Most Admired Companies' awards. Serco also ranked as the

fourth most admired company overall. Management Today's awards have become a benchmark for excellence.

Board

As announced on 31 August 2006, Kevin Beeston moved from Executive Chairman to Non-Executive Chairman on 1 September 2007. Grant Rumbles, our Chief Operating Officer, was appointed an Executive Director on 3 July 2007.

DeAnne Julius retired on 29 October 2007 as a Non-Executive Director and from her post as Senior Independent Director. We extend our thanks to DeAnne for her considerable contribution to our development and wish her well. Baroness Ford of Cunninghame was appointed the new Senior Independent Director from the same date.

Tom Corcoran joined Serco as a Non-Executive Director on 3 December 2007. Tom is a member of the Remuneration, Audit, Nomination and Training and Development committees.

Outlook

Our markets continue to generate a broad range of high-quality opportunities for Serco, both in the UK and internationally. The success we have achieved in 2007 underpins our confidence in delivering double-digit growth for the foreseeable future. At the same time, our focus on managing our contract portfolio, enhancing our efficiency and bidding selectively for higher-value work will allow us to further increase our margins.

Finance Review

1. Financial performance

Serco continued to grow strongly in 2007 with another double-digit increase in revenue. At the same time, we successfully increased our margins and free cash flow and further strengthened our balance sheet.

Serco's income statement for the year is summarised in Figure 1 below. This includes the results of joint ventures which are proportionately consolidated.

As announced in our 2007 interim results, we have adopted a new pro forma profit measure, profit before tax and amortisation of acquired intangibles (Adjusted profit before tax). Figure 1 also shows Adjusted earnings per share, which is calculated before the amortisation of acquired intangibles. For 2006, the adjusted measures also exclude the gain on sale of our PFI investments of £11.4m.

Figure 1: Income statement

Year ended 31 December	2007 £m	2006 £m	Increase
Revenue	2,810.7	2,548.2	10.3%
Gross profit	406.2	365.7	11.1%
Administrative expenses	(264.2)	(242.9)	
Adjusted operating profit	142.0	122.8	15.6%
Investment revenue and finance costs	(18.8)	(17.8)	
Adjusted profit before tax	123.2	105.0	17.3%
Amortisation of acquired intangibles	(8.6)	(9.0)	
Gain on sale of PFI investments	-	11.4	
Profit before tax	114.6	107.4	6.7%
Tax	(32.2)	(27.9)	
Profit for the year	82.4	79.5	3.6%
Effective tax rate	28.1%	26.0%	
Adjusted earnings per share	18.57p	15.92p	16.6%
Earnings per share	16.98p	16.62p	2.2%
Dividend per share	4.25p	3.60p	18.1%

1.1 Revenue

Revenue grew by 10.3% to £2,810.7m, benefiting from the growth of existing contracts and the contribution of new wins.

1.2 Gross margin

Gross margin – the average contract margin across our portfolio – was 14.5%, a small increase on 2006.

1.3 Investment revenue and finance costs

Investment revenue and finance costs totalled a net cost of £18.8m (2006: £17.8m). In December 2006, we sold a number of our PFI investments to Infrastructure Investors Limited. The loss of net interest income from these investments was largely offset by the increase in net interest income from our retirement benefit obligations.

1.4 Adjusted profit before tax

Adjusted profit before tax was £123.2m, an increase of 17.3%. This represented a margin of 4.4%, up from 4.1% last year.

1.5 Gain on sale of PFI investments

2006 included an £11.4m one-off gain on the sale of PFI investments. The sale was part of our creation of a strategic PFI investment partnership with I². There was no corresponding gain in 2007.

1.6 Profit before tax

Profit before tax increased by 6.7% to £114.6m. Profit before tax excluding the gain on sale in 2006 was up by 19.4%.

1.7 Tax

The tax charge of £32.2m (2006: £27.9m) represents an effective rate of 28.1%, compared with 26.0% in 2006. The underlying rate in 2006 was 29.1% before the gain on sale of the PFI investments. The decrease in the underlying rate is primarily due to the mix of taxable profits.

1.8 Earnings per share (EPS)

Adjusted EPS rose by 16.6% to 18.57p. EPS grew by 2.2% to 16.98p.

EPS and Adjusted EPS are calculated on an average share base of 482.4m during the period (2006: 471.2m). The increase in the average share base resulted from the exercise of employees' share options.

