Risk management

Committed to managing risk effectively

The Board recognises that the appropriate management of risk is key to the delivery of the Group's strategic objectives and the continued delivery of superior returns for all of our stakeholders. As set out on pages 8 and 9, we actively capitalise on the opportunities impacting our industry to ensure that the Group remains well positioned to deliver on the evolving needs of our customers. Our diversified business model means that we have low operational leverage with no single contract material to the Group. This enables us to take on a level of financial leverage in expanding the business. As a leading international transport company, however, the Group is exposed to an evolving landscape of risks, whether industry-wide or more specific to the Group, which could potentially impact performance or reputation negatively as well as positively.

RISK MANAGEMENT FRAMEWORK

The effective management of risk is a core component of the Group's day-to-day management activities, for example the usage of very granular, detailed KPI tracking in monthly divisional reports, or robust due diligence on acquisitions. This is only the 'first line' of the Group's risk management structure where internal control and risk management processes are based on the accepted 'three lines of defence' model. The Group Executive Committee as well as specialist functional teams provide a second level of defence, supporting front-line teams and building organisational capability. The Audit Committee provides additional assurance with 'deep-dive' reviews into specific areas of risk, for example cyber assurance. Ultimate oversight of the Group's risk appetite and processes is provided by 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
Third line	Audit Committee/ 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	– Supports divisions with 'first line' responsibilities Coordinate and report on Group-level risks – Builds risk capability and understanding
First line	Divisional Executive Committees Divisional management	– Identify, assess and report key risks – Regularly review and update divisional risk registers – Implement risk mitigation plans

Risk Appetite

The Board recognises that continuing to deliver superior returns for shareholders and other stakeholders is dependent upon accepting a level of risk. Our risk appetite sets out how we balance risk and opportunity in pursuit of our strategic objectives:

Zero Tolerance

The Group has zero tolerance for risk which may impact:

- The safety of our employees, customers or the general public
- Our reputation and brand
- Our legal and regulatory compliance

Core Business/ Operational Excellence

The Group has low tolerance for risk in its core operations.

Technology

The Group accepts a moderate levels of risk in investing in and adopting technologies that will enhance customer service or improve operational and safety performance.

Strategic growth/M&A

The Group accepts a moderate level of risk in pursuing new opportunities, including potential new markets.

Prioritising and reporting risks

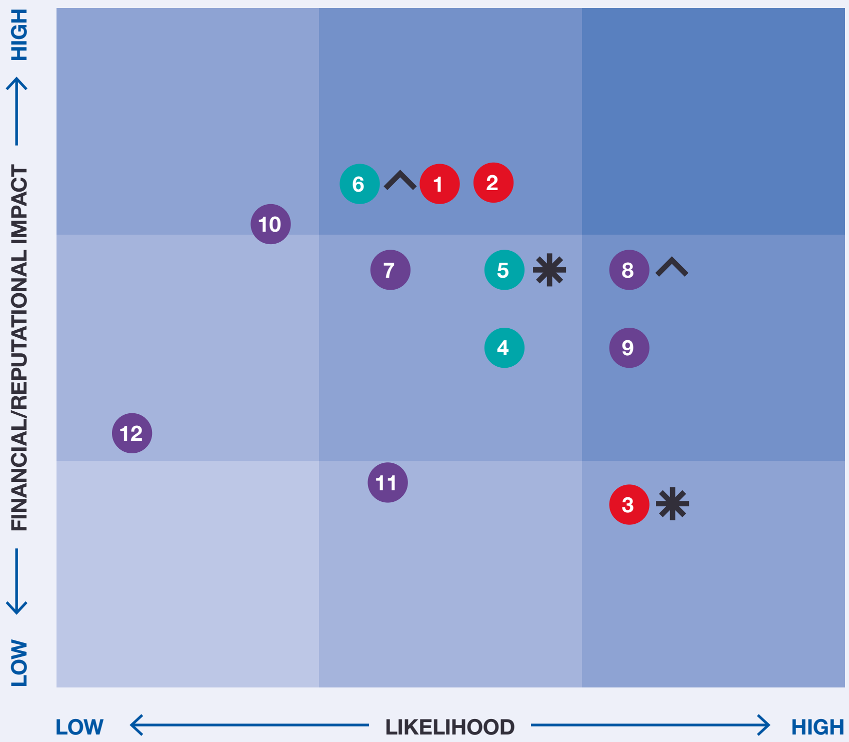
The management of risk is embedded in the day-to-day operations of divisional management teams. A key element of this is the regular review and update of detailed 'risk registers' in each division, in which risks are identified and assessed in terms of both the probability of the risk occurring, and its potential impact.

