# Royal Mail Holdings plc

Preliminary statement
for the full year ended 25 March 2012

Royal Mail Group

# Our Results Statement

## Royal Mail Group financial results for the year ended 25 March 2012

| Key Financial Highlights | FY to 25 March 2012 (£m) | FY to 27 March 2011 (£m) |
|---|---|---|
| Group external revenue | 9,532 | 9,156 |
| Operating profit after modernisation costs[1] | 211 | 39 |
| Free cash inflow/(outflow) | 234 | (213) |

### Profit and cash flow

- Group operating profit after modernisation costs[1] increased from £39 million to £211 million.
- UKPIL returned to operating profit after modernisation costs[1] of £23 million from a loss of £120 million in 2011.
- No pension deficit payment to the Royal Mail Pension Plan (RMPP) was made during the year (see Balance Sheet). In the previous year, a payment of £292 million was made.
- The Group's overall operating profit margin after modernisation costs[1] increased from 0.4 per cent in the prior year to 2.2 per cent. The margin remains low compared to many other major postal operators.

### External Revenue and Volumes

- Group external revenue increased four per cent to £9.5 billion after two successive years of decline. Parcels are the single biggest contributor to Group revenues.
- External revenues in UK Parcels, International and Letters (UKPIL), our core UK business, increased from £6.9 billion to £7.2 billion.
- UKPIL's domestic parcel volumes were up six per cent during the year. Traditional letter volumes declined six per cent.
- UKPIL parcels revenue increased 10 per cent to £2.6 billion, driven by strong growth in online retailing. Revenues at GLS, our continental European parcels business, increased by five per cent to £1.6 billion.

### Balance Sheet

- On 1 April 2012, almost all of RMPP's pension liabilities and pension assets, built up until 31 March 2012, were transferred to HM Government, leaving the RMPP fully funded at that date.
- In light of this post-balance sheet event, Royal Mail Group is a going concern.

Moya Greene, Chief Executive Officer, Royal Mail Group, said: "Royal Mail Group has made significant progress over the last year successfully addressing cash flow, profitability and balance sheet issues. We are cash positive for the first time in four years, our profitability is improving and we no longer have going concern issues.

"We have a clear strategy in place and it is delivering results. We are addressing the structural decline in the traditional letters market by improving efficiency across our operations and adapting our network to accommodate the ever-increasing number of parcels being sent. We recognise, however, that there is much more to be done. Our commitment to executing our strategies is key. Our increased focus on the parcels market and our growing international businesses is helping to build a strong commercial future for the Group."

[1] before other operating exceptional items

# Who we are

**As the sole provider of the Universal Service in the UK, Royal Mail Group reaches everyone. We deliver six days a week, to over 29 million addresses across the UK, at affordable and competitive prices.**

**The Group is a key component of the UK's economic and social infrastructure, providing services to private individuals, companies and communities. In 2011-12, we employed nearly 159,000 people in the UK, contributing £5.3 billion to the economy in wages and other related people costs, and a further £2.4 billion buying goods and services.**

We are proud to deliver the Universal Service. But, it does require a high fixed-cost network. Our strategy aims to tackle the key challenges facing Royal Mail Group to build a sustainable, diversified business, secure the future provision of the Universal Service and attract external capital.

The Postal Services Act 2011 has set out the steps the Group must take to secure external investment. We have made good progress restoring the Group to financial stability, obtained significant deregulation and secured European approval of the transfer of almost all of the Royal Mail Pension Plan's pension liabilities and pension assets to HM Government.

A great deal remains to be done to secure further profitable revenue growth and deliver the efficiencies required through the modernisation of our core network. This report explains how we will seek to do so.

Our modernisation programme – one of the largest ever undertaken in the UK – is about managing the structural decline in the traditional letters market by making our network more efficient and effective.

To succeed in one of the most liberalised and competitive markets in the EU, we are adapting our network, which has traditionally focused on delivering letters, to also accommodate ever increasing parcel volumes. This is a major strategic priority.

**Five year Group revenue (£m)**

| **2012** | 2011 | 2010 | 2009 | 2008 |
|---|---|---|---|---|
| **9,532** | 9,156 | 9,349 | 9,560 | 9,388 |

**Five year Group operating profit/(loss) after modernisation costs[1] (£m)**

| **2012** | 2011 | 2010 | 2009 | 2008 |
|---|---|---|---|---|
| **211** | 39 | 180 | 122 | (482) |

**Five year Group free cash inflow/(outflow) (£m)**

| **2012** | 2011 | 2010 | 2009 | 2008 |
|---|---|---|---|---|
| **234** | (213) | (545) | (678) | 237 |

On 1 April 2012, Royal Mail Group Ltd separated from Post Office Limited. References to "Royal Mail Group" or "the Group" with respect to the financial year ending 25 March 2012 (including financial information) include Post Office Limited unless expressly stated.

In forward looking statements or comments, including those with regard to the business strategy, "Royal Mail Group" or "the Group" excludes Post Office Limited. See the diagrams on p4 for changes to the Group's structure.

[1] Before other operating exceptional items.

# Who we are (continued)

Our parcels businesses now account for 48 per cent of Group revenue (excluding Post Office Limited). They contributed £4.2 billion of revenues to the Group in 2011-12, including £1.6 billion from our European logistics business, General Logistics Systems (GLS).

Despite increasing parcel volumes, the core UK parcels network is loss-making. We are taking steps to reduce these losses and make the network more efficient. At the same time, we are seeking to grow our profitable networks like Parcelforce Worldwide.

Royal Mail Group is building its marketing mail business, which delivers promotional direct marketing mail to UK homes and businesses, as well. It already accounts for more than £1 billion of our annual Group revenue. Working with a number of commercial partners, we will  provide to businesses, large and small, a “one stop shop” covering creative development, production, distribution and customer data management for advertising mail. This strategy is in the early stages of its delivery as we seek to add value for our customers at each point in the value chain.

