Shareholder Executive – Annual Review (2009/10)

Chief Executive's Report for 2010

Once again it's been a busy period for the Shareholder Executive. The continuing difficult economic conditions coupled with the change of Government have made 2010 an interesting and challenging year, and has seen our role change and expand to contribute more fully to the new Government's efficiency and growth agenda.

Annual Report

We have decided to change the way we report our performance this year. As part of our efforts to reduce costs, we have taken the decision not to produce our Annual Report in its usual form, and present a much briefer and more concise report instead.

We have summarised some of the key financial data from our portfolio of businesses. This represents published data which is accessible from the respective businesses website, where further performance information can be found if desired.

We will publish additional information shortly on our portfolio businesses' performance targets, dividend policy and progress on the biennial valuation of the portfolio.

Successes during the year

Since our last Annual Report there have been a number of successes to briefly report on, including:

- Operational Efficiency Programme – we played a significant part in the Asset Management and Sales strand of the previous Government's Operational Efficiency Programme. This led to a number of recommendations to improve efficiency and generate increased value in Government-owned assets;
- Public Expenditure (Assets) Committee – we are playing a leading role in shaping the agenda and the debates taking place at PEX(A) – the Cabinet Sub-committee which is specifically tasked with identifying new efficiencies, examining options for the potential sale of various Government assets and looking at how to remove potential obstacles blocking any asset sales;
- Vesting of the Royal Mint – ShEx has taken a proactive role in improving the performance of the Royal Mint over a number of years and this culminated in successful vesting on 31st December 2009. Vesting has allowed the Mint to enjoy the benefits of becoming a company, including a clearer governance framework and greater transparency and focus in its commercial decision-making;
- Banking – before the creation of UK Financial Investments (UKFI), the Shareholder Executive led the advice provided to HMG with regard to the support to Northern Rock and Bradford & Bingley. During 2009 ShEx led the separation of Northern Rock into two new legal entities - a new deposit taking and mortgage lending bank that takes over the old name, and the old entity (now known as Northern Rock Asset Management) which no longer takes customer savings and will run-off its portfolio of £60bn in mortgages over the next 20-30 years. Responsibilities for Northern Rock and Bradford & Bingley have now passed to UKFI; and
- Government interventions – our corporate finance team was heavily involved in the previous Government's support for industry, and the automotive industry in particular. For example, our team worked with GM and a number of European Governments to structure a support package for Opel / Vauxhall, leading the Government's negotiations with the company. Whilst GM ultimately declined the European Governments' support package, the UK Government's relationship with

GM has strengthened as a result, and the UK plants continue to perform a key role in the strategic direction of the group.

Changes at the Shareholder Executive

The success of the Shareholder Executive combined with the new Government's desire to drive value, increase efficiency and reduce the UK deficit has meant an increase in the Shareholder Executive's role and responsibilities, and a closer working relationship with the centre of Government in the Cabinet Office, HM Treasury and No. 10 in developing these initiatives.

Property

The Government Property Unit, under the leadership of John McCready, was established early in 2010 as a new Unit within the Shareholder Executive to provide a single focus for strategic property management throughout the public sector and to identify efficiencies in the way that the public sector uses its £370billion worth of estate. The Unit has been bolstered by the arrival of some 30+ property staff previously located in the Office for Government Commerce. The Unit's long term objective is to secure savings of £5bn pa in the cost of running the public sector estate and to deliver £20bn of capital receipts, both by 2020.

Portfolio of Businesses

In 2009 we took the decision to improve further our oversight of our portfolio of 27 businesses. With this in mind, we appointed Anthony Odgers as the Head of Portfolio Unit. Assets in this Unit will include those where we have a clear shareholding mandate and access to sufficient levers to be able to exercise those responsibilities.

Anthony's work will help to better define how we measure our success with respect to our businesses.

