

RAC plc 2002 preliminary results statement

26 February 2003

RAC plc announces another year of good progress

Highlights

- Strong operational cashflow of £73 million.
- Underlying profit* up 8% to £70.2 million.
- Underlying earnings per share* up 5% to 43.9p.
- Profit before tax £23.1 million (2001 - £62.3 million)**; FRS14 earnings per share 8.5p (2001 – 39.5p).

RAC Consumer Services profit increased to £45.2 million:

- Roadside revenues up 5% to £183 million;
- Non-roadside revenues up 22% to £51 million.
- Lex Vehicle Leasing profit up 11% to £17.5 million (our half share).
- Lifetime revenues from new contract wins of £620 million.
- Full year dividend up 5% to 23.0p.

Andy Harrison, Chief Executive, RAC plc, commented:

“RAC has delivered another robust performance with an 8% growth in underlying profit, backed up by strong cash flow. The quality of our underlying earnings continues to improve, with further growth in RAC Consumer Services including 22% growth in non-roadside services as we build on the strength of the RAC brand. We also won new business services contracts with lifetime revenues of £620 million.

“Our financial strength increased, with debt falling by £44.2 million, and we have taken active steps to manage our pension deficit. We believe all the ingredients are in place for another good year in 2003. This is supported by the Board’s decision to increase the dividend by 5% to 23p.”

* Before goodwill amortisation, exceptional items and tax

** Reduction primarily due to goodwill and other write-offs in Mechanical Handling compared with an exceptional gain on the sale of our investment in Synnex in 2001.

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Preliminary results for the year to 31 December 2002

Another year of good progress

In 2002 we made good progress towards our goal of being the first choice provider of motoring and vehicle solutions for consumers and businesses. We will continue to grow the business by selling more

services to our growing customer base, building on the strength of our brands, our service delivery and our unique motoring and vehicle expertise.

In Consumer Services we are growing our customer base, increasing the range and quality of our services and encouraging more members to buy multiple services. We continued the growth in our customer base in 2002 and now deliver roadside service to 6.5 million consumers across RAC Consumer Services and RAC Business Solutions. There is increasing customer loyalty in the individual membership base, as evidenced by the growing number (83.8%) who renewed their membership with RAC in 2002. Our investment in customer relationship management systems and infrastructure will enable us to understand more of our customers' individual motoring needs and provide tailored solutions from our expanding range of services. The systems are already delivering benefits including higher quality information and more effective direct marketing, and will be fully implemented in the middle of the year. At present 7% of individual customers buy more than one service; our goal is to increase this to 15%.

In the corporate market we have a number of businesses which have competitive strength in their own right. We aim to leverage these strengths by providing additional services to existing customers and by using our unique range of skills to supply tailored multi-service solutions for major customers. For example, we have won new contracts with the Ministry of Defence, including the renewal of our RAF White Fleet contract, and have broadened the range of services we provide to Norwich Union. These developments demonstrate our proven track record of building long term partnerships with customers such as these to add substantial value to their organisations.

The benefits of these long term relationships and organic growth can be seen in the quality of the group's earnings and our steady underlying profit growth over the past two years. The lifetime revenue of new contract wins in 2002 was £620 million, increasing the total lifetime value of our long term business to £2.83 billion in 2002 (2001 - £2.73 billion).

2002 saw another milestone in our development as a unique support services company as we renamed the company RAC plc to leverage the value of our strongest brand. We shall continue to develop the Lex brand in its business to business markets.

Financial results

Revenue increased by 4% to £1508 million. Underlying profit grew by 8% to £70.2 million (2001 - £65.1 million). This was after a £7 million increase in pension costs and includes a full year contribution from RAC Auto Windscreens (2001 - nine months). Underlying earnings per share increased by 5% to 43.9p (2001 - 41.9p). Profit before tax was £23.1 million (2001 - £62.3 million) with earnings per share calculated in accordance with FRS14 of 8.5p (2001 - 39.5p).

The Group tax rate on underlying profit increased to 28% as expected (2001 - 26%). This is before a one-off credit of £7 million in respect of deferred tax provided in previous years that is no longer required. The underlying tax rate is expected to remain at 28% in 2003 and then to rise to 31% over the following two years.

A reconciliation between underlying profit and profit before tax is included in note 2 and explained in this statement in the section entitled Significant Financial Items on page 7.

