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Stock Exchange Announcement

5 March 2013

Well placed for future growth following excellent achievements in 2012

Serco Group plc – 2012 results

12 months to 31 December	2012	2011	Change	Change at constant currency
Revenue	£4,913.0m	£4,646.4m	+5.7%	+6.2%
Revenue – ongoing activities*	£4,832.2m	£4,471.8m	+8.1%	+8.5%
Adjusted operating profit	£314.8m	£290.1m	+8.5%	+9.9%
Adjusted operating profit – ongoing activities*	£309.1m	£276.4m	+11.8%	+13.4%
Operating profit	£287.6m	£266.2m	+8.0%	+9.3%
Adjusted profit before tax	£278.1m	£262.2m	+6.1%	+7.3%
Profit before tax**	£302.0m	£238.3m	+26.7%	+27.8%
Adjusted earnings per share	42.55p	39.59p	+7.5%	+8.7%
Earnings per share**	49.94p	35.70p	+39.9%	+41.0%
Dividend per share	10.10p	8.40p	+20%	n/a
Group free cash flow	£181.2m	£168.3m	£12.9m	n/a

* Excludes the financial results of subsidiaries and operations disposed of during the year

** Includes the impact of exceptional items, principally the £51.1m non-cash gain arising from the step acquisition accounting for the DMS joint venture in Australia; full definitions of adjusted measures are provided on page 2 and the income statement is presented on page 29

Record level of contract wins and excellent operational performance

- £5.8bn of awards (2011: £5.1bn); increase in order book to £19.1bn (2011: £17.9bn)
- High revenue visibility (92% for 2013, 79% for 2014 and 70% for 2015)
- Excellent service delivery across existing operations and major new contracts progressing well

Strong financial result for the year

- Total revenue growth of 5.7% to £4.9bn; growth of 6.2% at constant currency
- Organic growth of 3.3%, with excellent performances in AMEAA (up 22%) and Global Services (up 12%)
- Adjusted operating profit growth of 9.9% at constant currency; margin increase from 6.2% to 6.4%
- Adjusted earnings per share growth of 7.5% to 42.55p; growth of 8.7% at constant currency
- Group free cash flow of £181.2m, with an exceptionally strong conversion rate of profits in the second half
- Proposed 2012 total dividend of 10.10p up 20%; increase reflects new policy to accelerate dividend growth on the path to a higher payout ratio

Greater exposure to international growth markets and sectors

- Growth prospects further underpinned by entry into new countries, services and private sector industries
- 31% total revenue growth in AMEAA increases region's exposure to 18% of the Group's portfolio
- 40% total revenue growth in our global Business Process Outsourcing (BPO) business increases non-frontline services to 15% of the Group's portfolio
- These achievements, together with a return to organic growth in the UK, more than offset US challenges

Strategic position further improved through ongoing proactive portfolio management

- Additional capabilities and market access from infill acquisitions such as Vertex and DMS Maritime
- Exits from non-core operations reflect our ongoing focus on strategic fit, performance and returns
- Leading BPO position after full integration of operations and successful launch of Global Services division

Extensive pipeline demonstrates attractive growth opportunities

- Estimated £31bn pipeline reflects growing demand for efficient, high quality and innovative services
- Positive developments opening up more frontline services markets; exciting new opportunities in AMEAA
- Good longer term opportunities in Americas beyond the current tough US federal contracting environment
- Excellent growth prospects in the global BPO market with both private and public sector customers

Confident of further growth and continued resilience of the Group

- Strength of portfolio provides resilience and enhances growth potential
- Group well positioned following excellent strategic and organisational progress in 2012
- For 2013, expect a modest improvement in organic growth and operating margin to be broadly maintained
- Beyond 2013, planning for continued delivery of strong financial performance
- Confidence in outlook and strength of financial position underpin plans for higher dividend payout ratio

Christopher Hyman, Chief Executive of Serco Group plc, said: "Serco improves the quality and efficiency of services that matter to millions of people around the world, helping our customers to focus their precious resources on what they do best. To continue developing our business we are providing more support to our existing customers, offering more to emerging markets and improving our ability to provide more complex services. This has resulted in a strong year for us in 2012 despite some very real challenges; we won more work than ever, we entered new markets, we built more capabilities and we established a global BPO business. Our unique breadth and depth leaves us strongly positioned to meet the growing demand from around the world for our skills and services. This confidence in our business prospects underpins our new dividend policy and commitment to a higher payout ratio over the coming years.

"I am also enormously proud of the achievements of our 120,000 people around the world and with their support, in celebration of our 25th anniversary, we have launched the Serco Foundation to help charities and other organisations make an even bigger impact on some of the world's most critical issues."

Notes:

Ongoing activities excludes the financial results of subsidiaries and operations disposed of during the year, being nuclear consulting services, defence-related German operations, education software and UK data hosting operations.

Adjusted operating profit is before amortisation of intangibles arising on acquisitions, acquisition-related costs and exceptional items (being profits or losses on disposals of subsidiaries and operations, and the one-off payment to establish the charitable foundation), as shown on the face of the Group's consolidated income statement and the accompanying notes. Adjusted profit before tax is also before the exceptional gain arising from the step acquisition accounting for the DMS joint venture in Australia.

Adjusted earnings per share is calculated on the basis of earnings before amortisation of intangibles arising on acquisitions, acquisition-related costs and exceptional items as noted above, together with the tax effect of these adjusting items.

Group free cash flow is free cash flow from subsidiaries and dividends received from joint ventures, and is reconciled to movements in cash and cash equivalents in Section 3 of the Finance Review.

Performance at constant currency has been calculated by translating non-Sterling revenue and earnings for the year to 31 December 2012 into Sterling at the average exchange rates for 2011.

The order book reflects the value of future revenues based on all existing signed contracts. It excludes contracts at the preferred bidder stage and excludes the award of new Indefinite Delivery, Indefinite Quantity (IDIQ) contract vehicles and Multiple Award Contracts (MACs) where Serco are one of a number of companies able to bid for specific task orders issued under the IDIQ or MAC. The value of any task order is recognised within the order book when subsequently won.

The pipeline is the estimated value of all future potential opportunities that are clearly defined and identifiable.

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Presentation

A presentation for investors and analysts will be held at the London Stock Exchange, 10 Paternoster Square, London EC4M 7LS at 9.30am today. The presentation will be webcast live on www.serco.com and subsequently available on demand.

Overview

2012 has been a year of significant progress operationally, financially and strategically. With a record level of contract wins driving £5.8bn of awards in total, our order book has grown to £19.1bn. Revenue and Adjusted operating profit were £4,913m and £314.8m, representing growth at constant currency of 6.2% and 9.9% respectively. The breadth of our portfolio has enabled our strength in the AMEAA region and the successful launch of our Global Services BPO division to offset challenges in the US federal contracting market. We have made further significant strategic progress in positioning our business to deliver strongly for the future. The pipeline of identified opportunities has been replenished to stand now at an estimated £31bn. We remain, therefore, confident of continued resilience in times of dynamic market conditions and of Serco's overall outlook and attractive future growth prospects.

Record level of contract wins and excellent operational performance

In 2012, across our wide portfolio of markets and geographies, we signed a record level of contracts valued at £5.6bn and were appointed preferred bidder for a further £0.2bn. The total £5.8bn of awards compares with £5.1bn in 2011. Our wins included smaller and medium-sized awards which are fundamental to our growth, as well as significant rebids, extensions, expansions and new contracts. Reflecting the substantial level of awards, our order book grew to £19.1bn at 31 December 2012 (£17.9bn at 31 December 2011).

Notable contract awards, along with approximate total value and contract length where appropriate, included:

- Ferry services to the Northern Isles in Scotland (£350m over six years);
- Environmental Services for Wycombe and Chiltern District Councils (£55m over seven years);
- UK asylum applicant accommodation and transport services (£175m over five years);
- Community Payback probation services in London (£38m over four years);
- Delivery of the UK's National Citizen Service (£70m over two years);
- NHS Suffolk community health services (£140m over three years);
- Next pricing period signed for Atomic Weapons Establishment (AWE) management and operation (£1.5bn over five years);
- Leadership for corporate services (DBS) for the UK Ministry of Defence (£36m over four years);
- US Army base closure support in Afghanistan (US$57m over three years);
- US Navy Automated Digital Network Systems engineering (US$68m over five years);
- San Francisco parking services (US$43m over five years);
- US MRAP military vehicle equipment and system upgrades (US$73m over fifteen months);
- Wiri Prison 25-year operating contract in New Zealand (approximately £15m a year from 2015);
- Wandoo Reintegration Facility in Western Australia (A$50m over five years);
- Bus operations in city of Indore, India (£13m over six years);
- Australian Tax Office contact centre services (£90m over five years);
- Major BPO contract with leading UK retailer Shop Direct Group (£430m over ten years);
- Contact and support services for AEGON UK (£170m over ten years); and
- Anglia Support Partnership shared services operation for UK health sector (£120m over four years).

More details of these and other contract awards can be found in the Operating Review, with further information and other smaller and medium-sized contract awards during the year described in the contract news updates and other announcements available on our website www.serco.com.

Visibility of future earnings remains high due to the signed contracts that make up our order book, contracts that we expect to extend and rebid, and contracts at the preferred bidder stage which we expect to sign. At 31 December 2012, revenue visibility was 92% for 2013, 79% for 2014 and 70% for 2015.

Across the Group we have maintained excellent service delivery. We were particularly proud of our achievements through the 2012 Olympic Games, where a number of our contracts were heavily involved. We carried record passenger numbers whilst maintaining exceptional service metrics on our transport-related services, most notably the Docklands Light Railway, where volumes were substantially ahead of forecasts and there were half a million passengers on the busiest day. We have also been delighted with service standards through the mobilisation and transition phases for major new contracts that commenced across our home affairs, transport, health and BPO operations.

Strong financial result for the year

Serco has delivered growth in revenues including further good organic growth, increased the operating margin, and maintained a strong cash generation profile and financing position.

Reported Group revenues were £4,913.0m, representing total growth of 5.7%. Excluding operations disposed of during the year, revenues from ongoing activities were £4,832.2m, with growth at constant currency of 8.5%. Within this, organic growth was 3.3% and the contribution from acquisitions added 5.2%.

Good organic growth, for the Group as a whole, demonstrated the resilience of the portfolio and our successful development in new markets and geographies. There was further very strong revenue growth in AMEAA - up 22% organically. Global Services, our newly created BPO division, saw organic growth of 12%, with underlying growth of over 30% after adjusting for the transfer back of the Bradford education contract and the government funding cuts to our previous work for the UK Regional Development Agencies. Our UK & Europe frontline services division, supported by new contract wins, saw a return to organic revenue growth of 2%. Growth in these three divisions more than offset the 14% decline in organic revenues for the Americas division that resulted from the challenging conditions of the US federal outsourcing market. Our divisional performance is described fully in the Operating Review.

Adjusted operating profit increased 8.5% to £314.8m. Excluding operations disposed of during the year, Adjusted operating profit from ongoing activities was £309.1m, representing growth at constant currency of 13.4% and an increase in the operating margin to 6.4%. Net finance costs were £8.8m higher, principally reflecting the incremental cost of funding acquisitions. Adjusted profit before tax of £278.1m and Adjusted earnings per share of 42.55p grew at constant currency by 7.3% and 8.7% respectively.

Following successful portfolio management activity, there was a £5.6m net exceptional profit on disposals of subsidiaries and operations in the year. This, together with the £5.0m one-off payment to establish the charitable foundation, is excluded from Adjusted operating profit. There was also an exceptional gain of £51.1m arising from the step acquisition accounting for the DMS joint venture in Australia. This significantly enhances reported profit before tax and earnings per share, but has been excluded from our measures of adjusted financial performance in order to aid comparability.

Group free cash flow was £181.2m compared with £168.3m in 2011. There was an exceptionally strong conversion rate of profits in the second half of the year, and dividend distributions from joint ventures were £16.3m higher. After the effect of acquisitions and disposals, the payment of dividends and other financing movements, total net debt reduced by £53m to £581m as at 31 December 2012.

Our dividend policy in the past has been to increase the total dividend each year broadly in line with the increase in underlying earnings. Reflecting this, in 2011 we increased the total dividend by 14% to 8.40p, which based on 39.59p of Adjusted earnings per share represented a payout of 21% and dividend cover of 4.7 times.

The Board is confident in the future growth prospects for the Group and of the strong financial position that we have. We therefore intend progressively to increase the payout ratio and thereby reduce our dividend cover over the next three years. Beyond that point, we anticipate a policy of maintaining dividend cover of between 2.5 and 3 times and therefore reverting to increasing the total dividend each year broadly in line with the increase in underlying earnings. The Board has proposed a final dividend for 2012 of 7.45p per share, bringing the total dividend for the year to 10.10p, up 20% compared with the previous year. This represents a payout of 24% based on 42.55p of Adjusted earnings per share, or dividend cover of 4.2 times. The final dividend will be paid, subject to shareholder approval, on 22 May 2013 to shareholders on the register on 15 March 2013.

Earnings, cash flow, financing and related matters are described fully in the Finance Review.

Greater exposure to international growth markets and sectors

Governments and companies face an increasing need to improve the quality of services to their citizens or customers whilst contending with constrained or reducing budgets. Competition and outsourcing offers a solution to this need, where: deep operational expertise can assure delivery; a breadth of knowledge and experience can bring fresh thinking; and a mixture of front, middle and back office expertise can enable transformation. We are already a leading player in our core markets of defence, transport, justice and health in the public sectors, and financial services, retail, travel and telecoms in the private sector, benefitting from the growth in these markets. Our strategy is to widen our exposure to emerging markets, where superior growth and margins can be achieved; and to deepen our transformational expertise to access larger, more complex and higher margin growth opportunities across our core markets.

Our achievements in 2012 supported this strategy, driven in particular by excellent performances in our AMEAA and BPO operations. Our AMEAA region grew total revenue by 31%, increasing to 18% the region's share of the Group's portfolio. Meanwhile our Global Services BPO business saw 40% total revenue growth, driven by the combination of the contribution from acquisitions and a series of very strong contract wins. Both the AMEAA region and our BPO operations are expected to account for an increasing proportion of the Group's revenue mix.

The excellent performances in the AMEAA and Global Services divisions, together with a return to organic growth in the UK, more than offset the performance of our Americas division. This has been impacted by extremely tough conditions for the US federal contracting market, due to the political challenges of the annual budgeting process and reaching agreement on future government funding.

As described in our Operating Review, 2012 has seen greater exposure to growth markets following entry into new countries in the Middle East as well as new frontline services in India, the provision of new service lines such as community healthcare, and breaking into new private sector industries such as the UK Life and Pensions segment of the financial services market. We also set out for each of our divisions areas of future growth opportunity, which we expect to pursue in 2013 and beyond.

Strategic position further improved through ongoing proactive portfolio management

As part of widening our exposure to emerging markets and deepening our transformational expertise, the launch of our Global Services division in 2012 has been key, adding significant capability in the fast growing, higher margin BPO market. The acquisition of Intelenet in 2011 was strategically important for Serco's development, as were other smaller infill acquisitions such as The Listening Company in the UK and Excelior in Australia. These acquisitions added specific customer contact capabilities and geographic reach. During 2012 these have been fully integrated with Serco's own BPO operations, while the acquisition of Vertex's UK public sector BPO operations has provided additional expertise and strategic partnerships. The success of bringing together our BPO skills and scale in one global division has been reflected in contract awards in the year totalling over £1bn and with Serco being recognised in independent studies and awards as a new leading force in the BPO industry.

Another acquisition in the year was our purchase of the remaining 50% stake in DMS Maritime from our joint venture partner. This strengthens Serco's position as a leading defence services provider in Australia and in the growing marine services market. While remaining primarily focused on organic growth, Serco will continue to look at potential acquisitions that similarly bring new skills, capabilities or market access.

Our proactive portfolio management also involves an ongoing assessment of our existing operations for strategic fit, together with expected future levels of performance and returns. As part of this, Serco made four disposals of operations that were non-core to the future development of the Group. These were: our Technical Services business which provided consulting and project solutions to the UK civil and nuclear defence markets; the majority of our mainly defence-related operations in Germany; our education software business; and our UK data hosting operations. We will continue to serve the energy, defence, education and IT-enabled BPO markets in other ways, but will focus on our long-term contract model to develop the best opportunities and a balanced portfolio.