The Corporate Finance Practice has been re-focused and is now responsible for a number of non-portfolio assets sales as well as continuing with its traditional corporate finance and project work. The non-portfolio assets are characterised by an absence of a formal shareholder mandate: our role is primarily to drive a transaction.

Future Challenges

The public finances will require the continued contribution of the Shareholder Executive to release value and increase efficiency. For example:

- The proposed sale of Royal Mail represents a key opportunity to bring private sector investment in to a company which is struggling for investment;
- We are making significant progress in our efforts to sell the Tote, with a sale anticipated in 2011;
- We are heavily involved in initiatives to increase the level of publicly available data produced by Government owned enterprises, to enhance opportunities for innovation and enterprise throughout the economy and create opportunities for private sector investment; and
- Management and realisation of value from the Government's holding of spectrum

I am keen for the Shareholder Executive to continue to play a valuable part at the centre of the Government's efficiency and growth agenda and we look forward to a challenging 2011. In this, we will continue to be ably supported by our Board and I and the senior management team would like to extend our thanks to them for their advice over the past year.

Stephen Lovegrove
Chief Executive

Portfolio Analysis Report for 2010

Financial performance of the portfolio

The challenging economic environment continued to have a negative impact on most of our portfolio businesses in the reporting period 2009/10. For businesses which are directly geared to the general economic environment such as Channel 4 and Royal Mail, turnovers fell. On the other hand, Working Links' results improved given that their work is even more relevant during difficult economic times. These varied results reflect the different nature of the markets which our businesses operate in.

In line with previous years and for the sake of consistency, we have consolidated the financial results of our portfolio of businesses. However, one should be cautious when comparing results from previous years. Year-on-year comparison at the aggregate level can be difficult due to the diversity of our portfolio, the uniqueness of the markets some of our businesses operate in, and the fact that businesses move in and out of our portfolio over the course of a year.

Changes to the portfolio

Several businesses previously in our portfolio have now been excluded from our analysis this year. As part of the Public Bodies Reform announced in October 2010, BNFL will be abolished and British Waterways will move to charitable status, and both have left out portfolio accordingly. Partnerships UK had also been merged with the Treasury's Infrastructure Finance Unit to form Infrastructure UK. Furthermore, following the recapitalisation of RBS and Lloyds Banking Group in October 2008, the Treasury set up UK Financial Investments (UKFI), with a specific focus on managing the Government's shareholding in financial institutions. Subsequently, the responsibility for Bradford & Bingley and Northern Rock was transferred from ShEx to UKFI.

Other points to note for the aggregated analysis

For businesses which report in foreign currencies, Actis (USD) and Urenco (EUR), we have used the average exchange rate for the year to translate the results into GBP. Also, for simplicity, we have made no adjustment for those businesses whose financial year ends in December rather than March. The analysis therefore includes results up to December 2009 for those businesses (Actis, CDC and Channel 4).

