serco

SERCO GROUP PLC

INTERIM REPORT 2003

turnover up

15.4%

to £722.6m

profit before tax – pre goodwill up

10.2%

to £31.3m

contracts awarded totalling

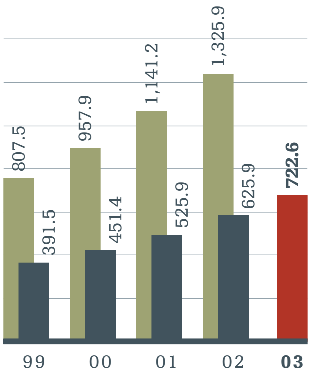
£3.5bn

Financial and operating highlights

	6 months to 30.6.03	6 months to 30.6.02	
Turnover	**£722.6m**	£625.9m	up 15.4%
Profit before tax – pre goodwill*	**£31.3m**	£28.4m	up 10.2%
Earnings per share – pre goodwill	**5.15p**	4.84p	up 6.4%
Dividend per share	**0.72p**	0.64p	up 12.5%

*Profit after goodwill and before tax for the six months to 30.6.03 was £27.0m (2002: £24.5m). More detail is provided in the financial review.

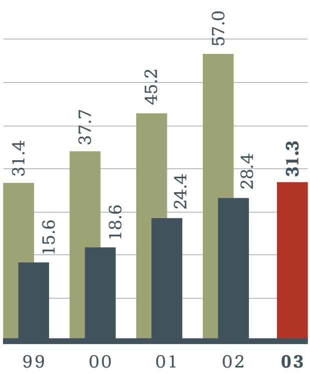
- **Double-digit increases in sales and profits for the 16th consecutive year**
  - Over 70% of increase in turnover came from extensions to the scope and scale of existing contracts
  - Profit before goodwill, tax and an incremental pension cost of £4.5m resulting from an increase in long term contribution is up 26%
- **Succession of sales records broken**
  - Largest new contract – 25-year Merseyrail Electrics contract worth £1.8bn
  - Largest rebid – 11-year contract at Goose Bay, Canada worth C$400m
  - Largest contract extension – 15-year extension to the Atomic Weapons Establishment contract worth over £1bn
  - Largest North American contract – 10-year Ontario driver examination services contract worth C$600m
- **Strong cash performance**
  - First half year free cash inflow £14.2m (2002: outflow of £11.5m)
  - Great Southern Railway sale and leaseback generated £5.8m of cash
- **Acquisition of remaining 50% share in Premier Custodial Group successfully completed in July**
- **Restructuring and review of underperforming businesses**
  - Business reorganisation resulted in exceptional charge of £4.5m while generating ongoing savings of £1.5m a year
  - Agreement reached with Network Rail to terminate East Midlands track maintenance contract in January 2004
- **Continued high visibility of earnings**
  - Forward order book up from £7.1bn to £9.9bn
  - 99% of 2003 turnover already secured
  - 86% of 2004 turnover already secured
- **Substantial range of future opportunities**
  - Bids worth £6bn submitted and under evaluation
  - £8bn of further opportunities identified



TURNOVER £m

Full year

Half year



PROFIT BEFORE TAX £m

Before amortisation of goodwill

Chairman's statement

Serco has had an excellent six months. While maintaining double-digit growth in sales and profits, we have won major new contracts that will contribute to the business for years to come. Trading, margins and cash generation remain strong.

Our forward order book grew from £7.1bn in December 2002 to £9.9bn as we broke a succession of sales records: our largest new contract, largest rebid and largest contract extension. A high rate of organic growth is our principal objective, and over 70% of the first half's incremental sales came from extensions to the scope and scale of existing contracts. Our success rate in rebids and contract extensions remained above 90%, and we continued to win over half of our new bids.

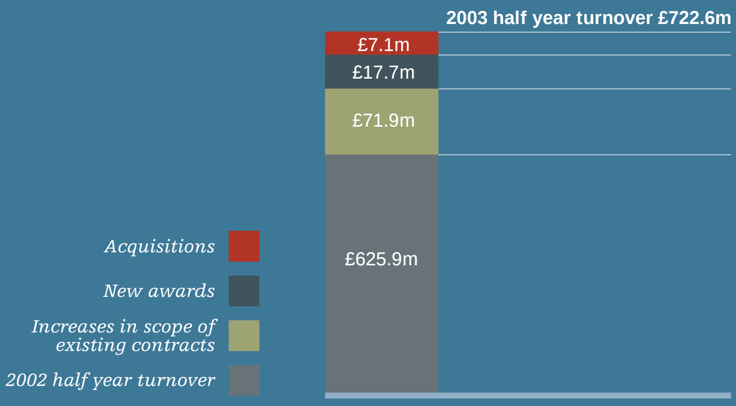
The keys to our record of dependable organic growth are the diversity of our markets, extending across many sectors and geographies, and the quality of the relationships we build with customers. There is no shortage of new opportunities: we currently have bids with a value of £6bn under evaluation and are addressing a further £8bn of opportunities.

Financial performance

Results

In the six months to 30 June 2003, turnover was £722.6m – 15.4% higher than the first half of 2002. Pre-tax profit (before goodwill) grew 10.2% to £31.3m. Earnings per share (before goodwill) grew 6.4% to 5.15p.

These results include an additional £4.5m of pension costs in the first half as a result of the increased pension funding requirement identified with our 2002 preliminary results. Excluding these costs, pre-tax profits (before goodwill) grew by 26%.



TURNOVER GROWTH TO 30 JUNE 2003

We continue to focus on cash generation. During the first half cash performance was strong, with positive free cash inflow of £14.2m compared with an outflow of £11.5m in the six months to 30 June 2002. This is a significant achievement in a business with consistently high growth, which brings incremental demand for working capital.

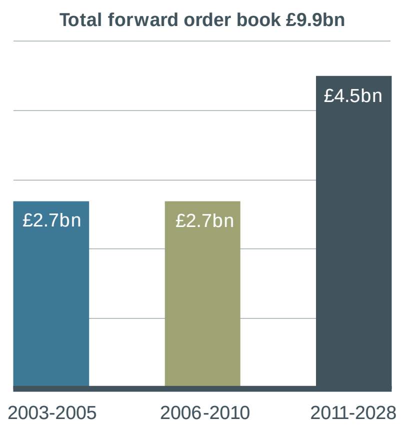
As part of the focus on cash generation, we arranged the sale and leaseback of the remaining rolling stock belonging to our Great Southern Railway business in Australia. This generated £5.8m of cash and £4m of profit and followed a similar arrangement completed in June 2001.

Further details of our financial performance are given in the financial review on page 11.

Dividend
We have increased the interim dividend by 12.5% to 0.72p per ordinary share. It will be paid on 10 October 2003 to shareholders on the register at close of business on 12 September 2003.

Balance sheet
Because of the rapid growth of the business and the scale of opportunities ahead of us, maintaining a strong balance sheet is a priority. In August we took advantage of historically low interest rates by issuing £117m of 8-12 year loan notes. This provides assured funding for the future and allows a mixed profile of debt facilities and maturity. It has also enabled us to repay the short term bank facilities we used to acquire the remaining 50% of Premier Custodial Group.

Operational performance
Notwithstanding excellent organic growth, the period was particularly notable for four business wins: our largest-ever new contract, rebid and extension plus a strategically important win in North America.