The successful Group reorganisation has also enhanced our strategic positioning. Creating the new BPO division as our first global business brought together all of Serco's middle and back office skills and capabilities, improving the services we provide to customers and enabling better targeting of opportunities around the world in both the private and public sectors. The reorganisation has also created a single UK & Europe division, supporting better customer relationship management and service development, as well as increased internal efficiencies. For example, since July 2012, the Global Services division has been operating an internal shared service centre for the Group. These organisational changes, which led to headcount reductions in management and our own back office support functions, have generated in-year savings to cover the associated costs.

Extensive pipeline demonstrates attractive growth opportunities

A significant number of opportunities were successfully converted to contract awards in 2012. Newly identified prospects across our portfolio have increased the pipeline value to an estimated £31bn. This increase reflects an ongoing demand for efficient, high quality and innovative service provision from public and private sector customers around the world.

There is a strong pipeline in AMEAA, with many exciting new opportunities such as those in the growing health markets in the region and in the justice sector. There also remain substantial prospects in: defence support, engineering and marine services; transportation markets including light rail, road networks and air traffic control; and integrated facilities management services to support major infrastructure projects in the region.

In the UK, markets continue to show stabilisation and increasing signs of improvement. There are further indications of new markets opening up, supported by the agenda for public service reform. New opportunities include those driven by the growth in commissioning of health services, defence organisation strategic partnerships and from competition being introduced to numerous areas of the home affairs market such as offender rehabilitation.

While the US is expected to remain very challenging in the short term, due to government budget and funding issues, we continue to develop our business and expect to secure new areas of work in defence technology and engineering, logistics and programme support and human capital management. Other civilian markets such as transport and health will be actively pursued. We therefore see good longer term opportunities in the US, as well as strong potential to develop our presence in the wider Americas region.

There are strong growth prospects in the global BPO market as well. Following significant recent wins in the private sector, further prospects are being pursued across a number of vertical markets including life and pensions, telecom, retail, travel and utilities. There are also opportunities in the UK public sector, including more strategic partnerships with local authorities to transform their services, and prospects for future central government shared service centres continue to develop.

Confident of further growth and continued resilience

Serco's portfolio breadth across different markets and economies continues to provide resilience while at the same time enhancing our growth potential. For example, whilst conditions remain very difficult and uncertain for the US federal outsourcing market, we anticipate further improvement in UK markets and strong performances from our AMEAA and Global Services BPO operations. The strategic and organisational activity in 2012 has also positioned the Group well for future growth.

For 2013, we are forecasting a modest improvement in the rate of organic revenue growth. The effect of acquisitions and disposals to date is likely to have a broadly neutral impact on total revenue growth. We are forecasting our Adjusted operating margin to be broadly maintained at the level achieved in 2012.

Net finance costs are anticipated to be approximately £45-50m including the impact from the forthcoming revision to IAS 19; this would represent a slight increase on the equivalent 2012 restated net finance cost. Reflecting anticipated further incremental working capital investment supporting BPO growth, together with lower dividends from joint ventures, free cash flow in 2013 may be lower than the level achieved in 2012.

Beyond 2013, we are planning for continued delivery of strong financial performance at Serco. Our confidence in continued resilience, the overall outlook and future growth prospects for the Group have also been reflected in our plans to increase the proportion of our profits paid as dividends to our shareholders.

Serco Foundation established

To mark Serco's 25th year as a publicly traded company dedicated to service excellence, we have established the Serco Foundation as an independent charitable foundation with a one-off endowment of £5m. The foundation will build partnerships with large charities to make donations and also support them in the delivery of their programmes through the application of Serco's people, skills and capabilities.

Operating Review and Growth Opportunities

This section is presented according to the four divisions based around our principal markets:

- UK & Europe,
- Americas,
- AMEAA (Australasia, Middle East, Asia and Africa), and
- Global Services.

The section outlines contract awards which are significant because of their value or their strategic contribution to our business. Further details of these, as well as other medium and smaller-sized contracts, can be found on our website www.serco.com.

UK & Europe – operating review

The UK & Europe division includes our frontline services in: Home Affairs (encompassing justice-related operations, immigration and border security, and welfare); Health; Transport and Local Direct Services; and Defence & Science.

Revenue from ongoing activities grew by 2% to £2,494m (2011: £2,434m), and represented 51% of Group ongoing revenue (2011: 55%). On an organic basis, revenue also grew by 2%. Adjusted operating profit from ongoing operations grew by 5% to £172.9m (2011: £165.0m), with the margin increasing to 6.9% (2011: 6.8%). Including the impact of disposals, reported revenue declined by 1% to £2,561m (2011: £2,595m) and Adjusted operating profit was broadly unchanged at £177.8m (2011: £177.6m).

The return to organic revenue growth, after a marginal decline in 2011, reflected the start of numerous new contracts that also reinforce our view of an improving outlook. This more than offset the impact of Serco operating fewer contracts in the welfare to work market and ongoing government austerity which places pressure on areas of more discretionary-related spend with Serco. The margin performance reflected the delivery of operational improvements, largely offset by the effect of the start of new contracts particularly in the second half of the year. The creation of a single UK & Europe division has involved significant organisational change during 2012, both to increase our own efficiency and, crucially, also to support the delivery of better services for our customers. In 2013 there will be further activity to drive operational improvements and efficiencies.

Home Affairs

Our operations across the Home Affairs market account for approximately 20% of UK & Europe revenues.

HMP Thameside, the new prison at Belmarsh West in London, became operational in 2012. As one of the most technologically advanced prisons in the world, it has, for example, advanced CCTV digital recording and monitoring, the latest drug and contrabands intervention equipment, biometric key vending for staff, and in-cell IT for prisoner education and administration. Currently HMP Thameside is a local Category B establishment with an operational capacity of 900 convicted and remand male prisoners, and the Ministry of Justice has recently announced that it will be expanded with the building of a new houseblock.

In the probation services market, which is expected to see substantial future development with the introduction of competition to improve services and efficiencies, Serco has been awarded the first UK contract. In partnership with the London Probation Trust, Serco is operating Community Payback which requires offenders to undertake unpaid work for the community. The partnership is providing an integrated service to manage the approximate 15,000 offenders who receive non-custodial sentences in London every year. The four-year contract is valued in total at £38m, with this delivering savings to the taxpayer of over 30%.

Our Payment by Results pilot at HMP & YOI Doncaster is also showing that it has real potential to reduce re-offending. Typical of the many innovative interventions in place are the Families First Programme, which supports prisoners' relationships with their partners and children, and Second Shot Productions, which teaches technical and creative skills in filming and graphic design. Both of these programmes won prestigious Butler Trust Awards in 2012.

For the UK Border Agency (UKBA), Serco commenced the delivery of the COMPASS project, providing accommodation, transport and associated services for asylum applicants in the northwest of England and in Scotland and Northern Ireland. Full Permit to Operate in both regions was awarded at the end of 2012 and Serco is now managing over 6,000 service users across 2,800 properties.

In the welfare to work market, our Work Programme performance continues to rank Serco as one of the leading performers in securing successful job outcomes from the referrals made to our services. Reflecting our approach and performance in this market, Serco's consortium was awarded a contract to deliver the National Citizen Service across six regions in the UK. Expanding our experience of working in partnership with the voluntary sector, Serco in association with National Youth Agency, UK Youth, Catch 22 and vInspired will offer 16 and 17-year olds from different backgrounds a six-week programme to develop life skills through community activities working with charitable organisations and business leaders. The estimated combined total value of the contracts over the initial two-year period is approximately £70m.

Health

Our operations across Health account for approximately 10% of UK & Europe revenues.

A number of significant new health contracts began during 2012. For the NHS in Suffolk, Serco commenced operations in October to provide a wide range of community health services. These include community nursing, specialist nursing, management and operation of community hospitals, speech and language therapy, specialist children's services and community equipment services. Serco is working with a range of NHS and third sector partners to create a unique model of integrated service delivery. The three-year contract has a total value of approximately £140m.

In integrated facilities management (FM) services for the health market, Serco began a new contract for the East Kent Hospitals University NHS Foundation Trust, delivering services to three acute hospitals, two community hospitals and several small clinics in the area. The contract has a total value of approximately £140m over a maximum ten-year period. For equivalent services at Forth Valley hospital where Serco has implemented a number of innovative technological solutions, we received the highest level of recognition in the 2012 Global FM Awards for Excellence in Facilities Management.

Elsewhere, we continue to transform the services at Braintree Community Hospital for which Serco became responsible in 2011, and our GSTS pathology joint venture is delivering the necessary efficiency improvements as it modernises services.

Transport & Local Direct Services

Our operations across Transport and Local Direct Services account for approximately 40% of UK & Europe revenues.

Our London transport contracts - comprising the Docklands Light Railway (DLR), the Barclays Cycle Hire scheme and traffic management operations - have all achieved excellent operational performance during the year. Serco continues to support growth in regular journeys as well as annual events such as the London marathon, and successfully executed the significant additional workload involved in the Diamond Jubilee and the 2012 Olympic Games. The DLR in particular was a key part of the London 2012 Games transport network, with the Stratford International Extension, opened last summer, adding four new stations and connecting five Games venues. According to Transport for London and the Olympic Delivery Authority, during the period of the Olympic Games, the DLR carried 7.2 million passengers - up by over 100 per cent on normal levels. On the busiest day, the DLR carried a record-breaking 500,000 people. Serco was named 'Light Rail Operator of the Year' in 2012 and since the year-end our DLR contract has been extended to September 2014. In July, Barclay's Cycle Hire rentals exceeded one million for the first time in any month.

Our other UK rail franchises in Northern Rail and Merseyrail are also supporting growth in passenger numbers and continued strong operational metrics. At Northern Rail, our performance has led to a further extension of the contract through to 1 April 2014.

In July, Serco began operating a new contract for lifeline freight and passenger ferry services to the Northern Isles in Scotland, building on our experience of managing and transforming other critical local transport services such as Northern Rail and Scatsta Airport on the Shetland Islands. Serco also has extensive operations in the international marine market including services for the Royal Navy through which it operates more ships under the UK flag than any other company. The new six-year contract has a total value of approximately £350m.

In direct services for local authorities, a number of contracts were awarded during the year. In April, Serco began providing refuse and recycling services for 127,000 households in the London Borough of Wandsworth, helping the council to meet Government recycling targets and reduce costs such as landfill taxes. The contract is valued at £44m over eight years. Serco has been appointed to operate a new joint environmental services contract for Wycombe and Chiltern District Councils. The integrated services include household waste, recycling collections and street cleansing, with the joint contract targeting operational efficiencies whilst increasing recycling rates across both districts. The initial seven-year contract is valued at approximately £55m. Serco has also successfully rebid its waste and recycling services contract and its landscapes and grounds maintenance services contract for Canterbury City Council. In our provision of a comprehensive and high quality range of health, leisure, fitness, wellbeing and community-focused services, Serco secured new contracts with North Down Borough Council, Mansfield District Council and Shropshire Council.

Defence & Science

Our operations across Defence and Science account for approximately 30% of UK & Europe revenues.

Our management and operation of the Atomic Weapons Establishment (AWE), as part of a joint venture with Lockheed Martin and Jacobs Engineering, has been achieving excellent results. The contract is delivering value for money for the Ministry of Defence (MOD) whilst achieving excellent performance in the quality and timeliness of our programme delivery. In recognition of this, arrangements for the next pricing period through to 31 March 2018 were successfully concluded. The next five-year period will see Serco's share of revenue expected to remain on average at approximately £300m a year, although under the back-end weighted agreed incentivisation arrangements, the earnings and margin rate in the initial years will be similar to those achieved in the initial years of the current pricing period.

In April 2012 Serco began operating a new contract for the MOD to provide training and support to the British Army prior to deployment on operations overseas. Known as the Contemporary Operating Environment Force (COEFOR), and awarded by Army Headquarters, critical pre-deployment training includes language, cultural and operational environment skills, and the creation of realistic training conditions to prepare UK military forces for operations in Afghanistan and other theatres of operation around the world. The contract runs to December 2014, including an option year, and has a total value of approximately £55m.

Our defence multi-activity contracts at RAF Northolt and RAF Brize Norton were expanded in the year. Additional services include IT, vehicle maintenance, expanded aircraft handling and the maintenance of two aircraft operating out of the Middle East using Sponsored Reserves. We successfully rebid our multi-activity contract at RAF Cranwell, home to the Royal Air Force College which selects and trains all new officers and aircrew and where we support 3,000 simulator hours and 5,500 flying hours per year. The combined total value of the expansions and rebid, which have two to three-year terms, is approximately £30m. A new contract for RAF Valley, supporting their crucial role in training fast jet pilots for both the RAF and the Royal Navy, also became operational in the year.

For Defence Business Services (DBS), Serco was awarded a contract to provide an executive leadership team. DBS provides corporate services for the MOD such as civilian human resources, finance, information and security vetting. Serco is working with DBS staff to transform the organisation into a lean and effective shared services centre, building on private sector best practice. The contract is valued at around £36m over its initial four-year duration.

At the National Physical Laboratory (NPL), which has been managed and operated by Serco since 1995, the Centre for Carbon Measurement was launched, ensuring the UK is a leading force in climate modelling, global carbon markets and green technology. Business and government welcomed the project, highlighting its potential to reduce emissions and stimulate the economy. The government has, however, announced that our current 10-year contract (with an original value totalling approximately £500m) will not be extended beyond March 2014, as they will look instead at alternative structures for operation, investment and ownership of the facilities. Serco is proud of its record at NPL and its contribution to its development over the past 17 years.

Serco is overseeing and delivering the Defence Science & Technology Laboratory's (Dstl) Helios programme, which will see the relocation of all of Dstl's activities from Fort Halstead to Porton Down and Portsdown West. The programme will help to support Dstl's future strategic goals, protect their capabilities and provide additional cost benefits, building on an already strong Total Facilities Management (TFM) partnership between Serco and Dstl.

UK & Europe – growth opportunities

The UK, which accounts for the vast majority of the division's operations, shows signs of increasing activity and good growth potential. Competitive outsourcing supports the UK Government's aim of achieving savings while improving services and social outcomes. The reform of public services provision is an ongoing process, but the Cabinet Office and spending departments appear increasingly focused on bringing new opportunities to market.

The 2012 reorganisation into a single division places Serco in a better position to target future growth opportunities across the wider public sector, including where customers are looking for more end-to-end services that combine frontline capability with middle and back office operations. In such instances, the UK & Europe division, as the relationship lead, will draw upon the skills and capabilities of the new Global Services division to deliver fully integrated services. We continue to strengthen our brand and account relationships at all levels, including central government, devolved authorities in Scotland and London, in local government and in public service frontline organisations such as the police and NHS.

Home Affairs

As part of opening up to competition existing public sector prison operations, Serco was short-listed for two groups consisting of five prisons in total. This is in excess of the maximum of four prisons that can be won under the competition structure. Serco is therefore pleased to be proceeding to the next stage as the single remaining bidder for the South Yorkshire group, comprising three HM Prisons (Moorland, Hatfield and Lindholme), and looks forward to further developing its bid to produce the compelling package of reforms for delivering cost reduction, improvements to regimes and a working prisons model in these prisons. Serco is also working with its customer to expand HMP Thameside, adding capacity under Serco's more modern and efficient design.

The Ministry of Justice is proposing to open up ancillary and 'through-the-gate' resettlement services across the whole public sector prison estate by spring 2015, rather than further prison-by-prison competitions. This includes recommendations to transform offender rehabilitation, opening up the approximate £600m per annum probation market to competition and rapidly expanding the payment by results approach to improve rehabilitation outcomes. This is expected to provide significant opportunities for Serco.

The growing use of court fines is also expected to generate opportunities for our collection services business, as well as a larger opportunity for the overarching management of compliance and enforcement that would draw upon skills and capabilities from within the Global Services division. Serco is currently in the process of rebidding its electronic monitoring contracts in England and Wales with preferred bidder appointments expected later in 2013.

Health

The UK health market is being driven by the impact of fiscal pressure and the proposed structural reforms which require increased introduction of competitive forces. In clinical services, we are developing opportunities to operate both hospital and community-based services. For example, our new innovation partnership with South Warwickshire Foundation Trust will seek to use the expertise and skills of both organisations to improve the care delivered to patients, whilst delivering best value. This partnership approach will enable the Trust to deliver benefits more quickly to patients, building on existing arrangements such as the Anglia Support Partnership. Initial discussions between the organisations started following a shared vision and interest in working with George Eliot NHS Hospital Trust on their plans for the future.