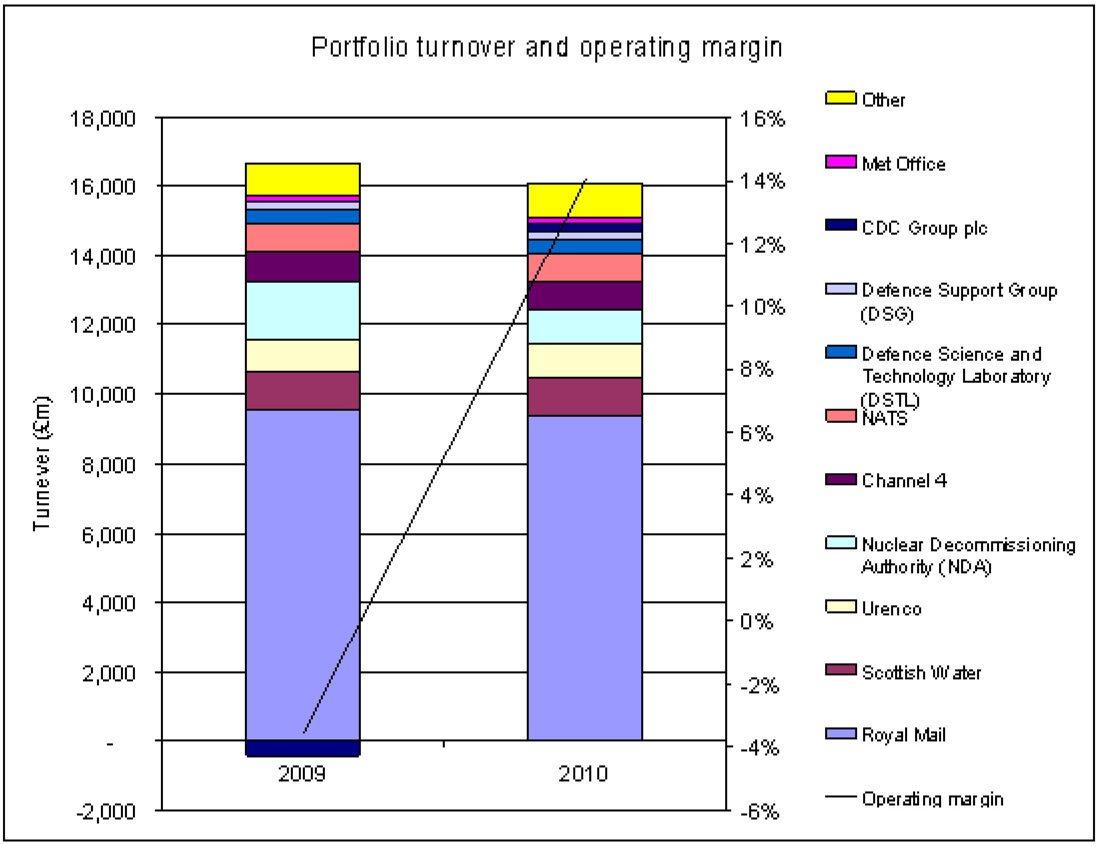
Although we manage our shareholding in the Post Office somewhat separately than that of Royal Mail (and have disclosed its results separately on our website), its financial results for this analysis have been included within that for Royal Mail Holdings plc.

Finally, note that the percentage of public sector's ownership has been ignored in the consolidated results. Therefore total dividends paid by our businesses, for example, do not reflect the total cash received by the public sector during the period.