As a result of strong cashflow of £44.2 million, net debt reduced to £155 million from £200 million at the end of 2001, as set out in note 5.

The Board proposes a final dividend of 13.8p (2001 - 13.2p) which, together with the interim dividend of 9.2p (2001 - 8.8p), increases the total dividend for 2002 by 5% to 23.0p per share (2002 - 22.0p). Subject to the approval of shareholders at the Annual General Meeting to be held on 30 April 2003, the final dividend will be paid on 2 May 2003 to members registered at the close of business on 4 April 2003.

RAC Consumer Services

RAC Consumer Services sells a comprehensive range of motoring solutions to private motorists, including financial, legal and travel services, breakdown cover, insurance, vehicle glass and driving tuition. This part of the business now accounts for over half of the group's underlying PBIT and has significant potential for continued growth.

In 2002 RAC Consumer Services maintained the strong growth it has achieved over the past three years. Revenue grew by 6% to £339 million, which includes £96 million from RAC Auto Windscreens (9 months to 31 December 2001 - £72 million). RAC Consumer Services grew profit to £45.2 million (2001 - £37.7 million). Profit grew by 7% on a like for like basis.

The roadside business continues to grow and the number of individual memberships increased by 6% to 2.15 million, with over 3.1 million people covered. Revenue from roadside operations grew by 5% to £183 million.

This is a strong business with high customer loyalty; renewal rates increased to 83.8% from 82.9%. Our long term relationship with members, together with the improved information provided by our customer relationship management systems, forms a sound platform for the continued growth of our non-roadside services, enabling us to meet an increasing range of our members' motoring needs.

Growth in non-roadside services, excluding RAC Auto Windscreens, accelerated in 2002, with revenue increasing by 22% to £51 million (2001 - £42 million). During 2002 we continued to broaden our service offering with the development of a range of new products.

RAC Auto Windscreens' performance was broadly in line with the previous year and we continue to develop synergies with RAC. Revenue was £96 million in 2002 (nine months from acquisition in 2001 - £72 million).

RAC Legal Services grew revenue by 33% and profit by 36%. The business grew the number of legal expense policy holders by 13% to 1.8 million and now has an 11% share of the motor legal expenses insurance market. Legal Services successfully launched RAC Accident Solutions, providing a range of co-ordinated services to members in the event of an accident, from vehicle recovery and legal advice to personal injury cases. This is a unique service which differentiates RAC in the marketplace. RAC Legal Services launched an accident care scheme with Avon and Somerset Constabulary during 2002 and is negotiating with a number of other police forces to expand the service across other parts of the UK. We believe the quality and range of the services we offer, together with our trusted brand name, can make legal services more accessible to people beyond our membership base.

RAC Financial Services, our joint venture with AXA, achieved revenue growth of 96% and profit growth of 126%. We renegotiated the joint venture terms with effect from 1 January 2003, providing the foundation for significant further growth in financial services. Under the new agreement RAC's share of profits will increase to 42% in 2003, rising to 50% in 2006 and 100% after 2011. We expect the number of our motor insurance policyholders to grow further with the launch of 'RAC Insure', which offers a broker panel drawn from the UK's leading insurers, enabling people to find competitive car insurance quickly and easily. We are working with MBNA to supply motor loans under the RAC brand.

RAC Travel Services increased revenue by 20% and profit by 76% in 2002. The renewal rate for travel insurance improved as a result of a focused renewals strategy. This area of the business is already benefiting from our investment in customer relationship management systems, which enabled us to generate significantly higher sales than in previous years from direct marketing activity.

BSM grew revenue by 17% and profit by 19%. The business is the largest driving school in the UK and has a 19% share of the driver tuition market. The average number of instructors during the year increased by 11% to 2,556 while the number of driving students grew by 8% to 145,000. Pass rates on both theory and practical tests increased. BSM has pioneered interactive tuition methods and lobbied successfully for the government to include a hazard perception assessment in the driving test. BSM's branding was refreshed in 2002 to strengthen its links with the RAC brand and further support our efforts to promote our full range of services to customers.

Systems: We are in the final stages of completing a major investment programme in RAC's core systems. This investment in our infrastructure will improve customer service and efficiency. It will also support future growth for both RAC Consumer Services and RAC Business Solutions by enhancing service delivery and enabling us to understand each individual customer and provide tailored solutions to their motoring needs.