2. Dividend

Serco's policy is to increase the total dividend each year broadly in line with the increase in underlying earnings. The Board has proposed a final dividend of 3.02p per share, representing an increase on the 2006 final dividend of 18.4% and bringing the total dividend for the year to 4.25p, growth of 18.1%. The final dividend will be paid on 21 May to shareholders on the register on 7 March.

3. Cash flow

The Group generated a free cash inflow of £97.6m (2006: £85.4m), an increase of 14.3%.

Figure 2 analyses the cash flow. As in previous years, we have designed the analysis to show the true cash performance of the Group – the cash flows generated by subsidiaries plus the dividends received from joint ventures. It therefore differs from the consolidated cash flow on page 23, which proportionately consolidates the cash flows of joint ventures. The adjustment line in Figure 2 reconciles the movement in Group cash to the consolidated cash flow.

Figure 2: Cash flow

Year ended 31 December	2007 £m	2006 £m
Operating profit excluding joint ventures	92.2	87.9
Non cash items	52.1	35.0
Group EBITDA	144.3	122.9
Working capital movement	(4.7)	(2.1)
Group operating cash flow	139.6	120.8
Interest	(25.6)	(10.6)
Tax	(5.4)	(6.7)
Expenditure on tangible and intangible assets	(47.9)	(47.7)
Dividends from joint ventures	36.9	29.6
Group free cash flow	97.6	85.4
Disposal of joint ventures	3.3	-
Acquisition of subsidiaries	(7.4)	-
Cash received on sale of PFI investments	-	76.5
Cash disposed of and transaction costs on sale of PFIs	-	(58.3)
Other financing	(71.0)	(98.6)
Special pension contribution	(51.0)	(19.0)
Dividends paid	(17.9)	(14.5)
Group net decrease in cash and cash equivalents	(46.4)	(28.5)
Adjustment to include joint venture cash impacts	6.7	10.3
Net decrease in cash and cash equivalents	(39.7)	(18.2)

Note: Group EBITDA is earnings from subsidiaries (excluding joint ventures) before interest, tax, depreciation, intangible amortisation and other non cash items

3.1 Group operating cash flow

Group operating cash flow of £139.6m (2006: £120.8m) reflects a conversion of Group EBITDA into cash of 97% (2006: 98%). This was a strong cash performance, given the level of organic growth in the business.

3.2 Interest

Net interest paid was £25.6m, compared to £10.6m in 2006. The increase is mainly due to lower cash interest receipts after the disposal of PFI investments in December 2006.

3.3 Tax

Tax paid was £5.4m (2006: £6.7m). Cash tax is below the equivalent tax charge in the income statement. This reflects timing differences and the availability of tax relief on the special pension contributions of £19m in December 2006 and £51m in January 2007.

3.4 Expenditure on tangible and intangible assets

Expenditure on tangible and intangible assets in the year was £47.9m (2006: £47.7m). This represents 2.2% of revenue excluding joint ventures (2006: 2.5%). Expenditure in 2007 included the completion of the roll-out of our SAP system in the UK.

3.5 Dividends from joint ventures

Dividends received from joint ventures totalled £36.9m (2006: £29.6m), a conversion rate of 100% (2006: 87%) of joint ventures' profit after tax and minority interest, excluding costs allocated by Group. Going forward, we expect conversion in the range of 80-90%.

3.6 Other financing

The movement in other financing resulted from repayments of our loans and the maturing of one of our private placements in December 2007 for £43.2m.

4. Net debt

Figure 3 analyses Serco's net debt.

Figure 3: Net debt

At	31 December 2007 £m	31 December 2006 £m
Group - cash and cash equivalents	138.1	177.8
Group - loans	(263.3)	(334.4)
Group - obligations under finance leases	(12.7)	(15.3)
Group recourse net debt	(137.9)	(171.9)
Joint venture recourse net cash	34.9	28.2
Total recourse net debt	(103.0)	(143.7)
Group non recourse debt	(59.3)	(62.2)
Total net debt	(162.3)	(205.9)

4.1 Group recourse net debt

Group recourse net debt decreased from £171.9m to £137.9m, due to the cash flows generated by the business.

Included within Group recourse net debt is £11.9m (31 December 2006: £10.6m) of encumbered cash. This is cash of PFI and other project companies securing credit obligations and customer advance payments.

4.2 Group non recourse debt

The Group's debt is non recourse if no Group company other than the relevant borrower – such as a special purpose company for a PFI – has an obligation to repay the debt under a guarantee or other arrangement. The debt is excluded from all of our credit agreements and other covenant calculations, and therefore has no impact on the Group's ability to borrow.

