RAC plc 2004 preliminary results statement

16 February 2005

RAC plc continues to deliver growth

Highlights

- Revenue growth from continuing operations up 8%
- Profit before goodwill amortisation, exceptional items and tax up by 2% to £88.6m (2003, £86.7m) - earnings per share on this basis up 2% to 55.7p (2003, 54.4p)
- Profits from continuing operations (excluding Paccar) up 12% to £71.2m (2003, £63.6m)
- Contribution from discontinuing Paccar activities down to £17.4m (2003, £25.6m)
- Profit before tax £77.7m (2003, £25.7m)
- FRS 14 earnings per share 45.8p (2003, 8.3p)
- Continuing strong cash flow, with net debt down £14.5m to £139.8m (2003, £154.3m)
- Full year dividend up 6.2% to 25.8p (2003, 24.3p)
- RAC Business Solutions profits up 271%
- Lex Vehicle Leasing profits up 16%
- No.1 in Roadside Assistance provider – JD Power survey
- Financial services strategy strengthened through AXA transaction

Andy Harrison, Chief Executive, RAC plc, commented:
"The continuing RAC businesses are growing strongly, with double digit profit growth, together with further improvements in our service levels. In addition, we have opened up a big and exciting new opportunity in financial services, following last year's AXA transaction. The new financial year has started well and I remain confident in our future prospects."

Notes:
A final dividend of 15.6p will be paid on 5 May 2005 to shareholders on the register on 8 April 2005.

A reconciliation between profit before goodwill amortisation, exceptional items and tax, and profit before tax, can be found in Note 1 of this preliminary statement.

A reconciliation between earnings per share on profit before goodwill amortisation, exceptional items and tax, and earnings per share on an FRS 14 basis, can be found in Note 10 of this preliminary statement.

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Building on our strengths

RAC plc is a leading motoring services company with strong, trusted brands recognised for service excellence across consumer and business markets. Our goal is to be regarded by our customers as providing the "best in motoring services" and we will achieve this through delivering inspirational service to them. In 2004 we took important steps toward achieving this goal.

We have strong brands in RAC, Lex and BSM. Our strategy is to deliver growth by leveraging their strength and our customer base. During 2004, we undertook extensive research on the RAC brand, and were pleased when it confirmed that our customers find us one of the most trustworthy brands in the UK, and rated us excellent for service. The internal research was confirmed by external awards, with our success as "The No.1 Roadside Assistance provider" in the annual JD Power survey and a near clean sweep for all our brands in the annual Fleet Excellence awards.

Our most important strategic step in 2004 was the restoration, in the autumn, of full ownership of our Financial Services business, through buying out our joint venture with AXA and the associated acquisition of renewal rights to AXA Direct's motor and home insurance policyholders. With a highly trusted brand we are ambitious in financial services.

For a number of years, the Group has anticipated the cessation of our parts distribution relationship with Paccar, the worldwide truck manufacturer. A disengagement was agreed in November 2004, although it will be late 2005 before this is completed. This will mark the conclusion of a highly cash generative trading relationship.

Financial Highlights

The continuing RAC businesses have been growing rapidly and it is encouraging that in 2004 the profits in these continuing businesses, excluding the contribution from Paccar, grew by 12% to £71.2m (2003, £63.6m). In 2004 the profit contribution from our Paccar contract reduced to £17.4m (2003, £25.6m).

Revenue growth from continuing operations was strong, up 8% to £1,509.1m (2003, £1,401.5m). Total revenues increased by 1% to £1,539.4m (2003, £1,526.2m) reflecting the disposal of our mechanical handling businesses.

Profit before goodwill amortisation, exceptional items and taxation grew by 2% to £88.6m (2003, £86.7m). This reflected the £7.6m reduction in the Paccar contribution as well as restructuring charges of £4.4m relating to the integration of the AXA Direct business and other business efficiency improvements, and costs of £2.0m in relation to the implementation of the Insurance Mediation Directive. Earnings per share on this basis increased by 2% to 55.7p (2003, 54.4p).

After exceptional items, primarily associated with business disposals and VAT repayments from prior periods, profit before tax was £77.7m (2003, £25.7m) and earnings per share calculated in accordance with FRS 14 were 45.8p (2003, 8.3p).