**Our business is changing**
We are embedding our strategy – and its delivery – across Royal Mail Group. In the full Annual Report, we set out the main elements of this strategy, the ways in which we will deliver it and the Key Performance Indicators (KPIs) we will use to track our progress.

Royal Mail has obtained significant deregulation. Last year, more than 80 per cent of our revenues were subject to direct price regulation. Following the announcement of Ofcom’s new regulatory approach on 27 March 2012, direct price control now affects almost 10 per cent of Royal Mail’s revenues.

**Revenue by business and market (£m)**

| | Growth | | Traditional | | | |
|---|---|---|---|---|---|---|
| Business segment/ product | Parcels | Marketing mail | Letters & other mail[2] | Counter services | Other services | Total |
| UK Parcels, International & Letters (UKPIL) | 2,592 | 1,063 | 3,509 | – | – | **7,164** |
| General Logistics Systems (GLS) | 1,562 | – | – | – | – | **1,562** |
| Post Office Limited | – | – | – | 801 | – | **801** |
| Other | – | – | – | – | 5 | **5** |
| | **4,154** | **1,063** | **3,509** | **801** | **5** | **9,532** |

**Percentage of revenue by market**

| | Group revenues | Group revenues (Excluding Post Office Limited) |
|---|---|---|
| Parcels | 44 per cent | 48 per cent |
| Letters & other mail[2] | 37 per cent | 40 per cent |
| Marketing mail | 11 per cent | 12 per cent |
| Counter services | 8 per cent | – |

[2] Includes traditional white letters, publishing, data and philatelic.

To reflect Royal Mail Group Ltd's separation from Post Office Limited on 1 April 2012, we are reporting our revenues including and excluding Post Office Limited. We are also showing the contributions of traditional and growth revenue streams to our business. We will continue to consolidate Post Office Limited's financial performance in future reports.

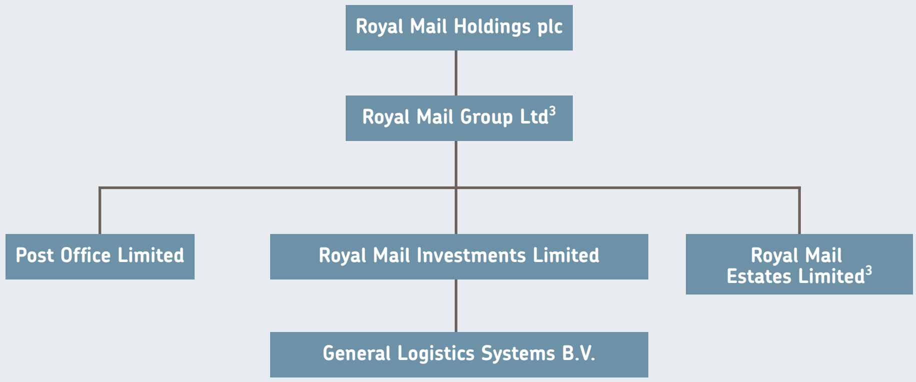
**Group legal structure**

Royal Mail Holdings plc is directly owned by HM Government. It is the ultimate parent company of Royal Mail Group Ltd. The Group primarily operates within the United Kingdom, including a number of subsidiaries, associates and a joint venture. It also has a presence in most European countries, mainly through General Logistics Systems. The basic legal structure of the Group as at 25 March 2012 is shown in Diagram one.

On 1 April 2012, Post Office Limited was transferred from under the ownership of Royal Mail Group Ltd to become a direct subsidiary of Royal Mail Holdings plc. The revised Group structure at this date is as shown in Diagram two.

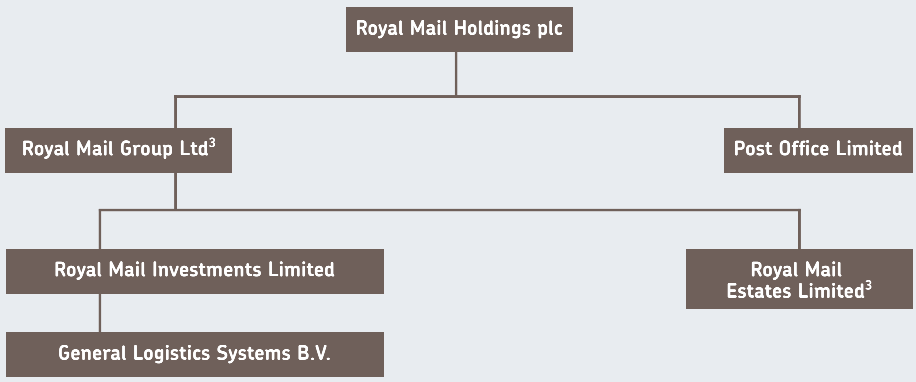
**25 March 2012 – pre-separation**

Diagram one




**1 April 2012 – post-separation**

Diagram two




[3] The UK Parcels, International & Letters (UKPIL) business unit is not a separate legal entity and is included within Royal Mail Group Ltd and Royal Mail Estates Limited. See p32 for details of the UKPIL business unit.