LONG TERM FORWARD ORDER BOOK

In May we signed our largest-ever contract, worth £3.6bn, to run the Merseyrail Electrics contract for 25 years from July in partnership with the Dutch rail operator NedRailways. Serco's share of the contract is worth £1.8bn.

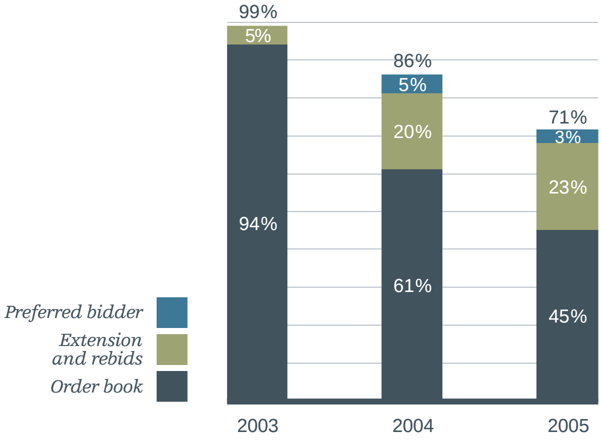
In February the Canadian Department of National Defence appointed us to provide site support services at its Goose Bay Canadian Forces Base for a second term in our largest-ever rebid: an 11-year contract worth some C$400m.

In January the UK government announced a 15-year extension to the 10-year contract under which we and our partners are managing the Atomic Weapons Establishment – adding £1bn to our order book and extending the contract to 2025.

In addition to these wins, we broke new ground in North America with a 10-year public private partnership under which we will provide driver examination services throughout the state of Ontario in Canada. This is the first contract of its kind in the North American market and is a model which could be replicated in future.

UK
The UK continues to be an exceptionally fruitful market for us. Two further important UK wins were a £60m multi-activity contract to provide flight training and support services at RAF Cranwell, and a Private Finance Initiative (PFI) contract to procure a 326-bed immigration detention centre in Colnbrook, Middlesex and operate it for eight years.

The contract at RAF Cranwell further strengthens our position in the buoyant defence market, where we currently have several very large bids under consideration including the £13bn Future Strategic Tanker Aircraft contract and the RAF's Airfield Support Services Project, which covers over 100 UK military bases and airfields.



NEAR TERM FORWARD ORDER BOOK
Percentage of planned revenue for the year

Our rail business continues to bid for carefully selected contracts. We were disappointed not to win the Wales & Borders franchise after reaching the final shortlist, but our Merseyrail success has encouraged us in our bids for the Northern Rail franchise and the third phase of the Manchester Metrolink.

In the road transport sector we continue to secure new business and are on schedule to open the Highways Agency's Traffic Control Centre in early 2004.

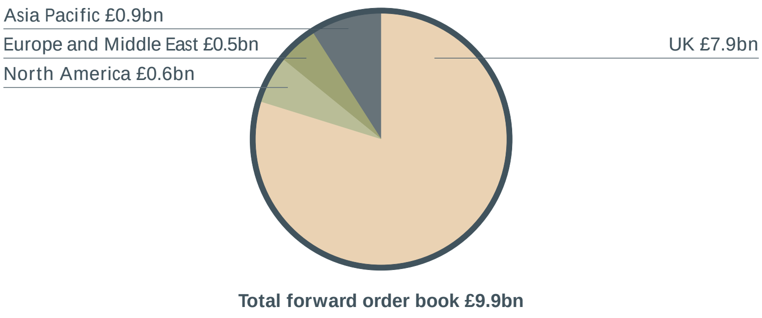
We are also making good progress in civil government. Our leisure, healthcare, education and local authority direct service businesses are all addressing opportunities with innovative solutions and a high rate of success.

We remain enthusiastic but selective participants in PFI contracts, which account for some 12% of our turnover. Our interest in PFIs is focused on the long term operating contracts that follow the construction or asset procurement phase. Over the past few years we have built a PFI forward order book worth some £3.4bn, and we are already generating net positive cash flows after our £13.2m equity and subordinated debt investment in these contracts.

International
We continue to attach great importance to our international growth strategy, and several of our primary target markets are beginning to show real promise.

In Canada we have achieved a degree of critical mass by securing the Goose Bay rebid and winning the Ontario driver examination services franchise.

In Australia our Great Southern Railway business will gain a further boost in February 2004, when the Alice Springs-Darwin link opens.



GEOGRAPHIC SEGMENTAL ANALYSIS – TOTAL FORWARD ORDER BOOK

Ticket sales for the extended journey to Darwin topped A$5m in the first five weeks after bookings opened – six months before the first train is due to run.

In Europe we continue to gain ground in Italy and Germany. In Germany we are making steady progress in the defence and government sectors; in Italy we have won our first facilities management contract as we build on our early successes in government IT outsourcing to gain entry into new and evolving market sectors.

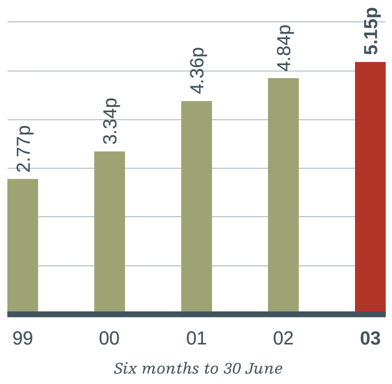
In the Middle East we are continuing to grow our core air traffic services business while developing newer markets in facilities management, technology and training services. We are on a shortlist of two bidders for the first Omani PFI, to build and operate a joint services technical training college.

Strategic developments

Acquisitions

During the first half we bought-out our partners in three businesses, two of which are PFI projects. At the National Physical Laboratory we took full control of Laser, formerly a joint venture with Laing Investments Limited. In Manchester we acquired the Altram consortium which had built Phase 2 of the Metrolink system and operates and maintains Phases 1 and 2. In Denmark we made a similar move by buying out the joint venture we formed with Arriva to commission and run the Copenhagen Metro, which opened last October.

In July we also acquired our partner's share of Premier Custodial Group, our custodial support services business. This £48.6m deal followed our partner's acquisition by a competitor and gives us the opportunity to develop the business in the UK and overseas. The custodial market is expanding rapidly and opportunities arising over the next few years in the UK alone will include new prisons, secure training facilities for



BASIC EARNINGS PER SHARE

Before amortisation of goodwill

juvenile offenders, and immigration accommodation centres. Premier has a number of PFI contracts, and its assets and non-recourse debt will be consolidated in the second half.

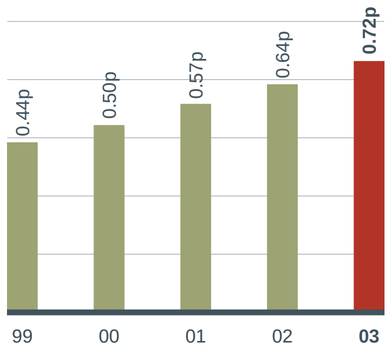
All our PFI acquisitions bring non-recourse debt onto the Group balance sheet. During the first half, the amount of non-recourse debt on the balance sheet increased from £29.7m to £117.8m. The Premier acquisition will add around £180m. All these debts are long term bank loans secured on the assets held in the companies which operate the PFI concessions and not on the assets of Serco Group. Although we consolidate these non-recourse loans on the balance sheet, they are ringfenced and do not affect our debt facility covenants or our ability to fund the Group going forward.