The implementation of the new £5 million automated patrol despatch system (ICAD) was completed in 2002. The implementation caused some service disruptions during the summer of 2002, but is now working well and delivering benefits in service and efficiency. The system coped robustly with the pressures caused by the recent severe weather, and can handle greater volumes than the previous system. Enhancements such as call line identification and text messaging will be introduced in 2003.

The implementation of our customer relationship management system will be completed in mid-2003, with a capital investment of £26 million. A data warehouse is already operational and providing higher quality information to the business to improve accuracy in target marketing. The front office system is fully implemented in RAC Business Solutions and provides a flexible platform for the continuing development of new services. There were additional implementation costs of £4.2 million in 2002 with a further £3 million expected in the first half of 2003.

We expect benefits, after taking into account additional depreciation, of £1 million from these systems in 2003, rising to £4 million annually in future years. In addition, the customer relationship management systems will support us in growing the proportion of customers who buy more than one service from its current level of 7% to our target of 15%.

Services to business

Revenue from business services grew to £557 million in 2002 (2001 - £533 million). Profit of £19.2 million was in line with last year (£19.3 million).

Our business services operations are focused on working together to provide a broad range of co-ordinated services to customers with whom we can develop strong partnerships, and the potential for continued growth remains good.

We continue to develop our relationship with the Ministry of Defence, through successful service delivery on existing contracts and the provision of new services such as a £12 million driver training contract and a £35 million hardware spares support contract, both signed in 2002. These were followed in February 2003 by the renewal of the Lex Defence White Fleet contract to supply the 3,300 strong RAF non-combatant fleet for a further eight years, extending the total number of vehicles we supply the armed forces to 12,500, with a combined lifetime contract value of over £600 million. We are shortlisted for a further two defence contracts with a potential revenue of £1400 million over 15 years.

We have broadened the services we provide to Norwich Union and RAC Business Solutions now supplies claims management, legal services, roadside services, windscreens and engineer deployment for the insurer. In addition, Lex Auto Logistics has successfully piloted a vehicle parts supply project with Norwich Union, with significant potential revenues.

RAC Business Solutions

RAC Business Solutions sells motoring and related business solutions to business customers and manages complex outsourcing bids for large public and private sector organisations. The business grew revenue by 16% to £146 million (2001 - £126 million) and grew profit to £2.3 million (2001 – £1.0 million).

New business wins for RAC Business Solutions in 2002 illustrate the potential to broaden the range of services we provide to existing customers. We signed contracts with the Volkswagen Audi Group to provide call centre support for Volkswagen's UK retail units and a dedicated network of Audi roadside technicians. Toyota added a vehicle inspections contract to the roadside assistance services already provided. New insurance claims management contracts were won with NFU Mutual and Lloyds TSB.

The quality of service we provide to business customers has been recognised in 2003 with a number of Fleet Excellence awards, voted for by fleet managers. RAC Business Solutions won awards for Best Accident Management Services provider, Top Fleet Software provider for RAC Software Solutions, and RAC also received commendations for Vehicle Recovery and Windscreens.

Lex Vehicle Leasing

Our half share of profit from Lex Vehicle Leasing, our joint venture with HBOS grew 11% to £17.5 million in 2002 from £15.7 million in 2001. The fleet under contract increased to 95,700 in 2002 (2001 – 93,700) and the quality of new business remains high.

In 2002, Lex Vehicle Leasing completed the £12 million implementation of new systems which provide an integrated platform for managing customers and suppliers. The systems are providing differentiated levels of service and reducing costs. A Six Sigma Quality programme, Q6, was also launched and has significant potential to enhance future performance. The business won Fleet Excellence Awards for Best Service Supplier and Best Contract Hire Company, and a commendation for Fleet Management.

Disposal losses on vehicles reaching the end of their contracts were comfortably absorbed within the £45 million provision we made at the end of 2000. We remain confident that the provision will be sufficient to meet future disposal losses.

Lex Industrial Solutions

Lex Industrial Solutions includes the hire, maintenance and fleet management of a range of commercial vehicles, mechanical handling and other industrial equipment. The business incurred a loss of £0.6 million in 2002 (2001 - £2.6 million profit). This result was before a number of one-off and exceptional costs affecting Mechanical Handling which are explained in the Significant Financial Items section below.