Group-level risks are either derived from a 'top down' review, or from the divisional risk registers, either because the risk affects multiple divisions, or is of a materiality in itself that is considered of Group significance.

Each of these Group-level risks is then assessed by the Board in terms of its potential impact on the Group and its key stakeholders. The Group prioritises risk mitigation actions by considering 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.

In 2018, in addition to considering current principal risks, the Board has established a process to identify and monitor emerging risks. This has led to the development of an emerging risk register which will be reviewed regularly by the Board.

PRINCIPAL RISK MATRIX



Key
- ^ Increase in risk during the year
- v Reduction in risk during the year
- * New risk in the year

Note: Given the continued levels of uncertainty, Brexit has been included as a specific risk for 2019, having previously been included within the broader Economic Environment risk area

Macro/external risks
1. Economic conditions
2. Political/geopolitical/regulatory landscape
3. Brexit

Strategic risks
4. Changing customer expectations in a digital world
5. Alternative Fuel Vehicles ('AFVs')
6. Competition and market dynamics

Operational risks
7. Attraction/Retention of talent/HR/labour relations
8. Cyber/IT failure/general data protection regulations ('GDPR')
9. Terrorism
10. Safety, litigation and claims
11. Natural catastrophe/extreme weather/loss of key facility
12. Credit/financing

Key

Core Business/Operational Excellence

Technology

Increase in risk during the year

Reduction in risk during the year

Strategic Growth/M&A

New risk in the year

Macro/external risks

1 ECONOMIC CONDITIONS

Potential impact
- Declining economic conditions potentially impact demand for discretionary travel
- Improving economic conditions may impact the Group's ability to recruit drivers and other staff, or cause inflationary pressure on costs

Management/mitigation
- Geographical diversification of the Group provides a natural hedge to some economic risk
- Strategic plans are stress-tested for differing economic scenarios
- Exit from the UK rail market and focus on international opportunities
- Strong strategic focus on people/talent management and recruitment/retention.
- Delivery of excellence in service and operations

Opportunity
- GDP growth in our major markets is forecast at 1.5%-2% per annum to 2023

Change in risk in the year
- Economies in our core markets have generally shown good growth
- Unemployment rates continue to fall in key markets, causing ongoing pressure on staff costs and turnover

2 POLITICAL/GEOPOLITICAL/ REGULATORY LANDSCAPE

Potential impact
- 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
- Franchise renewal risk in Spain
- UK bus franchising or alternative models
- Financial or reputational cost of failure
- To comply with changing regulations or legislation

Management/mitigation
- Constant monitoring of the political landscape and focus 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
- Focus on operational excellence and delivering value in our franchises and contracts, and to our fare paying customers

Opportunity
- Increasing city regulation and investment in bus and Bus Rapid Transit ('BRT') schemes
- Continued liberalisation of markets in many territories
- Political pressure on congestion and clean air favours public transportation.