Restructuring

In our 2002 preliminary results announcement and at our AGM in May, we referred to the review that we are undertaking to focus the business on areas with greatest potential and to reduce underperforming activities.

As our businesses grow, we need to back them with efficient and consistent support processes. So we have restructured our UK support operations, bringing them together on a single business campus in Hampshire to create Serco Business Services. We have also rationalised our Australian support offices to a single centre in Sydney. The redundancy and relocation costs result in an exceptional charge of £4.5m in the accounts for the first half, but will generate ongoing savings of some £1.5m a year.

A further result of the strategic review was an agreement with Network Rail in the UK to withdraw from our track maintenance contract for the East Midlands zone in January 2004.



Six months to 30 June

DIVIDEND PER SHARE

New capability
We have continually encouraged customers to let larger and more sophisticated contracts, and have developed the resources to handle them. Helping customers to develop and manage this type of contract has now become a growth opportunity in its own right. Having already built the financial capability to structure finance for complex, large-scale contracts and to manage our own investment portfolio, we have now supplemented and extended that capability to create a new business, Serco Government Consulting. The team currently includes some 20 management consultants who provide strategic consulting advice and help customers shape, define and implement business solutions. It will also provide strategic advice and management support to our operating businesses.

People
In June we appointed David Richardson to the board as a non-executive director. David is finance director of Whitbread, the FTSE 100 leisure group. His previous roles there have included eight years as strategy director. He will take over as chairman of the audit committee when Rhidian Jones retires in April 2004.

A further change to the board is planned in March next year, when Iestyn Williams retires as a director. Iestyn has been with the company for 25 years and a board member since 1986. He will continue his association with the company as non-executive chairman of our education business, Serco Learning.

One of our major objectives, as a business employed predominantly by the public sector, is to demonstrate that a private sector business can have a public service ethos. There can be few more convincing examples of this than the conduct of our 500 support staff working in Hong Kong hospitals during the SARS outbreak. Almost 1,750 people caught the disease in Hong Kong – and more than a fifth of them were hospital workers. Many of our people admitted they were scared. But that didn't stop them from delivering much-needed services on the front line throughout the crisis. We respect all of them for their courage and thank them for their dedication.

As always, we also thank all our people for their part in Serco's continuing growth and success.

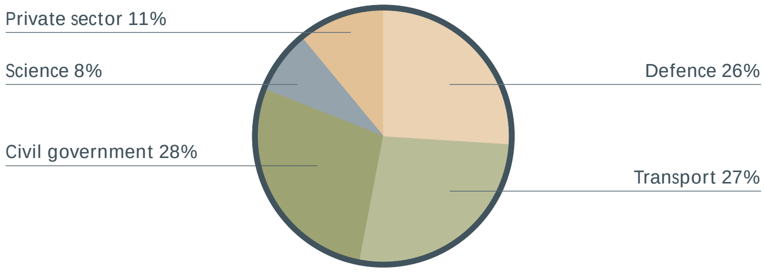
Corporate social responsibility
Social responsibility has been an integral part of our culture for over 40 years. We have a structured approach which delegates accountability for corporate social responsibility performance to every contract manager. This ensures that initiatives are managed at a local level, where they have most impact. The first Business in the Community Corporate Responsibility Index, announced in March, indicates that this approach is delivering encouraging results: Serco was ranked in the second quintile, and our overall score of 79% only just fell short of the top quintile.

Outlook
Our total order book has increased from £7.1bn to £9.9bn – equivalent to about seven times last year's turnover. We are currently addressing a further £14bn of opportunities. Assuming a continuing 90% renewal rate on rebids, we already have contracts in place to provide 99% of planned revenue this year, 86% in 2004 and 71% in 2005.

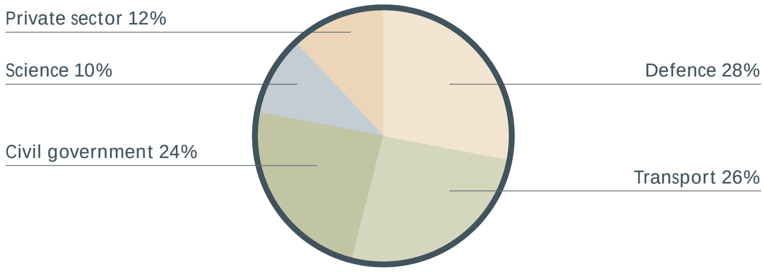
The unremitting pressure on governments to deliver value for taxpayers' money plays to our strengths. We are confident that our standing among customers and potential customers remains high, and our credibility is underpinned by a track record of delivery. We look forward to sustained, profitable growth – in the second half and for the foreseeable future.

3 September 2003

SECTOR SEGMENTAL ANALYSIS – TOTAL GROUP

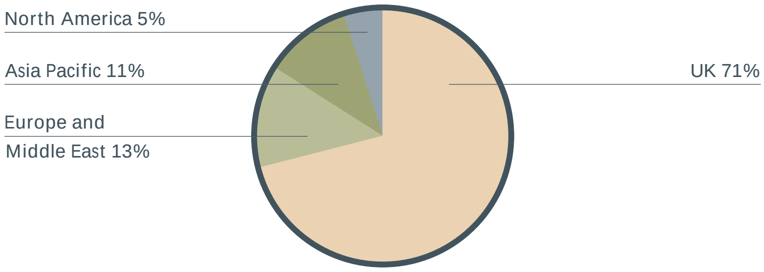


2003 half year turnover £722.6m
Including share of joint ventures

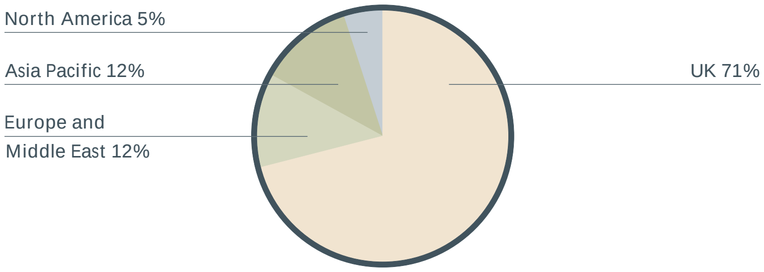


2002 half year turnover £625.9m
Including share of joint ventures

GEOGRAPHIC SEGMENTAL ANALYSIS – TOTAL GROUP



2003 half year turnover £722.6m
Including share of joint ventures



2002 half year turnover £625.9m
Including share of joint ventures

1 Financial performance

The first half of 2003 has been another period of strong performance. Further analysis is provided below:

Six months to 30 June	2003 £m	2002 £m	Change
Total turnover	722.6	625.9	15.4%
Group turnover	608.6	522.0	
Joint venture turnover	114.0	103.9	
Gross profit	83.2	71.1	16.9%
Administrative expenses	(61.8)	(50.4)	
Exceptional items (net)	(0.5)	–	
Joint venture profit	11.8	10.1	
Net Group interest	(1.4)	(2.4)	
PROFIT BEFORE GOODWILL AND TAX	31.3	28.4	10.2%
Goodwill	(4.3)	(3.9)	
Profit before tax	27.0	24.5	10.0%
Tax	(9.2)	(8.3)	
Profit after tax	17.8	16.2	
Effective tax rate	34%	34%	
Average number of shares	429.6m	414.1m	
Earnings per share before goodwill	5.15p	4.84p	6.4%
Earnings per share after goodwill	4.14p	3.91p	5.9%

1.1 Turnover

Total turnover in the six months to 30 June 2003 increased by 15.4% to £722.6m. This includes £114.0m of turnover relating to joint ventures, an increase of 9.7%. Group turnover increased by 16.6% to £608.6m.