Turnover

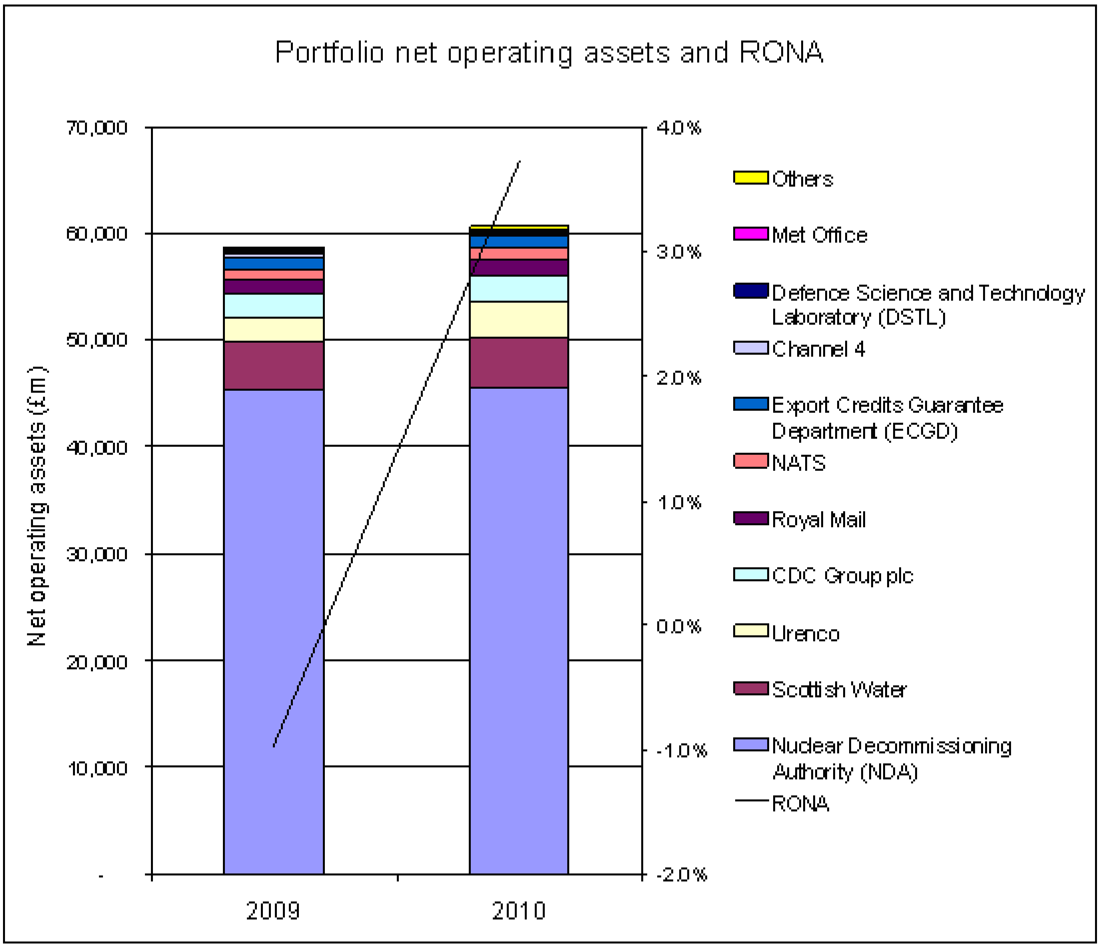
Total turnover for the portfolio fell by 0.9% to £16.1bn on a like-for-like basis. The decline is mainly driven by the 43% reduction in turnover at NDA, where, as expected, its plant reached the end of its economic life.

Several businesses recorded a rise in revenue during this period, such as Urenco with turnover up 13%, mainly reflecting the Euros' appreciation against Sterling. CDC's investment return (which is their nearest equivalent to turnover) turned positive in the year (year-end December 2009) after a loss-making 2008.



Operating profits and losses

Consolidated operating results changed from a loss of £569m in 2009 to a profit of £2.3bn in 2010. This is primarily driven by NDA which moved from a loss of £1.7bn to a profit of nearly £4bn. This swing in operating profit reflects a reduction in the estimated cost of decommissioning, from an increase of £2.1bn in 2009 to a reduction of £0.1bn in 2010. Other significant movements in the portfolio include a return to a positive investment return at CDC and a 24% and 32% jump in profits at Urenco and Royal Mail respectively (although Royal Mail remains in some difficulty below the operating profit line).