Group non recourse debt reduced by £2.9m to £59.3m during the year, due to scheduled repayments. The non recourse debt relates to the Kilmarnock prison contract and our Driver Examination Services contract in Canada.

5. Pensions

At 31 December 2006, the net liability included in the balance sheet arising from our defined benefit pension scheme obligations was £52.2m (2006: £120.0m). Figure 4 provides further analysis.

Figure 4: Defined benefit pension schemes

At	31 December 2007 £m	31 December 2006 £m
Group schemes – non contract specific	(67.9)	(157.8)
Contract specific schemes		
– reimbursable	(60.7)	(67.6)
– not certain to be reimbursable	(14.0)	(23.9)
Net retirement benefit liabilities	(142.6)	(249.3)
Intangible assets arising from rights to operate franchises and contracts	17.4	20.6
Reimbursable rights debtor	60.7	67.6
Deferred tax assets	12.3	41.1
Net balance sheet liabilities	(52.2)	(120.0)

Serco has three main types of scheme which are accounted for as defined benefit pension schemes. Each type has its own accounting treatment under International Financial Reporting Standards. These are:

- *Non contract specific* – schemes which do not relate to specific contracts or franchises. For these schemes, we charge the actuarial gain or loss for the period to the consolidated statement of recognised income and expense (the SORIE)
- *Reimbursable* – schemes where we have a right of full cost reimbursement and therefore include both the pension scheme deficit and offsetting reimbursable rights debtor in the balance sheet, and
- *Not certain to be reimbursable* – schemes relating to specific contracts or franchises, where the deficit will pass back to the customer or on to the next contractor at the end of the contract. For these schemes, we charge the actuarial gain or loss on our share of the deficit for the period to the SORIE, recognise a recoverable intangible asset on the balance sheet at the start of the contract or franchise and amortise the intangible asset to the income statement over the contract or franchise life.

Serco has limited commercial risk in relation to the contract specific schemes, due to either the right of cost reimbursement or because the deficit will pass back to the customer or on to the next contractor at the end of the contract. Among our non contract specific schemes, the largest is the Serco Pension and Life Assurance Scheme (SPLAS). At 31 December 2007, SPLAS had a deficit of £28.7m (31 December 2006:

£117.0m). The reduction in the deficit reflects the movement in bond yields and the action we have taken to ensure appropriate funding for the scheme, including the special pension payment of £51m in January 2007.

Figure 5 shows the sensitivity of the liabilities of our pension schemes to changes in discount rates and to adjustments in the actuarial assumptions for the rate of inflation, members' salary increases and life expectancies.

Figure 5: Pension assumption sensitivities

	Change in assumption	Change in liability
Discount rate	+0.5%	(9)%
	(0.5)%	+10%
Price inflation	+0.5%	+7%
	(0.5)%	(7)%
Salary	+0.5%	+3%
	(0.5)%	(3)%
Longevity	Increase by one year	+2.75%

6. Treasury

The Group's principal debt finance consists of a £400m bank credit facility comprising a term loan facility and a revolving credit facility. At 31 December 2007 we had £141m (31 December 2006: £163m) outstanding on the term loans and the revolving facility was undrawn. Interest is charged at a rate of 45 basis points over LIBOR on borrowings under the facility. The facility is unsecured and matures in December 2009.

Serco has also issued loan notes under two private placements. The first private placement, for £43.2m, matured in December 2007 and was fully repaid. The second, for £117.0m, amortises evenly from 2011 to 2015.

Consolidated income statement

For the year ended 31 December 2007

	Note	2007 £m	2006 £m
Continuing operations			
Revenue	2	2,810.7	2,548.2
Cost of sales		(2,404.5)	(2,182.5)
Gross profit		406.2	365.7
Administrative expenses		(264.2)	(242.9)
Other expenses – amortisation of intangibles arising on acquisition		(8.6)	(9.0)
Total administrative expenses		(272.8)	(251.9)
Gain on sale of PFI investments		-	11.4
Operating profit	2	133.4	125.2
Investment revenue	3	12.2	31.7
Finance costs	3	(31.0)	(49.5)
Profit before tax		114.6	107.4
Tax		(32.2)	(27.9)
Profit for the year		82.4	79.5
Attributable to:			
Equity holders of the parent		81.9	78.3
Minority interest		0.5	1.2
Earnings per share (EPS)			
Basic EPS	4	16.98p	16.62p
Diluted EPS	4	16.74p	16.43p