1.2 Gross profit

Gross profit of £83.2m increased by 16.9% and represents a return on group turnover of 13.7% (2002: 13.6%).

1.3 Pre-tax profit

Pre-tax profit before goodwill amortisation increased 10.2% to £31.3m.

1.4 Exceptional items

Two exceptional items during the period result in a net charge of £0.5m.

The sale and leaseback of the remaining rolling stock belonging to our Great Southern Railway (GSR) business in Australia generated cash of £5.8m and profit of £4.0m.

We have also undertaken a fundamental review of our support office and underperforming operations, resulting in a number of redundancies, office closures and relocations. The £4.5m cost of this restructuring has been charged to the profit and loss account in the first half of the year.

1.5 Pensions costs

As disclosed in our 2002 Accounts, to address the net deficit on our UK defined benefit scheme we have increased our long term contribution rates. For 2003 we have increased our pension contribution by £9m, which is accounted for evenly over the year. Excluding this additional cost, our first half profit before goodwill and tax increased by 26%.

1.6 Tax

The tax charge of £9.2m (2002: £8.3m) represents an effective rate of 34% (2002: 34%).

1.7 Earnings per share

Earnings per share before goodwill amortisation grew by 6.4% to 5.15p. The average number of shares increase reflects the impact of a share placement in March 2002.

2 Dividends

The proposed interim dividend of 0.72p per share is a 12.5% increase on 2002.

3 Cash flow

During the six months to 30 June 2003 we generated free cash inflow of £14.2m against an outflow of £11.5m in the first six months of 2002.

This is further analysed below:

Six months to 30 June	2003 £m	2002 £m
Operating profit before exceptional item	17.1	16.8
Exceptional item: Reorganisation costs	(4.5)	–
Operating profit	12.6	16.8
Non cash items: Depreciation and goodwill	13.7	11.5
Group EBITDA	26.3	28.3
One-off pension fund contribution	–	(15.5)
Working capital movement	(10.9)	(16.6)
Operating cash flow	15.4	(3.8)
Dividends from joint ventures	4.6	6.2
Interest and taxation	(5.1)	(5.4)
Capital expenditure/disposals of assets	(7.6)	(7.9)
Exceptional item: GSR sale and leaseback	5.8	–
Other items	1.1	(0.6)
FREE CASH FLOW	14.2	(11.5)
Acquisitions/disposals	(5.3)	(3.2)
Share issues/other financing	(1.5)	116.0
Dividends paid	(6.2)	(5.5)
Net cash flow	1.2	95.8
Closing cash	70.6	60.0
Long term loans	(48.2)	(45.3)
Other loans and finance leases	(22.2)	(17.5)
Net cash/(recourse debt)	0.2	(2.8)
Non-recourse debt to fund PFI assets	(117.8)	(19.7)
Total net debt	(117.6)	(22.5)

3.1 Operating cash flow

There was an operating cash inflow for the period of £15.4m (2002: outflow of £3.8m). This converts 122% (2002: n/a) of our operating profit and 59% (2002: n/a) of Group EBITDA into cash.

3.1 Operating cash flow *(continued)*

The working capital increase of £10.9m (2002: £16.6m) reflects the continuing strong level of organic growth shown by the Group in 2003 and equates to approximately one month's incremental period on period turnover, reflecting the typical invoicing cycle of our contracts.

3.2 Joint ventures

Dividends received from joint ventures in the first six months of 2003 of £4.6m (2002: £6.2m) represent a 56% (2002: 88%) conversion of profit after tax of joint ventures into cash. Dividends received in 2002 included a dividend of £3.3m from a refinancing of the Joint Services Command and Staff College PFI.

3.3 Capital expenditure

Capital expenditure, excluding investment in PFI Special Purpose Companies (SPCs), for the six months to 30 June 2003 was £12.5m (2002: £8.2m). As a proportion of Group turnover this expenditure represents 2% and has remained at a similar level to previous years.

3.4 Pensions

A £15.5m pension payment in 2002 was made to assist the merger of Serco's two defined benefit schemes by achieving a similar funding level across both schemes.

Operating cash flow for the six months to 30 June 2003 includes an additional £4.5m of pension costs as a result of the increased pension funding requirement referred to in 1.5.

3.5 Non-recourse debt

At 30 June 2003 non-recourse loans totalled £117.8m (2002: £19.7m). These loans fund the construction and development of the Traffic Control Centre and the National Physical Laboratory.

The completion of the acquisition of our partner's share in Premier Custodial Group in July, together with the funding of the Ontario driver examination services franchise payment, will lead to additional non-recourse loans being included in our balance sheet, along with the related assets at the end of 2003.

Non-recourse debt is excluded from the Group's banking facility covenants but is consolidated on the Group's balance sheet. The corresponding asset is included within 'Debtors: amounts due after more than one year' in the balance sheet. The loans are secured on those assets held within the SPC to operate the PFI concessions and not on the assets of Serco Group.

4 Pensions

We continue to apply the transitional rules and disclosures of FRS 17 *Retirement Benefits*. This required the market value of assets and liabilities for defined benefit schemes to be calculated and disclosed in a note to the 2002 Group accounts. At 31 December 2002 we identified a net deficit of £74m in relation to the main UK defined benefit schemes and an asset base of approximately £295m, while the Minimum Funding Rate (MFR) funding level was 100%. While we are not required to undertake a full actuarial valuation of the scheme at 30 June 2003, it is estimated that the net deficit is approximately the same.

4 Pensions (continued)

As noted above, the two principal defined benefit schemes in the UK were merged in February 2003. The investment profile of the merged scheme will be changed such that equities will become a smaller proportion of total assets to help achieve a closer matching of the asset and liability profiles.

5 Treasury

5.1 Treasury management

The Group's tax and treasury function is responsible for managing the Group's exposure to financial risk. It operates within policies approved and reviewed by the board, which include controls on the use of financial instruments. The Group reviews the credit quality of counterparties and limits individual aggregate credit exposures accordingly.

5.2 Liquidity management

The Group funds its operations through bilateral bank credit facilities and a long term US private placement of loan notes ('the US notes'). Borrowings under the bank facilities are floating rate, unsecured obligations with covenants and obligations typical of these types of arrangements. The US notes mature in December 2007.

At the end of June 2003 bank facilities totalled £160m, of which £50m was committed funding. The committed bank facilities mature in November 2005.

On 20 August 2003, the Group completed a private placement for £117m sourced from a number of institutions. This private placement is designed to lengthen the maturity profile of the Group's debt, with a final maturity of 12 years and an average term of 10 years. The placement will be used to refinance the debt used to acquire Premier Custodial Group and to help position the Group for future growth. The debt was issued in Sterling and US Dollars at a fixed average coupon of 5.7%. The debt issued in US Dollars has been swapped into Sterling.