Our frontline health services business has already had success in working closely with the Anglia Support Partnership shared services operations, led by the Global Services division. This has seen growth by providing additional occupational health and counselling services and a separate clinical strategic procurement contract. Further growth through this strategic partnership framework is being pursued.

The Department of Health currently spends £12bn per annum on community-based services, and this is anticipated to grow given the changing nature of care and patient demographics. The Department's national 'Transforming Community Services' guidance stipulates that all primary care trusts will no longer directly provide community services and will instead commission them. Serco therefore anticipates building on its Suffolk contract award.

There is a growing market for enabling services – both in the UK and elsewhere around the world – that combine facilities management, support services and patient administration to improve service quality and productivity in hospitals and other health establishments.

At our GSTS pathology joint venture, the management team has been further strengthened in the year with the appointment of an independent Chairman. This role is integral in helping GSTS take forward its strategy for modernising NHS pathology and implementing its plans to deliver growth of the business. GSTS has recently been successful in bidding to provide pathology services to the NHS Midlands & East Strategic Health Authority cluster.

Transport and Local Direct Services

Serco's excellent credentials in transportation systems will support selecting future growth opportunities in the UK and other countries. For example, Serco has signed a cooperation agreement with Strömma Tourism & Maritime to make a joint bid to manage and operate the ferry services in Stockholm's archipelago and harbour from 2014. As well as transferring skills and capabilities to new markets, we are pursuing further existing contract expansion as has been demonstrated in our support of the growth of the Barclays Cycle Hire scheme in London. We will also be progressing with the rebid processes for our DLR contract which runs to 14 September 2014 and our Northern Rail contract with runs to 1 April 2014, while other potential opportunities may emerge as part of governments' future structuring of transport networks and services.

In local government frontline services, growth in environmental services and other areas of integrated facilities management such as leisure services are expected to emerge. Reductions in funding and increased service demands from citizens are driving more interest in strategic partnering, service sharing and personalisation of services.

Defence & Science

The defence market is expected to develop further opportunities for support in areas such as infrastructure management, business process and whole enterprise outsourcing, and technical and engineering services. Serco will also seek similar opportunities in the science market and emerging markets for energy management.

Developing from Serco's operation of Defence Business Services and supported by the skills and capabilities of the Global Services division, we will be pursuing opportunities for strategic partnerships such as the Defence Infrastructure Organisation (DIO). The DIO is responsible for managing and maintaining land and property for the MOD in the UK and abroad, with the potential for further efficiencies to be achieved across its operations. A similar opportunity is for the Defence Equipment & Support division (DE&S), which is currently going through further review as to how a competitive process could be run.

Serco has formed a partnership with two other leading nuclear companies, CH2M HILL and AREVA, to participate in the Nuclear Decommissioning Authority's competition to oversee management of decommissioning activities at 12 UK nuclear sites. The CAS Restoration Partnership brings together the unparalleled UK and international expertise of its three partners across nuclear operations, site management, decommissioning, and waste management.

Serco has successfully expanded the scope of existing contract relationships to broaden its services. For example, within the scope of the original Dstl contract, options can be exercised for additional Target Services and in 2012 Serco added the provision of an end-to-end procurement service for laboratory assets across Dstl's three core sites. Serco will pursue further contract expansions in the future to continue driving additional value for our defence and science customers.

Americas – operating review

Our Americas segment provides professional, technology and management services focused primarily on the US federal government including every branch of the military, a broad range of civilian agencies and the National Intelligence community. We also provide services to the Canadian government, selected US state governments and municipal governments.

Revenue on a constant currency as well as on an organic basis declined by 14%. Revenue on a reported currency basis, given the marginal strengthening of the US dollar, fell by 13% to £753m (2011: £868m) and represented 16% of Group ongoing revenue (2011: 19%). Adjusted operating profit reduced by 24% on a reported currency basis to £55.2m (2011: £73.0m), with the margin decreasing to 7.3% (2011: 8.4%).

The US federal contracting market has remained very difficult. The decline in revenues reflects challenges that have faced the US Government's fiscal 2012 and 2013 annual federal budgeting processes, with a series of Continuing Resolutions again being necessary due to political difficulties in reaching agreement on budget funding. Both the Department of Defense and civilian agencies have been facing cuts, with the threat of these being on an automatic basis via a mechanism known as 'sequestration'. These factors have severely disrupted the industry, with government agencies further postponing contract award announcements, delaying work under existing contracts and cancelling or reducing the scope of many contracts and task orders. The Bureau of Economic Analysis reported that, with the threat of sequestration looming, in the final quarter of 2012 Federal government's defence spending was down 22%, the biggest reduction for 40 years. Further pressures have included an increase in 'small business set asides' in Serco's served markets that restrict our ability to be prime contractor in some cases, and the federal government shifting to awarding primarily on a methodology of 'Lowest Price Technically Acceptable' rather than 'Best Value'.

Significant cost reduction was undertaken in 2011, allowing margins to be held at the time. Whilst cost actions have continued, the challenging market conditions have led inevitably to lower margins in 2012, with this likely to continue while the difficult and uncertain environment persists.

Whilst revenues have reduced due the market conditions, new task orders, contract awards and rebids do continue to be secured in numerous areas that are less affected by the general budgetary challenges.

Serco's US Army Career Alumni Program (ACAP) contract secured two expansions during the year. ACAP services include transition and employment assistance counselling for military personnel at 54 ACAP locations across the United States, Korea, Italy, Kuwait and Germany. Under the program, Serco has served more than 2.3 million active personnel, their families, and members of the Guard and Reserves for over two decades, with this now expanding to extend support to Guard and Reserve members who are not able to visit an ACAP Center for services. Serco's second expansion includes the addition of financial planning counsellors at ACAP centres around the world. The two expansions over the two remaining option years are valued in total at US$54m.

In the area of mission critical logistical support services, Serco began a new contract valued in total at US$57m over a maximum three years. This supports the United States Forces Afghanistan (USFOR-A) base closure and transition initiative through the coordination of logistics and deconstruction of bases throughout Afghanistan. Similar to the services we provided in Iraq, Serco's Base Closure Assistance Teams (BCATs) are assisting military units with the key aspects of redeployment. Serco also provides logistics expertise to the US Army under the Logistics Civil Augmentation Program (LOGCAP), where we provide programme management, cost analysis, logistics planning and administrative services around the world in support of the United States and allied forces during operations. Additional task orders awarded in the year were valued in total at US$12m.

Also for the US Army, we have been awarded a new contract for a full range of technical support services to assist in forecasts that reflect the changes in the political and military climate. The contract has a total value of US$9m over a maximum five years. Under an IDIQ vehicle with the US Navy, Serco has been awarded a US$11m task order for similar work to provide forecasting models to support Navy personnel readiness. Under the same IDIQ, a further US$4m task order has been awarded to provide counsellors in support of wounded Sailors and Coast Guardsmen.

Serco was awarded a new production and engineering services contract for the US Navy to support Automated Digital Network Systems (ADNS). Serco will perform hardware integration and testing to deliver the Navy's newest ADNS configuration on shore, ships and submarines. The contract has a total value of US$68m over a maximum five years.

Serco was awarded a new contract to upgrade Command, Control, Communications, Computers, Intelligence, Technology, Surveillance and Reconnaissance (C4ITSR) equipment and systems on Mine Resistant Ambush Protected (MRAP) vehicles for the US Air Force, US Army, US Marine Corp and US Navy. The installation is being carried out on-site in Afghanistan, Kuwait and Qatar, enabling immediate deployment with Serco also providing in-country maintenance support services. The fifteen-month contract, awarded under the Sea Enterprise IDIQ contract vehicle, has a nine-month base period and a six-month option period with a total value of US$73m. Serco provided additional services under this IDIQ contract vehicle to the US Navy's Space and Naval Warfare Systems Command (SPAWAR), with task orders awarded in the year valued at US$19m.

Serco provides a range of other mission-critical engineering and IT services to the Department of Defence under the C4ITSR contract vehicle. These services include engineering, systems integration, hardware procurement, software development, technical support, installation testing operations and maintenance. Additional task orders awarded in the year were valued in total at US$59m. During the period Serco was also officially granted ISO/IEC 20000 certification which measures our approach and capability in delivering world-class IT managed services.

Serco also secured important rebids and extensions for defense and security customers. Serco signed a one-year extension valued at approximately US$100m for its contract with a US intelligence agency, where we provide IT architecture, systems and systems engineering, financial management and procurement support, risk management performance assessment and reporting. Our contract to support undersea surveillance for the US Navy was successfully rebid at a total value of US$19m over a maximum five years.

Beyond our defense and security work, Serco has also rebid and extended other important relationships. For the San Francisco Municipal Transportation Agency, under a five-year US$43m contract Serco will continue to provide a range of parking related services, infrastructure and systems support including deploying GPS vehicle tracking technology. For Seminole County Florida, Serco has rebid its management and maintenance services contract for a 2,200 vehicle and equipment fleet, worth US$20m over five years. For the Federal Retirement Thrift Investment Board, Serco will continue to support the US Government retirement plan delivering records management and processing solutions in an extension valued at US$26m over a maximum two years. For the US Patent and Trademark Office, where Serco will now classify approximately 1,500 patent applications a day, our contract has been extended and expanded, valued in total over three years at US$43m. Serco's long-standing work with United States Citizenship and Immigration Services has been extended to manage and process an additional two million records as a result of an Executive Order issued by President Obama in support of Immigration Qualifications, Deferred Action for Childhood Arrival. This two-year extension is valued in total at US$25m.

Americas – growth opportunities

The federal contracting market is likely to face continued attrition due to the ongoing budget uncertainty and the protracted challenges facing Congress in dealing with the growing national debt. The threat of sequestration, as originally included in 2011's debt ceiling deal, was due to take effect from 2 January 2013 unless some form of agreement was reached by the government on tax and spending issues, but received a short-term postponement. Current federal funding is also continuing to operate under short-term Continuing Resolutions, which often limit commitments to new programs. As a result, the outlook for spending on government services remains both unclear and severely challenged. Industry studies suggest the total budget addressable by government contractors could decline by approximately 10% or more annually in 2013 and potentially beyond until the cycle turns.

As is normal for our Americas division, there is a higher frequency of rebids than is typical for our operations elsewhere around the world. The development of our business will also be shaped by the successful outcome of rebids within a challenging market environment. Important short-term extensions have been secured as noted, while other significant rebids are due over the next 12 months such as Ontario Driver Examination Services, the National Visa Center, the Federal Retirement Thrift Investment Board and the Department of Veteran Affairs.

Serco continues to focus on markets that we expect will receive ongoing funding support, and on assisting government customers to achieve greater efficiencies and higher productivity with constrained resources. Our key areas are: Logistics & Program Management; Communication & Information Systems; National Intelligence; Human Capital Management; Business Process Outsourcing; and Transportation & Asset Management. US government agencies are increasingly using multi-award contract vehicles to issue task orders on a rapid-cycle, competitive basis. Continuing to qualify for and win business under such IDIQ contract vehicles will be a key contributor to Serco's growth.

In IT services and solutions, Serco is one of 54 awardees on a government-wide acquisition contract (GWAC) with a ceiling value of US$20bn over a ten-year period. Serco will bid on a range of task orders for all federal civilian and Department of Defense agencies that require services and solutions including biomedical IT systems, cloud computing, cybersecurity, mobility, telecommunications, and data center consolidation. Serco is one of seven recent awards on a new SPAWAR Systems Center (SSC) Atlantic Pillar Multiple Award Contract (MAC) for Production, Installation and In-Service (PII) support. This MAC has a potential ceiling value of US$900m over a maximum five years, and enables Serco to bid on task orders to provide PII support, life-cycle logistics, training and large scale integration to deliver engineering, equipment and systems support.
Serco is also one of eight awards on a new MAC supporting SSC with integrated Command and Control (C2) engineering and technical support services for command centers. This MAC has a potential ceiling value of US$145m over a maximum three years.

Serco has been awarded a place on the new Consultant, Advisory, and Technical Services (CATS) contract vehicle that will provide support services to the US Air Force Medical Service (AFMS) at 69 Air Force Medical Treatment Facilities in the United States and its territories. Serco is among 13 award winners on the IDIQ contract, which is valued at US$985m over a five-year period. Serco will compete for task orders for Advisory & Assistance Services (A&AS) that will help reduce critical workload demands being placed on the AFMS. Services will include support in the areas of healthcare administration, executive assistance, financial analysis, business process consulting, policy analysis, engineering and technical services.

Serco Americas pipeline includes numerous further areas of longer term opportunity. For our Navy customers, we expect growth through modernisation work to extend the service life of the existing fleet. The Department of Defense is expected to increase its focus on areas such as Intelligence, Surveillance and Reconnaissance (ISR), unmanned flight, space and cybersecurity. Human capital management and transformation programmes are widening in scope to support future changes to the size and shape of the armed forces. As a result of the US government's Affordable Care Act, we see opportunities to deliver solutions supporting patient satisfaction requirements and health insurance enrolment initiatives. BPO opportunities with federal and other customers will be pursued to deliver enhanced service and more cost-effective solutions. We plan to leverage our strong capabilities in economic cost analysis and programme management to support the Department of Defense's drive for cost savings. The transportation market is expected to provide opportunities for our air traffic control, traffic management systems and other transport infrastructure and operational management skills and capabilities. We will also continue to review markets in both North America and South America for potential to transfer more of Serco's skills and capabilities.

AMEAA – operating review

Our AMEAA segment consists of Australasia, Middle East, Asia and Africa, in which we provide a range of frontline services including transport, justice, immigration, health, defence and other direct services such as facilities management.

Revenue on a reported currency basis grew 31% to £883m (2011: £672m), and represented 18% of Group ongoing revenue, up from 15% in 2011. Revenue on a constant currency basis grew by 30%. Excluding the contribution from acquisitions, revenue on an organic basis grew by 22%. Adjusted operating profit grew by 25% on a reported currency basis to £64.3m (2011: £51.4m), with the margin decreasing to 7.3% (2011: 7.6%).

The very strong organic growth reflects revenue from new contracts begun in 2012 and those that had started but were not fully operational throughout 2011, as well as the expansion of existing contracts, particularly an increase in the amount of work undertaken for the Australian Department of Immigration and Citizenship (DIAC). The reduction in margin principally reflects the return to a more normal level of margin on the DIAC contract.

In Immigration Services in Australia, the level of irregular maritime arrivals has increased in 2012, leading to a growth in the number of people in our care. In response, we successfully managed the opening of new detention centres in the Northern Territory and Western Australia. The level of our future activity is still likely to fluctuate based on country conditions in the Middle East and Asia where most people in our care originate, and the prevailing government policy, speed of visa processing and the application of the Australian Government's recent off-shore processing legislation. Serco has a very strong customer relationship with DIAC, with both parties working closely to maintain a safe and stable network of centres, responding with humanity and respect in the operation of this sensitive contract.

A number of other contract awards in Australia generated incremental revenues. Serco's operation of Court Security and Custodial Services (CSCS) for the Western Australian Department of Corrective Services was fully operational, achieving over 30,000 client movements in the year. A new contract valued at A$50m over five years (with potential to extend to 15 years in total) for the new Wandoo Integration Facility in Western Australia became fully operational in November 2012. Serco also expanded the scope of its contracts at Acacia Prison in Western Australia and for the new South Queensland Correctional Centre (SQCC) which replaced the previous facility at Borallon. While in New Zealand, Serco's operation of the Mount Eden Corrections facility in Auckland successfully completed its first full year of operation.

The pre-operational phase of the new-build Fiona Stanley Hospital in Perth has continued to see Serco's involvement grow. Plans are on track for the opening in 2014, at which point Serco's full facilities management and support services contract to ensure the smooth running of the whole hospital will begin. The first phase of recruiting over 1,000 non-clinical staff required to operate the hospital has already begun. Elsewhere in our transport operations, Great Southern Rail, in adverse conditions for the Australian tourism market has continued to hold revenue broadly stable through additional operating investment. The business was presented with the Service Excellence award at the 2012 Australian Business Awards, while The Ghan was voted 'best luxury rail journey' worldwide in Luxury Travel Magazine for the third year running.