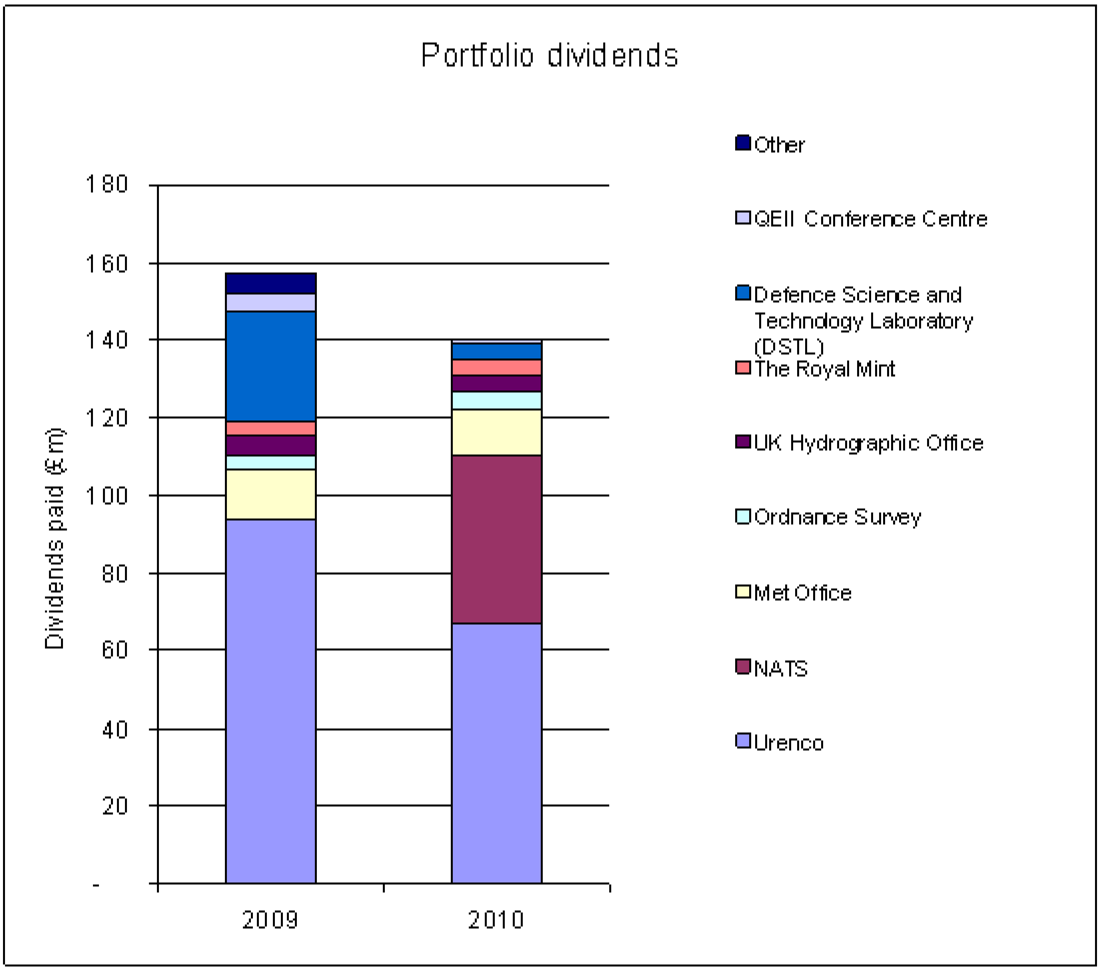
Return on net assets (RONA)

Total net operating assets increased by 3% in 2010. This is mainly driven by the increase in assets at Urenco (+48%) reflecting higher investment in fixed assets. Overall, RONA changed from -1% to +4% following the return of our businesses to operating profit at the aggregate level.

Dividends

Given the continuous headwinds faced by many of our businesses, it is not surprising that total dividends paid in the year 2009/10 were lower than that in 2008/09. Only 8 businesses in our portfolio paid dividends with a total of £139m, an 11% decline from 2008/09.

As with previous years, Urenco was the largest contributor in dividends paid (£67m). This however is lower than the previous figure of £94m as the company preserved more cash to invest in capital expansion. Other significant developments include a payout of £44m from NATS, having paid no dividends in 2009, despite a fall in profits, and a sharp drop in payout at DSTL (from £28m to £3m), which was to be expected given last year's one-off special dividend of £25m paid to MOD.



This publication is also available on our website at www.bis.gov.uk
Any enquiries regarding this publication should be sent to:

Department for Business, Innovation and Skills
1 Victoria Street,
London SW1H 0ET
Tel: 020 7215 5000

If you require this publication in an alternative format, email enquiries@bis.gsi.gov.uk, or call 020 7215 5000.

URN 10/405