6 Auditors

While there is no statutory requirement to do so, the financial statements and notes in this Interim Report have been reviewed by our auditors, Deloitte & Touche LLP. Their review conclusion is included on page 23.

7 Events after 30 June 2003

On 2 July we completed the acquisition of Wackenhut Corrections UK Limited's 50% share in Premier Custodial Group ('Premier'). Serco paid £48.6m for the shares, which represents 90% of their fair market value, as determined by independent valuation.

In the year ended 31 December 2002 Premier's turnover was £127.4m and profit before tax was £10.0m. The net assets employed in Premier at 31 December 2002 were £25.0m, which included non-recourse debt of £179.2m. Serco's share of Premier's gross assets and liabilities is included within the share of joint venture assets and liabilities shown on Serco's balance sheet. The acquisition of Premier will result in 100% of these assets and liabilities being consolidated for the second half of 2003.

Defence
The defence sector, which accounted for 26% of sales this half year, is our longest-established market.

Our largest win was the extension to our management contract at the Atomic Weapons Establishment (AWE), which will now run until 2025 – adding £1bn to the forward order book. With our partners Lockheed Martin and British Nuclear Fuels (BNFL), we will now be able to raise private finance as required to invest in major capital projects that provide environmental and operational improvements and increase efficiency. New facilities will ensure that AWE continues to develop as a world-class facility.

Another important business win was the successful rebid of our site support services contract at the Canadian Forces Base, Goose Bay – the cornerstone of our Canadian operations. The new contract, worth C$36m a year, extends our original five-year contract by a further 11 years and broadens our responsibilities by transferring to us the base's vehicle fleet including snow clearing vehicles and other emergency equipment.

Among a series of contracts and rebids from the UK Ministry of Defence (MOD), we were particularly pleased to win the £60m support services multi-activity contract and multi-engine interim aircraft solution contract at RAF Cranwell. This includes introducing a new training aircraft, the King Air B200, to the RAF: we are leasing seven B200s to the station, which provides initial officer training, aircrew training and all the RAF's multi-engine pilot training. We also extended our support services multi-activity contracts at RAF Brampton, Wyton and Henlow, with contracts worth a total of £18m.

We further broadened our relationship with the Defence Procurement Agency at its Abbey Wood site – one of the largest office complexes in Europe. Abbey Wood provides a good example of organic growth based on strong customer relationships: since starting our original contract there, we have won over £2m of additional work spanning the next five years.

In May we formally signed an interim contract with Paradigm Services Limited to provide Skynet 4 satellite communications network and facilities management services for the UK armed forces. The contract began on 30 May after a seven-month phase-in period, and involved the transfer of these services from the RAF. This contract is a precursor to the main Skynet 5 contract, which we expect to sign in September: this will cover provision of these services for both the Skynet 4 and Skynet 5 communications networks.

In April we completed the phase-in of the communications and information services contract for the Defence Science and Technology Laboratory, to provide support to over 3,500 scientists at 17 locations across the UK. This eight-year partnership contract further enhances our portfolio of IT support contracts in the defence and scientific sectors.

We also broadened our Merlin Avionics Test Systems contract for Lockheed Martin, and successfully rebid our contract to manage the Southern Air Weapons Ranges, worth some £8.6m over five years.

In October we begin transportation and supply services contracts covering United States Air Force Europe operations at five RAF sites. This is a significant step, taking us into a new market area in the UK. The five-year £5.5m contract includes ground passenger transportation, cargo transportation services, vehicle management, vehicle maintenance, personal property, supply support and supply training.

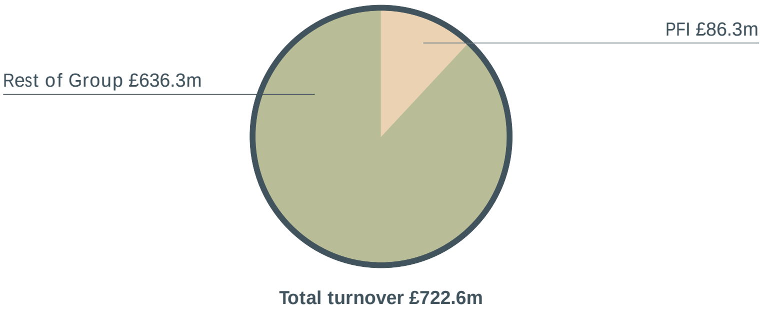
In Germany the Ministry of Defence decided not to outsource training services at the Panzertruppenschule armoured training centre. But we continued to build new defence business with a contract to supply NATO with mobile self-powered IT and communications modules including road trailers.

Transport

The transport sector has been a strong source of growth for us in recent years and now accounts for 27% of our turnover.

Road

In the UK we won a £4.7m contract to support Glasgow's Quality Bus Corridors scheme. We are installing automatic vehicle location, bus fleet management and real time passenger information systems over an 18-month period, and will maintain them for a further five years.



TURNOVER ANALYSIS – TOTAL GROUP

We also successfully rebid a five-year contract to maintain the London Core Traffic Data Collection System for the Department for Transport.

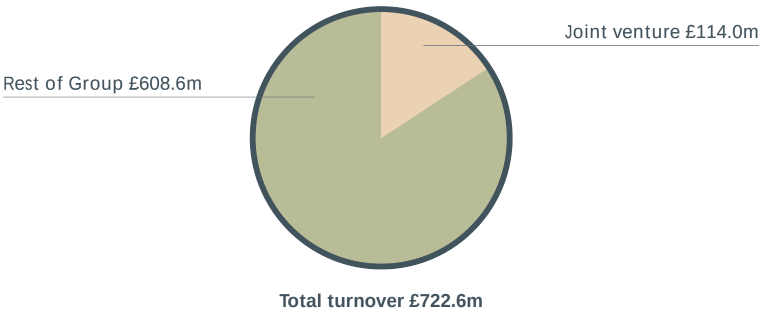
The design, build and implementation stages of the Highways Agency National Traffic Control Centre are nearing completion. The team that will operate the centre is undertaking final system testing and pre-trialling to prove system operation. We have also completed the phase-in of a new contract to provide 24-hour fault repair and maintenance services to the communications equipment on the motorways in southeast England. In San Francisco we completed the installation of over 22,500 ‘smart’ parking meters ahead of schedule.

Rail
Our biggest-ever contract, the £1.8bn, 25-year agreement to operate the Merseyrail Electrics network, began in July. We and our partners, NedRailways, have undertaken to deliver innovative and tangible improvements to the existing service. Merseyrail Electrics is a self-contained railway network in and around Liverpool with 66 stations, 1,000 staff and two dedicated maintenance depots.

In Manchester we acquired 100% of Altram, which operates the Metrolink tramway system, and began a new revenue-sharing arrangement with the local transport authority.

Angel Trains, one of the three UK train leasing companies, awarded us an open-ended contract to dismantle obsolete rolling stock at Shoeburyness. We are one of only two companies in the UK able to provide these services and currently hold two of the three national contracts.

In Denmark the second phase of the Copenhagen Metro added two more stations to the system. For a nominal sum we bought-out our partners in the joint venture which will run and maintain the system for the next five years.



TURNOVER ANALYSIS – TOTAL GROUP

Aviation

We continue to increase our presence in aviation. In the US the Federal Aviation Administration added the 59th tower to our air traffic control contract. The new tower, at Vandenburg Air Force Base, is the first active duty military facility to outsource its air traffic control services.

