Motability Operations Group plc

Half Year Report

for the six months ended 31 March 2010

During the first half of the year Motability Operations met or exceeded business objectives in all key customer and financial areas. Solid financial performance enabled the continuing provision of affordability and choice to our customers.

Motability Operations is overseen and directed by the Charity, Motability, and comprises the 'not-for-profit' group of companies that provide lease cars to eligible disabled customers. The overarching objective is to consistently provide affordable leases and choices to customers. This objective is sustained through a reserves policy which aims to ensure that surpluses, which are all reinvested back into the business, are maintained at a level commensurate with a predetermined Economic Capital Requirement (ECR). This ECR is set at a level appropriate to protect the Motability Scheme from all but the most extreme risks and related financial shocks. As regards ordinary shareholders, there is no dividend entitlement.

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How we operate

We operate a unique business model, working with Motability, stakeholders and partner suppliers for the benefit of our customers.

The Charity directs and oversees the Scheme

Motability Operations

Mobility allowance
Customers choose to assign their mobility allowance to obtain a vehicle

Owned by four shareholder banks

Motability Operations manages the Motability Car Scheme

Dealers deliver product

Funding
Funding from the financial market

Suppliers
Vehicles, servicing, breakdown assistance, insurance

Customers
Customers choose from a range of vehicles to meet their needs

Vehicle remarketing
Resale of used vehicles into the marketplace

Motability (the Charity)

Motability is a national charity, set up in 1977, to assist disabled people with their mobility needs. The Charity's prime purpose is to ensure that those disabled people who want to use their mobility allowance to obtain a vehicle on the Motability Scheme always receive the best possible value for money and service.

At Motability Operations, our relationship with Motability is governed by the Scheme Agreement, which sets out the Charity's role of directing and overseeing the Scheme.

Motability and Motability Operations are constitutionally and operationally separate entities.

Mobility allowance

There are currently over 1.9 million recipients of qualifying 'mobility' allowances. To take a vehicle on the Scheme, the individual must receive either the Higher Rate Mobility Component of the Disability Living Allowance (administered by the Department for Work and Pensions (DWP); in Northern Ireland this is administered by the Social Security Agency and in the Isle of Man by the Department of Health and Social Security) or the War Pensioners' Mobility Supplement (which is administered by the Service Personnel and Veterans' Agency (SPVA)). Receipt of a qualifying allowance is the sole eligibility criterion for people wishing to access a vehicle on the Scheme. Through its relationship with Motability, the DWP arranges for the allowance to be paid directly to us on behalf of those people who choose to use the Scheme.

Motability Operations

The UK's largest car leasing company, we have over 30 years' experience in the industry and have supplied over two million vehicles since the Motability Scheme was launched.

Our objective is to offer affordable, worry-free motoring to the 1.9 million people in the UK with qualifying allowances. Through the Motability Scheme, potential customers can choose to divert the allowance into leasing or the hire purchase of a new car. We aim to provide sustained value and choice, combined with first-class customer service.

Our customer numbers have increased rapidly in recent years, and our fleet currently stands at over 540,000 vehicles. We bought circa 190,000 new cars and resold 162,000 into the used car marketplace during the financial year ended September 2009.

Underpinning this growth is our strong financial position. This reflects our prudent reserves and risk management methodology, our diversified fleet portfolio, our excellent business culture and best-practice governance. As a result of these strengths we are able to provide our customers with sustained affordability throughout the economic cycle. As a 'not-for-profit' plc, we reinvest any surpluses back into the business for the benefit of our customers.

At Motability Operations, we provide:

- Worry-free motoring through a Contract Hire product including insurance; maintenance and servicing; tyre and windscreen replacement; breakdown assistance and a 60,000 mileage allowance over three years
- Excellent brand choice with 39 manufacturers represented on the Scheme
- Over 200 vehicles on the price list that are available by using the mobility allowance alone ('nil advance payment')
- A full range of adaptations and wheelchair accessible vehicles

To achieve this we:

- Manage and develop relationships with key manufacturers
- Work in partnership with over 4,900 dealers to provide excellent customer service
- Proactively manage suppliers to ensure an excellent and sustained customer experience on very affordable terms
- Provide telephone support to our customers through our best-practice call centre, supported by a fully interactive web-based query tool
- Employ an engaged workforce of over 700 people across our two sites in London and Bristol

Interim management report

The first six months of the financial year to March 2010 saw continued strong performance, with the consistent delivery of all customer and financial objectives.

3.2%
Increase in customer numbers

97%
Overall customer satisfaction with the Scheme

>200
Cars available at nil advance payment throughout the year

Performance

Overview

Targets for affordability and choice were exceeded throughout the period, with over 200 cars available on the price list using only the mobility allowance and requiring no extra customer contribution. These choices included a range of more fuel efficient options, enabling customers to make greener selections, with the average CO_2 emissions from new business reducing by 7.9% year-on-year.