# Financial and business performance highlights

## Our financial performance

| Business unit | External revenue 2012 £m | External revenue 2011 £m | Operating profit/(loss) after modernisation costs[1] 2012 £m | Operating profit/(loss) after modernisation costs[1] 2011 £m |
|---|---|---|---|---|
| UK Parcels, International & Letters (UKPIL) | **7,164** | 6,857 | **23** | (120) |
| General Logistics Systems (GLS) | **1,562** | 1,485 | **128** | 118 |
| Other | **5** | 38 | **1** | 20 |
| **Royal Mail Group excluding Post Office Limited** | **8,731** | 8,380 | **152** | 18 |
| Post Office Limited | **801** | 776 | **59** | 21 |
| **Royal Mail Group** | **9,532** | 9,156 | **211** | 39 |

### Revenues and volumes

- Group external revenue increased by four per cent from last year to £9.5 billion, after two successive years of decline. Parcels are the single biggest contributor to Group revenues.
- Revenues in UKPIL, our core UK business, increased from £6.9 billion to £7.2 billion.
- UKPIL domestic parcel volumes were up six per cent during the year. Traditional letter volumes declined by six per cent, compared to five per cent in the prior year.
- UKPIL parcels revenue increased 10 per cent to £2.6 billion, driven by strong growth in online retailing. Revenues at GLS, our continental European parcels business, increased by five per cent to £1.6 billion.
- UKPIL letters & other mail revenue increased to £3.5 billion as a result of necessary price increases. Marketing mail revenues increased to £1.1 billion (2011 £1 billion).

### Profits and margin

- Group operating profit after modernisation costs[1] increased from £39 million to £211 million.
- UKPIL returned to operating profit after modernisation costs[1] of £23 million (2011 £120 million loss).
- The UK parcels operation is currently loss-making. The cost allocation methodology for this part of the business is under review. We recognise that steps must be taken to grow margin, revenues and volumes and to make the operation more efficient.
- GLS and Post Office Limited remain the biggest contributors to Group operating profit after modernisation costs[1]. Their contributions were £128 million and £59 million respectively.
- The Group's overall operating profit margin after modernisation costs[1] increased from 0.4 per cent in the prior year to 2.2 per cent. However, the margin remains low compared to many other major postal operators. At 0.3 per cent, UKPIL's operating profit margin after modernisation costs[1] is also very modest.

### Cash flow

- Addressing the Group's cash position has been a major priority. The Group recorded a free cash inflow of £234 million, compared to a free cash outflow of £213 million last year. Excluding disposals, the Group's free cash outflow was £8 million, compared to an outflow of £450 million in the previous year.
- No pension deficit payment to the Royal Mail Pension Plan (RMPP) was made during the year. This was a result of the transfer of almost all of the pension liabilities and pension assets of the RMPP to HM Government on 1 April 2012. In the previous year, a payment of £292 million was made.
- Significant cash items in the year were: £467 million (2011 £479 million) spent on ongoing pension contributions and £429 million (2011 £377 million) on modernisation investment in UKPIL.

### Events after the balance sheet date

- On 1 April 2012, almost all of RMPP's pension liabilities and pension assets, built up until 31 March 2012, were transferred to HM Government, leaving the RMPP fully funded at that date.
- However, ongoing pension costs relating to the pensions of approximately 115,000[2] active members, will continue to be material.

### Going concern

- In light of the events after the balance sheet date, Royal Mail Group is a going concern.

[1] Before other operating exceptional items.

[2] Excludes Post Office Limited.

# Financial and business performance highlights (continued)

## Our business performance

### Our modernisation programme

- The modernisation programme, one of the largest business transformations in the UK, is delivering efficiencies and a more customer-focused Royal Mail:
  - Reduction in gross frontline (upstream and downstream) hours[3] of three per cent;
  - 75 per cent of all letters are now automatically sequenced to reflect the order in which they are delivered, this compares with eight per cent in 2009-10, after the first year the programme was deployed;
  - Group reported accidents and injuries in the workplace have reduced by 22 per cent during the year; and
  - New delivery methods have now been introduced in 448 delivery offices. The maximum period of change is now underway. 908 operating delivery offices remain to be modernised.

### Our customers

- Royal Mail handled over 58 million UK inland addressed items daily, compared to nearly 62 million in the previous year. Across its domestic and international operations, the Group handled 1.2 billion parcels during the year.
- Against the backdrop of the modernisation programme, Royal Mail achieved a 92.7 per cent First Class retail Quality of Service performance. At 93 per cent, the First Class retail Quality of Service target is the highest of all major EU countries. With a 98.7 per cent performance, Royal Mail exceeded the Second Class retail Quality of Service target of 98.5 per cent.
- During Christmas 2011, a key trading time for Royal Mail in the UK, 1.4 billion UK inland addressed items were handled, including 86 million parcels. A high quality service was successfully delivered to customers throughout this important period.
- A number of customer initiatives were successfully introduced, including the delivery to neighbour trial, which received a customer satisfaction rating of 92 per cent.

### Regulation

- The announcement by Ofcom of a new regulatory framework on 27 March 2012 has significantly increased Royal Mail's commercial freedom. Direct price controls now affect almost 10 per cent of our revenues.

[3] Includes processing hours.

# Chief Executive Officer's review

**Our Group operating profit margin[1] has improved to 2.2 per cent from 0.4 per cent last year. This remains modest, however, compared to other major postal operators.**

**Moya Greene**
Chief Executive Officer

**A year of significant progress**
In my first review as Chief Executive Officer last year, I explained that the Group was in a precarious financial position and there were many significant regulatory and legislative milestones to achieve.

I am pleased to say we have made significant progress on all fronts. Most importantly, we are now on the way to restoring Royal Mail Group's financial health. Details of our key financial and business achievements can be found on p5. However, it is worth repeating that the business is cash positive[2] for the first time in four years. We have grown revenues in UK Parcels, International & Letters (UKPIL) and it has returned to profitability. General Logistics Systems (GLS) and Post Office Limited have also increased revenues and operating profits[1] during the year.

Of course, this is only the beginning of the process of returning the business to a sound financial footing. Our Group operating profit margin[1] has improved to 2.2 per cent from 0.4 per cent last year. This remains modest, however, compared to other major postal operators.

**Regulatory and legislative environment**
Last year, Royal Mail Group was balance sheet insolvent and had been for some years. That is why, just after the year end on 1 April 2012, we welcomed the transfer of almost all of the pension liabilities and pension assets of the Royal Mail Pension Plan (RMPP) to HM Government. We are grateful to the Secretary of State and his colleagues at the Department for Business, Innovation and Skills (BIS) for their tireless commitment to delivering this transformational milestone.