At the end of the last financial year we teamed-up with a South African partner, Equity Alliance, to acquire 51% of Apron Services from the South African government. Apron Services is a ground handling business operating at the country's six major airports and employing 1,900 staff. The acquisition, part of the government's public private partnership programme, extends our civil aviation activities and provides an opportunity for measured development in South Africa. Our performance improvement programme has already helped our major customer, South African Airways, to achieve record on-time departure rates, and has attracted new customers.

At Dubai International Airport we broadened our aeronautical services contract, adding a further six air traffic controllers and two engineers. The new contract is worth £10.2m over two years.

In the UK the Civil Aviation Authority Safety Regulation Group approved our aviation safety management system (ASMS) – which is only the second ASMS to gain this approval. And we began a new £4.8m four-year contract to manage Newquay Airport in Cornwall.

Civil government

This is our most rapidly evolving market, with opportunities emerging in sectors such as justice, education and healthcare, where outsourcing is relatively new. It now accounts for 28% of sales.

The formation of Serco Government Consulting (SGC) has augmented our capability in this rapidly evolving sector. Its relationships and insights will also help our operating divisions to bid for a wider variety of contracts, including IT-enabled business change work. Since its formation earlier this year, SGC has won and successfully delivered strategic work for a number of central government departments, local authorities and the police. Its capability is expected to double over the next 12 months.

Justice

Since Premier opened Doncaster Prison in June 1994 it has grown to employ 3,500 people. In July we took full control of the business: under the terms of the original joint venture agreement we paid our partner £48.6m for its 50% share, which represented 90% of the independently assessed fair value.

The business continues to grow strongly. In March it won a new eight-year contract to design, build and operate a second immigration centre. The 326-bed Colnbrook centre in Middlesex will begin operations in mid-2004 – bringing our share of total capacity in this market to almost a quarter. Premier has also been awarded a one-year extension to its electronic monitoring contracts in the Midlands & Wales and London & Eastern regions.

One of the benefits of taking full control of Premier is that we now have full responsibility for management performance. Last year the Premier-operated Ashfield Prison and Young Offenders Institution was criticised for some aspects of its management regime and processes. We took prompt action, and the restoration of acceptable standards has been acknowledged in subsequent reports from the Prisons and Probation Ombudsman and a Standards and Security Audit.

Our Enforcement Services team, which provides road safety equipment, won new contracts worth a total of £3.7m with Essex, Lancashire, Cheshire and London Camera Safety Partnerships. The contracts form part of the Government's national initiative on road casualty reduction.

The National Crime Squad formally accepted the ChildBase biometric identification system into service; this marks the successful completion of a complex partnership development programme. Serco is uniquely placed to exploit this technology, which has a very broad range of potential uses.

Education

The contract we hold with Bradford Council for the provision of educational services is now entering its third year. We are implementing its requirements and standards in Bradford schools have risen overall in each of the last two years. Our contract to manage the Walsall Local Education Authority is also making good progress and successfully raising performance standards.

We successfully rebid our one-year school inspections contract with the regulator, Ofsted, increasing the contract size from £3m to £5m. We also successfully re-tendered to provide the National College for School Leadership's head teacher induction programme for England. This three-year contract maintains our prominence in leadership training to schools and Local Education Authorities as well as increasing our access to schools.

CCM Software Services, which provides management information systems and other solutions to schools, colleges and universities internationally, has increased sales ahead of forecast since acquisition in December 2002.

Other public services

Our contract to provide driver examination services in Ontario is currently in its transition phase. We will be providing all driver examination services for Ontario's 12m residents at 92 centres throughout the province and the contract is expected to generate revenue of C$600m. We are paying an upfront fee of C$114m for the concession: up to C$15m will be funded from existing cash resources and the rest from non-recourse debt under a ringfenced facility.

Bolton Borough Council has made us preferred bidder to operate its sports and leisure facilities. The £73.5m turnover, 15-year partnership would involve transferring over 300 staff to Serco. We are also preferred bidder for a similar 15-year, £24m contract to operate Eastbourne's sports and leisure sites.

In April we began an innovative partnership to provide Woking Borough Council's ground maintenance and street cleaning services using area-based multifunctional service teams. The contract features a gain share mechanism to stimulate investment in service enhancements and future projects, and should be worth £25-30m over 10-20 years.

In Australia we won an asset maintenance contract from Melbourne water utility City West Water. Worth over A$8m a year, the contract is for a minimum of three years.

Science

In the science sector, which accounts for 8% of sales, we were an early entrant and have established a strong competitive position.

At Britain's National Physical Laboratory (NPL) we have been building world-class new science facilities under a PFI with Laing Investments Limited, our construction partner. The construction phase is close to completion and we have acquired Laing's 50% share in the joint venture for £0.8m. We are currently rebidding the scientific service provision contract under which we manage NPL itself.

Over the past six months NPL has won a number of UK government contracts including major projects to investigate the characterisation of tissue scaffolds, where NPL will be playing a leading role, and to develop a standard for measuring extremely small forces.

CERN, the European Organisation for Nuclear Research, awarded us a contract to provide electrical, mechanical and electronic support services for its particle accelerator and experimental areas in Switzerland. We are collaborating with two French companies and the value to Serco will be some £7m over five years.

At the European Space Research and Technology Centre (ESTEC) in the Netherlands – where we have been providing support services for over 30 years – we successfully rebid a contract worth over €1m a year to provide site services for up to five years. ESTEC's Earth Observation Projects Department also appointed us in a consortium to provide project engineering, documentation and administrative support services.

At the European Space Operations Centre in Darmstadt, Germany, we successfully rebid the contract we have held for 23 years to maintain and run the operational computing and communications infrastructure; the new contract adds five more years plus a five-year renewal option.

Serco Assurance relocated its two Oxfordshire sites into one new building at Harwell. It won a contract to provide regulatory advice, assessment and inspection support to the MOD's new Nuclear Weapon Regulator; and the MOD also selected it as one of the contractors to develop an integrated sensor management system.

Private sector

Because of the scope available to us in the public sector, this has not been a primary focus for us so far. But it does provide opportunities which we address selectively, and currently accounts for 11% of sales.

In the UK GlaxoSmithKline added a three-year extension to the facilities management contract that we have held at its Ware site since 1995.

In Germany Audi awarded us a five-year contract to train service engineers for its A8 and A3 models. And we won our first facilities management contract in Italy, covering the external areas of Rome's EUR district. This wide-ranging contract includes parks and gardens maintenance and a call centre operation; it has an initial annual value of €1.7m.

In North America the Canada Mortgage and Housing Corporation awarded us a five-year extension to the contract under which we provide document services, project management, customer services, call centre operations and general contract support. East Kentucky Power awarded us a US$1.5m fleet maintenance contract covering 250 light and heavy duty vehicles and equipment.

Telecom New Zealand broadened a long-established relationship by appointing us as property manager for its corporate, mobile and network estates throughout New Zealand under a new three-year NZ$6.9m contract. This is an exciting development, giving us responsibility for managing the company's property assets in line with its strategic business objectives. Successful rebids included a NZ$5.2m facilities maintenance contract with New Zealand Steel, a NZ$4m traffic management contract with Transit NZ and a NZ$1.3m rebid of the contract we have held since 1997 to operate the famous Wellington Cable Car.