Change in risk in the year
- Continued delays in Spanish franchise renewals
- Continued strengthening of our relationships with key political stakeholders and our reputation as a high quality, innovative partner

3 BREXIT

Potential impact
- Continued uncertainty around the terms of the UK's exit from the EU creates general and specific risks in our markets in the UK, Spain and Germany
- An economic downturn in the UK could adversely impact demand for our services
- Reduced travel volumes to/from UK airports could affect demand for our UK coach services

Management/mitigation
- Ongoing close monitoring of specific Brexit-related risk issues
- Geographical diversification reduces Group-level risk; exposure to UK market is circa 25% of total revenue
- Restructured our small UK to Europe coach partnership

Opportunity
- Translated profits from our international operations will increase in the event of a weakening GBP

Change in risk in the year
- Increased possibility of a 'no-deal' exit adds to uncertainty

Strategic risks

4 CHANGING CUSTOMER EXPECTATIONS IN A DIGITAL WORLD

Potential impact
- Increasing expectations of customers 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 expectations could affect profitability, customer satisfaction and the business' ability to capitalise on valuable customer data to enable commercial initiatives

Management/mitigation
- Comprehensive digital strategies developed in each division
- Divisional 'digital scorecards' are reviewed monthly by the Executive Committee to monitor the effectiveness of various digital channels
- Developing strategies for demand responsive services

Opportunity
- Leadership in adopting new technologies will enhance our service to existing customers and attract new ones
- Millennials are an increasingly important target market and more inclined to use public transportation if the service is right

Change in risk in the year
- Appointment of Chief Digital Officer
- Continued increases in bookings through online and digital mobile platforms
- Continued roll-out of ticketless operations

5 ALTERNATIVE FUEL VEHICLES ('AFVs')

Potential impact
- Increasing popular, political and customer demand for alternative fuel (electric, hydrogen etc.) vehicles
- Transition involves potentially material changes in financing, maintaining and operating the assets, creating execution risk
- Requires significant change to infrastructure

Management/mitigation
- Cross-division executive leadership of AFV strategy
- Close engagement with new and existing original equipment manufacturers ('OEMs')
- Pilot testing underway in a number of areas

Opportunity
- AFVs present potential opportunities to reduce the cost base of the business, while helping cities solve the challenges of the drive for a cleaner air environment

Change in risk in the year
- New risk – elevated from emerging risk status
- All major OEMs continue to invest heavily in developing products for the mass market

6 COMPETITION AND MARKET DYNAMICS

Potential impact
- Competition arises from direct price competition; inter-modal (eg coach vs rail); and, more recently, emerging threats such as new market entrants or disruptive technologies
- Changes in customer demographics impact demand and the nature of services required
- Potential 'disintermediation' risk created by aggregators seeking to 'own' the customer relationship

Management/mitigation
- Commitment to service excellence, providing the best solutions to our customers
- Price leadership and value for money
- Revenue trends are closely monitored and RMS deployed
- Investment in technology
- Focus on operational excellence – even with an aggregator model, service delivery is critical
- Targeted acquisitions and growth in the most attractive markets

Opportunity
- Ageing population in major markets creates additional paratransit opportunities
- Continuing urbanisation drives cities to partner with high quality transportation operators

Change in risk in the year
- Disruptors such as Uber, Lyft and others continue to grow and expand their role in Mobility as a Service ('MaaS')

Key

- Core Business/Operational Excellence
- Technology
- ^ Increase in risk during the year
- v Reduction in risk during the year
- Strategic Growth/M&A
- ✱ New risk in the year

Operational risks

7 ATTRACTION/RETENTION OF TALENT/HR/LABOUR RELATIONS

Potential impact
- Lack of available management talent/leadership skills can inhibit growth
- Shortages in drivers and other key staff can disrupt operations and lead to wage and benefits cost inflation
- Increased unionisation and/or poor labour relation presents increased risk of strike or operational disruption

Management/mitigation
- 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
- Focus on the effective management of stakeholder and union relationships, and the advice of specialist outside counsel is sought where necessary

Opportunity
- Ensuring we have an agile, skilled workforce will enable us to adapt to emerging challenges and opportunities