DMS Maritime, our defence and marine services business, has continued to show good organic growth. As one of Australia's largest maritime service operators, it has facilities in every major port and a technical support network that extends a wide range of engineering and technical services across Asia Pacific. DMS Maritime manages, operates and maintains over 600 vessels in the region, with commercial, defence and government agency customers including the Royal Australian Navy and the Australian Customs & Border Protection Service. Towards the end of the year, Serco successfully completed the purchase of the remaining 50% equity stake in the business from its joint venture partner P&O Maritime Services.

In the Middle East, service on the Dubai Metro has continued to see world class operational standards, with 99.9% of all trains on time and the Roads and Transport Authority (RTA) reporting a record number of Metro passengers in 2012, up by 58% on 2011. During the year, Serco also added additional engineering and maintenance responsibilities required to support network expansion. Our logistics and base support operations in the region for the Australian Defence Force (ADF) successfully completed their first year of operations, whilst our integrated facilities management operations in the region have also delivered strong growth.

AMEAA – growth opportunities

The AMEAA region has experienced the fastest growth of our portfolio for a number of years and we continue to see good opportunities for further strong growth. Our existing operations in Australasia, the Middle East and India each present prospects. In addition, there is further growth potential from expanding into new regions as emerging market governments take steps to adopt international best practice in procurement processes to support their social infrastructure improvement programmes.

In the justice sector, we see further opportunities in the operation of new-build and existing prisons as governments deal with capacity and efficiency challenges. For example, Serco's consortium signed a contract during the year to provide and operate the new Wiri prison in Auckland. Under the design, construct, manage and finance contract, Serco will manage the new 960-place male prison for 25 years once it becomes operational in 2015. The contract will deliver revenues of approximately £15m a year. Related services such as court escorting services also represent opportunities.

In transport, Serco is seeking to leverage its international expertise particularly in urban transportation and metro systems. In India, Serco has been awarded its first frontline services contract to operate and maintain the new Bus Rapid Transit Services (BRTS), a dedicated 11.3km bus corridor in the city of Indore in central India. Further expanding our services with the Dubai Airports Company, Serco will be providing the operations and maintenance for the new Automated People Mover (APM) at the airport. Numerous bidding opportunities throughout the AMEAA region are expected to support other road and rail operation and maintenance contracts as well as traffic management systems.

Serco is also a global leader in air navigation, and sees opportunities to expand services both within the region and into new geographies. For example, in 2012 Serco's management of Iraqi airspace at Baghdad International Airport was expanded to deliver air traffic control services at Erbil in Iraqi Kurdistan. Our ability to mobilise highly skilled aviation teams quickly is well established, and we are in discussions with a number of potential customers seeking a step change in air navigation safety, capacity and performance.

Integrated facilities management contracts in the commercial and other sectors are expected to grow, particularly given ongoing completion of major construction projects in the UAE. Last year's acquisition of a small regional specialist in the region is delivering strong results. Serco has also capitalised on its new business development presence in the Kingdom of Saudi Arabia. Two new consultancy agreements will provide asset management strategies to implement operational efficiency processes for building maintenance and infrastructure.

Our defence business in Australia has a strong base from which to expand services, including garrison and maritime support, training, engineering and maintenance. In the growing marine services market, our presence has been strengthened by our full ownership of DMS Maritime. Serco will now be well placed to pursue more complex opportunities that may emerge from new capability requirements for the Australian Defence Force to be detailed in its forthcoming White Paper 2013. It will allow Serco to fully leverage DMS Maritime's defence systems integration, supply chain management and through-life support capabilities across the maritime, land, systems and ultimately aerospace domains. DMS Maritime additionally provides Serco with a platform to further expand the breadth of our marine services to the commercial maritime market. This includes port infrastructure and related services to the resources sector, driven by the ongoing high demand for commodities and energy.

In the emerging and rapidly growing health markets in the region, governments are increasingly looking to involve private sector provision. Across the region Serco will be pursuing potential opportunities for the operation of hospitals and related services, building on the strength of our UK operations and the Fiona Stanley Hospital in Australia. For example, Serco was also awarded a new support services contract for the Prince of Wales Hospital, one of the busiest in Hong Kong with over 1,000 beds and complex facilities.

The AMEAA division will also be supported by the Global Services division in joint growth opportunities for its customers. Relationships, skills and capabilities will be pooled for opportunities such as providing shared services to government departments.

Global Services – operating review

In 2012, Serco created a new global BPO division, bringing together all of Serco's middle and back office skills and capabilities across customer contact, transaction and financial processing, and related consulting and technology services. The new Global Services division improves the services we provide to customers and addresses a wider range of opportunities in both the private and public sectors. Customers around the world are increasingly looking for end-to-end services that combine frontline capability with middle and back office operations, helping them to drive more efficiency and better quality services. In addition to seeking specific BPO opportunities, the division will also work alongside the regional divisions to deliver fully integrated services for their customers. The establishment and growth of Serco Global Services, with global annual revenues in excess of $1.1 billion, places Serco as a top tier international BPO organisation.

Revenue on a reported currency basis grew 40% to £716m (2011: £511m). This represented 15% of Group ongoing revenue, up from 11% in 2011. Revenue on a constant currency basis grew by 45%. Excluding the contribution from acquisitions, principally Intelenet and Vertex, revenue on an organic basis grew by 12%. In the previous year there were revenues from the Bradford education contract which transferred back to the Council in September 2011, and from our Business Link services the majority of which have now closed due to the government funding cuts borne by the Regional Development Agencies (RDAs). Excluding these two areas, underlying revenue growth for our new global BPO division has been over 30%.

Adjusted operating profit grew by 83% on a reported currency basis to £62.1m (2011: £34.0m), with the margin increasing to 8.7% (2011: 6.7%). The margin increase was driven principally by the contribution from the higher margin Intelenet operations and significant private sector wins.

Over the course of 2012, we concluded the significant programme of integrating the acquisitions made in 2011, combining them with Serco's existing strength in IT-enabled service delivery. Tools such as Workforce Management have been rolled out, as well as standardising and strengthening all management and compliance procedures. Significant investment has been made in IT integration, and this will continue to be a feature to place the business in the strongest position for future growth. In 2013 there will also be further additional investment costs for new delivery centres and business development initiatives around the world, supporting the strong pipeline of growth opportunities.

In its first full year of Serco ownership, the former Intelenet operations have met our expectations as set out at the time of acquisition. Intelenet has been a key part of the strong underlying revenue growth for the whole of Serco Global Services. As well as incremental revenues already achieved, numerous major strategic wins made part way through 2012 will also support expected strong revenue growth into 2013.

In July 2012 Serco began operating a new ten-year contract for Shop Direct Group, the UK's leading online and home shopping retailer, valued in total at approximately £430m. Serco has taken over responsibility for providing all customer contact services across Shop Direct's brands. The partnership will work together to significantly enhance service levels and efficiency through investment in the latest technology, such as web chat and mobile digital services, which are designed to integrate seamlessly online and mobile customer contact management.

Our solution combines capabilities from the Intelenet and The Listening Company acquisitions as well as the additional scale advantage from Serco's other BPO operations.

In November 2012 Serco began a new outsourcing partnership to provide customer contact and support services for AEGON, the leading life and pensions company, marking Serco's entry into this important segment of the financial services market. The initial ten-year contract is valued in total at around £170m. Delivering a wide range of services for AEGON's UK-based protection business, Serco is managing all aspects of the customer journey from initial underwriting through to claims processing as well as servicing a small number of closed book policies. Serco is responsible for the administration of approximately 500,000 current and closed book policies in total.

Many other new private sector BPO operations began during 2012. In retail, a £55m ten-year contract with Freemans Grattan Holdings sees Serco delivering all aspects of customer contact services including customer enquiries, inbound and outbound sales, credit applications, payments, order processing, white mail and e-mail handling. Serco also secured new relationships with two of the UK's most prestigious retailers to provide services including order line and customer management, while for a leading European media company Serco is providing frontline customer contact, back office and specialist support from an expanded service centre in Teltow, near Berlin, Germany. These three contracts, which have three to five-year terms have a total combined value of approximately £50m.

Serco was awarded a new contract to provide multi-lingual customer contact services for leading European airline easyJet. Serco has responsibility for the operation, administration and management of easyJet's multi-channel customer contact, delivered through a blend of near-shore and off-shore provision from Poland and India. This initial three-year contract has a total value of approximately £18m. Serco also began a wide range of customer sales services for British Gas in the UK, delivering customer acquisition activities for energy, domestic appliance and drain care services in a new three-year contract valued in total at approximately £16m.

Other new contract awards include: support to a UK General insurance provider to reduce their backlog of Financial Services Authority (FSA) regulated complaints; providing 1,800 customer contact employees and multi-channel services for a large banking and financial services company in India; supporting the booking processes for travel and hospitality services for an award-winning loyalty program on behalf of a leading US-based global online travel company; and establishing off-shore delivery centres to provide back office services such as indexing, invoice processing, claims adjudication and policy maintenance for a leading UK-based healthcare insurance provider.

In the public sector, The Anglia Support Partnership (ASP), which has an initial value of £120m over four years, began operating in April 2012. This is Serco's first shared services proposition in the emerging market for middle and back office support to the UK health sector. Current support services include operational and specialist IT, finance operations, employment services, contracts management, procurement, primary care support services, occupational health, risk management, catering and estates and property. The framework agreement also permits the call-off of additional services and other NHS organisations to access services.

The Peterborough City Council strategic partnership, which had an initial value of £100m over 10 years, saw the transfer of the in-house shared service centre to Serco in late 2011. Serco is already successfully growing this contract with further services such as procurement being brought into scope as part of the Council's transformation. The Hertfordshire County Council operations which commenced in April 2011 have also widened their scope, with staff numbers more than doubling and new operations such as the Adult Social Care Access Service now being provided. Additionally, Serco's property and IT joint venture with Glasgow City Council, known as ACCESS, has seen Information, Communications and Technology (ICT) support for the authority's schools added to its responsibilities.

Other strategically important existing relationships were also developed in the period. Serco has extended and expanded its relationship with a leading telecom provider in India for a further three-year term. Providing contact services and transaction support, the contract which began in 2006 from three delivery centres has expanded to ten today and handles an average 14 million calls and transactions per month. Our expertise in this relationship also supported the award of a new contract with a further leading telecom provider, where five delivery centres will provide contact services under this new relationship. These three-year contracts on a combined basis have a total value of approximately £60m.

Serco successfully renewed its contract with the Australian Tax Office to provide contact centre services to Australian taxpayers, businesses and tax professionals across a diverse range of taxation and superannuation-related issues. Serco, in partnership with the ATO and other suppliers, is responsible for providing advice and responding to enquiries relating to tax numbers, refunds, business activity statements, debt management, return submissions and tax information packs. The renewed contract has an initial five-year term with a total value of approximately £90m. Serco also successfully renewed its contract to provide a comprehensive range of customer services for the National Rail Enquiries service in the UK. The contract which has been operated by Serco and the former Intelenet business since 2004 includes Help Point support, customer care, enquiries and complaint handling across a range of channels including voice, email and web chat. Responding to changing patterns of consumer engagement, this innovative five-year contract is valued in total at approximately £10m.

Recognising the substantial amount of new business won during the year, Serco was identified as one of the top three global BPO service providers by the leading BPO industry analyst firm NelsonHall in their 2012 BPO Index. This index measures the performance of leading BPO service providers based on the total contract value (TCV) of wins achieved in 2012. Recognising the overall scale of our operations, we were also named as one of the top 15 BPO providers within leading technology insights and advisory services firm ISG's TPI Index.

During 2012, our operations have continued to win various accolades in the crucial area of employee development. According to NASSCOM's ranking of IT-BPO employers in India, Serco Global Services is now the largest pure-play BPO business. Awards in 2012 include recognition within 'Asia's Best Employer Brand Awards' and 'India's Best Companies to Work For', the latter being for 'Best Company in Career Growth'.

Global Services – growth opportunities

Serco has built significant capability in the fast growing, higher margin BPO market, broadening Serco's customer and geographic reach. This has added scale and depth to provide private and public sector customers with a range of end-to-end, integrated business services as they seek to reduce costs and improve efficiencies by transforming their operations.

Serco's approach is increasingly recognised for leadership in transforming a customer's operations as opposed to simple 'lift and shift' solutions. Serco's bids benefit from our substantial scale and global reach, in particular from the ability to provide a blend of on-shore, near-shore and off-shore service provision. We are also a clear leader in areas such as multi-channel customer contact services. Significant contract wins in 2012 such as Shop Direct and AEGON have demonstrated these factors and provide excellent short-term growth into 2013 as these annualise, but importantly also provide strong referenceability for similar work in the future.

We are addressing a large number of private sector market opportunities. The significant pipeline of prospects continues to be spread across large and diverse industry groups: Banking, Financial Services & Insurance; Travel, Hospitality & Transportation; Retail, Healthcare, Utilities, & Manufacturing; Telecom, Technology, Online Services & Media.

Our geographic reach both for customers and service centre locations has expanded to support future growth. This has included new operations in Germany, South Africa and Saudi Arabia. The latter, following our first centre launch in Dubai in 2011, supports further expansion in the largest economy within the Middle East region. Additionally, Global Services also expanded its India-based Agra facility, further strengthening its dominant position in the India domestic BPO market. The management team in the Americas region has also been strengthened to target significant growth opportunities.

In the public sector, the Global Services division is working alongside the regional divisions in order to bid and deliver fully integrated solutions for their customers. Significant revenue synergies have already been achieved where the Group's combined capabilities are able to transform public services, and we expect more to continue to emerge in the future.

In June 2012 Serco acquired Vertex's UK public sector BPO operations, bringing additional expertise and strategic partnerships to support expansion into new areas of middle and back office support and at the same time increase Serco's operational scale. This will help develop future opportunities in both the central and local government markets, with Vertex bringing significant customer referenceability and specific skills in HR and payroll, revenues and benefits, complex case management and administration services. Its 3,000 employees handle approximately 4.5 million citizen interactions a year.

In the UK, the government has recently set out how it intends to achieve efficiencies in shared service centres and has also set out the transaction costs involved in providing services for citizens. The Global Services division would provide support in bidding for operations such as contact centre services, case management, identity verification, transaction processing, ICT, human resources and payroll, finance and accounting, and any other middle or back office support function that is required. For example, for the Ministry of Justice, Global Services is providing support to the UK & Europe division for court fines and compliance and enforcement, electronic monitoring and prison management. The future development of the Ministry of Defence's DIO opportunity, similar in nature to the DBS contract already led by the UK & Europe division, would also see Global Services support, as would tenders expected for the Home Office in areas such as visa services.

The ASP contract is expected to be a key enabler to growing Serco's combination of health support services and BPO operations. We are already seeing growth in areas such as procurement services, and expect the framework agreement to support significant further growth. Other opportunities in providing business services to NHS organisations are also being pursued.

We recently signed a new contract to provide multi-channel contact centre services to the Department of Health to cover a range of public health programmes. Other central government shared service centre opportunities are expected to be developed. For example, the Department for Work and Pensions is assessing the case for a shared services centre to process claims and payments. There is also the potential to expand the scope of support for existing customers such as Job Centre Plus and emerging BPO opportunities for other agencies and departments.

Our work with local authorities to transform their services continues to show a good pipeline of opportunities. Local authorities are further developing their strategies based on a smaller proportion of services that they deem to be core, thereby increasing the potential to outsource other non-core supporting operations. Existing Serco strategic partnerships at Hertfordshire, Glasgow and Peterborough have all demonstrated the potential for expansion, and the addition of the Thurrock and Westminster contracts previously operated by Vertex adds to our ability to increase the scope of services. Research by YouGov supports the view that local authorities are looking for further outsourcing, with this increasingly focused on transformational change.

Finance Review

Overview

Our business delivered a strong financial performance in 2012, with revenue growing 5.7% and Adjusted operating profit increasing by 8.5% to £314.8m. Excluding currency effects, revenue growth was 6.2% (3.3% organic) and Adjusted operating profit growth was 9.9%. Our Adjusted operating margin increased by 17 basis points (22 basis points excluding currency effects). Adjusted profit before tax grew by 6.1% (7.3% excluding currency effects). Group free cash flow increased by 7.7% to £181.2m, principally as a result of the increase in profits and an exceptionally high level of dividends received from joint ventures.

For 2013, we are forecasting a modest improvement in the rate of organic revenue growth. The impact of acquisitions and disposals to date is likely to have a broadly neutral impact on total revenue growth. We are forecasting our Adjusted operating margin to be broadly maintained at the level achieved in 2012.