Training and development

Serco is committed to investment in training and developing its people throughout their careers.

One of the keys to our sustained growth is the way we identify and develop our managers. In the first half we finalised our comprehensive approach to development at director level and began creating personal plans for all directors worldwide. We are currently establishing a programme to identify managers with high potential and accelerate their development.

In May, 39 people completed the development programme we run in conjunction with the Institute of Directors (IoD), achieving an above-average pass rate in Certificate and Diploma level exams. The link with the IoD enables directors and managers with director potential to obtain accredited qualifications and further develop their capability.

Safety

As a public service business we take health and safety issues very seriously – in relation both to our own employees and to the wider public. This applies especially where we are operating in sensitive environments such as nuclear and defence installations.

So we and our partners at AWE were particularly pleased to win two prestigious categories in the Royal Society for the Prevention of Accidents (RoSPA) and Occupational Health and Safety Awards. AWE won the Defence Industry Sector Award – for the third year running – and the Astor Trophy for the UK's best managed occupational health programme.

Serco Assurance, which operates in the nuclear industry and other sectors where safety and quality are crucial, won RoSPA's Gold Award for Occupational Safety for the second year running. During the first half it also extended its ISO14001:1996 certification, gained the latest ISO9001:2000 certification and was shortlisted for the 2003 Warrington Business Awards for Environmental Training.

Other RoSPA Gold Award winners included Air Surveillance and Control Systems at four sites, Serco Aerospace, Serco Denholm, and Works Service Management at 28 sites. Our team at Fylingdales was highly commended in the defence category.

Lowdham Grange prison, operated by Premier, won the British Safety Council's National Safety Award for 2002.

Independent review report to Serco Group plc

Introduction

We have been instructed by the company to review the financial information for the six months ended 30 June 2003 which comprises the consolidated profit and loss account, the consolidated balance sheet, the consolidated cash flow statement and related notes 1 to 4. We have read the other information contained in the interim report and considered whether it contains any apparent misstatements or material inconsistencies with the financial information.

This report is made solely to the company in accordance with Bulletin 1999/4 issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the company those matters we are required to state to them in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company, for our review work, for this report, or for the conclusions we have formed.

Directors' responsibilities

The interim report, including the financial information contained therein, is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the interim report in accordance with the Listing Rules of the Financial Services Authority which require that the accounting policies and presentation applied to the interim figures are consistent with those applied in preparing the preceding annual accounts except where any changes, and the reasons for them, are disclosed.

Review work performed

We conducted our review in accordance with the guidance contained in Bulletin 1999/4 issued by the Auditing Practices Board for use in the United Kingdom. A review consists principally of making enquiries of group management and applying analytical procedures to the financial information and underlying financial data and, based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit performed in accordance with United Kingdom auditing standards and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the financial information.

Review conclusion

On the basis of our review we are not aware of any material modifications that should be made to the financial information as presented for the six months ended 30 June 2003.

Deloitte & Touche LLP.

Deloitte & Touche LLP
Chartered Accountants
London

3 September 2003

Notes

A review does not provide assurance on the maintenance and integrity of the website, including controls used to achieve this, and in particular on whether any changes may have occurred to the financial information since first published. These matters are the responsibility of the directors but no control procedures can provide absolute assurance in this area. Legislation in the UK governing the preparation and dissemination of financial information differs from legislation in other jurisdictions.

Consolidated Profit & Loss Account

For the six months ended 30 June 2003

	6 months to 30.6.03 £'000 (unaudited)	6 months to 30.6.02 £'000 (unaudited)	Year to 31.12.02 £'000 (audited)
TURNOVER: GROUP AND SHARE OF JOINT VENTURES	**722,551**	625,936	1,325,948
Less: Share of joint ventures	**(113,997)**	(103,895)	(228,670)
Group turnover	**608,554**	522,041	1,097,278
Cost of sales	**(525,376)**	(450,903)	(947,313)
Gross profit	**83,178**	71,138	149,965
Administrative expenses	**(70,556)**	(54,296)	(120,862)
Amortisation of goodwill	**(4,330)**	(3,870)	(8,098)
Exceptional item: Reorganisation costs	**(4,489)**	–	–
Other administrative expenses	**(61,737)**	(50,426)	(112,764)
Operating profit	**12,622**	16,842	29,103
Exceptional item: GSR sale and leaseback	**3,977**	–	–
Share of operating profit in joint ventures	**10,384**	9,589	21,883
Net interest			
Group	**(1,421)**	(2,416)	(4,064)
Share of joint ventures	**1,394**	510	2,019
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	**26,956**	24,525	48,941
Taxation on profit on ordinary activities	**(9,165)**	(8,339)	(16,639)
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION	**17,791**	16,186	32,302
Dividends	**(3,092)**	(3,257)	(9,441)
RETAINED PROFIT	**14,699**	12,929	22,861
Earnings per ordinary share (EPS) of 2p each:			
Basic EPS, after amortisation of goodwill	**4.14p**	3.91p	7.66p
Basic EPS, before amortisation of goodwill	**5.15p**	4.84p	9.58p
Diluted EPS, after amortisation of goodwill	**4.14p**	3.90p	7.63p
Diluted EPS, before amortisation of goodwill	**5.15p**	4.84p	9.54p
Dividend per share	**0.72p**	0.64p	2.08p

Consolidated Balance Sheet

As at 30 June 2003

	As at 30.6.03 £'000 (unaudited)	As at 30.6.02 £'000 (unaudited)	As at 31.12.02 £'000 (audited)
FIXED ASSETS			
Intangible assets	**141,130**	141,570	147,473
Tangible assets	**71,002**	51,379	62,479
Investments in joint ventures	**41,074**	30,650	35,883
Share of gross assets	**267,846**	320,355	317,831
Share of gross liabilities	**(226,772)**	(289,705)	(281,948)
Investment in own shares	**17,766**	18,487	18,207
	270,972	242,086	264,042
CURRENT ASSETS			
Stocks	**37,264**	29,771	38,744
Debtors: Amounts due within one year	**256,597**	210,303	220,042
Debtors: Amounts due after more than one year	**190,358**	84,751	108,932
Cash at bank and in hand	**72,815**	168,685	71,774
	557,034	493,510	439,492
CURRENT LIABILITIES			
Bank loans and overdrafts	**2,190**	108,646	2,386
Trade creditors	**77,755**	68,793	74,377
Other creditors including taxation and social security	**94,707**	74,244	93,843
Accruals and deferred income	**141,976**	119,004	136,766
Proposed dividend	**3,093**	2,831	6,184
	319,721	373,518	313,556
NET CURRENT ASSETS	**237,313**	119,992	125,936
TOTAL ASSETS LESS CURRENT LIABILITIES	**508,285**	362,078	389,978
Creditors: Amounts falling due after more than one year	**182,915**	72,847	87,588
Provisions for liabilities and charges	**36,987**	27,276	34,533
NET ASSETS	**288,383**	261,955	267,857
CAPITAL AND RESERVES			
Called up share capital	**8,697**	8,695	8,697
Share premium account	**190,791**	191,203	190,791
Capital redemption reserve	**143**	143	143
Profit and loss account	**88,752**	61,914	68,226
EQUITY SHAREHOLDERS' FUNDS	**288,383**	261,955	267,857