Consolidated statement of recognised income and expense

For the year ended 31 December 2007

	Note	2007 £m	2006 £m
Net actuarial gain on defined benefit pension schemes	7	62.2	78.9
Actuarial loss on reimbursable rights	7	(19.4)	(53.4)
Net exchange gain/(loss) on translation of foreign operations	7	12.8	(12.3)
Fair value gain on cash flow hedges during the year	7	9.0	2.2
Tax charge on items taken directly to equity	7	(11.5)	(7.0)
Net income recognised directly in equity		53.1	8.4
Profit for the year		82.4	79.5
Total recognised income and expense for the year		135.5	87.9
Attributable to:			
Equity holders of the parent		134.9	87.1
Minority interest		0.6	0.8

Consolidated balance sheet

At 31 December 2007

	Note	2007 £m	2006 £m
Non-current assets			
Goodwill		542.1	528.5
Other intangible assets		139.4	126.1
Property, plant and equipment		95.1	93.6
Trade and other receivables		104.6	110.5
Deferred tax assets		51.6	73.7
Derivative financial instruments		1.2	-
		934.0	932.4
Current assets			
Inventories		46.3	51.7
Trade and other receivables		573.6	463.3
Cash and cash equivalents		185.0	217.9
Derivative financial instruments		1.5	-
		806.4	732.9
Total assets		1,740.4	1,665.3
Current liabilities			
Trade and other payables		(670.0)	(541.9)
Current tax liabilities		(14.8)	(13.0)
Obligations under finance leases		(7.7)	(8.3)
Loans		(13.5)	(57.9)
Derivative financial instruments		(2.1)	(10.6)
		(708.1)	(631.7)
Non-current liabilities			
Trade and other payables		(13.3)	(10.4)
Obligations under finance leases		(8.7)	(11.5)
Loans		(317.4)	(346.1)
Derivative financial instruments		(11.2)	(14.2)
Retirement benefit obligations		(142.6)	(249.3)
Provisions		(18.6)	(22.3)
Deferred tax liabilities		(22.0)	(19.9)
		(533.8)	(673.7)
Total liabilities		(1,241.9)	(1,305.4)
Net assets		498.5	359.9
Equity			
Share capital		9.7	9.5
Share premium account		299.3	283.5
Capital redemption reserve		0.1	0.1
Retained earnings	7	260.6	196.6
Retirement benefit obligations reserve	7	(90.2)	(119.5)
Share-based payment reserve	7	34.6	25.5
Own shares reserve	7	(15.1)	(16.4)
Hedging and translation reserve	7	(1.8)	(21.3)
Equity attributable to equity holders of the parent		497.2	358.0
Minority interest		1.3	1.9
Total equity		498.5	359.9

Consolidated cash flow statement

For the year ended 31 December 2007

	Note	2007 £m	2006 £m
Net cash inflow from operating activities	5	134.1	159.5
Investing activities			
Interest received		10.3	32.4
Disposal of joint ventures		2.5	18.2
Proceeds from disposal of intangible assets		1.7	-
Proceeds from disposal of property, plant and equipment		2.9	1.4
Acquisition of subsidiaries, net of cash acquired		(9.1)	-
Purchase of other intangible assets		(30.6)	(30.4)
Purchase of property, plant and equipment		(26.2)	(27.8)
Net cash outflow from investing activities		(48.5)	(6.2)
Financing activities			
Interest paid		(34.2)	(42.2)
Dividends paid		(17.9)	(14.5)
Dividend paid to minority interest		(1.2)	(1.0)
Repayment of borrowings		(74.6)	(103.4)
New loan advances		2.2	9.4
Capital element of finance lease repayments		(8.4)	(8.6)
Proceeds from issue of share capital and exercise of share options		17.1	14.1
Decrease in non recourse loans		(8.3)	(25.3)
Net cash outflow from financing activities		(125.3)	(171.5)
Net decrease in cash and cash equivalents		(39.7)	(18.2)
Cash and cash equivalents at beginning of year		217.9	240.7
Net exchange gain/(loss)		6.8	(4.6)
Cash and cash equivalents at end of year	6	185.0	217.9

Notes to the Preliminary Announcement

1. General information

The basis of preparation of this preliminary announcement is set out below.

The financial information in this announcement, which was approved by the Board of Directors on 27 February 2008, does not constitute the Company's statutory accounts for the years ended 31 December 2007 or 2006, but is derived from these accounts.

