Committed to managing risk effectively

The Group is exposed to a variety of risks that can adversely affect business and financial performance, or potentially damage our reputation. These risks may be industry wide or more specific to the Group. The Board recognises that creating shareholder returns is the reward for accepting a level of risk. The effective management of risk is therefore critical in supporting the delivery of the Group's strategic objectives.

Risk management framework

The Group has a well-established governance structure with appropriate internal control and risk management systems. Our approach is centred on the accepted 'three lines of defence' model, with ultimate oversight from the Board.

Defence	Responsibility	Actions
Oversight	Board	– Sets strategic objectives – Determines overall risk culture and appetite – Establishes organisational structure with defined lines of responsibility, delegated authorities and clear operating processes – Ultimate oversight of internal control and risk management systems
Third line	Group Audit	– Provides reasonable assurance that systems of risk management, internal control and governance are effective
Second line	Group Executive Committee Group functions including Risk	– Support divisions with 'first line' responsibilities – Coordinate and report on Group-level risks – Build risk capability and understanding
First line	Divisional Executive Committees Divisional management	– Identify, assess and report key risks – Regularly review and update divisional risk registers – Assign risk 'owners' – Implement risk mitigation plans

Many risk controls are embedded and evidenced in the Group's day-to-day management activities, including:

- Detailed KPI tracking in monthly divisional executive reports;
- Well-established bid evaluation controls; and
- Robust due diligence on acquisitions.

Prioritising and reporting risks

Each division regularly reviews and updates a detailed 'risk register', in which risks are identified and assessed in terms of both the probability of the risk occurring, and its potential impact. Risk is assessed on a 'gross' and 'net' basis, taking into account known and proposed mitigating actions.

Group-level risks are assessed as:

- Macro risks which affect the majority of, or all, divisions; or
- Individual divisional risks where the materiality of the risk is considered of Group significance.

The Group has developed a 'risk radar' to supplement the Group risk register, and the radar and register are reported to the Group Executive, Audit Committee and Board, twice a year. At both the Divisional and Group level, the consideration of risk includes:

- Categorisation of risk as Strategic, Financial, Operational or Hazard;
- New or emerging risks (eg cyber risk, GDPR, Brexit);
- Longer-term risks such as developments in autonomous vehicles;
- Latest guidance from the Financial Reporting Council on best practice risk reporting;
- The impact of the Group's risk and operations on other stakeholders as well as the Group itself; and
- Acknowledgement that many risks are also opportunities (for example, the liberalisation of EU transport markets) and a balance needs to be struck in terms of the Group's risk appetite.

The Group prioritises risk mitigation actions by considering both risk likelihood and potential severity, coupled with our ability to effectively intervene to reduce the risk profile – for example, reducing the risk of a safety failure through the implementation of technology and new Group safety standards.

Summary risk radar

Risks are shown on a 'net' basis after mitigations.
The closer to the centre of the radar the greater the perceived risk.

Looking forward, the Group will focus on the following key areas of risk:

Potential impact	Management/mitigation
1. Economic conditions, including Brexit implications	
Declining economic conditions potentially impact demand for the Group's services in some divisions; improving economic conditions may impact the Group's ability to recruit drivers and other staff, or cause inflationary pressure on costs. The terms on which Brexit is negotiated (specifically in relation to the means by which any limitation on free movement/immigration is traded off against access to the single market) may affect the Group's ability to bid competitively within the EU.	The geographical diversification of the Group provides a natural hedge to some economic risk. The Group continues to monitor the position regarding Brexit. Robust bid modelling takes into account differing economic scenarios. Our exit from the UK rail market and focus on international opportunities mitigates risk in this area.
2. Political/geopolitical/regulatory landscape	
The political and regulatory landscape within which the Group operates is constantly changing. Changes to government policy, funding regimes or the legal and regulatory framework may result in structural market changes or impact the Group's operations in terms of reduced profitability, increased costs and/or a reduction in operational flexibility or efficiency. The Group's exposure to franchise renewal risk in Spain is a specific example.	The Group constantly monitors the political landscape and is focused on effective stakeholder management. Political risk is specifically considered when considering bids or new market entry. Strategic alliances and partnerships are used where appropriate to mitigate risk. The Group carries out appropriate lobbying and communication, highlighting especially the importance of public transport to central and local government. Most importantly, we continue to focus on operational excellence and delivering value in our franchises.
3. Increasing competition	
The Group's divisions are facing increasing competition in various ways: price competition, inter-modal (eg coach vs rail), and more recently emerging threats such as new market entrants or disruptive technologies.	The Group is committed to operational and service excellence and the effective management of cost. Revenue trends are closely monitored and revenue management systems deployed. Our market strategy is to provide our customers with a compelling and differentiated offering. Effective processes are in place to ensure best practices are shared across the Group in many areas.
4. Terrorism	
The Group can be either directly impacted by a terrorist event, or indirectly, through softening demand from the travelling public.	The Group liaises closely with government agencies and industry partners. Major incident/emergency plans are developed in all Divisions. Insurance coverage is available and in place for some terrorism-related risks.