1. Income statement

Serco's income statement for the year is summarised in Figure 1 below. This includes the results of joint ventures which are proportionately consolidated. The table shows separately the revenue and Adjusted operating profit of ongoing activities, which exclude the financial results of subsidiaries and operations disposed of during the year. Measures of Adjusted operating profit, Adjusted profit before tax and Adjusted earnings per share are presented, which are calculated before amortisation of intangibles arising on acquisitions, acquisition-related costs and exceptional items (being profit or losses on disposal of subsidiaries and operations, the donation to the Serco Foundation and the gain arising from step acquisition accounting on the DMS joint venture).

Figure 1: Income statement

Year ended 31 December	2012 Before exceptional items £m	2012 Exceptional items £m	2012 Total £m	2011 £m	
Revenue ongoing activities	**4,832.2**	**-**	**4,832.2**	4,471.8	8.1%
Revenue disposed activities	**80.8**	**-**	**80.8**	174.6	
Total revenue	**4,913.0**	**-**	**4,913.0**	4,646.4	5.7%
Gross profit	**743.5**	**-**	**743.5**	700.4	6.2%
Administrative expenses	**(428.7)**	**-**	**(428.7)**	(410.3)	4.5%
Adjusted operating profit ongoing activities	**309.1**		**309.1**	276.4	11.8%
Adjusted operating profit disposed activities	**5.7**		**5.7**	13.7	
Adjusted operating profit	**314.8**	**-**	**314.8**	290.1	8.5%
Amortisation of intangibles arising on acquisition	**(24.1)**	**-**	**(24.1)**	(20.0)	
Acquisition-related costs	**(3.7)**	**-**	**(3.7)**	(3.9)	
Exceptional net profit on disposal of subsidiaries and operations	**-**	**5.6**	**5.6**	-	
Exceptional donation to Serco Foundation	**-**	**(5.0)**	**(5.0)**	-	
Operating profit	**287.0**	**0.6**	**287.6**	266.2	8.0%
Exceptional other gain	**-**	**51.1**	**51.1**	-	
Investment revenue and finance costs	**(36.7)**	**-**	**(36.7)**	(27.9)	
Profit before tax	**250.3**	**51.7**	**302.0**	238.3	26.7%
Tax	**(62.6)**	**6.5**	**(56.1)**	(63.1)	
Profit for the year	**187.7**	**58.2**	**245.9**	175.2	40.4%
Effective tax rate	**25.0%**		**18.6%**	26.5%	
Adjusted operating margin	**6.4%**		**6.4%**	6.2%	
Adjusted profit before tax	**£278.1m**	**-**	**£278.1m**	£262.2m	6.1%
Adjusted earnings per share	**42.55p**	**-**	**42.55p**	39.59p	7.5%
Earnings per share	**38.09p**	**11.85p**	**49.94p**	35.70p	39.9%
Dividend per share			**10.10p**	8.40p	20.2%

1.1 Revenue

Revenue grew by 5.7% to £4,913.0m (6.2% excluding currency effects). Organic revenue growth, excluding currency effects and acquisitions, was 3.3% reflecting the growth of existing contracts and the contribution of new contracts started in 2011 and 2012.

1.2 Adjusted operating profit

Adjusted operating profit increased by 8.5% to £314.8m representing an Adjusted operating profit margin of 6.4%. Adjusted operating profit margin increased by 17 basis points (22 basis points excluding currency effects).

1.3 Reportable segments and ongoing activities

The table below shows the segmental results split between ongoing activities, being the part of the business which will continue in to 2013, and disposed activities, being the part of the business which contributed to the 2012 and 2011 results but was disposed of during the year.

Figure 2: Reportable segments

Year ended 31 December 2012	**UK & Europe £m**	**Americas £m**	**AMEAA £m**	**Global Services £m**	**Total £m**
Segment revenue					
Ongoing activities	**2,494.0**	**753.4**	**883.0**	**701.8**	**4,832.2**
Disposed activities	**67.1**	**-**	**-**	**13.7**	**80.8**
Revenue	**2,561.1**	**753.4**	**883.0**	**715.5**	**4,913.0**
Segment Adjusted operating profit					
Ongoing activities	**172.9**	**55.2**	**64.3**	**61.3**	**353.7**
Disposed activities	**4.9**	**-**	**-**	**0.8**	**5.7**
Segment Adjusted operating profit	**177.8**	**55.2**	**64.3**	**62.1**	**359.4**
Corporate expenses					**(44.6)**
Adjusted operating profit					**314.8**

Year ended 31 December 2011	UK & Europe £m	Americas £m	AMEAA £m	Global Services £m	Total £m
Segment revenue					
Ongoing activities	2,434.1	868.2	672.1	497.4	4,471.8
Disposed activities	161.1	-	-	13.5	174.6
Revenue	2,595.2	868.2	672.1	510.9	4,646.4
Segment Adjusted operating profit					
Ongoing activities	165.0	73.0	51.4	32.9	322.3
Disposed activities	12.6	-	-	1.1	13.7
Segment Adjusted operating profit	177.6	73.0	51.4	34.0	336.0
Corporate expenses					(45.9)
Adjusted operating profit					290.1

1.4 Acquisition-related costs

These represent incremental costs arising from acquisition activity during the year. The £3.7m of costs principally related to the acquisitions of Vertex Public Services Limited (Vertex) and the remaining 50% share of DMS Maritime Pty Limited (DMS) that are described in more detail in Section 4 below.

1.5 Exceptional net profit on disposal of subsidiaries and operations

The £5.6m exceptional item represents net profit on disposal of the four subsidiaries and operations during the year which are described in more detail in Section 5 below.

1.6 Exceptional donation to Serco Foundation

To mark Serco's 25th year as a publicly traded company dedicated to service excellence, we have established the Serco Foundation as an independent charitable foundation. An exceptional one-off payment of £5.0m has been made in the year to establish the charitable foundation.

1.7 Operating profit

Operating profit after exceptional items was £287.6m, an increase of 8.0%.

1.8 Exceptional other gain

The exceptional other gain represents the gain arising from step acquisition accounting of the DMS joint venture. This requires that, before accounting for the purchase of the remaining 50%, the original 50% shareholding held at book value in Serco's accounts is restated to fair value. The revaluation of this original 50% is recognised in the consolidated income statement, which resulted in a £51.1m non-cash exceptional gain.

1.9 Investment revenue and finance costs

Investment revenue and finance costs totalled a net cost of £36.7m (2011: £27.9m), an increase of £8.8m. The increase excluding currency effects was £9.6m. The principal driver of the cost increase was the full year effect of additional loans raised in the prior year to finance acquisition activity.

For 2013, net finance costs are anticipated to be approximately £45-50m including the impact from the forthcoming revision to IAS 19; this would represent a slight increase on the equivalent 2012 restated net finance cost.

1.10 Tax

The tax charge of £56.1m (2011: £63.1m) represents an effective rate of 18.6% (2011: 26.5%). Excluding exceptional items the effective rate was 25.0% (2011: 26.5%). Excluding exceptional and other adjusting items, the effective rate was 24.6% (2011: 25.9%). The decrease in the effective tax rate is primarily due to changes in the mix of taxable profits and the impact of the reduction in the UK headline tax rate from 26% to 24% on 1 April 2012.

1.11 Earnings per share (EPS)

Adjusted EPS rose by 7.5% to 42.55p (8.7% excluding currency effects). EPS grew 39.9% to 49.94p while EPS excluding exceptional items grew by 6.7% to 38.09p. EPS and Adjusted EPS are calculated on an average share base of 491.2m during the year (2011: 490.5m).

1.12 Expected impact of changes to accounting standards

In 2013 there will be two significant changes to accounting under International Financial Reporting Standards ('IFRS') which will affect Serco's 2013 results and require the restatement of 2012 comparative figures. These relate to changes in the joint venture accounting rules (IFRS 11) and to the pension accounting rules (IAS 19 revised).

The change to joint venture accounting rules (IFRS 11) will remove the option for proportional consolidation of joint ventures and require equity accounting for joint ventures instead. The estimated effect on the 2012 results for this change would be to reduce statutory reported revenue by £852.9m and profit before tax by £15.1m. There is no impact on post tax profits, earnings per share, or net assets from this change. In addition to the statutory measures, the 2013 income statement will also disclose revenue and Adjusted operating profit including the proportional share of joint venture results, to provide consistency in the presentation of the results.

The change to the pension accounting rules (IAS 19 revised) will principally require pension interest return to be calculated using the value of scheme assets multiplied by the discount rate rather than the expected rate of asset return. After accounting for IFRS 11, the additional estimated effect on the 2012 results for this change reduces Adjusted pre tax profits by £6.5m.

2. Dividend

The Board is confident in the future growth prospects for the Group and of the strong financial position that we have. We therefore intend progressively to increase the payout ratio and thereby reduce our dividend cover over the next three years. Beyond that point, we anticipate a policy of maintaining dividend cover of between 2.5 and 3 times and therefore reverting to increasing the total dividend each year broadly in line with the increase in underlying earnings. The Board has proposed a final dividend for 2012 of 7.45p per share, bringing the total dividend for the year to 10.10p, up 20% compared with the previous year. This represents a payout of 24% based on 42.55p of Adjusted earnings per share, or dividend cover of 4.2 times. The final dividend will be paid, subject to shareholder approval, on 22 May 2013 to shareholders on the register on 15 March 2013.

3. Cash flow

The Group generated a free cash inflow of £181.2m (2011: £168.3m), with the increase arising principally from the increase in profits and the exceptionally high level of dividends received from joint ventures.

For 2013, it is anticipated that there will be further incremental working capital investment to support growth in our BPO business and lower dividends from joint ventures, which may result in free cash flow being lower than the level achieved in 2012.

Figure 3 provides cash flow analysis. As in previous years, we have designed the analysis to show the underlying 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 44, which proportionately consolidates the cash flows of joint ventures. The adjustment line in Figure 3 reconciles the movement in Group cash to the consolidated cash flow.

Figure 3: Cash flow

Year ended 31 December	**2012 £m**	2011 £m
Adjusted operating profit excluding joint ventures	**237.4**	208.5
Non cash items	**56.0**	64.2
Adjusted EBITDA excluding joint ventures	**293.4**	272.7
Working capital movement	**(47.6)**	(32.3)
Operating cash flow excluding joint ventures	**245.8**	240.4
Interest	**(44.7)**	(32.7)
Tax	**(33.6)**	(32.2)
Net expenditure on tangible and intangible assets	**(66.9)**	(71.5)
Dividends from joint ventures	**80.6**	64.3
Group free cash flow	**181.2**	168.3
Acquisition of subsidiaries net of cash acquired	**(141.8)**	(325.3)
Disposal of subsidiaries and operations net of cash disposed	**131.0**	-
Acquisition-related costs	**(3.9)**	(3.7)
Purchase of own shares and issue proceeds of share capital	**(10.3)**	(6.7)
Financing	**(152.0)**	236.0
Exceptional donation to Serco Foundation	**(5.0)**	-
Special pension contribution	**-**	(40.0)
Dividends paid	**(41.9)**	(37.3)
Group net decrease in cash and cash equivalents	**(42.7)**	(8.7)
Adjustment to include joint venture cash impacts	**(4.5)**	(15.1)
Net decrease in cash and cash equivalents before exchange loss	**(47.2)**	(23.8)
Exchange loss	**(9.0)**	(0.7)
Net decrease in cash and cash equivalents	**(56.2)**	(24.5)

Notes:
Adjusted EBITDA excluding joint ventures is earnings before interest, tax, depreciation, intangible amortisation, profit on disposal of subsidiaries and operations, charitable donation, other exceptional gains and other non cash items.

Net expenditure on tangible and intangible assets excludes asset funded under finance lease arrangements. Financing is stated net of directly reimbursed capital expenditure.

3.1 Operating cash flow excluding joint ventures

Operating cash flow excluding joint ventures of £245.8m (2011: £240.4m) reflects a conversion of Adjusted EBITDA into cash of 83.8% (2011: 88.2%). The increase in working capital movement to £47.6m (2011: £32.3m) principally reflects the timing of transition and mobilisation of new contract awards and an increased level of investment in supporting growth of our BPO business.

3.2 Interest

Net interest paid increased to £44.7m (2011: £32.7m), principally reflecting higher average Group recourse net debt following acquisitions during the current and prior year.

3.3 Tax

Tax paid was £33.6m (2011: £32.2m). The increase in cash tax is principally as a result of higher overseas taxable profits arising in the year. Cash tax remains below the equivalent charge in the income statement principally as a result of the availability of accelerated capital allowances and other timing differences.

3.4 Net expenditure on tangible and intangible assets

Net expenditure on tangible and intangible assets was £66.9m (2011: £71.5m). The spend principally comprises required contract capital investment. This expenditure represents 1.6% of Group revenue excluding joint ventures (2011: 1.9%). The expenditure in 2011 included additional investment in SAP systems.

3.5 Dividends from joint ventures

Dividends received from joint ventures totalled £80.6m (2011: £64.3m), reflecting a higher than normal conversion rate of joint ventures' profit after tax into dividends of 125%. We expect the conversion rate to return to a more normal rate of approximately 90% in 2013.

3.6 Purchase of own shares and issue proceeds of share capital

This represents £16.0m (2011: £24.0m) for the purchase of own shares for the Employee Share Ownership Trust (ESOT) in order to satisfy options granted under the Group's share option schemes, net of cash inflows of £5.7m (2011: £17.3m) relating to proceeds from the issue of share capital and exercise of share options.

4. Acquisitions

On 13 April 2012, Serco entered into an agreement to acquire the trade and assets of Anglia Support Partnership (ASP). ASP provides support services to the Cambridge and Peterborough NHS Foundation Trust, together with a further five partnering NHS organisations. The initial cash consideration in respect of the business combination was £5.2m and deferred consideration of £3.5m was paid in the year.

On 1 June 2012, Serco acquired 100% of the issued share capital of Priority Properties North West Limited (PPNW). PPNW is a property management company specialising in the provision of short and long term housing. The cash cost of the acquisition in the period was £2.7m. In addition, deferred consideration of up to £1.1m is payable contingent on financial performance in the period to 31 January 2013.

On 11 June 2012, Serco acquired 100% of the issued share capital of Vertex Public Services Limited (Vertex), a provider of high quality business process outsourcing services to UK local and central government. The cash cost of the acquisition was £55.5m. Vertex brings additional expertise and strategic partnerships to support expansion into new areas of middle and back office support . This acquisition considerably increases Serco's market presence and further improves Serco's position for large scale outsourcing opportunities.

On 16 November 2012, Serco acquired the remaining 50% stake in DMS Maritime Pty Limited from our joint venture partner P&O Maritime Services. The transaction strengthens Serco's position as a leading defence services provider in Australia and in the growing marine services market. The cash cost of the acquisition was £69.1m (A$106.3m). DMS was formerly accounted for as a joint venture and following the acquisition of further shares it became a wholly owned subsidiary. In accordance with IFRS 3 (Revised 2008) – Business Combinations, which requires that before accounting for the purchase of the remaining 50%, the value of the previously held 50% shareholding was restated to fair value on the acquisition date. This resulted in a gain of £51.1m being recognised in the income statement.

£3.7m of acquisition-related costs incurred on the above acquisitions have been expensed to the income statement. The cash flow impact of these costs included in the cash flow statement was £3.9m which includes £0.2m of acquisition-related costs from prior year acquisitions.

A deferred payment of £6.6m has also been made in relation to the prior year acquisition of Serco Listening Company Limited (formerly The Listening Company Limited).

5. Disposals

On 29 June 2012, the Group disposed of its Technical Services business which provides consulting and project solutions primarily to the UK civil and nuclear defence markets for net consideration of £135.3m. Net assets disposed amounted to £70.3m, giving a gain of £57.6m, after accounting for disposal costs of £7.4m.

On 29 June 2012, the Group disposed of its interest in Serco GmbH. The fair value of consideration receivable was £nil. The business provides support services for the German air defence radar systems, engineering and administrative support services for the defence sector as well as training services, facilities management, field installation and maintenance services and IT consulting and related services. Net assets disposed amounted to £21.8m, giving a loss of £27.7m, after accounting for disposal costs of £5.9m.

On 31 December 2012, the Group disposed of its education software business. There was £6.3m of consideration received and the net assets disposed amounted to £17.7m, giving a loss of £12.8m, after accounting for disposal costs of £1.4m.