Statutory accounts for 2006 have been delivered to the Register of Companies and those for 2007 will be delivered following the Company's annual general meeting. The auditors have reported on these accounts; their reports were unqualified and did not contain statements under S237 (2) or (3) of the Companies Act 1985.

The preliminary announcement has been prepared in accordance with International Financial Reporting Standards (IFRS) adopted for use in the European Union. Whilst the financial information included in this preliminary announcement has been computed in accordance with IFRS, this announcement does not itself contain sufficient information to comply with IFRS. The Company expects to publish full financial statements that comply with IFRS in April 2008.

The financial statements have been prepared on the historical cost basis.

Previously, amortisation of intangibles was shown separately within administrative expenses in the income statement and was excluded from the Adjusted earnings per share calculation. Only amortisation of intangibles arising on acquisition (amortisation of customer relationships and licences and franchises) is now shown separately in the income statement and excluded from the Adjusted earnings per share calculation. The 2006 comparatives have been re-presented. There is no change to operating profit or administrative costs in total as a result of this change in presentation.

2. Segmental information

The Group manages its business on a market segment basis and these segments are the basis on which the Group reports its primary segment information.

Market segments	Civil Government	Defence	Transport	Science	Total
Year ended 31 December 2007	£m	£m	£m	£m	£m
Revenue	952.2	720.5	655.0	483.0	2,810.7
Result					
Segment result	46.8	49.8	26.7	45.7	169.0
Unallocated expenses					(35.6)
Operating profit					133.4
Investment revenue					12.2
Finance costs					(31.0)
Profit before tax					114.6
Tax					(32.2)
Profit for the year					82.4

	Civil Government	Defence	Transport	Science	Total
Year ended 31 December 2006	£m	£m	£m	£m	£m
Revenue	875.0	644.8	625.7	402.7	2,548.2
Result					
Segment result	42.0	41.2	26.7	36.9	146.8
Unallocated expenses					(33.0)
Gain on sale of PFI investments					11.4
Operating profit					125.2
Investment revenue					31.7
Finance costs					(49.5)
Profit before tax					107.4
Tax					(27.9)
Profit for the year					79.5

Geographical segments	United Kingdom	North America	Europe and Middle East	Asia Pacific	Total
Year ended 31 December 2007	£m	£m	£m	£m	£m
Revenue	2,125.6	300.9	222.1	162.1	2,810.7

	United Kingdom	North America	Europe and Middle East	Asia Pacific	Total
Year ended 31 December 2006	£m	£m	£m	£m	£m
Revenue	1,886.5	295.3	213.4	153.0	2,548.2

3. Investment revenue and finance costs

	2007 £m	2006 £m
Net fair value adjustments on derivative financial instruments	0.3	-
Interest receivable by PFI companies	3.2	25.6
Interest receivable on other loans and deposits	5.5	6.1
Net interest receivable on retirement benefit obligations	3.2	-
Investment revenue	12.2	31.7
Net fair value adjustments on derivative financial instruments	-	(0.5)
Interest payable on non recourse loans	(3.7)	(18.0)
Interest payable on obligations under finance leases	(1.0)	(0.6)
Interest payable on other loans	(26.3)	(28.5)
Net interest payable on retirement benefit obligations	-	(1.9)
Finance costs	(31.0)	(49.5)
Net finance costs	(18.8)	(17.8)

4. Earnings per share

Basic and diluted earnings per ordinary share (EPS) have been calculated in accordance with IAS 33 'Earnings Per Share'. EPS is shown both before and after amortisation of intangible assets arising on acquisition and the gain on sale of PFI investments to assist in the understanding of the underlying performance of the business.

The calculation of the basic and diluted EPS is based on the following data:

Number of shares

	2007 millions	2006 millions
Weighted average number of ordinary shares for the purpose of basic EPS	482.4	471.2
Effect of dilutive potential ordinary shares: share options	6.8	5.5
Weighted average number of ordinary shares for the purpose of diluted EPS	489.2	476.7

Earnings

	2007		2006	
	Earnings £m	Per share amount Pence	Earnings £m	Per share amount Pence
Earnings for the purpose of basic EPS being net profit attributable to the equity holders of the parent	81.9	16.98	78.3	16.62
Less:				
Gain on sale of PFI investments	-	-	(11.4)	(2.42)
Add back:				
Amortisation of intangible assets arising on acquisition, net of tax of £0.9m (2006 : £0.9m)	7.7	1.59	8.1	1.72
Adjusted earnings before amortisation of intangible assets and gain on sale of PFI investments	89.6	18.57	75.0	15.92
Earnings for the purpose of basic EPS	81.9	16.98	78.3	16.62
Effect of dilutive potential ordinary shares	-	(0.24)	-	(0.19)
Diluted EPS	81.9	16.74	78.3	16.43