Our call centre continued to perform at outstanding levels, reaching the milestone of answering over 80% of calls in less than 20 seconds for 36 consecutive months. Customer satisfaction continued to track at 97% in our independently measured survey and renewal rates remain steady in excess of 92%.

The sustained levels of high satisfaction and renewal rates, combined with a stable and affordable price list have precipitated a continued increase in customer numbers, with the fleet standing at over 540,000 at the end of March, representing 3.2% growth for the first six months of the financial year.

Financial performance

With the continued growth in customer numbers, there has been a corresponding growth in the Income Statement and Balance Sheet metrics. Revenue for the six months to March 2010 was up 12.5% year-on-year, at £1,195m (FY2009: £1,063m); Operating Lease Assets increased 5.1% since September 2009 to £3,892m at the half-year point.

Transfer to reserves, which is retained in the business for the benefit of our customers, was £120m, with closing Balance Sheet reserves remaining in line with the target corridor, based on our Economic Capital Requirement. This solid financial position both underpins our ability to provide sustained affordability and choice to customers, and equips the business well to accommodate further growth.

Assets and residual values

We carry out a quarterly reassessment of the residual value of our leased assets. At the financial period end this can lead to the need for accounting adjustments which are usually made by recalibrating vehicle depreciation for the period and over the remaining life of the lease. Our in-house model, which has been externally validated, has consistently outperformed alternative external benchmarks and remains less volatile and typically more conservative in outlook than other market views.

Given the volatility in new and used car prices over the last 24 months, we made significant and prudent write-downs in previous periods. Following a sustained market recovery over the last 12 months, and with a more stable outlook, these conservative provisions continue to unwind – with additional depreciation previously charged being reversed in the first half of the financial year. However our forecast remains more conservative than the alternative market view.

In terms of the resale of vehicles at the end of lease, the remarketing team continued to maximise opportunities through both our online and physical sales channels, with 81,000 vehicles sold in the six months to March 2010. A net gain of £23m (4.7% on turnover) was realised in the disposal of these assets.

Financing and liquidity

During the first six months of the year, the Group continued to implement its refinancing strategy. Following the successful issue of two bonds under the A+/A2 rated £2bn European Medium Term Note (EMTN) programme during the financial year to September 2009, we further diversified into the bond market with a £400m twelve-year Sterling issue in January 2010. Whilst the proceeds of the first two issues were used to settle our £1bn three-year bank debt, the most recent issue provides headroom for further growth. It is the Group's policy to ensure that it has sufficient funding headroom in place to cover for at least twelve months of growth plus 10%.

The Group targets a ratio of Total Group Assets: Total Net Debt of not less than 1.25:1. At the Balance Sheet date this ratio was 1.69:1.

Outlook

Over the last 24 months we have demonstrated the strength of our business model through the economic cycle – this has enabled us to continue to offer our customers excellent service and affordable motoring through the recession.

Whilst there remains uncertainty in the economic outlook into the medium term, we are confident that we remain well placed to respond flexibly to any challenges as they emerge.

Our strategy and performance

We have developed a clear strategic agenda designed to satisfy our prime purpose of providing our customers with independence and mobility by offering a wide choice of vehicles at affordable prices. We aim to deliver first-class customer service, and believe that understanding how disability affects our customers' needs is critical in meeting this objective. Ensuring the long-term sustainability of our business is essential for the delivery of these objectives.

Build our customer and disability expertise

We maintain consistently excellent levels of customer service throughout the leasing proposition, and demonstrate disability expertise in our approach to our customers and in our role as an employer

Performance

- Overall customer satisfaction: remains at

97%

- Call answering:

84%

of calls answered within 20 seconds

- Continuous mobility: roadside 'fix-rate'

87%

Provide value and choice

We provide a wide range of vehicles to our customers at competitive and affordable prices

Performance

- Affordable choice: continued availability of over

200

cars available at 'nil advance payment' during the first half of the year

- Range of choice:

39

manufacturers represented on the Scheme, and a choice from over 99% of vehicle brands (weighted by share of the UK market)

- Dealer coverage: excellent coverage across over

4,900

approved dealers

Improve reach and awareness

We seek to create improved awareness and understanding of the Scheme proposition within our potential market. In doing so we attract new customers to the Scheme

Performance

- Growth in customer numbers:

3.2%

growth in customer numbers, driven by improved awareness of the Scheme offering

- Renewal rate: sustained above

92%

through the economic cycle

- Customer advocacy of the Scheme: Over

95%

of customers would recommend the Scheme to a friend or relative

Ensure long-term sustainability

We ensure that our business model, finances, people, reputation and infrastructure are geared to support the long-term sustainability of the Scheme