Lex Transfleet, our commercial vehicle contract hire, vehicle rental and fleet management business achieved a record year, growing revenue, profit and new business. Our fleet management business grew to 17,500 trucks (2001 – 15,300). This progress was offset by a difficult year for Mechanical Handling, which experienced continued market difficulties. The underlying business remains profitable; however restructuring costs were incurred as the business was reorganised to become more customer-focused and efficient. We have also been exploring alternative approaches to create value, for example by reworking our relationship with lift truck manufacturers. As we signalled at the half year, we do not expect significant profit improvement before 2004.

Manufacturer Support Services

Manufacturer Support Services provide outsourced marketing and inventory management services, primarily to vehicle manufacturers. Revenue grew to £607 million in 2002 (2001 - £563 million) and profit increased to £23.2 million in 2002 (2001 - £21.9 million). These figures are before the one-off items set out in the Significant Financial Items section below.

Lex Auto Logistics has developed a strong pipeline for new business and won new contracts with £226 million lifetime revenue in 2002. Paccar, the parent company of DAF and Leyland, did not renew its contract to supply DAF parts, which ends in June 2003; however, the financial impact of this was offset by an additional £8.4 million profit in 2002 from the contract to supply Leyland parts (set out in the Significant Financial Items section below). Total Paccar profits are expected to continue at the same level in 2003 and then at lower levels until 2006. Lex Auto Logistics' base profit, excluding Paccar, is around £5 million, with good potential to increase with new contract wins, such as the parts supply initiative with Norwich Union.

Hyundai maintained its market share at 1.1% and grew registrations to 29,300 (2001 – 27,800). The company has a strong model range, including the new Getz and Coupe which were launched in 2002 to critical acclaim. The Getz has been named the What Car? Budget Car of the Year 2003. Hyundai's reputation for service and reliability was strengthened when the company pioneered a new industry standard with the launch of a five-year warranty. Profits from the sale of Hyundai parts, a source of high quality earnings, continued to grow in 2002.

Our truck businesses, Lex Commercials and Isuzu Truck, made good progress in 2003.

Significant financial items

As mentioned in our December trading update, the financial results for 2002 include several one-off and exceptional items. These relate to:

Mechanical Handling: falling lift truck prices and a weak trading performance has led to an asset write-down of £7.2 million in the UK, the bulk of which relates to accelerated depreciation of fork lift trucks; and a £6.4 million impairment in our French fork lift truck business. In the light of these issues we have prudently written off acquired goodwill of £22.2 million.

Changing Group Structure: one of the group's major contracts is with Paccar for the distribution of Leyland and DAF parts. Last September Paccar decided to bring the contract in-house and in 2002 we benefited from £8.4 million of additional Leyland margin as the contract winds down. In 2002 we incurred a cost of £2.9 million completing the integration of RAC Auto Windscreens, which was acquired in March 2001. Disposals of businesses, primarily the sale of Lex Autocentres in April 2002, led to an exceptional cost of £9.5 million.

Systems: the cost of implementing new systems for automatic despatch and customer relationship management in RAC Motoring Services (£4.2 million).

For reporting purposes these items are treated differently. The table below shows their classification in the results:

	Mechanical handling	Group structure	Systems	Other	Total
Profit before one-off & exceptional charges					73.2
One-off charges	-7.2	8.4	-4.2		-3.0
Underlying Profit					70.2
Operating exceptionals	-6.4	-2.9			-9.3
Goodwill amortisation	-22.2			-7.1	-29.3
Exceptional items		-9.5		1.0	-8.5
Profit before tax					23.1

The exceptional charge of £8.5 million in 2002 compares with an exceptional credit of £9.3 million in 2001, which included a profit of £25.3 million from the sale of our investment in Synnex, the Taiwanese electronic components distributor.

At the end of 2002 the pension deficit calculated under the accounting standard FRS17 was £129 million after tax. As announced in December the Company will increase its cash contribution by £2.5 million in the second half of 2003 and by £5 million a year thereafter. We are maintaining our final salary scheme which we believe is an important and competitive benefit to provide for our employees. We have taken steps to reduce the ongoing cost of the scheme, which are described in the attached statement on pensions.

Outlook

The sustained growth and improved quality of earnings we have achieved over the past two years show the benefits of our transformation as a unique support services company. There is significant opportunity for continued growth in both our consumer and business markets by increasing the number of services we provide to our customers. Our investments in systems should enhance our growth potential; the benefits are already beginning to flow through in terms of service delivery, higher quality information and improved sales targeting.

In addition, our strong cash flow has further strengthened our financial position. We expect our organic growth to continue to drive improved performance in 2003.