5. Reconciliation of operating profit to net cash inflow from operating activities

	2007 £m	2006 £m
Operating profit for the year	133.4	125.2
Adjustments for:		
Share-based payment expense	5.0	4.8
Depreciation of property, plant and equipment	30.2	30.0
Amortisation of intangible assets	23.2	16.2
Loss on disposal of property, plant and equipment	1.3	1.1
Profit on disposal of joint ventures	(0.7)	-
Gain on derivatives	(1.1)	-
Gain on sale of PFI investments	-	(11.4)
Operating cash inflow before movements in working capital	191.3	165.9
Decrease/(increase) in inventories	5.9	(13.9)
(Increase)/decrease in receivables	(101.4)	10.7
Increase in payables	108.6	21.8
Movement in provisions	(4.3)	(4.5)
Special contribution to defined benefit pension scheme	(51.0)	(19.0)
Cash generated by operations before PFI debtor movement	149.1	161.0
Movement on PFI debtor	1.5	17.4
Cash generated by operations after PFI debtor movement	150.6	178.4
Tax paid	(16.5)	(18.9)
Net cash inflow from operating activities	134.1	159.5

6. Analysis of net debt

	At 1 January 2007 £m	Cash flow £m	Acquisitions/ disposals £m	Exchange differences £m	Non cash movements £m	At 31 December 2007 £m
Cash and cash equivalents	217.9	(38.3)	(1.4)	6.8	-	185.0
Non recourse loans (related to PFI assets)	(24.8)	2.3	-	-	-	(22.5)
Other non recourse loans	(37.4)	6.0	-	(5.4)	-	(36.8)
Other loans	(341.8)	72.4	0.2	1.7	(4.1)	(271.6)
Obligations under finance leases	(19.8)	8.4	-	(0.4)	(4.6)	(16.4)
	(205.9)	50.8	(1.2)	2.7	(8.7)	(162.3)

Non cash movements in 2007 primarily relate to fixed assets acquired under finance leases, and the crystallisation of the fair value adjustment of £4.0m to the value of one of the private placement loans. The loan was hedged by forward foreign exchange contracts and cross currency swaps.

7. Reserves

Retained earnings

	2007 £m	2006 £m
At 1 January	196.6	132.8
Dividends paid	(17.9)	(14.5)
Profit for the year attributable to equity holders of the parent	81.9	78.3
At 31 December	260.6	196.6

Other reserves

	Retirement benefit obligations reserve £m	Share-based payment reserve £m	Own shares reserve £m	Hedging and translation reserve £m	Total £m
At 1 January 2007	(119.5)	25.5	(16.4)	(21.3)	(131.7)
Net actuarial gain on defined benefit pension schemes	62.2	-	-	-	62.2
Actuarial loss on reimbursable rights	(19.4)	-	-	-	(19.4)
Credit in relation to share-based payment expense	-	5.0	-	-	5.0
Net exchange gain on translation of foreign operations	-	-	-	12.8	12.8
Fair value gain on cash flow hedges during the year	-	-	-	9.0	9.0
Exercise of share options	-	(0.2)	1.3	-	1.1
Tax charge on cash flow hedges	-	-	-	(2.3)	*(2.3)
Tax (charge)/credit on items taken directly to equity	(13.5)	4.3	-	-	*(9.2)
At 31 December 2007	(90.2)	34.6	(15.1)	(1.8)	(72.5)

* in 2007 these amounts represent £11.5m of tax charge taken directly to equity in the SORIE

8. Joint ventures

The Group's interests in joint ventures are reported in the consolidated financial statements using the proportionate consolidation method.

The effect of the Group's joint ventures on the consolidated income statement is as follows:

	2007 £m	2006 £m
Revenue	680.1	643.3
Expenses	(638.9)	(606.0)
Operating profit	41.2	37.3
Investment revenue	4.9	3.3
Finance costs	(0.9)	(1.3)
Profit before tax	45.2	39.3
Tax	(12.1)	(8.6)
Profit for the year	33.1	30.7
Minority interest	(0.3)	(0.6)
Share of post-tax results of joint ventures	32.8	30.1

Operating profit is after allocating £4.0m (2006: £4.0m) of costs incurred by Group.