Performance

- Credit rating:

A+/A2

rating maintained, with a stable oulook

- Reserves sufficiency: Balance sheet reserves continue to track within the target corridor
- Financing: Further diversified into the bond market, with average tenor of financing in excess of 6.5 years

Interim management report continued

Summary of our key risks and mitigations

At Motability Operations we recognise that sound risk management is fundamental to the successful and sustainable operation of the business. Through our comprehensive risk management processes we identify and assess the potential risks that we face. Having understood the nature of these risks, we ensure that we have the appropriate mitigants in place to reduce these exposures. We use Economic Capital principles to determine and manage our reserves position in the context of these risks. Through this policy and approach we ensure that the business remains sustainable through the economic cycle. The table below summarises our key risks and mitigations. There is no material change in the risk profile compared with that reported at the September 2009 financial year end.

Risk factors	Potential impact	Mitigation
Residual values		
Unexpected movements in used car values, failure to achieve market value on disposal	• Volatility in profitability, reserves and pricing. Potential impact on affordability and choice	• Sophisticated in-house residual value setting and forecasting process • Risk Capital management for asset risk using Economic Capital principles • Market-leading remarketing approach
Supplier failure		
Failure of key manufacturer or other key Scheme supplier	• Compromised customer service provision and potential financial impact of securing alternative supplier • In case of manufacturer failure, likely impairment of residual values and threatened availability of parts and warranties	• Active monitoring of credit ratings and market announcements • Strong supplier relationships and communication • Diversified portfolio
Credit		
Risk of default of key income-streams and exposure to bad debt	• Potential impact on cash inflows and consequent write-off to Income statement	• Principal income stream received directly from DWP – therefore minimal credit risk • Residual credit risks are managed through credit assessments and an effective credit control function
Treasury		
Exposure to interest movements, liquidity, funding, counterparty and operational risk	• Potential impacts include volatility in funding costs, with knock-on effects on lease pricing, and lack of availability of growth funding	• Majority of funding on fixed rates or fixed through interest rate swaps • Balanced portfolio of funding maturities and diversification into bond market • Maintenance of good credit rating • Good treasury system, controls and governance

Statement of Directors' responsibilities

The Directors confirm that this condensed consolidated interim financial information has been prepared in accordance with IAS 34 as adopted by the European Union and that the interim management report includes a fair review of the information required by DTR 4.2.7 namely:

- an indication of important events that have occurred during the first six months and their impact on the condensed set of financial statements, and
- a description of the principal risks and uncertainties for the remaining six months of the financial year.

By order of the Board

Mike Betts
20 May 2010
Chief Executive

David Gilman
20 May 2010
Finance Director

Independent review report to the Directors of Motability Operations Group plc

We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 31 March 2010, which comprises the Consolidated Income Statement, the Consolidated Balance Sheet, the Consolidated Cash Flow Statement, the Consolidated Statement of Comprehensive Income, the Consolidated Statement of Changes in Equity and related notes. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

Directors' responsibilities

The half-yearly financial report is the responsibility of, and has been approved by, the Directors. The Directors have voluntarily elected to be responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

As disclosed in note 2, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting", as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review. This report, including the conclusion, has been prepared for and only for the Directors as a body for management purposes and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing. We consent to disclosure of our report to assist the Company to comply with the Disclosure and Transparency Rules of the Financial Services Authority, as adopted, without accepting or assuming responsibility to any other party on our part.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 31 March 2010 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants
London, United Kingdom
20 May 2010

Consolidated income statement

For the six months ended 31 March 2010

	Note	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Revenue	4	1,194,672	1,062,596
Net operating costs	6	(959,887)	(931,700)
Total surplus from operations		234,785	130,896
Finance costs	7	(68,352)	(74,163)
Surplus before tax		166,433	56,733
Tax	8	(46,699)	(15,982)
Surplus for the period		119,734	40,751

All amounts in current and prior periods relate to continuing operations (see note 2).

The surplus is non-distributable and held for the benefit of the Scheme.

Consolidated statement of comprehensive income

For the six months ended 31 March 2010

	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Surplus for the period	119,734	40,751
Other comprehensive income:		
Gains/(losses) on cash flow hedges	14,859	(54,262)
Tax on items taken directly to equity	(4,161)	15,193
Other comprehensive income/(deficit) for the period, net of tax	10,698	(39,069)
Total comprehensive income for the period attributable to equity	130,432	1,682