Change in risk in the year
- Low levels of unemployment in key markets have led to recruitment and retention challenges and cost inflation
- Appointment of Group Talent Director

8 ^ CYBER/IT FAILURE/GENERAL DATA PROTECTION REGULATIONS ('GDPR')

Potential impact
- Major IT failure could disrupt operations and lead to loss of revenue, especially in the Coach businesses
- Data breach involving a loss of customer data could result in reputational damage and significant remedial costs
- Breach of the EU Regulation ('GDPR') could result in reputational damage and additional costs

Management/mitigation
- Comprehensive back-up procedures and disaster recovery plans are established
- Dedicated Cyber Risk Security Committee
- Extensive independent expert testing has been carried out for cyber risk and recommendations implemented
- GDPR compliance plans in place, tailored to each division's exposure

Opportunity
- Strengthened resilience against cyber threats and IT outages increases awareness and expertise across the Group and facilitates greater leverage of technology

Change in risk in the year
- Cyber threat environment continues to be challenging, as demonstrated by high profile data breaches in other companies
- Significant improvements in our resilience, supported by an ongoing maturity programme

9 TERRORISM

Potential impact
- Direct impact through asset damage, disruption to operations and revenue loss
- Potential indirect impact from a general reduction in the public's appetite to travel reducing demand and revenue

Management/mitigation
- Close liaison 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
- Risk assessment of any new business growth opportunity

Opportunity
- n/a

Change in risk in the year
- Although we have not seen the same level of attacks in the UK as we saw in 2017, the Government threat level remains unchanged at 'Severe'

Operational risks continued

10 SAFETY, LITIGATION AND CLAIMS

Potential impact
- Major safety-related incident could impact the Group both financially and reputationally
- Higher than planned claims or cash settlements could adversely affect profit and cash outflow
- Non-compliance with regulations can create legal and financial risk

Management/mitigation
- Very strong safety culture driven from the Group Chief Executive
- Dedication to leading edge safety technology
- Appropriate insurance coverage for accident-related claims to employees and third parties
- Experienced claims management and legal teams in each division
- All divisions have established safety audit programs, supported by Group Internal Audit

Opportunity
- Continued relentless focus on safety and investment in technology should facilitate risk and cost reductions and enable differentiation in our customer offering

Change in risk in the year
- Reduced incident severity in most divisions as safety improvements continue to gain traction

11 NATURAL CATASTROPHE/EXTREME WEATHER/LOSS OF KEY FACILITY

Potential impact
- 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 and lost revenue
- Widespread events such as extreme weather can also interrupt operations and cause revenue loss even if the Group's assets are undamaged

Management/mitigation
- Geographical diversification of the Group provides a natural hedge to this risk.
- Established emergency and continuity plans in each division
- Insurance coverage is available and in place for some hazard-related risks

Opportunity
- n/a

Change in risk in the year
- n/a

12 CREDIT/FINANCING RISK

Potential impact
- Contract-based operations such as North America and Spanish urban are exposed to late or non-payment risk from customers, impacting Group liquidity
- A material increase in interest rates would increase the Group's cost of borrowing
- Material tightening in investment-grade credit markets could impact the Group's liquidity

Management/mitigation
- Close monitoring of receivables and appropriate provisions made for possible non-collection
- Strong relationships with a number of banks
- Appropriate liquidity maintained through committed bank facilities, finance lease programme, and debt capital market issuances

Opportunity
- Investment grade rating and proven track record give efficient access to credit markets enabling investment in growth

Change in risk in the year
- Increase in USD interest rates
- Amended and extended RCF for further 2+2 years
- Bridging finance in place to next bond maturity

Assessment of prospects

The Board continues to believe that the Group's prospects are positive in the medium to long term.