Consolidated Cash Flow Statement

For the six months ended 30 June 2003

	6 months to 30.6.03 £'000 (unaudited)	6 months to 30.6.02 £'000 (unaudited)	Year to 31.12.02 £'000 (audited)
Operating profit pre exceptional item	**17,111**	16,842	29,103
Exceptional item: Reorganisation costs	**(4,489)**	–	–
Operating profit	**12,622**	16,842	29,103
Depreciation and amortisation of goodwill	**13,671**	11,494	23,632
Movement in working capital	**(10,911)**	(16,652)	(13,124)
One-off pension fund contribution	**–**	(15,500)	(15,500)
NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES BEFORE PFI ASSET EXPENDITURE	**15,382**	(3,816)	24,111
Expenditure on PFI assets in the course of construction	**(13,327)**	(5,063)	(14,950)
Net cash inflow/(outflow) from operating activities after PFI asset expenditure	**2,055**	(8,879)	9,161
Dividends received from joint ventures	**4,602**	6,172	11,095
RETURNS ON INVESTMENT AND SERVICING OF FINANCE			
Interest received	**448**	299	1,223
Interest paid	**(1,869)**	(3,251)	(7,362)
Net cash outflow from returns on investments and servicing of finance	**(1,421)**	(2,952)	(6,139)
TAXATION			
Tax paid	**(3,658)**	(2,468)	(5,738)
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENT			
Purchase of tangible and intangible fixed assets	**(12,499)**	(8,211)	(23,596)
Sale of tangible fixed assets	**4,895**	343	8,125
Exceptional item: GSR sale and leaseback	**5,761**	–	–
Net cashflows with joint ventures	**780**	(1,039)	1,235
Net cash outflow from capital expenditure and financial investment	**(1,063)**	(8,907)	(14,236)
ACQUISITIONS AND DISPOSALS			
Acquisitions	**(829)**	(4,213)	(11,353)
Net cash acquired with acquisitions	**66**	26	397
Subscription for shares in joint ventures	**(4,552)**	–	(370)
Proceeds on disposal of joint ventures	**–**	1,000	1,030
Net cash outflow from acquisitions and disposals	**(5,315)**	(3,187)	(10,296)
EQUITY DIVIDENDS PAID			
Dividends paid	**(6,183)**	(5,536)	(8,283)
Net cash outflow from equity dividends paid	**(6,183)**	(5,536)	(8,283)
Net cash outflow before financing	**(10,983)**	(25,757)	(24,436)
FINANCING			
Issue of Ordinary Share Capital	**–**	117,945	117,929
Debt due within one year:			
(Decrease)/increase in other loans	**(32)**	115	(300)
Debt due beyond one year:	**14,384**	5,270	15,624
Increase/(decrease) in other loans	**734**	(330)	24
Increase in non-recourse debt financing PFI assets	**13,650**	5,600	15,600
Capital element of finance lease repayments	**(2,132)**	(1,699)	(3,594)
Net cash inflow from financing	**12,220**	121,631	129,659
Increase in cash	**1,237**	95,874	105,223
Opening balance	**69,388**	(35,835)	(35,835)
Closing balance	**70,625**	60,039	69,388

1 Basis of preparation

The interim financial statements for the six months ended 30 June 2003 have been prepared in accordance with the accounting policies detailed in the financial statements for the year ended 31 December 2002 and were approved by the directors on 3 September 2003. The accounting information contained in the Interim Report for 2003 does not comprise a full set of accounts within the meaning of Section 240 of the Companies Act 1985 and no full accounts have been filed with the Registrar of Companies. The interim results for both 2002 and 2003 are unaudited, but have been reviewed by the auditors and their report to the company is set out on page 23. The financial information for the full year 2002 is an abridged version of the financial statements for that year, on which the auditors gave an unqualified report and which did not contain statements under section 237(2) or (3) of the Companies Act 1985. The 2002 full year accounts have been delivered to the Registrar of Companies.

2 Earnings per share

The calculation of basic earnings per Ordinary Share after goodwill is based on profits of £17,791,000 for the six months ended 30 June 2003 (2002: £16,186,000) and the weighted average number of 429,640,399 (2002: 414,132,355) Ordinary Shares of 2p each in issue during the period.

The calculation of basic earnings per Ordinary Share before goodwill is based on profits of £22,121,000 for the six months ended 30 June 2003 (2002: £20,056,000) and the weighted average number of 429,640,399 (2002: 414,132,355) Ordinary Shares of 2p each in issue during the period.

The calculation of diluted earnings per Ordinary Share after goodwill is based on profits of £17,791,000 for the six months ended 30 June 2003 (2002: £16,186,000) and the weighted average number of 429,640,399 (2002: 414,798,700) Ordinary Shares of 2p each in issue during the period.

The calculation of diluted earnings per Ordinary Share before goodwill is based on profits of £22,121,000 for the six months ended 30 June 2003 (2002: £20,056,000) and the weighted average number of 429,640,399 (2002: 414,798,700) Ordinary Shares of 2p each in issue during the period.

Notes

For the six months ended 30 June 2003

3 Reconciliation of operating profit to net cash inflow/(outflow) from operating activities

	6 months to 30.6.03 £'000 (unaudited)	6 months to 30.6.02 £'000 (unaudited)	Year to 31.12.02 £'000 (audited)
Operating profit pre exceptional item	**17,111**	16,842	29,103
Exceptional item: Reorganisation costs	**(4,489)**	–	–
Operating profit	**12,622**	16,842	29,103
Depreciation	**9,341**	7,624	15,534
Amortisation of goodwill and intangible fixed assets	**4,330**	3,870	8,098
Profit on sale of tangible fixed assets	**(1,249)**	(136)	(1,948)
Decrease/(increase) in stocks	**1,480**	6,067	(2,906)
(Increase) in debtors	**(9,221)**	(20,701)	(41,870)
(Decrease)/increase in creditors	**(2,900)**	(3,515)	30,795
Increase in provisions	**979**	1,633	2,805
One-off pension fund contribution	**–**	(15,500)	(15,500)
NET CASH INFLOW/(OUTFLOW) FROM OPERATING ACTIVITIES BEFORE PFI ASSET EXPENDITURE	**15,382**	(3,816)	24,111
Expenditure on PFI assets in the course of construction	**(13,327)**	(5,063)	(14,950)
Net cash inflow/(outflow) from operating activities after PFI asset expenditure	**2,055**	(8,879)	9,161

4 Analysis of total net debt

	As at 30.6.03 £'000 (unaudited)	As at 30.6.02 £'000 (unaudited)	As at 31.12.02 £'000 (audited)
Cash at bank and in hand	**72,815**	168,685	71,774
Overdrafts	**(2,190)**	(108,646)	(2,386)
Cash net of overdrafts	**70,625**	60,039	69,388
Other loans due after more than one year	**(48,167)**	(45,312)	(47,433)
Other loans due within one year	**(340)**	(6,562)	(372)
Finance leases	**(21,888)**	(10,976)	(15,291)
Net cash/(recourse debt)	**230**	(2,811)	6,292
Non-recourse debt to fund PFI assets	**(117,828)**	(19,700)	(29,700)
Total net debt	**(117,598)**	(22,511)	(23,408)

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