On 27 March 2012, we were also pleased with the introduction of a new regulatory framework. Our new regulator, Ofcom, has recognised that the prior framework was not appropriate, that price controls had failed and that there was a very real risk to the sustainability of the Universal Service. The new regulatory approach provides us with increased commercial freedoms, to better position us to earn a reasonable return on the services we deliver. This new approach underpins the regulator's primary duty and commitment to safeguarding the Universal Service in the UK.

**Much remains to be done**
Royal Mail Group continues to face significant challenges. The traditional letters market remains in structural decline. Volumes in this market have fallen by more than 25 per cent since 2005-06. We will continue to manage this decline by improving efficiency through the modernisation programme and a range of other measures. We will also adapt our network, which has traditionally handled and delivered letters, to accommodate the ever increasing number of parcels in the traffic mix.

Our core parcels network in the UK – Royal Mail – remains loss-making. We will address this in the coming years with a number of measures that are designed to return parcels to profitability, while adding value through service enhancements our customers want.

We will also continue to deliver significant productivity gains across the business. More than 50,000 people have left the Group in the last decade. As we have said before, we will be a smaller, but a more sustainable, business in the years to come. However, as we are taking costs out, we need to do so without jeopardising our ability to deliver on our Universal Service commitments at the service levels which our customers expect.

**Becoming the best delivery and marketing mail business in the UK**
Our business strategy is about:

**Being brilliant at the basics**

**Building a commercial future**

**Driving profitable growth**

I will now deal with each in turn.

**Brilliant at the basics**
Royal Mail Group is the only business that can deliver the Universal Service – overnight, to more than 29 million addresses across the country, six days a week.

To achieve this, we need to engage and equip our people to deliver a consistently high quality service. Royal Mail must deliver on the promises it makes to its customers and make the right products available at the right prices. In addition, we need to continue to modernise, introduce new technology and delivery methods, cut costs and improve productivity across the business.

[1] After modernisation costs before other operating exceptional items.

[2] Free cash inflow.

# Chief Executive Officer's review (continued)

**Our people**
Royal Mail's postmen and women meet our customers every day on the doorsteps of their homes and businesses. They are our ambassadors: a credit to the company.

Nothing is more important to me than the safety of our employees in the workplace and out on their delivery rounds. Over the course of the year, reported accidents and injuries at work have reduced by 22 per cent. Tragically however, in the past 12 months, seven people have lost their lives due to road traffic accidents. A number of initiatives, including safety courses for all our drivers, are being rolled out across the country to maintain our focus in this critical area.

To ensure all of our people are jointly engaged in our success, we have taken significant steps to overhaul our internal communications. From the beginning of the financial year to mid-April 2012, we published 17 regular and special editions of Courier, our employee magazine. Many senior managers have visited all 11 Royal Mail regions in the UK, talking to around 23,000 colleagues and listening to their concerns. Weekly programmes on Royal Mail TV (RMTV) keep our frontline staff up-to-date on changes we are making and competitive challenges we must meet. So too does myroyalmail.com, our extranet for colleagues.

**Our customers**
We need to continue to put our customer at the centre of every discussion we have – from the Boardroom to the delivery office. Our customer satisfaction levels for business customers are improving, but are still lower than we would like.

We are focused on successfully addressing the root cause of customer complaints. That is why we are working with our customers to identify the five key areas in which we can improve customer service – redirections, misdeliveries, "Something for You" cards, redeliveries and proof of delivery. We have already introduced a range of measures to address them.

Royal Mail is the only postal operator in the UK that is required to publish its performance against delivery targets every quarter. I am proud that we exceeded our target to deliver 98.5 per cent of Second Class retail mail on time. We ended the year just shy of our 93 per cent target for First Class retail mail, with a performance of 92.7 per cent. Against the backdrop of the UK's largest ever business transformation, we still delivered 1.53 billion First Class retail items on a next day basis.

**Modernisation**
Every process that we are involved in – collecting, transporting, sorting and delivering mail – is changing as part of our modernisation programme. The aim of this process is to make our network more efficient: increasing productivity, improving the service our customers receive and reducing the cost of maintaining the Universal Service.

We are optimising our mail centre network, and have closed 16 mail centres in recent years. We are also investing: the automation of the handling of mail in our mail centres is nearly complete. We have installed 64 intelligent letter sorting machines, easing the load on our delivery centres. We are a year ahead of plan in our installation of our walk sequencing equipment. We have put in 574 walk sequencing machines. This means that 75 per cent of mail is now route-ready for our postmen and women.

We are now implementing a fundamental change in the way we work across our delivery operations. This is in order to accommodate the changing traffic mix – more parcels and fewer letters. Delivery revisions have taken place in 448 delivery offices since the modernisation programme began. We need to modernise the remaining 908 operating delivery offices and deliver the targeted savings consistently across the country. The executive management team and our union colleagues agree that the need for transformation is clear and pressing. We are working closely with the Communication Workers Union (CWU) to ensure the consistent and timely implementation of delivery revisions. Together, we will deliver our change agenda as sensitively and transparently as possible.

**Building a commercial future**
Building a commercial future is the second part of our business strategy.

Ofcom's new regulatory approach, announced just after the end of the financial year, is a key first step. The new regulatory approach provides us with increased commercial freedoms. But, more remains to be done in this area.

We have had to increase our prices over the last few years. Of course, nobody likes to raise prices in the current economic climate. But, like all businesses, we must earn a reasonable return for the services we provide. Our rate of return is improving but is still well below commercial levels.

The development of end-to-end competition, where a new entrant could target the most profitable business (typically in urban areas) without having to meet the obligations that we must, is one of the biggest threats to the Universal Service.