Potential impact	Management/mitigation

5. Safety, litigation and claims

A major safety-related incident (eg bus or rail accident) could impact the Group both financially and reputationally. The Group self-insures a proportion of certain risks such as workers' compensation and auto liability, and higher than planned claims or cash settlements could adversely affect profit and cash outflow. The Group's operations are also subject to potential litigation from other sources such as environmental legislation or wage and hour matters in the US. The Group is increasingly subjected to regulation in many areas and non-compliance with regulations can create legal and financial risk.

The Group has a strong safety culture driven from the Chief Executive and divisional leadership. The Group is dedicated to leading edge safety technology and has accelerated investment in the Lytx DriveCam technology. A new compliance steering committee has been establish in the Group's North American business, chaired by the Divisional CEO. Appropriate insurance coverage is available and in place for accident-related claims to employees and third parties, and the Group has experienced claims management and legal teams in each Division. All Divisions have established safety audit programs, supported by Group Internal Audit.

6. HR and labour relations

A lack of available talent/leadership skills can inhibit growth. Shortages in drivers and other key staff can disrupt operations. Increased unionisation and/or poor labour relations presents increased risk of strike or operational disruption; inflation of wage and benefit costs; and possible reputational damage.

The Group is committed to employee engagement and invests in a number of retention programmes. Appropriate training is provided for managers and supervisors. Reward and recognition programmes are established to further enhance employee engagement. The Group is focused on the effective management of stakeholder and union relationships, and the advice of specialist outside counsel is sought where necessary.

7. Changing customer expectations in a digital environment

Customers increasingly expect to be able to buy tickets and manage their travel plans through a variety of digital platforms. Failure to develop applications and digital channels that meet these increasing customer expectations could affect profitability, customer satisfaction and the business' ability to capitalise on valuable customer data to enable commercial initiatives.

The Group has appointed a Chief Digital Officer; and comprehensive digital strategies are being developed in each Division. Divisional 'digital scorecards' are reviewed monthly by the Executive Committee to monitor the effectiveness of various digital channels.

8. IT, cyber risks and GDPR

A major IT failure could disrupt operations and lead to loss of revenues, especially in the Coach businesses. The Group recognises a wide range of cyber threats, including loss of data, social engineering, hacking and extortion.

The Group also recognises potential risks arising from the implementation of the EU General Data Protection Regulation (GDPR).

At a Divisional and Group level, comprehensive back-up procedures and disaster recovery plans are established. A dedicated Cyber Risk Security Committee was established in 2016, chaired by the Group Finance Director. External expert testing has been carried out for cyber risk and recommendations implemented.

The Group is in the process of implementing plans to ensure compliance with GDPR by 25 May 2018, when the new regulation becomes effective. These plans have been tailored at Divisional level to reflect the type of personal data of European subjects and the nature of processing such personal data which is carried on by each Division and to build on measures that are already in place in each Division which are designed to comply with current national data protection laws.

Looking forward, the Group will focus on the following key areas of risk:

Potential impact	Management/mitigation
9. Credit risk	
As contracted operations, the North American and Spanish urban businesses are exposed to the risk that customers are either late or unable to pay sums owed to the Group, impacting Group liquidity.	Receivables in each business are closely monitored, based on robust and thorough documentation; provisions are then made where appropriate on a prudent basis for a certain level of non-collection. Group Treasury actively manages the relationships with 18 banks who provide £544 million of committed bank facilities maturing in November 2021, giving the Group an appropriate level of liquidity when combined with a series of debt capital market issuances and a programme of finance leases.
10. Hazard risk to key site (eg fire); natural catastrophe; extreme weather	
The loss of a key location to either a man-made hazard such as fire, or natural catastrophe such as a hurricane, can result in asset loss, a loss of revenue and profit, and a potential loss of competitive position in the market. Widespread events such as extreme weather events can also interrupt operations and cause revenue loss even if the Group's assets are undamaged.	The geographical diversification of the Group provides a natural hedge to this risk. Even at the Divisional level, the business operates from multiple locations. Each Division has established emergency and continuity plans. Insurance coverage is available and in place for some hazard related risks.
11. Foreign exchange	
The Group's exposure to foreign currency earnings through its overseas operations creates a risk that movement in exchange rates may adversely impact translation of profit and cash flows.	The Group hedges all transactional risk and also actively manages the effective currency of its debt portfolio to manage gearing ratios and safeguard covenants. A range of tools are employed including local currency debt and currency swaps. In addition, management has flexibility to adjust Group capital allocation.
12. Fuel cost	
Fuel represents a significant cost to the Group and unplanned increases in fuel price potentially impact profitability.	The Group operates a three year rolling hedge policy, hedging 100% of the next 15 months' demand, with decreasing levels of cover in the latter periods topped up each month.
13. Pension costs	
Market conditions and/or deficit may lead to increase in service costs and/or increased deficit recovery payments.	The Group's Defined Benefit schemes are closed to new entrants. The UK Bus Dundee scheme was transferred to the local authority in 2017. Triennial valuations for the UK Group and West Midlands Travel schemes have been completed and contributions agreed to 2020.