On 21 December 2012, the Group agreed to dispose its UK data hosting operations. There was £nil cash consideration and the net assets disposed amounted to £7.8m, giving a loss of £11.5m, after accounting for disposal costs of £3.7m.

6. Net debt

Figure 4: Net debt

At 31 December	**2012 £m**	2011 £m
Group – cash and cash equivalents	**142.8**	194.6
Group – loans	**(699.5)**	(819.4)
Group – obligations under finance leases	**(50.2)**	(45.0)
Group recourse net debt	**(606.9)**	(669.8)
Joint venture – cash and cash equivalents	**55.8**	60.2
Joint venture – loans	**(3.9)**	(7.9)
Joint venture – obligations under finance leases	**(0.6)**	(0.9)
Total recourse net debt	**(555.6)**	(618.4)
Group non recourse debt	**(25.1)**	(15.5)
Total net debt	**(580.7)**	(633.9)

6.1 Group recourse net debt

Group recourse net debt reduced by £62.9m to £606.9m. Sources of funding are described in Section 8 below.

Cash and cash equivalents includes encumbered cash of £7.5m (2011: £5.5m). This is cash relating to customer advance payments.

6.2 Group non recourse debt

The Group's debt is non recourse if no Group company other than the relevant borrower 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 increased by £9.6m to £25.1m. The increase is mainly due to additional asset financing on the National Physical Laboratory contract.

7. Pensions

The Group is a sponsor of a number of defined benefit schemes and defined contribution schemes. At 31 December 2012, the net retirement benefit asset included in the balance sheet arising from our defined benefit pension scheme obligations was £14.1m (2011: £16.8m), on a pension scheme asset base of £1.9bn.

Figure 5: Defined benefit pension schemes

At 31 December	**2012 £m**	2011 £m
Group schemes – non contract specific	**45.6**	58.8
Contract specific schemes:		
– reimbursable	**(214.7)**	(188.7)
– not certain to be reimbursable	**(32.2)**	(26.5)
Net retirement benefit liabilities	**(201.3)**	(156.4)
Intangible assets arising from rights to operate franchises and contracts	**6.2**	6.3
Reimbursable rights debtor	**214.7**	188.7
Deferred tax liabilities	**(5.5)**	(21.8)
Net balance sheet assets	**14.1**	16.8

The total pension charge included in operating profit for the year ended 31 December 2012, including the proportionate share of joint ventures, increased to £112.5m (2011: £112.3m). Within this charge, the Group's contributions to UK and other defined contribution pension schemes increased to £85.1m (2011: £80.4m). The service charge relating to the Group's defined benefit schemes decreased to £27.4m (2011: £31.9m) principally as a result of a £6.1m curtailment gain relating to the disposal of the Technical Services business. This curtailment gain resulted from active members of SPLAS becoming deferred members creating a reduction in scheme liabilities. The gain is recognised in the income statement within the gain on disposal of the Technical Services business.

Serco has three main types of scheme which are accounted for as defined benefit pension schemes. Each type has its own accounting treatment under IFRS. 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 year to the consolidated statement of comprehensive income (the SOCI);
- 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 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 year to the SOCI, 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 either to the right of cost reimbursement or because the deficit will, in general, 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 2012, SPLAS had a surplus of £69.7m (2011: surplus of £122.3m). This is calculated under IAS 19 using market-derived rates at 31 December 2012. It therefore reflects the effect of the market conditions through the actual investment returns in the year and the impact of an increase in inflation assumptions and a decrease in the applicable discount rate.

The estimated actuarial deficit of SPLAS as at 31 December 2012 was approximately £10.9m (2011: £27.3m). The value calculated in the latest triennial review was a deficit of £141m at 6 April 2009. We continue to review the level of benefits and contributions under the scheme in the light of our business needs and changes to pension legislation.

Retirement benefit obligations reduced by £50.5m as a result of the disposal of Serco GmbH. The acquisition of Vertex Public Services Limited included the acquisition of £13.4m of net retirement benefit obligations as at 11 June 2012.

Figure 6 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 6: Pension assumption sensitivities

	Assumption	Change in assumption	Change in liability
Discount rate	4.3%	+0.5% (0.5)%	(9)% +10%
Price inflation	3.0% (RPI) and 2.20% (CPI)	+0.5% (0.5)%	+9% (8)%
Salary	3.40%	+0.5% (0.5)%	+1% (1)%
Longevity	21.0 – 24.6 *	Increase by one year	+2%

*Post retirement mortality range for male and female, current and future pensioners.

8. Treasury

The Group's committed bank credit facilities total £730.0m (2011: £726.7m). As at 31 December 2012 £177.6m had been drawn down on bank facilities (2011: £241.3m). The bank facility is solely comprised of a £730.0m syndicated revolving credit facility, which matures in March 2017. It was signed in March 2012 and replaced all existing committed bank credit facilities.

In addition to the bank credit facility, Serco has US private placements totalling £460.8m which will be repaid between 2013 and 2023. All of the Group's credit facilities detailed above are unsecured.

9. Going concern

The Directors have acknowledged the guidance 'Going Concern and Liquidity Risk: Guidance for Directors of UK Companies 2009' and 'An update for Directors of Listed Companies: Responding to Increased Country and Currency Risk in Financial Reports', published by the Financial Reporting Council in October 2009 and January 2012 respectively. Whilst the current economic environment remains uncertain, the broad base of our contract portfolio and with over 90% of our customers being government bodies, the Group is well placed to manage its business risks successfully and has adequate resources to continue in operational existence for the foreseeable future.

The Group's revenues are largely derived from long-term contracts with governments. Historically, these contracts have been relatively resilient to changes in the general economy. The contract portfolio is diverse and a downturn in any particular market, sector or geography has a more limited effect on the Group as a whole. In addition, with an order book of £19.1bn and high visibility of future revenue streams (92% in 2013; 79% in 2014 and 70% in 2015), the Group is well placed to manage its business risks despite the current uncertain economic climate.

As at 31 December 2012, the Group's principal financing is through a revolving credit facility and US private placements. The Group has approximately £1,191m of committed credit facilities. The headroom on the facilities was approximately £552m as at 31 December 2012. Scheduled repayments in 2013 in respect of US private placement maturities are £23.4m in August. The revolving credit facility matures in March 2017 whilst repayments of the US private placements occur between 2013 and 2023. The Group fully expects to meet these repayments through operational cash flows. Based on the information set out above, the Directors believe that it is appropriate to prepare the financial statements on a going concern basis.

Financial Statements

Consolidated Income Statement

For the year ended 31 December

		2012			2011
		Before exceptional items	Exceptional items	**Total**	
	Note	£m	£m	**£m**	£m
Continuing operations					
Revenue	2	4,913.0	-	**4,913.0**	4,646.4
Cost of sales		(4,169.5)	-	**(4,169.5)**	(3,946.0)
Gross profit		743.5	-	**743.5**	700.4
Administrative expenses		(428.7)	-	**(428.7)**	(410.3)
Adjusted operating profit		314.8	-	**314.8**	290.1
Other expenses – amortisation of intangibles arising on acquisition		(24.1)	-	**(24.1)**	(20.0)
Other expenses – acquisition-related costs		(3.7)	-	**(3.7)**	(3.9)
Exceptional net profit on disposal of subsidiaries and operations	9	-	5.6	**5.6**	-
Exceptional donation to Serco Foundation	3	-	(5.0)	**(5.0)**	-
Operating profit		287.0	0.6	**287.6**	266.2
Investment revenue	4	12.4	-	**12.4**	12.2
Exceptional other gain	5	-	51.1	**51.1**	-
Finance costs	4	(49.1)	-	**(49.1)**	(40.1)
Profit before tax		250.3	51.7	**302.0**	238.3
Tax		(62.6)	6.5	**(56.1)**	(63.1)
Profit for the year		187.7	58.2	**245.9**	175.2
Attributable to:					
Equity owners of the Company		187.1	58.2	**245.3**	175.1
Non-controlling interest		0.6	-	**0.6**	0.1
Earnings per share (EPS)					
Basic EPS	7	38.09p	11.85p	**49.94p**	35.70p
Diluted EPS	7	37.21p	11.57p	**48.78p**	35.08p

Adjusted operating profit is stated before net profit on disposals of subsidiaries and operations, the exceptional donation to the Serco Foundation, amortisation of intangibles arising on acquisitions and acquisition-related costs.

Consolidated Statement of Comprehensive Income

For the year ended 31 December .

	Note	2012 £m	2011 £m
Profit for the year		**245.9**	175.2
Other comprehensive income for the year:			
Net actuarial loss on defined benefit pension schemes[1]	16	**(201.2)**	(51.0)
Actuarial gain on reimbursable rights[1]	16	**110.2**	116.5
Net exchange loss on translation of foreign operations[2]		**(17.9)**	(2.2)
Fair value loss on cash flow hedges during the year[2]		**(5.5)**	(35.7)
Tax relating to components of other comprehensive income[3]		**29.9**	(5.9)
Recycling of cumulative hedging and translation reserve[2]		**-**	0.3
Total comprehensive income for the year		**161.4**	197.2
Attributable to:			
Equity owners of the Company		**160.8**	197.1
Non-controlling interest		**0.6**	0.1

1 Recorded in retirement benefit obligations reserve in the consolidated statement of changes in equity.
2 Recorded in hedging and translation reserve in the consolidated statement of changes in equity.
3 Of the tax charge a credit of £25.4m (2011: debit of £14.7m) was recorded in the retirement benefit obligations reserve and a credit of £4.5m (2011: £8.8m) was recorded in the hedging and translation reserve.

Consolidated Statement of Changes in Equity

For the year ended 31 December

	Share capital £m	Share premium account £m	Capital redemption reserve £m	Retained earnings £m	Retirement benefit obligations reserve £m	Share-based payment reserve £m	Own shares reserve £m	Hedging and translation reserve £m	Total equity £m	Non-controlling interest £m
At 1 January 2011	9.9	306.7	0.1	568.5	(142.8)	58.7	(27.5)	67.7	841.3	-
Total comprehensive income for the year	-	-	-	175.1	50.8	-	-	(28.8)	197.1	0.1
Shares transferred to option holders on exercise of share options	-	16.0	-	-	-	(2.0)	3.3	-	17.3	-
Dividends paid	-	-	-	(37.3)	-	-	-	-	(37.3)	(0.1)
Expense in relation to share-based payment	-	-	-	-	-	11.2	-	-	11.2	-
Tax credit in relation to share-based payments	-	-	-	-	-	(1.8)	-	-	(1.8)	-
Purchase of own shares for Employee Share Ownership Trust (ESOT)	-	-	-	-	-	-	(24.0)	-	(24.0)	-
At 1 January 2012	**9.9**	**322.7**	**0.1**	**706.3**	**(92.0)**	**66.1**	**(48.2)**	**38.9**	**1,003.8**	**-**
Total comprehensive income for the year	**-**	**-**	**-**	**245.3**	**(65.6)**	**-**	**-**	**(18.9)**	**160.8**	**0.6**
Shares transferred to option holders on exercise of share options	**0.1**	**3.8**	**-**	**-**	**-**	**(3.6)**	**5.4**	**-**	**5.7**	**-**
Dividends paid	**-**	**-**	**-**	**(41.9)**	**-**	**-**	**-**	**-**	**(41.9)**	**(0.4)**
Expense in relation to share-based payment	**-**	**-**	**-**	**-**	**-**	**12.1**	**-**	**-**	**12.1**	**-**
Tax charge in relation to share-based payments	**-**	**-**	**-**	**-**	**-**	**3.1**	**-**	**-**	**3.1**	**-**
Purchase of own shares for Employee Share Ownership Trust (ESOT)	**-**	**-**	**-**	**-**	**-**	**-**	**(16.0)**	**-**	**(16.0)**	**-**
Change in non-controlling interest	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**1.1**
At 31 December 2012	**10.0**	**326.5**	**0.1**	**909.7**	**(157.6)**	**77.7**	**(58.8)**	**20.0**	**1,127.6**	**1.3**

Consolidated Balance Sheet

At 31 December

	Note	2012 £m	2011 £m
Non-current assets			
Goodwill		**1,312.3**	1,259.0
Other intangible assets		**226.9**	184.9
Property, plant and equipment		**190.6**	194.8
Trade and other receivables		**260.5**	261.9
Retirement benefit assets	16	**69.7**	122.3
Deferred tax assets		**43.3**	28.2
Derivative financial instruments		**0.1**	2.0
		2,103.4	2,053.1
Current assets			
Inventories		**64.4**	58.8
Trade and other receivables		**856.1**	798.6
Current tax assets		**21.0**	9.2
Cash and cash equivalents		**198.6**	254.8
Derivative financial instruments		**3.6**	7.6
		1,143.7	1,129.0
Total assets		**3,247.1**	3,182.1
Current liabilities			
Trade and other payables		**(883.1)**	(804.2)
Current tax liabilities		**(14.0)**	(17.8)
Obligations under finance leases		**(10.8)**	(10.3)
Provisions	12	**(11.5)**	(10.4)
Loans		**(64.6)**	(206.6)
Derivative financial instruments		**(13.8)**	(12.3)
		(997.8)	(1,061.6)
Non-current liabilities			
Trade and other payables		**(42.5)**	(61.4)
Obligations under finance leases		**(40.0)**	(35.6)
Loans		**(665.1)**	(636.2)
Derivative financial instruments		**(24.5)**	(26.3)
Retirement benefit obligations	16	**(271.0)**	(278.7)
Provisions	12	**(46.2)**	(56.2)
Deferred tax liabilities		**(31.1)**	(22.3)
		(1,120.4)	(1,116.7)
Total liabilities		**(2,118.2)**	(2,178.3)
Net assets		**1,128.9**	1,003.8
Equity			
Share capital		**10.0**	9.9
Share premium account		**326.5**	322.7
Capital redemption reserve		**0.1**	0.1
Retained earnings		**909.7**	706.3
Retirement benefit obligations reserve		**(157.6)**	(92.0)
Share-based payment reserve		**77.7**	66.1
Own shares reserve		**(58.8)**	(48.2)
Hedging and translation reserve		**20.0**	38.9
Equity attributable to owners of the Company		**1,127.6**	1,003.8
Non-controlling interest		**1.3**	-
Total equity		**1,128.9**	1,003.8

The financial statements were approved by the Board of Directors on 4 March 2013 and signed on its behalf by:

Christopher Hyman — Chief Executive

Andrew Jenner — Finance Director

Consolidated Cash Flow Statement

For the year ended 31 December

	Note	**2012 £m**	2011 £m
Net cash inflow from operating activities before special pension contribution		**303.4**	257.0
Special contribution to defined benefit pension schemes		**-**	(40.0)
Net cash inflow from operating activities	10	**303.4**	217.0
Investing activities			
Interest received		**3.1**	3.4
Increase in security deposits		**-**	(8.2)
Proceeds from disposal of property, plant and equipment		**21.0**	9.2
Proceeds from disposal of intangible assets		**0.1**	-
Proceeds on disposal of subsidiaries and operations	9	**131.0**	-
Acquisition of subsidiaries, net of cash acquired (excluding acquisition-related costs)	8	**(141.8)**	(325.3)
Purchase of other intangible assets		**(49.9)**	(35.2)
Purchase of property, plant and equipment		**(52.7)**	(49.7)
Net cash outflow from investing activities		**(89.2)**	(405.8)
Financing activities			
Interest paid		**(47.4)**	(35.8)
Dividends paid	6	**(41.9)**	(37.3)
Non-controlling interest dividends paid		**(0.4)**	(0.1)
Cash inflow from matured derivative financial instruments		**-**	4.9
Repayment of loans		**(366.6)**	(559.8)
Repayment of non recourse loans		**(8.7)**	(7.9)
New loan advances		**216.8**	818.4
Capital element of finance lease repayments		**(2.9)**	(10.7)
Purchase of own shares for Employee Share Ownership Trust (ESOT)		**(16.0)**	(24.0)
Proceeds from issue of share capital and exercise of share options		**5.7**	17.3
Net cash (outflow)/inflow from financing activities		**(261.4)**	165.0
Net decrease in cash and cash equivalents		**(47.2)**	(23.8)
Cash and cash equivalents at beginning of year		**254.8**	279.3
Net exchange loss		**(9.0)**	(0.7)
Cash and cash equivalents at end of year		**198.6**	254.8

Notes to the consolidated financial statements

1. General information, going concern and accounting policies

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

The financial information in this announcement does not constitute the Company's statutory accounts for the years ending 31 December 2012 or 2011, but is derived from these accounts.