Consolidated balance sheet

As at 31 March 2010

	Note	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Assets				
Non-current assets				
Intangible assets		4,665	5,929	7,002
Property, plant and equipment		3,066	3,675	3,842
Assets held for use in operating leases	9	3,892,158	3,704,716	3,513,931
Deferred tax asset		6,774	10,935	16,279
Hire purchase receivables		51,620	50,423	44,026
Derivative financial instruments	13	–	–	–
		3,958,283	3,775,678	3,585,080
Current assets				
Trade and other receivables		170,035	144,454	246,601
Hire purchase receivables		22,511	22,029	20,303
Inventories	10	60,719	52,912	38,703
Cash and bank balances		33,497	57	24,375
		286,762	219,452	329,982
Total assets		4,245,045	3,995,130	3,915,062
Current liabilities				
Deferred income	11	(127,932)	(116,579)	(110,957)
Trade and other payables		(93,847)	(99,033)	(179,842)
Corporation tax payable		(53,425)	–	–
Derivative financial instruments	13	(10,901)	(31,098)	–
Financial liabilities	12	(78,635)	(95,968)	(32,469)
		(364,740)	(342,678)	(323,268)
Net current liabilities		(77,978)	(123,226)	6,714
Non-current liabilities				
Deferred income	11	(135,969)	(132,795)	(129,287)
Derivative financial instruments	13	(5,424)	(86)	(51,168)
Financial liabilities	12	(2,447,642)	(2,352,115)	(2,484,950)
Deferred tax liabilities		(409,533)	(416,259)	(352,706)
Long-term provisions		(1,753)	(1,645)	(1,536)
		(3,000,321)	(2,902,900)	(3,019,647)
Total liabilities		(3,365,061)	(3,245,578)	(3,342,915)
Net assets		879,984	749,552	572,147
Equity				
Share capital		50	50	50
Fair value reserve		(11,754)	(22,452)	(36,841)
Retained reserves (*)		891,688	771,954	608,938
Issued share capital and reserves		879,984	749,552	572,147

(*) All reserves are retained for the benefit of the Scheme. As regards ordinary shareholders, there is no dividend entitlement.

These financial statements were approved by the Board of Directors on 20 May 2010.

Mike Betts
Chief Executive

Consolidated statement of changes in equity

For the six months ended 31 March 2010

	Share capital £'000	Fair value reserve £'000	Retained reserves £'000	Total £'000
At 1 October 2008	50	2,228	568,187	570,465
Comprehensive income				
Surplus for the period	–	–	40,751	40,751
Other comprehensive income				
Change in fair value of hedging derivatives (net of tax)	–	(39,069)	–	(39,069)
Total comprehensive income		(39,069)	40,751	1,682
At 31 March 2009	50	(36,841)	608,938	572,147
At 1 October 2009	50	(22,452)	771,954	749,552
Comprehensive income				
Surplus for the period	–	–	119,734	119,734
Other comprehensive income				
Change in fair value of hedging derivatives (net of tax)	–	10,698	–	10,698
Total comprehensive income		10,698	119,734	130,432
At 31 March 2010	50	(11,754)	891,688	879,984

Consolidated cash flow statement

For the six months ended 31 March 2010

	Note	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Cash flows from operating activities	14	(43,926)	(88,998)
Cash flows from investing activities			
Purchase of corporate property, plant and equipment and intangible assets		(306)	(3,292)
Proceeds from sale of corporate property, plant and equipment		210	264
Net cash used in investing activities		(96)	(3,028)
Financing activities			
Issue of preference shares		–	–
Issue of ordinary shares		–	–
New loans raised		395,106	100,000
Bank loans repaid		(352,500)	–
Net cash generated from financing activities		42,606	100,000
Net increase/(decrease) in cash and cash equivalents		(1,416)	7,974
Cash and cash equivalents at beginning of period		(29,201)	(14,792)
Cash and cash equivalents at end of period		(30,617)	(6,818)

The notes on pages 12 to 19 form part of these financial statements

Notes to the interim financial statements

1. General information

Motability Operations Group plc is a company incorporated in the United Kingdom under the Companies Act 1985, whose shares are privately owned. The address of the registered office is City Gate House, 22 Southwark Bridge Road, London SE1 9HB.

Motability Operations Group plc ('the Company') and its subsidiaries will be referred to as 'the Group' in this report.

These condensed financial statements are presented in pounds sterling because that is the currency of the primary economic environment in which the Company operates.

This condensed consolidated half-yearly financial information does not comprise statutory accounts within the meaning of section 434 of the Companies Act 2006. Statutory accounts for the year ended 30 September 2009 were approved by the Board of Directors on 9 December 2009 and delivered to the Registrar of Companies. The report of the auditors on those accounts was unqualified, did not contain an emphasis of matter paragraph and did not contain any statement under section 498 of the Companies Act 2006.

This condensed consolidated half-yearly financial information has been reviewed, not audited.

Accounting convention

The financial statements have been prepared under the historical cost convention as modified by the revaluation of derivatives and in accordance with applicable accounting standards.