- We are diversified:
  - No one contract contributes more than 2% to revenue;
  - No one geography contributes more than 40% to normalised operating profit
  - The Group receives only 3% of its revenue in the form of grants and subsidies
- We are positioned to benefit from the future trends in transportation:
  - Transport demand continues to grow whilst private car ownership is beginning to decline; the gap is likely to be filled by public transport
  - Public transport helps deliver against the pressing urban challenges of congestion and poor air quality
- We invest in the business to secure its future:
  - Over the last five years, 64% of free cash flow has been re-invested into the business whilst gearing has remained flat and dividends have grown by 44%
  - The Group owns and continually invests in market-leading consumer brands in each of our main consumer markets
  - We invest in technology to allow customers to access our products at competitive prices and to deliver our services safely and efficiently

The Group's strong financial position is characterised by operating cash conversion of 98% and free cash generation of £198.6m underpinned by 6% revenue growth. The Group's credit rating is investment grade with committed facilities of £1.6 billion at 31 December 2018.

Principal risks and assessment period

The Board reviewed the Group's principal risks (page 40), looking at each risk's impact, likelihood and the timeframe over which the risk was likely to reduce Group cash flows. On this basis, the highest impact and highest likelihood risks were considered in modelling a severe but plausible downside to assess the Group's future viability.

The Board concluded that three years would continue to be an appropriate timeframe over which to assess the Group's ongoing viability, as within that timeline a number of risks' impact/likelihood was expected to reduce:

- Regulatory: the majority of the major Spanish concession renewals are expected to complete
- Brexit: the immediate impact of Brexit will be felt
- Credit/financing: €250m of the Group's bonds will expire and a £225m refinancing is necessary in 2020

Assessment of viability

The Group's viability assessment is an output of the annual strategic planning process. To assess viability, multiple, material risks are selected by the Board (above) and are assumed to crystallise in parallel during the assessment period, putting the financial and operational performance of the business under plausible, but unlikely, stresses as outlined below.

Risk stress tests

Brexit: no-deal Brexit assumed, with material Europe-wide economic downturn and disruption to travel between the EU and the UK.

Economic environment: driver wage inflation continues in North America; and high speed rail aggressively undermines profitability in Spanish long haul coach travel.

Regulatory landscape: material margin loss in ALSA following resolution of long haul franchise renewal process.

Terrorism: terrorism event hits both UK and Spanish consumer confidence, resulting in lower levels of discretionary travel.

Cyber: IT system failure and data loss following cyber attack in UK and Spain causes significant revenue loss and financial penalties.

Credit/Financing risk: material increase in the cost of borrowing and reduction in liquidity following period of reduced cash generation and profitability.

In the unlikely event of this concurrence of events, the Board would mitigate through reduced operating costs and capital expenditure to preserve the business's cash flow. During assessment, the Group's robust business model; continued cash generation; access to liquidity and funding; and mitigation actions demonstrated that it could tolerate the impact of the risk scenarios without breach of covenants or threat to business viability.

Viability Statement

Based on the results of the analysis, the Board has a reasonable expectation that the Group will continue in operation and be able to meet its liabilities as they fall due over the three-year period of assessment.

Going concern

The financial position of the Group, its cash flows, liquidity position and borrowing facilities are set out in the Group Finance Director's review on pages 17 – 21, and the Group's business activities, together with the factors likely to affect its future development performance and position, are set out in the Strategic Report (pages 1-45). Note 30 to the Financial Statements includes the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposure to credit risk and liquidity risk.

The Board has reviewed assumptions about current trading performance, and has taken account of reasonably possible adverse changes to performance impacting availability of resources to June 2020. The Board confirms that it has a reasonable expectation that the Group has adequate resources to continue in operation for the period reviewed, and accordingly the Board continues to adopt the going concern basis of accounting in preparing the financial statements for the year ended 31 December 2018.

Our 2018 Strategic Report, from page 1 to page 45, has been reviewed and approved by the Board.

Dean Finch

Dean Finch
Group Chief Executive
28 February 2019