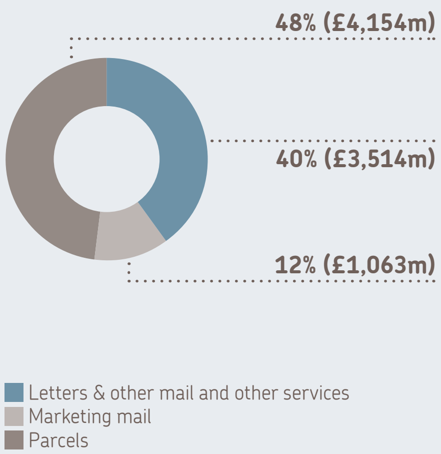
If Royal Mail's competitors are able to target profitable business through focused end-to-end competition, of course, the cost of delivering the balance of our competitors' mail increases, as the revenue available to pay these costs is siphoned away. We are planning to review our Access contracts during the coming year and will be looking at this issue amongst many others; we will be seeking the views of our customers and Ofcom.

Royal Mail Group Ltd and Post Office Limited became sister companies on 1 April 2012. In January 2012, both companies signed a major commercial agreement, which provides continuity and a close working relationship over the long-term. Post Office Limited, with the largest retail network in the country, including a significant presence in rural areas, will remain a key partner in our future. Our mutual commercial success is best served by working closely together for the benefit of customers.

### Profitable growth

The third and final part of the business strategy is to create profitable revenue growth in marketing mail, parcels and data to counter the decline in the traditional letters market.

**Royal Mail Group's revenues**
(excluding Post Office Limited)




**We are a significant British company, with a growing proportion of our revenues generated by incoming and outgoing international mail. Revenues generated outside the UK from GLS and UKPIL now form 20 per cent[3] of our annual revenues, excluding Post Office Limited.**

Royal Mail Group currently has a £4.2 billion revenue-generating parcels business that includes UKPIL's Royal Mail UK network and Parcelforce Worldwide; and GLS. Parcels made up 48 per cent of Group revenue[4] across the year. Our UKPIL parcels business grew its revenue by 10 per cent, while GLS's revenue grew by five per cent.

By 2016, online retailing is expected to account for 23 per cent of the UK's overall retail spend[5]. In addition, UK consumers will buy products online from overseas providers, benefiting both our parcels and international businesses. Royal Mail Group is well placed to benefit from these growth trends. Our parcels businesses are best-in-class operators in their respective markets.

During Christmas 2011[6], Royal Mail's core network delivered around 79 million parcels and Parcelforce Worldwide nearly seven million express parcels. Parcelforce Worldwide achieved a 96.6 per cent first-time delivery rate during this period alone. Growing our parcels business is a key strategic priority.

We are also developing our marketing mail business, which contributed £1.1 billion in revenues this year. Utilising our own assets, and with the support of several partners, we will be able to offer a full service solution for businesses, large and small, covering creative development, production, distribution and customer data management for advertising mail. See "Our strategy in action" on p16 for more details.

### Outlook

We are in a stronger financial position. But, much remains to be done to ensure we are leveraging every opportunity our business has to offer.

The EU State Aid decision has improved our cash position. As a result of deregulation, we are better able to generate a reasonable return in the core UK business. Our margin is improving, albeit from a very low base. Our strategies and initiatives are geared towards delivering, in time, the 5-10 per cent margin set by our regulator, and a more commercial margin as compared to other successful postal operators.

Looking forward, we expect that continued growth in online retailing will benefit our domestic and international parcels businesses. The decline in our core letters business is expected to continue. We will press on with our modernisation programme, cutting costs in the network. We will also adapt the network to carry increasing numbers of parcels.

We are developing alternative sources of future profitable revenue growth, leveraging our key strengths and focusing on our marketing mail and data businesses.

Very few companies face the prospect of continued change on the scale that we do. I am very grateful for the continued help and support we have received from HM Government: Secretary of State for Business, Innovation and Skills, Vince Cable; both Edward Davey and Norman Lamb as Parliamentary Under-Secretary of State for Postal Affairs, and their officials. In addition, the Group has continued to benefit greatly from the guidance and thoughtful oversight of our Board of Directors. I also thank our union colleagues Dave Ward, Deputy General Secretary (Postal) of CWU and Brian Scott, Assistant National Secretary, Unite, for their ongoing engagement and constructive challenge to ensure our success.

And, of course, I would like to thank all our colleagues across the Group. I know what we are asking of them is difficult. I am grateful for their continued dedication, hard work and commitment. They continue to be the main driver of our success as we look towards a secure and profitable future.

**Moya Greene**

[3] Comprises GLS (£1.6 billion) and UKPIL's Royal Mail International (£0.2 billion).

[4] Excludes Post Office Limited revenue.

[5] Boston Consulting Group: "The £4.2tn Opportunity, the Internet Economy in the G20".

[6] 28 November 2011-25 December 2012.

# Our strategy in action: parcels and marketing mail

## Royal Mail Group is more than just a UK-focused, letter delivery business.

## We are leveraging our capacity, reach and expertise to grow profitable revenue streams in parcels and marketing mail. This is a key part of our strategy as we seek to attract private capital.

### Parcels

Our parcels business has three networks in the UK: Royal Mail's UK parcels operation; Parcelforce Worldwide and Royal Mail Specialist Services. Internationally, it has Royal Mail International (which uses Royal Mail's UK parcels network), and our European parcels operator, General Logistics Systems (GLS).

Together and with the support of global partners, these businesses handled 1.2 billion parcels. Over the last year, this represented a six per cent increase in UKPIL domestic volumes and a three per cent increase in GLS' volumes. Total parcel revenues for the year stood at approximately £4.2 billion, with GLS generating £1.6 billion.