2. Significant accounting policies

Basis of preparation

This condensed consolidated half-yearly financial information for the six months ended 31 March 2010 has been prepared in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Service Authority and IAS 34, 'Interim financial reporting' as adopted by European Union. The condensed consolidated half-yearly financial information should be read in conjunction with the annual financial statements for the year ended 30 September 2009, which have been prepared in accordance with IFRSs as adopted by the European Union.

Except as described below, the accounting policies applied are consistent with those of the annual financial statements for the year ended 30 September 2009, as described in those annual financial statements.

Taxes on income in the interim periods are accrued using the tax rate that would be applicable to expected total annual earnings.

In the first half of the financial year, the Group adopted IAS 1 "Presentation of Financial Statements- Revised". Adoption of the revised standard has amended the presentation of the financial statements. The effect has been to replace the statements of recognised income and expense and the reconciliation of changes in equity with a statement of comprehensive income and a statement of changes in equity. There has been no change to the recognition, measurement or disclosure of transactions and events resulting from the adoption of the revised IAS 1.

The following standards and amendments and interpretations to existing standards, issued after the issue of the last annual accounts, are not yet effective and will not be effective for the financial year beginning on 1 October 2009 and have not been early adopted by the Group:

IFRS 9, 'Financial Instruments: Classification and measurement' (November 2009)

IFRS for SMEs 'International Financial Reporting Standards for Small and Medium-sized Entities'

IAS 24, 'Related Party Disclosures – Revised definition of related parties'

IAS 32, 'Financial Instruments: Presentation' – Amendments relating to classification of rights issues

IFRIC 19, 'Extinguishing Financial Liabilities'

IFRIC 14, (amendment) – 'Prepayments of a Minimum Funding Requirement'

The Directors anticipate that the adoption of these standards, interpretations and amendments in future periods will have no material impact on the financial statements of the Group.

3. Critical accounting judgments and key sources of estimation uncertainty

In the application of the Group's accounting policies, the Directors are required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources.

The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Critical judgments in applying the Group's accounting policies:

Residual values of operating lease assets

The method by which the Directors have determined the Group's residual values of the operating lease assets is described in note 9. Because of the inherent uncertainty associated with such valuation methodology, and in particular the volatility of the prices of second-hand vehicles, the carrying value of the residual values of the operating lease assets may differ from their realisable value (see note 9).

3. Critical accounting judgments and key sources of estimation uncertainty continued

Derivatives

As described in note 13, the Directors use their judgment in selecting appropriate valuation techniques for financial instruments not quoted in an active market. For derivative financial instruments, assumptions are made based on the quoted market rates adjusted for the specific features of the instruments.

4. Revenue

An analysis of the Group's revenue is provided below.

	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Rentals receivable	699,318	639,008
Proceeds from disposal of operating lease assets	491,083	419,576
Contingent rentals	152	60
Hire purchase earnings	3,701	3,268
Other income	418	684
Total revenue	1,194,672	1,062,596

Contingent rentals relate to variable charges for excess mileage.

5. Segmental analysis

The Motability Operations Group is managed as a single integrated business unit. Accordingly no segmental analysis is applicable.

6. Net operating costs

An analysis of the Group's net operating costs is provided below:

	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Net book value of disposed operating lease assets	468,193	423,562
Fleet operating costs including insurance, maintenance and roadside assistance costs	172,046	178,599
Other product costs including continuous mobility costs, adaptations support, communications	7,517	6,950
Employee costs	16,027	15,636
Other operating costs	9,953	8,946
Legal and professional fees	1,093	4,344
Bad debt charges and movement in bad debt provisions	3,329	3,707
Management fees	1,250	1,250
Motability levy and rebates	1,950	2,221
Net operating costs before depreciation	681,358	645,215
Depreciation on assets used in operating leases (*)	276,532	285,530
Depreciation on property, plant and equipment and intangible assets	1,997	955
Net operating costs	959,887	931,700

(*) The depreciation charge on assets used in operating leasing includes a £11.8m release (six months ended 31 March 2009: £18.3m charge) relating to the change in estimate during the period of future residual value (see note 9).

7. Finance costs

	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Interest and charges on bank loans and overdrafts	33,576	71,736
Interest on debt issued under the Euro Medium Term Note Programme	32,006	–
Interest receivable	(30)	(38)
Amortisation of fees relating to financing	2,451	2,116
Preference dividends	349	349
Total finance costs	68,352	74,163

Notes to the interim financial statements continued

8. Tax

The major components of the Group tax expense are:

	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Current tax		
Charge for the period	53,425	–
Total	53,425	–
Deferred tax		
Origination and reversal of temporary differences	(6,726)	15,982
Total	(6,726)	15,982
Tax on surplus from continuing operations	46,699	15,982

Income tax expenses have been recognised based on management's best estimate of the weighted average annual income tax rate expected for the full financial year. Estimated average annual tax rate used for the year to 30 September 2010 is 28.1% (the estimated tax rate for the six months ended 31 March 2009 was 28.2 %).