Statutory accounts for 2011 have been delivered to the Registrar of Companies and those for 2012 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 S498 (2) or (3) or the Companies Act 2006 or equivalent preceding legislation.

The preliminary announcement has been prepared in accordance with International Financial Reporting Standards (IFRSs) adopted for use in the European Union. Whilst the financial information included in this preliminary announcement has been computed in accordance with IFRSs, this announcement does not itself contain sufficient information to comply with IFRSs. The Company expects to publish full Group and parent company only financial statements that comply with IFRSs and FRS101 respectively, in April 2013.

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

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Operating Review on pages 9 to 27. The Finance Review includes a summary of the Group's financial position, its cash flows and borrowing facilities.

The Group's revenues are largely derived from long-term contracts with governments. Historically, these contracts have been relatively resilient to changes in the general economy. The contract portfolio is diverse and a downturn in any particular market, sector or geography has a more limited effect on the Group as a whole. In addition, with an order book of £19.1bn and high visibility of future revenue streams, the Group is well placed to manage its business risks despite the current economic climate.

The Group's committed bank credit facilities total £730.0m. As at 31 December 2012, £177.6m had been drawn down on these combined bank facilities (2011: £241.3m). In addition to the bank credit facilities, Serco has US private placements totalling £460.8m which will be repaid between 2013 and 2023. The headroom on the Group's total facilities as at 31 December 2012 was approximately £552m.

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the condensed set of financial statements.

2. Segmental information

Information reported to the Chief Operating Decision Maker for the purposes of resource allocation and assessment of segment performance focuses on the categories of customer identified using their respective markets. Details of the different products and services provided by each operating segment are included in this report. From 1 April 2012, the Group has reapportioned its business into four segments resulting in a restatement of the 2011 segmental information. The Group's reportable operating segments under IFRS 8 Operating Segments are:

Reportable Segments	**Operating Segments**
UK & Europe	UK and Europe frontline services in areas including home affairs, defence, health, transportation and local government direct services;
Americas	US defence, intelligence and federal civilian agencies operations, and Canadian operations;
AMEAA	Frontline contracts in Australasia, Middle East, Asia (including Hong Kong and India) and Africa; and
Global Services	Global BPO middle and back office services

The following is an analysis of the Group's revenue and results by reportable segment in the year ended 31 December 2012.

Reportable segments **Year ended 31 December 2012**	**UK & Europe 2012 £m**	**Americas 2012 £m**	**AMEAA 2012 £m**	**Global Services 2012 £m**	**Total 2012 £m**
Revenue	**2,561.1**	**753.4**	**883.0**	**715.5**	**4,913.0**
Result					
Segment Adjusted operating profit	**177.8**	**55.2**	**64.3**	**62.1**	**359.4**
Amortisation of intangibles arising on acquisition	**(0.4)**	**(13.7)**	**(0.3)**	**(9.7)**	**(24.1)**
Acquisition-related costs	**(0.1)**	**-**	**(1.8)**	**(1.8)**	**(3.7)**
Exceptional net profit on disposal of subsidiaries and operations	**31.0**	**-**	**-**	**(25.4)**	**5.6**
Segment result	**208.3**	**41.5**	**62.2**	**25.2**	**337.2**
Exceptional donation to Serco Foundation					**(5.0)**
Corporate expenses					**(44.6)**
Operating profit					**287.6**
Investment revenue					**12.4**
Exceptional other gain					**51.1**
Finance costs					**(49.1)**
Profit before tax					**302.0**
Tax					**(56.1)**
Profit for the year					**245.9**

Group Adjusted operating profit is £314.8m and comprises segment Adjusted operating profit of £359.4m less Corporate expenses of £44.6m.

2. Segmental information (continued)

Reportable segments **Year ended 31 December 2011- restated**	**UK & Europe 2011 £m**	**Americas 2011 £m**	**AMEAA 2011 £m**	**Global Services 2011 £m**	**Total 2011 £m**
Revenue	2,595.2	868.2	672.1	510.9	4,646.4
Result					
Segment Adjusted operating profit	177.6	73.0	51.4	34.0	336.0
Amortisation of intangibles arising on acquisition	(0.2)	(13.6)	-	(6.2)	(20.0)
Acquisition-related costs	(0.2)	-	-	(3.7)	(3.9)
Segment result	177.2	59.4	51.4	24.1	312.1
Corporate expenses					(45.9)
Operating profit					266.2
Investment revenue					12.2
Finance costs					(40.1)
Profit before tax					238.3
Tax					(63.1)
Profit for the year					175.2

Group Adjusted operating profit is £290.1m and comprises segment Adjusted operating profit of £336.0m less Corporate expenses of £45.9m.

	2012 £m	2011 £m
Segment assets comprise:		
Goodwill	**1,312.3**	1,259.0
Other intangible assets	**226.9**	184.9
Property, plant and equipment	**190.6**	194.8
Trade and other receivables – non-current	**260.5**	261.9
Retirement benefit assets	**69.7**	122.3
Inventories	**64.4**	58.8
Trade and other receivables – current	**856.1**	798.6
Total segment assets	**2,980.5**	2,880.3
Unallocated assets	**266.6**	301.8
Consolidated total assets	**3,247.1**	3,182.1

Segment assets exclude all derivative financial instruments, current and deferred taxation assets and cash.

	2012 £m	2011 £m
Segment liabilities comprise:		
Trade and other payables – current	**(883.1)**	(804.2)
Trade and other payables – non-current	**(42.5)**	(61.4)
Retirement benefit obligations	**(271.0)**	(278.7)
Total segment liabilities	**(1,196.6)**	(1,144.3)
Unallocated liabilities	**(921.6)**	(1,034.0)
Consolidated total liabilities	**(2,118.2)**	(2,178.3)

Segment liabilities consist of all trade and other payables and retirement benefit obligations.

2. Segmental information (continued)

Geographic information

	Revenue 2012 £m	Non-current assets* 2012 £m	Revenue 2011 £m	Non-current assets* 2011 £m
United Kingdom	**2,731.4**	**1,012.0**	2,587.3	1,008.8
United States	**694.4**	**437.4**	802.1	460.8
Australia	**824.8**	**189.4**	660.4	61.5
Other countries	**662.4**	**421.2**	596.6	491.8
Total	**4,913.0**	**2,060.0**	4,646.4	2,022.9

*Non-current assets exclude financial instruments and deferred tax assets.

Revenues from external customers are attributed to individual countries on the basis of the location of the customer.

3. Exceptional donation to Serco Foundation

	2012 £m	2011 £m
Exceptional donation to Serco Foundation	**5.0**	-

To mark Serco's 25th year as a publicly traded company dedicated to service excellence, we have established the Serco Foundation as an independent charitable foundation. An exceptional payment of £5.0m has been made in the year to establish the charitable foundation.

4. Investment revenue and finance costs

	2012 £m	2011 £m
Interest receivable on other loans and deposits	**3.2**	4.0
Net interest receivable on retirement benefit obligations	**9.2**	8.2
Investment revenue	**12.4**	12.2
Interest payable on non recourse loans	**(0.9)**	(1.0)
Interest payable on obligations under finance leases	**(2.9)**	(2.1)
Interest payable and amortisation of capitalised financing transaction costs on other loans	**(43.4)**	(35.6)
Movement in discount on provisions and deferred consideration	**(1.9)**	(1.4)
Finance costs	**(49.1)**	(40.1)
Net finance costs	**(36.7)**	(27.9)

5. Exceptional other gain

	2012 £m	2011 £m
Gain on step acquisition accounting of joint venture (note 8)	**51.1**	-

On 16 November 2012 Serco acquired the remaining 50% equity stake in DMS, taking its equity ownership to 100%. DMS was formerly accounted for as a joint venture and following the acquisition of further shares it became a wholly owned subsidiary. In accordance with IFRS 3 (Revised 2008) – Business Combinations, before accounting for the purchase of the remaining equity stake, the value of the previously held 50% shareholding was restated to fair value on the acquisition date. This resulted in an exceptional gain of £51.1m being recognised in the income statement.

6. Dividends

	2012 £m	2011 £m
Amounts recognised as distributions to equity holders in the year:		
Final dividend for the year ended 31 December 2011 of 5.9p per share on 490.2 million ordinary shares (2011: Final dividend for the year ended 31 December 2010 of 5.15p per share on 488.5 million ordinary shares)	**28.9**	25.2
Interim dividend for the year ended 31 December 2012 of 2.65p per share on 488.2 million ordinary shares (2011: Interim dividend for the year ended 31 December 2011 of 2.50p per share on 486.6 million ordinary shares)	**13.0**	12.1
	41.9	37.3
Proposed final dividend for the year ended 31 December 2012 of 7.45p per share on 488.3 million ordinary shares (2011: 5.90p on 489.1 million ordinary shares)	**36.4**	28.9

The proposed final dividend for 2012 is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. A dividend waiver is effective for those shares held on behalf of the Company by its Employee Share Ownership Trust.

7. 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 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

	2012 Millions	2011 Millions
Weighted average number of ordinary shares for the purpose of basic EPS	**491.2**	490.5
Effect of dilutive potential ordinary shares: share options	**11.7**	8.6
Weighted average number of ordinary shares for the purpose of diluted EPS	**502.9**	499.1

Earnings per share

	Earnings 2012 £m	**Per share amount 2012 Pence**	Earnings 2011 £m	Per share amount 2011 Pence
Earnings for the purpose of basic EPS being net profit attributable to the equity holders of the parent	**245.3**	**49.94**	175.1	35.70
Add back:				
Exceptional profit on disposal of subsidiaries, net of tax credit of £5.3m (2011: £nil)	**(10.9)**	**(2.22)**	-	-
Exceptional donation to Serco Foundation, net of tax of £1.2m (2011: £nil)	**3.8**	**0.77**	-	-
Exceptional gain on step acquisition, net of tax of £nil (2011: £nil)	**(51.1)**	**(10.40)**	-	-
Amortisation of intangible assets arising on acquisition, net of tax of £5.4m (2011: £4.3m)	**18.7**	**3.81**	15.7	3.20
Acquisition-related costs, net of tax of £0.5m (2011: £0.5m)	**3.2**	**0.65**	3.4	0.69
Adjusted earnings	**209.0**	**42.55**	194.2	39.59
Earnings for the purpose of basic EPS	**245.3**	**49.94**	175.1	35.70
Effect of dilutive potential ordinary shares	**-**	**(1.16)**	-	(0.62)
Diluted EPS	**245.3**	**48.78**	175.1	35.08

8. Acquisitions

During the year, the Group completed the following acquisitions which have been accounted for in accordance with IFRS 3 Business Combinations (2008).

8 (a) Vertex Public Services Limited

On 11 June 2012, Serco acquired 100% of the issued share capital of Vertex Public Services Limited (Vertex), a provider of high quality business process outsourcing services to UK local and central government. The cash cost of the acquisition was £55.5m.

Net assets acquired were:	Book value £m	Fair value adjustments £m	Provisional fair value £m
Goodwill	23.0	(23.0)	-
Intangible assets	3.7	3.7	7.4
Property, plant and equipment	1.2	(0.6)	0.6
Deferred tax asset	-	3.8	3.8
Trade and other receivables	28.5	(0.7)	27.8
Trade and other payables	(23.3)	-	(23.3)
Retirement benefit obligations	(13.4)	-	(13.4)
Provisions	-	(4.9)	(4.9)
Net liabilities acquired	19.7	(21.7)	(2.0)
Goodwill			57.5
Total consideration			55.5
Satisfied by:			
Cash			55.5
Working capital adjustment			-
Total consideration			55.5
Net cash outflow arising on acquisition:			
Purchase consideration			55.5

The provisional fair value of the financial assets acquired includes trade receivables with a fair value of £24.3m and a gross contractual value of £24.4m.

The goodwill of £57.5m arising from the acquisition represents future opportunities in the UK outsourced contact centre services industry. None of the goodwill is expected to be deductible for corporate income tax purposes.

£1.0m of acquisition-related costs incurred on the Vertex acquisition have been expensed to the income statement.

Vertex Public Services Limited contributed £64.0m revenue and £8.4m to the Group's Adjusted operating profit for the period between the date of acquisition and the balance sheet date. If the acquisition of Vertex Public Services Limited had been completed on the first day of the financial year, Group Revenue for the period would have been £5,041.0m and the Group's Adjusted operating profit would have been £331.6m.

8. Acquisitions (continued)

8 (b) DMS Maritime Pty Limited

On 16 November 2012, Serco acquired the remaining 50% stake in DMS Maritime Pty Limited from our joint venture partner P&O Maritime Services. The transaction strengthens Serco's position as a leading defence services provider in Australia and in the growing marine services market. The initial cash cost of the acquisition was £69.1m (A$106.3m). DMS was formerly accounted for as a joint venture and following the acquisition of further shares it became a wholly owned subsidiary. In accordance with IFRS 3 (Revised) the difference between the fair value of the equity owned prior to the acquisition of £55.3m and the book value of the joint venture of £4.2m was recognised in the consolidated income statement, with the gain of £51.1m reported in the exceptional other gain line.

Net assets acquired were:	Book value £m	Fair value adjustments £m	Provisional fair value £m
Intangible assets	-	32.7	32.7
Property, plant and equipment	4.8	-	4.8
Inventories	5.5	-	5.5
Trade and other receivables	10.0	-	10.0
Loans	(14.8)	-	(14.8)
Bank overdrafts	(0.4)	-	(0.4)
Deferred tax liability	(0.5)	(9.8)	(10.3)
Provisions	(0.4)	-	(0.4)
Net assets acquired	4.2	22.9	27.1
Gain on remeasurement to fair value			(51.1)
Goodwill			93.1
Total consideration			69.1
Satisfied by:			
Cash			69.1
Contingent consideration			-
Total consideration			69.1
Net cash outflow arising on acquisition:			
Purchase consideration			69.1

The provisional fair value of the financial assets acquired includes trade receivables with a fair value of £5.9m and a gross contractual value of £6.0m

The goodwill of £93.1m arising from the acquisition represents future opportunities in the Australian marine services industry. None of the goodwill is expected to be deductible for corporate income tax purposes. £1.8m of acquisition-related costs incurred on the above acquisitions have been expensed to the income statement.

8. Acquisitions (continued)

The additional stake in DMS Maritime Pty Limited contributed £5.9m to revenue and £1.5m to the Group's Adjusted operating profit for the period between the date of acquisition and the balance sheet date. If the acquisition of DMS Maritime Pty Limited had been completed on the first day of the financial year, Group revenue for the period £4,948.8m and the Group's Adjusted operating profit would have been £321.3m.

8 (c) Other Acquisitions

Anglia Support Partnership

On 13 April 2012, Serco entered into an agreement to acquire the trade and assets of Anglia Support Partnership (ASP). ASP provides support services to the Cambridge and Peterborough NHS Foundation Trust, together with a further five partnering NHS organisations. The initial cash cost of the business combination was £5.2m. In addition, £3.5m of deferred consideration was paid on 30 September 2012. Up to a further £7.2m of deferred consideration is payable from 2013 to 2020, contingent on the financial performance of the acquired business. The fair value of this deferred contingent consideration is £3.3m. The provisional fair value of net assets acquired totalled £4.0m.

£0.8m of acquisition-related costs incurred on this acquisition have been expensed to the income statement.

Due to the immaterial nature of this acquisition, full disclosures under IFRS 3 are not presented.

Priority Properties North West Limited

On 1 June 2012, Serco acquired 100% of the issued share capital of Priority Properties North West Limited (PPNW). PPNW is a property management company specialising in the provision of short and long term housing. The cash cost of the acquisition in the period was £2.7m. In addition, deferred consideration of up to £1.1m is payable contingent on financial performance in the period to 31 January 2013. The fair value of this deferred, contingent consideration is £0.5m. The provisional fair value of net assets acquired totalled £1.8m.

£0.1m of acquisition-related costs incurred on this acquisition have been expensed to the income statement.

Due to the immaterial nature of this acquisition, full disclosures under IFRS 3 are not presented.