### Our UK parcel networks:

- Royal Mail's UK parcels operation delivered 585 million Universal Service Obligation (USO) and account tracked and untracked parcels during the year;
- Parcelforce Worldwide, our express parcels business, has a separate UK network. It has one of the highest quality of service performances in the UK express parcel market, with a first-time delivery rate of 96.8 per cent; and
- Royal Mail Specialist Services is a small but growing part of our parcels operations, servicing bespoke delivery needs, including sameday, parts distribution and very high value deliveries.

### Our main parcels businesses

| | UKPIL | | | GLS |
|---|---|---|---|---|
| | Royal Mail UK parcels network | Parcelforce Worldwide | Royal Mail International | |
| Revenues (£bn) | 1.7 | 0.4 | 0.5 | 1.6 |
| Volume growth (%) | 6 | 5 | 1[1] | 3 |
| Items handled (m) | 585 | 66 | 179 | 375 |
| Network | 57 operating mail centres and 1,356 operating delivery offices | 52 depots and two delivery "hubs" | Heathrow "hub" | 660 depots 37 central shipment points |
| Fleet | 37,287 vehicles | 2,009 vans | | 16,510 vehicles |

### International operations:

- Royal Mail's International operation handled and delivered 179 million import and export parcels. It works closely with other overseas postal administrations to connect businesses and individuals in the UK and abroad;
- GLS, our continental European logistics business, is a significant contributor to profits. Revenues grew five per cent to £1.6 billion, primarily driven by higher volumes. Its margin is 8.2 per cent; and
- GLS has shown it can grow in an uncertain European market. But, competition continues to be intense and prices remain under pressure. There is significant overcapacity in the market, putting downward pressure on prices, especially in core markets like Germany.

### Our strategy

By 2016, online retailing is expected to account for 23 per cent of the UK's overall retail spend[2]. Our strategy is to maximise profitable revenue growth by utilising our multi-network parcels platform in highly competitive markets in the UK and overseas.

The Royal Mail UK parcels operation is loss-making. We recognise that steps must be taken to address these losses and make it more cost efficient.

We need to continue to improve customer experience across all our businesses. In the core UK operations, initiatives such as our delivery to neighbour trial, aim to do just that.

We continue to focus on our presence in the business to business market, which is closely linked to GDP growth.

We are pursuing growth in Europe through GLS. Working with Royal Mail International, it is well-positioned to benefit from future growth in borderless online retailing.

[1] Based on a simplified basis which is currently being refined.

[2] Boston Consulting Group: "The £4.2tn Opportunity, the Internet Economy in the G20".

Our strategy in action
case study **1**

**Marketing mail**
We aspire to become the best marketing mail and services company in the UK. Approximately £1.1 billion of Group revenues in 2011-12 (equivalent to 12 per cent[3]) came from marketing mail.

We believe there is potential in this market, where targeted addressed and unaddressed marketing mail is delivered to consumers across the UK.

Royal Mail is well-positioned to manage the distribution of this mail. Working with a number of commercial partners, we will hone a full-service offer for businesses covering creative development, production, distribution and customer data management.

Working across the value chain, we aim to increase our share of this lucrative market. Our specialist sales team has already begun contacting some of the UK's biggest advertisers and securing campaigns.

## Businesses thrive thanks to Royal Mail Tracked

Parcel delivery is an increasingly important part of Royal Mail's business. Growth in online retailing gives us an opportunity to build our capability in this area if we get fulfilment right.

Serving businesses of every size, we connect them with their customers. We help enterprises thrive and grow. From their shops and warehouses to their customers' front doors, Royal Mail Tracked gives businesses peace of mind and confidence in our ability to deliver their goods safely and in good time.

Royal Mail is a key service provider for TalkTalk, a leading broadband supplier. TalkTalk sends out hundreds of parcels every week and needs to know where the goods are at any stage in the mail pipeline. Royal Mail Tracked enables them to do just that.

**"We use Royal Mail Tracked because we believe it is the best value for money."**

says Mike Wakley, the company's head of supply chain logistics at TalkTalk.

**"We value the fact that the equipment that goes to our customers is fully traceable."**

For more information visit
**www.royalmailgroup.com**

[3] Excluding Post Office Limited.

# UK Parcels, International & Letters

| Trading performance | 2011-12 | 2010-11 |
|---|---|---|
| External revenues (£m) | **7,164** | 6,857 |
| Operating profit/(loss) after modernisation costs (£m)[1] | **23** | (120) |
| Margin (%) | **0.3** | (1.7) |
| Inland addressed volumes (m) | **14,997** | 15,909 |
| People employed | **151,156** | 155,181 |

### UK Parcels, International & Letters (UKPIL)

UKPIL delivers letters and parcels to more than 29 million addresses in the UK, in line with the Group's Universal Service Obligation.

In addition, the business is also responsible for:

- Express parcel services through Parcelforce Worldwide;
- Design and production of UK stamps and philatelic products;
- Processing incoming and outgoing international mail; and
- The growing marketing mail business.

### Trading performance

Revenues increased for the first time in four years, rising four per cent to £7.2 billion.

The increase in revenues resulted in an operating profit after modernisation costs[1] of £23 million, compared to a loss of £120 million the previous year. This generated an operating margin after modernisation costs[1] of 0.3 per cent, which remains very modest compared to other major postal operators.

### Parcels

- Revenues increased by ten per cent to £2.6 billion;
- Domestic volumes grew six per cent to 651 million; and
- Parcelforce Worldwide first time delivery Quality of Service was 96.8 per cent.

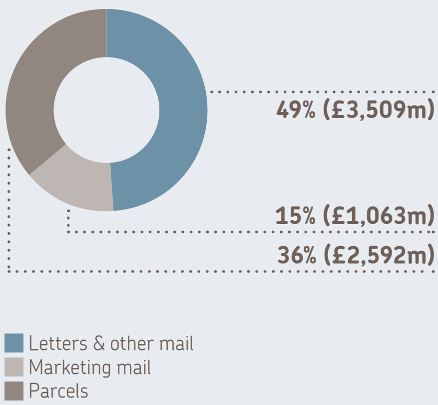
"Our strategy in action" (p16) provides further detail on our Group parcels strategy, of which UKPIL is an integral part.