9. Assets held for use in operating leases

	Motor vehicle assets £'000
Cost	
At 1 October 2008	4,250,780
Additions	817,439
Transfer to inventory (note 10)	(603,103)
At 31 March 2009	4,465,116
At 1 October 2009	4,679,239
Additions	940,344
Transfer to inventory (note 10)	(689,016)
At 31 March 2010	4,930,567
Accumulated depreciation	
At 1 October 2008	868,152
Charge for the period	285,530
Eliminated on transfer to inventory (note 10)	(202,497)
At 31 March 2009	951,185
At 1 October 2009	974,523
Charge for the period	276,532
Eliminated on transfer to inventory (note 10)	(212,646)
At 31 March 2010	1,038,409
Carrying amount	
At 31 March 2010	3,892,158
At 30 September 2009	3,704,716
At 31 March 2009	3,513,931

Residual values

Residual values represent the estimated net sale proceeds expected from the sale of the asset at the end of the leasing period. A review is undertaken at the balance sheet date using market data to identify net residual values which differ from the sum anticipated at the inception of the lease.

In addition, the assets' resale market value and disposal costs structure are monitored and the process of realising asset values is managed in order to seek to maximise the net sale proceeds.

9. Assets held for use in operating leases continued

The following residual values are included in the calculation of the net book value of fixed assets held for use in operating leases:

Years in which unguaranteed residual values are recovered

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Within 1 year	965,849	796,063	682,901
Between 1-2 years	939,579	983,109	890,182
Between 2-5 years	985,793	936,221	1,050,582
Total exposure	2,891,221	2,715,393	2,623,665

The total unguaranteed residual value exposure presented above consists of the original priced residual values net of revisions in estimation (see the 'Critical accounting judgments' policy in note 3). The amounts resulting from changes in estimates on the live fleet at the balance sheet date are detailed below, together with the timing of the effects on the income statement.

Effects of changes in estimates included in the unguaranteed residual values above

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Prior years	(12,085)	(39,471)	(66,755)
Current year	4,315	27,386	(18,271)
Amounts carried at 31 March/30 September	(7,770)	(12,085)	(85,026)
Amounts to be charged in future years	(7,153)	(44,145)	8,537
Total effect of changes in estimated residual value	(14,923)	(56,230)	(76,489)

The Group and Company as lessor

The rentals receivable are determined by the Disability Allowances and as such include income in respect of services and insurance. The future rentals receivable under non-cancellable operating leases with customers, in total, for each of the following three periods after the balance sheet date are:

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Within 1 year	1,105,007	1,070,552	1,036,627
Between 2-5 years	878,867	857,210	994,101
	1,983,874	1,927,762	2,030,728

10. Inventories

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Ex-operating lease assets held for sale	61,446	53,269	38,953
Provisions	(727)	(357)	(250)
Ex-operating lease assets held for sale (net)	60,719	52,912	38,703

Inventories represent the operating lease assets previously held for rental to others and which cease to be rented and become held for sale as of the balance sheet date. As of the balance sheet date, £727k has been provided against irrecoverable vehicles (30 September 2009: £357k, 31 March 2009: £250k).

The cost of inventories recognised as expense and included in net operating costs amounted to £468,193k (31 March 2009: £423,562k).

The movement of the inventories in first six month period ended 31 March 2010 and 2009 respectively are as follows;

	£'000
At 1 October 2008	61,909
Transfer from operating lease assets (note 9)	400,606
Disposals	(423,562)
At 31 March 2009	38,953
At 1 October 2009	53,269
Transfer from operating lease assets (note 9)	476,370
Disposals	(468,193)
At 31 March 2010	61,446

Notes to the interim financial statements continued

11. Deferred income

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Customers' advance payments (*)	101,478	96,793	89,473
Vehicle maintenance income	9,832	8,748	9,508
Vehicle good condition bonus income	16,622	11,038	10,455
Deferred funding break costs benefits	–	–	1,521
Total current	127,932	116,579	110,957
Customers' advance payments (*)	86,905	87,269	83,965
Vehicle maintenance income	33,408	34,076	34,202
Vehicle good condition bonus income	15,656	11,450	11,120
Total non-current	135,969	132,795	129,287
Total	263,901	249,374	240,244

(*) Customers may choose a leased vehicle where the price exceeds the mobility allowance. In such cases they make an advance payment which is recognised over the life of the lease.