8. Acquisitions (continued)

Other acquisitions (in aggregate):

Net assets acquired were:	Book value £m	Fair value adjustments £m	Provisional fair value £m
Intangible assets	**4.3**	**-**	**4.3**
Property, plant and equipment	**1.2**	**(0.6)**	**0.6**
Trade and other receivables	**2.1**	**-**	**2.1**
Cash and cash equivalents	**0.8**	**-**	**0.8**
Trade and other payables	**(1.2)**	**-**	**(1.2)**
Tax liabilities	**(0.1)**	**-**	**(0.1)**
Provisions	**-**	**(0.7)**	**(0.7)**
Net assets acquired	**7.1**	**(1.3)**	**5.8**
Goodwill			**9.4**
Total consideration			**15.2**

Satisfied by:	
Cash	**11.4**
Contingent consideration arrangement	**3.8**
Total consideration	**15.2**

Net cash outflow arising on acquisitions:	
Purchase consideration	**11.4**
Cash and cash equivalents acquired	**(0.8)**
Net cash outflow arising on acquisitions	**10.6**

Serco Listening Company Limited (formerly The Listening Company Limited)

During the year, a cash payment of £6.6m was made in respect of deferred contingent consideration payable following the acquisition of The Listening Company Limited in 2011.

9. Disposals

During the year, the Group generated the following net profit on disposal of subsidiaries and operations:

	2012 **£m**	2011 £m
Gain on disposal of Serco Technical Services	**57.6**	-
Loss on disposal of Serco GmbH	**(27.7)**	-
Loss on disposal of UK data hosting operations	**(11.5)**	-
Loss on disposal of education software business	**(12.8)**	-
Net profit on disposal of subsidiaries and operations	**5.6**	-

9 (a) Serco Technical Services

On 29 June 2012, the Group disposed of its Technical Services business which provides consulting and project solutions primarily to the UK civil and nuclear defence markets for a consideration of £135.3m.

The net assets at the date of disposal were:	**£m**
Goodwill	**64.4**
Intangible assets	**0.8**
Property, plant and equipment	**1.6**
Trade and other receivables	**13.2**
Cash and cash equivalents	**0.6**
Trade and other payables	**(5.1)**
Deferred tax liabilities	**(5.2)**
Net assets disposed	**70.3**

The profit on disposal is calculated as follows:

	£m
Cash consideration	**135.3**
Less:	
Net assets disposed	**(70.3)**
Disposal-related costs	**(7.4)**
Profit on disposal	**57.6**

The net cash inflow arising on disposal is as follows:

	£m
Consideration received	**135.3**
Less:	
Cash and cash equivalents disposed	**(0.6)**
Disposal-related costs paid during the period	**(4.9)**
Net cash inflow on disposal	**129.8**

9. Disposals (continued)

9 (b) Serco GmbH

On 29 June 2012, the Group disposed of its interest in Serco GmbH. The fair value of consideration receivable is £nil. The business provides support services for the German air defence radar systems, engineering and administrative support services for the defence sector as well as training services, facilities management, field installation and maintenance services, and IT consulting and related services.

The net assets at the date of disposal were:	£m
Goodwill	**22.0**
Intangible assets	**1.2**
Property, plant and equipment	**6.0**
Deferred tax asset	**5.2**
Trade and other receivables	**21.4**
Loans receivable	**25.9**
Cash and cash equivalents	**0.6**
Trade and other payables	**(8.6)**
Bank overdrafts	**(1.3)**
Retirement benefit obligations	**(50.5)**
Provisions	**(0.1)**
Net assets disposed	**21.8**

The loss on disposal is calculated as follows:

	£m
Net assets disposed	**(21.8)**
Disposal-related costs	**(5.9)**
Loss on disposal	**(27.7)**

The net cash outflow arising on disposal is as follows:

	£m
Cash and cash equivalents disposed	**(0.6)**
Disposal-related costs paid during the period	**(2.9)**
Net cash outflow on disposal	**(3.5)**

9. Disposals (continued)

9 (c) Other disposals

On 21 December 2012, the Group agreed to dispose its UK data hosting operations. There was £nil cash consideration and the net assets disposed amounted to £7.8m, giving a loss of £11.5m, after accounting for disposal costs of £3.7m.

On 31 December 2012, the Group disposed of its education software business. There was £6.3m of consideration received and the net assets disposed amounted to £17.7m, giving a loss of £12.8m, after accounting for disposal costs of £1.4m.

The net assets at the date of disposal were:	£m
Goodwill	**0.4**
Intangible assets	**2.6**
Property, plant and equipment	**11.4**
Trade and other receivables	**19.1**
Cash and cash equivalents	**0.2**
Trade and other payables	**(1.9)**
Finance lease obligations	**(6.2)**
Other loans	**(0.1)**
Net assets disposed	**25.5**

The loss on disposal is calculated as follows:	£m
Cash consideration	**6.3**
Less:	
Net assets disposed	**(25.5)**
Disposal-related costs	**(5.1)**
Loss on disposal	**(24.3)**

The net cash inflow arising on disposal is as follows:	£m
Consideration received	**6.3**
Less:	
Cash and cash equivalents disposed	**(0.2)**
Disposal-related costs paid during the period	**(1.4)**
Net cash inflow on disposal	**4.7**

10. Notes to the consolidated cash flow statement

Reconciliation of operating profit to net cash inflow from operating activities

	2012 £m	2011 £m
Operating profit for the year	**287.6**	266.2
Adjustments for:		
Share-based payment expense	**12.1**	11.2
Depreciation of property, plant and equipment	**51.4**	46.0
Amortisation and impairment of intangible assets	**45.7**	39.5
Exceptional profit on disposal of subsidiaries and operations	**(5.6)**	-
(Profit)/loss on disposal property, plant and equipment	**(0.9)**	0.5
Movement in provisions	**(19.8)**	(9.8)
Other non-cash movements	**(2.8)**	3.4
Operating cash inflow before movements in working capital	**367.7**	357.0
(Increase)/decrease in inventories	**(1.5)**	9.2
(Increase)/decrease in receivables	**(48.7)**	26.8
Increase/(decrease) in payables	**38.6**	(84.5)
Special contribution to defined benefit pension scheme	**-**	(40.0)
Cash generated by operations	**356.1**	268.5
Tax paid	**(52.7)**	(51.5)
Net cash inflow from operating activities	**303.4**	217.0

Additions to fixtures and equipment during the year amounting to £14.4m (2011: £29.6m) were financed by new finance leases.

11. Analysis of net debt

	At 1 January 2012 £m	**Cash flow £m**	**Acquisitions* £m**	**Disposals £m**	**Exchange differences £m**	**Non cash movements £m**	**At 31 December 2012 £m**
Cash and cash equivalents	**254.8**	**(46.6)**	**0.8**	**(1.4)**	**(9.0)**	**-**	**198.6**
Non recourse loans	**(15.5)**	**(9.7)**	**-**	**-**	**0.1**	**-**	**(25.1)**
Other loans	**(827.3)**	**136.2**	**(15.2)**	**(24.4)**	**27.3**	**-**	**(703.4)**
Obligations under finance leases	**(45.9)**	**2.9**	**-**	**6.2**	**0.2**	**(14.2)**	**(50.8)**
	(633.9)	**82.8**	**(14.4)**	**(19.6)**	**18.6**	**(14.2)**	**(580.7)**

	At 1 January 2011 £m	Cash flow £m	Acquisitions* £m	Disposals £m	Exchange differences £m	Non cash movements £m	At 31 December 2011 £m
Cash and cash equivalents	279.3	(32.2)	8.4	-	(0.7)	-	254.8
Non recourse loans	(23.7)	7.9	-	-	0.3	-	(15.5)
Other loans	(490.4)	(258.6)	(73.3)	-	(5.0)	-	(827.3)
Obligations under finance leases	(26.4)	10.7	(0.8)	-	0.2	(29.6)	(45.9)
	(261.2)	(272.2)	(65.7)	-	(5.2)	(29.6)	(633.9)

*Acquisitions represent the net cash/(debt) acquired on acquisition.

12. Provisions

	Employee related £m	Property £m	Contract £m	Other £m	Total £m
At 1 January 2011	11.0	6.6	8.0	14.0	39.6
Arising from acquisitions	0.4	3.6	29.2	6.9	40.1
Charged to income statement	4.5	0.4	-	-	4.9
Released to income statement	-	(0.2)	(1.2)	(3.2)	(4.6)
Utilised during the year	(1.0)	(1.5)	(7.5)	(0.1)	(10.1)
Unwinding of discount	-	0.3	0.2	-	0.5
Exchange differences	0.1	(0.3)	(2.6)	(1.0)	(3.8)
At 1 January 2012	**15.0**	**8.9**	**26.1**	**16.6**	**66.6**
Arising from acquisitions	**0.6**	**1.6**	**6.4**	**0.1**	**8.7**
Derecognised on disposal of subsidiary	**(0.1)**	**-**	**-**	**-**	**(0.1)**
Charged to income statement	**1.4**	**-**	**-**	**9.0**	**10.4**
Released to income statement	**(0.8)**	**(0.7)**	**(5.7)**	**(0.1)**	**(7.3)**
Utilised during the year	**(0.7)**	**(1.7)**	**(11.3)**	**(4.7)**	**(18.4)**
Unwinding of discount	**-**	**0.2**	**0.3**	**-**	**0.5**
Exchange differences	**(0.6)**	**(0.4)**	**(0.9)**	**(0.8)**	**(2.7)**
At 31 December 2012	**14.8**	**7.9**	**14.9**	**20.1**	**57.7**
Analysed as:					
Current	**-**	**0.9**	**5.2**	**5.4**	**11.5**
Non-current	**14.8**	**7.0**	**9.7**	**14.7**	**46.2**

* Included in amounts charged to income statement is an amount of £6.6m relating to businesses disposed in the year.

13. 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 and consolidated balance sheet is as follows:

Income statement	**2012 £m**	2011 £m
Revenue	**852.9**	819.3
Expenses	**(775.5)**	(737.7)
Operating profit	**77.4**	81.6
Investment revenue	**2.7**	2.7
Finance costs	**(0.5)**	(0.7)
Profit before tax	**79.6**	83.6
Tax	**(15.1)**	(20.0)
Share of post-tax results of joint ventures	**64.5**	63.6

Operating profit is after allocating £nil (2011: £1.0m) of costs incurred by Group.

Balance sheet	**2012 £m**	2011 £m
Non-current assets	**237.9**	218.4
Current assets	**146.0**	171.6
Current liabilities	**(134.4)**	(138.9)
Non-current liabilities	**(238.9)**	(212.5)
Net assets	**10.6**	38.6

14. Related party transactions

Transactions between the Company and its wholly owned subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note. Transactions between the Group and its joint venture undertakings are disclosed below, with the relevant proportion being eliminated on consolidation.

Trading transactions

During the year, Group companies entered into the following material transactions with joint ventures:

	2012 £m	2011 £m
Royalties and management fees receivable	**2.3**	1.5
Dividends receivable	**80.6**	64.3
	82.9	65.8

The following receivable balances relating to joint ventures were included in the consolidated balance sheet:

	2012 £m	2011 £m
Current:		
Loans	**1.0**	0.5

	2012 £m	2011 £m
Non-current:		
Loans	**2.6**	3.2

Joint venture receivable and loan amounts outstanding have arisen from transactions undertaken during the general course of trading, are unsecured, and will be settled in cash. Interest arising on loans is based on LIBOR, or its equivalent, with an appropriate margin. No guarantee has been given or received. No provisions are required for doubtful debts in respect of the amounts owed by the joint ventures.

15. Share-based payments

In accordance with IFRS 2, a charge of £12.1m (2011: £11.2m) relating to the fair value of share-based schemes has been charged to the consolidated income statement.

16. Defined benefit pension schemes

The Group operates defined benefit schemes for qualifying employees of its subsidiaries in the UK and Europe. In addition, the Group has interests in joint ventures, which operate defined benefit schemes for qualifying employees.

The assets of the funded schemes are held independently of the Group's assets in separate trustee administered funds. The Group's major schemes are valued by independent actuaries annually using the projected unit credit actuarial cost method. This reflects service rendered by employees to the dates of valuation and incorporates actuarial assumptions primarily regarding discount rates used in determining the present value of benefits, projected rates of salary growth, and long-term expected rates of return for scheme assets. Discount rates are based on the market yields of high-quality corporate bonds in the country concerned. Long-term expected rates of return for scheme assets are based on published brokers' forecasts for each category of scheme assets. Pension assets and liabilities in different defined benefit schemes are not offset unless the Group has a legally enforceable right to use the surplus in one scheme to settle obligations in the other scheme and intends to exercise this right.

The assets and liabilities of the schemes at 31 December are:

	Virtually certain costs reimbursed 2012 £m	**Not certain costs reimbursed 2012 £m**	**Non contract specific 2012 £m**	**Total 2012 £m**
Fair value of scheme assets	**283.6**	**504.8**	**1,155.8**	**1,944.2**
Present value of scheme liabilities	**(498.3)**	**(755.2)**	**(1,115.3)**	**(2,368.8)**
Net amount recognised	**(214.7)**	**(250.4)**	**40.5**	**(424.6)**
Members' share of deficit	**-**	**67.2**	**4.2**	**71.4**
Franchise adjustment	**-**	**151.0**	**-**	**151.0**
Effect of IFRIC 14	**-**	**-**	**0.9**	**0.9**
	(214.7)	**(32.2)**	**45.6**	**(201.3)**
Analysed as:				
Net pension liability	**(214.7)**	**(32.2)**	**(24.1)**	**(271.0)**
Net pension asset	**-**	**-**	**69.7**	**69.7**
Related assets				
Intangible assets	**-**	**6.2**	**-**	**6.2**
Trade and other receivables	**214.7**	**-**	**-**	**214.7**
	214.7	**6.2**	**-**	**220.9**

	Virtually certain costs reimbursed 2011 £m	Not certain costs reimbursed 2011 £m	Non contract specific 2011 £m	Total 2011 £m
Fair value of scheme assets	252.6	429.3	1,065.3	1,747.2
Present value of scheme liabilities	(441.3)	(594.9)	(1,001.3)	(2,037.5)
Net amount recognised	(188.7)	(165.6)	64.0	(290.3)
Members' share of deficit	-	43.7	2.2	45.9
Franchise adjustment	-	95.4	-	95.4
Effect of IFRIC 14	-	-	(7.4)	(7.4)
	(188.7)	(26.5)	58.8	(156.4)
Analysed as:				
Net pension liability	(188.7)	(26.5)	(63.5)	(278.7)
Net pension asset	-	-	122.3	122.3
Related assets				
Intangible assets	-	6.3	-	6.3
Trade and other receivables	188.7	-	-	188.7
	188.7	6.3	-	195.0

16. Defined benefit pension schemes (continued)

Assumptions in respect of the expected return on scheme assets are based on market expectations of returns over the life of the related obligation. Due consideration has been given to current market conditions as at 31 December 2012 in respect to inflation, interest, bond yields and equity performance when selecting the expected return on assets assumptions.

The expected yield on bond investments with fixed interest rates is derived from their market value. The yield on equity investments contains an additional premium (an 'equity risk premium') to compensate investors for the additional anticipated risks of holding this type of investment, when compared to bond yields. Management have concluded that an appropriate equity risk premium is 4.6% (2011: 4.6%).

The overall expected return on assets is calculated as the weighted average of the expected returns for the principal asset categories held by scheme.

	2012	2011
	%	%
Main assumptions:		
Rate of salary increases	**3.40**	3.30
Rate of increase in pensions in payment	**2.20 (CPI) and 3.00 (RPI)**	2.10 (CPI) and 2.90 (RPI)
Rate of increase in deferred pensions	**2.20 (CPI) and 3.00 (RPI)**	2.10 (CPI) and 2.90 (RPI)
Inflation assumption	**2.20 (CPI) and 3.00 (RPI)**	2.10 (CPI) and 2.90 (RPI)
Discount rate	**4.30**	4.70
Expected rates of return on scheme assets:		
Equities	**7.70**	7.70
Bonds except LDI	**4.30**	4.70
LDI	**3.90**	3.90
Gilts	**3.10**	3.10
Property	**4.35**	4.35
Cash and other	**0.50**	0.50
Annuity policies	**4.30**	4.70

	2012	2011
	Years	Years
Post-retirement mortality:		
Current pensioners at 65 – male	**21.0**	20.9
Current pensioners at 65 – female	**23.5**	23.4
Future pensioners at 65 – male	**22.5**	22.5
Future pensioners at 65 – female	**24.6**	24.6