### Our customers include:

amazon.co.uk
MARKS & SPENCER
asos discover fashion online
SCREWFIX
BT

| Parcels volumes (m) | 2011-12 | 2010-11 | Growth |
|---|---|---|---|
| Royal Mail UK domestic parcels network | **585** | 551 | 6% |
| Parcelforce Worldwide | **66** | 63 | 5% |
| Total UKPIL domestic parcels | **651** | 614 | 6% |

### UKPIL revenues




### Letters & other mail and marketing mail

- Revenues have increased by one per cent to £4.6 billion, this included £3.5 billion from letters & other mail and £1.1 billion from marketing mail;
- We delivered over 14 billion inland addressed letters and large letters, and over three billion inland unaddressed items;
- Inland addressed volumes declined by six per cent; and
- First Class retail Quality of Service performance was 92.7 per cent.

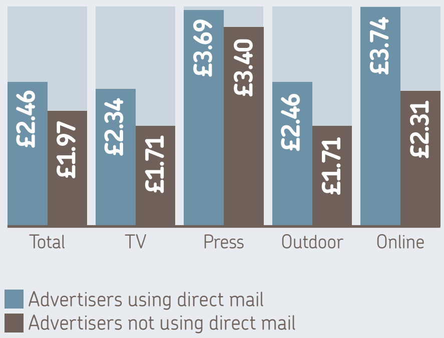
### Marketing mail

£1.1 billion of our Group revenues were generated by marketing mail in 2011-12.

We are prioritising the development of this business as a key driver of future profitable growth. The business' strategy is to reinvigorate our share of the advertising market and increase our share of the value chain by targeting the UK's top 3,000 advertisers – many of whom do not use direct mail in their direct marketing mix and do not realise its potential.

[1] Before other operating exceptional items.

**Return on Investment of direct mail**




Source: OMD/Brand Science (2009)

### Letters & other mail

Across letters and other mail, necessary price increases were offset by volume decline in inland addressed letters items of six per cent. The number of addresses we deliver to continues to grow, expanding by almost one per cent every year.

### Social mail

Social mail includes stamped letter mail of a consumer to consumer (C2C) or consumer to business basis (C2B). This part of the mail market is declining as UK consumers move to other forms of digital communication.

### Business mail

Business mail comprises statements, orders, invoicing and bill payments that are generally of a business-to-business (B2B) and business-to-consumer (B2C) nature. This is the part of the mail market experiencing the largest decline due to competition from online and other digital media.

Royal Mail believes that it can reduce the decline in business mail by repositioning it as a high value and durable customer communication. This supports customer retention and loyalty when complemented with other media.

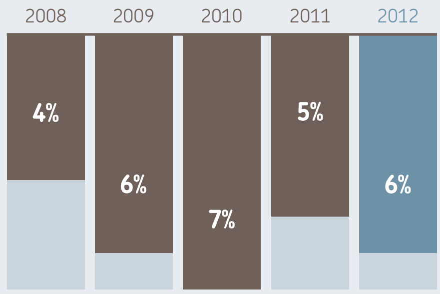
### Special stamps

Royal Mail's stamp programme has had a successful year. Among the highlights were the stamps we produced to mark the Royal Wedding. We issued these, featuring the official engagement photographs by Mario Testino, shortly before the day itself.

Stamps produced for the two great events of 2012, the Queen's Diamond Jubilee and the London 2012 Olympic and Paralympic Games, could prove to be even more successful.


Further information regarding our special stamps can be found at: www.royalmail.com/stamps

**Decline in addressed inland letter volumes**



# Post Office Limited

| Trading performance | 2011-12 | 2010-11 |
|---|---|---|
| External revenues (£m) | **801** | 776 |
| Operating profit after modernisation costs (£m)[1] | **59** | 21 |
| People employed | **7,798** | 7,782 |
| Post Office branches | **11,818** | 11,820 |
| Customer satisfaction (%) | **87** | 85 |

Post Office Limited is visited by nearly 20 million customers a week through its network of 11,818 branches, providing around 170 different products and services. This includes savings, insurance, loans, mortgages, credit cards, Government services, telephony, foreign currency, travel insurance and retail mail services.

External revenues increased by £25 million in 2011-12 to £801 million. Growth in identity related work, lottery, retail and personal financial services was more than offset by the decline in traditional products such as bill payment and from a reduction in the number of telephony customers. The main driver of this growth, therefore, was a £30 million increase to the Network Subsidy Payment to £180 million (2011 £150 million).

The £25 million external revenue increase was the main driver of the improvement in operating profit after modernisation[1] from £21 million to £59 million.

On 1 April 2012, Post Office Limited became a sister company to Royal Mail Group Ltd. Alice Perkins was appointed Chair of the Post Office Limited Board on 22 September 2011. Over the last year, the Post Office has undertaken rigorous planning in anticipation of this significant development. A long-term commercial agreement with Royal Mail was signed on 19 January 2012 to ensure that the Post Office continues to provide unrivalled access and retail customer service in mails and parcels services.

Post Office Limited's strategy is based around growth supported by modernisation and improved customer service and there are a number of key programmes in place to support this.

**Modernising the Post Office network**
In accordance with the Government funding agreement in October 2010, thousands of Post Office branches will be modernised. This will mean service improvements and longer opening hours to make Post Office branches more accessible for customers. There will be no programme of closures.

Over the last financial year, more than 124 new main and local-style Post Office branches have been opened, bringing the nationwide total to 200. After further testing and refinement of the new-style branches, Post Office Limited will roll out the modernisation programme more widely from summer 2012. By March 2015, around 6,000 branches will have been converted to the new-style branches, strengthening the overall network that reaches every community in the UK.