12. Financial liabilities

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Current bank loans	–	52,500	–
Accrued interest and coupon	14,521	14,209	1,276
Bank overdrafts	64,114	29,259	31,193
Total current	78,635	95,968	32,469
Non-current			
Bank borrowings	1,100,000	1,400,000	2,475,000
Debt issued under the Euro Medium Term Note Programme (less unamortised discount and transaction costs)	1,337,692	942,165	–
Preference shares	9,950	9,950	9,950
Total non-current	2,447,642	2,352,115	2,484,950
Total	2,526,277	2,448,083	2,517,419
The financial liabilities are repayable as follows:			
On demand or due within one year	78,635	95,968	32,469
Due within two years	–	–	–
Due within two to five years	1,100,000	1,400,000	2,475,000
Due in more than five years	1,347,642	952,115	9,950
Total	2,526,277	2,448,083	2,517,419

All borrowings are denominated in sterling.

Bank borrowings

All bank borrowings as at 31 March 2010 and 2009 are at floating rates.

As at 31 March 2010 the Group has the following principal bank loans:

a) A five year Term Loan of £1,000m (30 September 2009: £1,000m, 31 March 2009: £1,000m) taken out 26 June 2008. Loan repayment date is 26 June 2013.

b) A five year Revolving Credit Facility of £900m (30 September 2009: £900m, 31 March 2009: £900m) taken out 26 June 2008 of which £100m drawn as at 31 March 2010 (30 September 2009: £400m, 31 March 2009: £475m). Facility repayment date is 24 June 2013.

During the period, a three year Term Loan of £50m taken out 26 June 2008 (with an original repayment date of 24 June 2011) was repaid early in October 2009.

All bank borrowings carry LIBOR interest rates plus bank margins at a market rate.

12. Financial liabilities continued

Debt issued under the Euro Medium Term Note Programme

During the period the Company issued fixed rate bonds on 28 January 2010 with a nominal value of £400m with a semi-annual coupon of 5.375%. These bonds mature on 28 June 2022. Bonds were issued under the £2,000m Euro Medium Term Note Programme of the Company with denominations of £50,000. The bonds were admitted to trading on London Stock Exchange's regulated market and have been admitted to the Official List. The £2,000m Euro Medium Term Note Programme of the Company is unconditionally and irrevocably guaranteed on a joint and several basis by the Group companies, namely Motability Operations Limited, Motability Leasing Limited and Motability Hire Purchase Limited. The payments of all amounts due in respect of notes will be unconditionally and irrevocably guaranteed on a joint and several basis by these companies. Total nominal value of the issued bonds as at 31 March 2010 amounts to £1,350m (30 September 2009: £950m, 31 March 2009: £nil).

Preference shares

Cumulative preference shares of £9,950,000 were issued on 30 June 2008 at an issue price of £1 per share. The shares carry interest at 7%. The preference shares of the Group are classified as a financial liability in accordance with the contractual obligation to deliver cash (both dividends and repayment of principal) to the shareholders on winding up as stated in the Memorandum and Articles of Association of the Company.

The weighted average interest rates on borrowings as at 31 March 2010, 30 September 2009 and 31 March 2009 were as follows:

	31 March 2010 %	30 September 2009 %	31 March 2009 %
Current bank loans and overdrafts	–	1.8	–
Non-current bank loans	1.4	1.4	1.9
Non-current debt issued under the Euro Medium Term Note Programme	5.7	5.9	–
Non-current preference shares	7.0	7.0	7.0

At 31 March 2010, 30 September 2009 and 31 March 2009, the Group had the following undrawn committed borrowing facilities:

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Working capital facility (*)	100,000	97,500	100,000
Revolving credit facility	800,000	500,000	425,000
Total	900,000	597,500	525,000

(*) Working Capital facilities of the Group are cross guaranteed between Group companies Motability Operations Limited and Motability Operations Group plc.

Undrawn committed facilities expire as follows:

	31 March 2010 £'000	30 September 2009 £'000	31 March 2009 £'000
Within 1 year	100,000	97,500	100,000
Within 1-2 years	–	–	–
Within 2-5 years	800,000	500,000	425,000
Total	900,000	597,500	525,000

Notes to the interim financial statements continued

13. Derivative financial instruments

	31 March 2010		30 September 2009		31 March 2009	
	Fair value £'000	Notional amounts £'000	Fair value £'000	Notional amounts £'000	Fair value £'000	Notional amounts £'000
Cash flow hedges						
Interest rate swaps	(16,325)	1,900,000	(31,184)	1,325,000	(51,168)	2,100,000
	(16,325)	1,900,000	(31,184)	1,325,000	(51,168)	2,100,000
Included in non-current liabilities (*)	(5,424)	1,000,000	(86)	100,000	(51,168)	2,100,000
Included in current liabilities	(10,901)	900,000	(31,098)	1,225,000	–	–
Derivative financial instrument liabilities	(16,325)	1,900,000	(31,184)	1,325,000	(51,168)	2,100,000

(*) During the period, the Company entered into two forward starting swaps effective dates of which are June and September 2010 and which will replace the maturing extant swaps. £900m of the notional amounts in non-current liabilities belongs to these forward starting swaps. The fixed rates of the forward starting swaps vary from 1.92% to 2.45%.

