



Post Office Ltd

Quarterly Review

April 2012

RESTRICTED – POLICY & COMMERCIAL

Quarterly update

1. Separation from Royal Mail

- On 1 April 2012, Post Office Ltd (POL) and Royal Mail Group Ltd separated operationally.
- POL now has its own Board (see below) and operational autonomy from Royal Mail.
- A 10-year (reviewable after 5) distribution agreement is now in place between the two businesses, giving POL greater certainty over its largest revenue stream.

2. Board and Governance

- POL's Board now has 4 (non-ShEx) NEDS and a further NED with financial services expertise is to be sought.
- Susannah Storey has joined the Board as a ShEx representative.
- New articles of association have been adopted giving ShEx direct special shareholder rights over POL.

3. Strategic Plan and Funding Position

- State aid approval for POL's funding package to March 2015 was received in March.
- Payment of FY12/13's £410m was made on 2 April.
- Piloting of new network models continues, with more than 200 now in place. Formal rollout begins this summer.
- Major other areas of focus to ensure strategic plan targets are met are Crown office losses and new revenues.

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4. Policy questions raised at Annual Review

- A new AD focussing on the next SR package will join in May. An initial project will be to examine the most efficient basis to provide subsidy to branches – particularly in the context of mutualisation and the longer term (initial analysis suggests fixed cost must be removed before differentiated models can be introduced).
- Read across from FSS to POL: Similarities: decline in traditional markets and uncertainty on future markets; high fixed cost base; solutions need to include a gvt wide view; the need to convert market position to innovate in new areas. Differences: policy and politics around the future of the companies; network strategy attempts to address fixed-cost base and POL is seeking to innovate in GS (not tackled in FSS).

5. Financial Reporting Improvements

- The team has taken/is taking forward the reporting improvements suggested at the last annual review.
- EG POL now reports profitability ex-subsidy; planned rise in agency pay as % of revenue due to fewer crowns.
- Additionally, the new Chair of POL's Audit, Risk and Compliance Committee takes his position shortly, and he and the FD will look in detail at the appropriateness of POL's financial reporting.
- The team's new AD (to be supported by Charles Stevenson and Katie Wake) brings dedicated financial expertise to the POL team for the first time.

6. Incentives

- Following separation, POL now has its own RemCo.
- POL has set out initial proposals for principles on which the LTIP will be founded (reducing pre-subsidy losses, network transformation and growth in revenues). We will now engage on this, looking to build in a Crown profitability metric.

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Trading update

£m	Current Month			YTD (11 months)			Prior Year YTD		2012/13
	Actual	Budget	Variance	Actual	Budget	Variance	2011 Actual	Variance	FY Budget
External Income	50.9	49.9	1.0	570.9	566.4	4.5	571.6	-0.7	n/a
Interbusiness Income	27.4	26.3	1.1	329.7	321	8.7	318.7	11	n/a
POFS/FRES Share of Op Profit	1.2	1.7	-0.5	28.6	26	2.6	22.4	6.2	n/a
Total Income	79.5	77.9	1.6	929.2	913.4	15.8	912.7	16.5	1015.8
Cost of Sales	-9.3	-9.4	0.1	-104.4	-111.2	6.8	-112.7	8.3	-117.9
Gross Profit	70.2	68.5	1.7	824.8	802.2	22.6	800.0	24.8	897.9
Expenditure (excl-POOC)	-79.2	-75.7	-3.5	-876.5	-892.8	16.3	-878.2	1.7	-1018.8
POOC Costs	-3.9	-1.5	-2.4	-17.8	-16.7	-1.1	-13.7	-4.1	-37.7
Group Overhead Allocations	-1.7	-1.7	0.0	-18.8	-18.7	-0.1	-15.2	-3.6	n/a
Other (inc Interest & Impairment)	-0.9	-3.2	2.3	-25.5	-40.8	15.3	-59.9	34.4	n/a
Total Costs	-85.7	-82.1	-3.6	-938.6	-969.0	30.4	-967.0	28.4	-1056.5
Share of Op Profit from JVs									32.6
Profit pre-Network Payment	-15.5	-13.6	-1.9	-113.8	-166.8	53.0	-167.0	53.2	-126.0
Network Payment	13.8	13.8	0.0	166.2	166.2	0.0	138.5	27.7	210

- Profits are significantly ahead of budget and 2011 comparable.
- Increase in revenue has been driven by outperformance vs prior year and budget on the mails (driven by 2nd class and special deliveries) and financial services (driven by internet saver and ATMs) sides of the business. Government Services revenues are also up by c£5m on the previous year (driven by ID services) though this is less than budgeted.
- Decline in operating costs has been driven by non-people cost savings of c£16m. This has been driven by a renegotiation of POL's IT contract with Fujitsu, as well as other savings from squeezing supply contracts.
- New budget for 2012/13 has been approved

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Traffic light analysis

1. Shareholder Relationship	Green	
2. Implementation of Shareholder Model	Green	Policy and shareholder roles are combined.
3. Quality of Management Team & Board	Green	Succession plan for POL MD is unclear. Governance changes around separation will increase scrutiny and support for POL executives.
4. Strategy	Amber	Strategy is sound but its execution faces risks. In particular ShEx is working hard on the Government services side to ensure that POL has the best possible chance of realising revenues.
5. Financial Performance	Amber	POL does not make a profit because HMG imposes a number of SGEI requirements such as maintaining a network of 11,500 outlets.
6. Balance Sheet & Risk	Amber	POL still relies on HMG subsidy but a strategic plan is in place to reduce this.