New features of our main Post Office branches include more modern environments with open plan counters, dedicated travel services counters and fast track services for small and medium sized businesses. Among the new technology offered in many locations are self service post & go machines and leading edge biometric data capture technology which has been instrumental in growing new Government business.

In local branches, customers now benefit from open plan counters next to retail counters that enable people to pay for their groceries and make the most of Post office products and services at the same time.

**Serving as a front office for Government**
As well as developing the financial services and mails business, the Post Office is increasingly becoming established as an effective front office for local and national Government. This builds on a long history of delivering essential Government services. Post Office Limited continues to manage more than three million Post Office card accounts for people receiving benefits, state pensions and tax credit payments. The Post Office is ideally positioned as an intermediary between the public and national and local Government.

Post Office Limited can offer cost-effective delivery of services; a secure IT infrastructure in seamless conjunction with back offices and full front-office service for payments, applications, identity verification, data capture and information. The Post Office also offers digital services for customers who do not have internet access, and a face-to-face channel for those transactions that cannot be done online.

Post Office Limited is working with Government departments, agencies and local councils to explore new forms of service delivery that improve accuracy, eliminate fraud and reduce costs. For example, the Post Office Application, Enrolment and Identity (AEI) unit uses advanced biometric technology to capture fingerprints, electronic signatures and digital facial images. Customers in 752 branches can now use this facility to renew photo card driving licences and, in around 100 of these branches, to apply for biometric residence permits. In February 2012, the millionth customer used this AEI digital service.

**Sales strength**
Post Office products continue to earn accolades: for the sixth year running, the British Travel Awards cited the Post Office as the "Best Travel Insurance Provider" and the

[1] Before other operating exceptional items.

"Best Foreign Exchange/Travel Money Provider" for the fifth year running. Post Office Limited also won "Best Savings Provider" at the MoneySupermarket 2011 Supers Awards.

The mail sector continues to account for around a third of the business. Income from Royal Mail has increased this year due to an increase in volumes of parcels and international mail sold through the Post Office and the effect of necessary price increases.

Within financial services, deposits have grown to £15.8 billion and opportunities to increase the range of savings accounts are being sought. The Post Office recently launched a new Premier Cash ISA, for example, which is already proving popular with customers.

Through relationships with partner banks, around 80 per cent of all UK debit card holders now have access to cash withdrawals and balance enquiries at Post Office branches.

This year's results have been achieved against a backdrop of taking steps to secure new business and services while trialling new-style branches and preparing to roll out the largest modernisation programme in the history of the business over the next three years.


# General Logistics Systems

**General Logistics Systems (GLS) is one of the biggest ground-based parcel service providers in Europe today.**

**GLS is a pan-European business, providing reliable, business-to-business, high-quality parcel and express services as well as value-added logistics solutions. Established in 1999, it has historical networks in each of the domestic markets in which it operates.**

| General Logistics Systems | 2011-12 | 2010-11 |
|---|---|---|
| External revenues (£m) | **1,562** | 1,485 |
| Operating profit after modernisation costs (£m)[1] | **128** | 118 |
| Margin (%) | **8.2** | 7.9 |
| Volumes (m) | **375** | 363 |
| People employed | **13,362** | 13,167 |

### Overview: continued success in the face of uncertainty in Europe

GLS is a European leader in quality – provided through a network coverage of 42 countries, through wholly-owned and partner companies – and is globally connected via contractual agreements.

The GLS network comprises 37 central transhipment points in Europe, made up of 660 depots and 16,510 vehicles. Its 13,362 people deliver over 375 million parcels annually for 212,000 customers throughout Europe.

### Trading results

External revenues were £77 million higher than the prior year. Underlying revenues were four per cent higher than the prior year after adjusting for exchange rate movements as the Euro strengthened, compared to 2010-11.

Revenue growth was principally volume driven, with domestic volumes three per cent higher and export volumes nine per cent higher.

Operating profit increased by £10 million to £128 million, generating a margin improvement to 8.2 per cent.

### Strategy in light of European uncertainty

GLS' strategy remains the same – a relentless focus on high service quality, expanding its European network, and continued innovation through investment in technology.

During 2011-12, the core GLS markets in mainland Europe experienced a weakening in demand, particularly during the second half, as governments implemented austerity measures to reduce their fiscal deficits.

Despite the challenging conditions, GLS increased parcel volumes by three per cent in total, with higher domestic and export volumes compared with the prior year.

In particular, export volume growth has benefited from the leveraging of GLS' pan-European network. GLS continued to invest in its European network in 2011-12 by strengthening its physical infrastructure through investments in operational facilities and by extending its geographical coverage.

**GLS pan-European network**
(including partners)

- Albania
- Andorra
- Austria
- Belgium
- Bosnia-Herzegovina
- Bulgaria
- Croatia
- Cyprus
- Czech Republic
- Denmark
- Estonia
- Finland
- France
- Germany
- Greece
- Hungary
- Iceland
- Ireland
- Italy
- Latvia
- Liechtenstein
- Lithuania
- Luxembourg
- Macedonia
- Malta
- Monaco
- Montenegro
- Netherlands
- Norway
- Poland
- Portugal
- Romania
- San Marino
- Serbia
- Slovakia
- Slovenia
- Spain
- Sweden
- Switzerland
- Turkey
- United Kingdom
- Vatican City

(As at March 2012)

[1] Before other operating exceptional items.

**In May 2012, GLS teamed up with Itella Logistics for the export and delivery of parcels to Lithuania and Latvia. As both parcel specialists have already been working together in Estonia since 2009, this now means they can serve all three Baltic states.**

### Innovating through technology

The parcels market in Europe continues to develop, with growth increasingly driven by online retailing. GLS has invested and will continue to invest in technology which will optimise delivery services. New flexible delivery solutions are being developed which will enable GLS to communicate directly with recipients, so that parcels can be delivered to locations most convenient to them.

## Vision & core values of GLS