At 31 March 2010, the fixed interest rates vary from 1.62% to 5.95% (30 September 2009: 1.62% to 5.95%, 31 March 2009: 1.62% to 5.95%,) and the main floating rates are LIBOR. Gains and losses recognised in the fair value reserve in equity on interest rate swap contracts as of 31 March 2010 will be continuously released to the income statement in accordance with the maturity of the swap contracts. The undiscounted cash flows are settled on a net basis.

14. Notes to the cash flow statement

Reconciliation of surplus to net cash flow from operating activities:

	Six months ended 31 March 2010 £'000	Six months ended 31 March 2009 £'000
Operating surplus from operations	234,785	130,896
Adjustments for:		
Depreciation charge on corporate assets	1,997	955
Depreciation charge on operating lease assets	276,532	285,530
(Gains)/losses on disposal of operating lease assets	(22,890)	3,986
Gains on disposal of corporate assets	(28)	(6)
(Decrease)/increase in provisions	(1,261)	168
Operating cash flows before movements in working capital	489,135	421,529
Purchase of assets held for use in operating leases	(940,344)	(817,439)
Proceeds from sale of assets held for use in operating leases	491,083	419,576
(Increase)/decrease in receivables	(25,522)	26,015
Increase in deferred income	14,527	14,148
Increase in creditors	(5,186)	(25,185)
Cash generated from operations	23,693	38,644
Net interest paid	(67,619)	(76,993)
Income taxes paid	–	(50,649)
Net cash flows from operating activities	(43,926)	(88,998)

Cash and cash equivalents are net of cash and bank balances (which include uncleared cash transactions in the last two business days) and the bank overdrafts.

15. Analysis of changes in net debt

	At 1 October 2009 £'000	Cash flows £'000	Non-cash flows £'000	At 31 March 2010 £'000
Cash and bank balances	57	33,441	–	33,498
Borrowings due within one year	(95,968)	17,643	(310)	(78,635)
Borrowings due after one year	(1,400,000)	300,000	–	(1,100,000)
Debt issued under the Euro Medium Term Note Programme due after one year	(942,165)	(395,106)	(421)	(1,337,692)
Preference shares	(9,950)	–	–	(9,950)
	(2,448,026)	(44,022)	(731)	(2,492,779)

	At 1 October 2008 £'000	Cash flows £'000	Non-cash flows £'000	At 31 March 2009 £'000
Cash and bank balances	7,525	16,850	–	24,375
Borrowings due within one year	(23,377)	(8,876)	(216)	(32,469)
Borrowings due after one year	(2,375,000)	(100,000)	–	(2,475,000)
Preference shares	(9,950)	–	–	(9,950)
	(2,400,802)	(92,026)	(216)	(2,493,044)

16. Retirement benefit schemes

The Motability Operations Limited pension plan is a non-contributory group personal pension (money purchase) scheme. The charge for the six months ended 31 March 2010 amounted to £1,358k (six months ended 31 March 2009: £1,305k). Net contributions due at the balance sheet date were £227k (31 March 2009: £232k).

17. Related parties

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

Related parties comprise Directors (and their close families and service companies), the Motability Charity and the Shareholder Banks. Transactions entered into with related parties are in the normal course of business and on an 'arm's length' basis.

The relationship of the Group to the Motability Charity is set out on pages 2 and 3.

Transactions

During the six months ended 31 March 2010 Motability grants totalling £10,866k were awarded to customers and paid to the Group to enable vehicles to be purchased on their behalf (six months ended 31 March 2009: £9,247k). During the same period, the Group also paid £1,463k relating to Motability administration costs (six months ended 31 March 2009: £1,362k). A further £1,356k (six months ended 31 March 2009: £884k) was paid as rebates in respect of grant awards towards advance payments where customers terminated their hire agreements and rebates in respect of grants made where the Group managed adaptations could not be processed. In addition, £487k was paid as a rebate negotiated with Motability which effectively removes the risk pricing from vehicles acquired with charitable grants (six months ended 31 March 2009: £859k). £860 was donated to Motability's charitable funds during the period (six months ended 31 March 2009: £918).

The funding of the Group through bank loans is provided by the Shareholder Banks on commercial terms as detailed in note 12 (see note 7 for details of financing costs). Additionally, total fees of £1,250k (six months ended 31 March 2009: £1,250k) were due to the Shareholder Banks in equal proportions for management and advisory services.

Notes

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Motability Operations Group plc

City Gate House
22 Southwark Bridge Road
London SE1 9HB
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Company Number 6541091

www.motabilityoperations.co.uk