The Group continued to generate cash, investing £31m in the AXA transaction and injecting capital into Lex Vehicle Leasing to support the Ford Financial transaction. Net debt fell by £14.5m to £139.8m (2003, £154.3m).

The Board proposes a final year dividend of 15.6p to bring the total dividend for the year to 25.8p, an increase of 6.2% on 2003 (24.3p).

Operating review

RAC Consumer Services

The RAC brand is one of the most trusted in the UK. We give peace of mind to millions of customers through our 24 hour roadside and replacement windscreen services, our range of motor, legal and home insurance products and advice on personal injury claims. In BSM we are the market leader in driving tuition, providing training to 157,000 pupils each year, from beginners starting on our unique simulators to experienced drivers requiring advanced skills for personal or business use.

Consumer Services has grown steadily in recent years and now contributes over half the Group's operating profit.

Highlights

- Total revenues up 6% to £374.8m, (2003, £353.1m)
- Roadside revenues up 3%
- Motoring Services (Financial Services, Legal Services, BSM), revenues up 29%
- Underlying profits up 5%, after adjusting for restructuring charges associated with the integration of the acquired AXA business and other business efficiency improvements, and the costs of implementing the Insurance Mediation Directive
- Major strategic step forward in financial services through the acquisition of renewal rights for AXA Direct's 270,000 motor and home insurance policyholders
- Voted No.1 Roadside Assistance provider, by customers, in the JD Power survey

Roadside
2004 saw us deliver our best service standards ever at the roadside, with customers voting our breakdown business No.1 in Roadside Assistance in the JD Power annual customer survey, and No.1 breakdown provider in the Fleet Service awards. This success comes on the back of investment made over the last few years in state of the art equipment and diagnostic tools for our patrol force and customer service teams.

Revenue grew in 2004 by 3% to £205.4m (2003, £198.7m); membership remained static at 2.2 million members after a number of years of strong growth. Following the implementation of new customer management systems late in 2003, we encountered difficulties with call handling times in our contact centres and some issues with collecting cash from customers whose bank or credit card details had changed since we last took payment. We worked hard to minimise the impact on our customers, and saw progressive improvement in these issues as the year progressed. There was a resulting dip in our high renewal rate, from 83% in 2003 to 80% in 2004 as a whole, but it is encouraging to note that the rate for December was back above 82% and that this has been maintained in January.

Motoring Services: -

Financial Services
With strong brand recognition, high renewal rates and access to our Roadside membership base, developing RAC Financial Services is one of our biggest strategic opportunities. In 2004 we took a major step towards exploiting this strategy through acquiring the renewal rights to AXA Direct's 270,000 motor and home insurance policyholders, and regaining ownership of the RAC Financial Services brand, previously jointly owned with AXA. These initiatives should increase our motor, home and personal insurance policy book to approximately 450,000 by the end of 2005.

Integration costs for this acquisition were £1.9m in 2004, and we expect the acquisition to be earnings enhancing (before goodwill amortisation) in 2005, and substantially so beyond that. Revenues grew by 59% to £13.8m, (2003, £8.7m), including organic growth of 16%.

Legal Services
We provide legal expense insurance and assistance in personal injury claims for both members and non-members. Our customers trust us to pursue their claims honestly and professionally, and insurers know that we will not pursue frivolous claims. We have been growing our in-house legal practice strongly and now employ 45 lawyers as well as a panel of 24 firms of solicitors around the UK. Personal injury claims handled increased by 10% to 21,400 (2003, 19,400) and the number of legal expense policies sold grew by 14% to 2.4m, (2003, 2.1m) with total revenues growing by 46% to £15.0m (2003, £10.3m).

BSM
The UK's largest driving school, BSM, welcomed its 3000th instructor in June this year and provided tuition to 157,000 new and experienced drivers. BSM utilises the latest techniques - such as on-line training tools and driving simulators - to give those new to driving the best start and those looking for additional skills the right support and access to advanced training. The dynamics of the market remain attractive, with the young driver population growing, tests getting progressively harder and the demand for further tuition beyond the test (which can enable young drivers to obtain favourable insurance rates) increasing. Revenues grew by 10% to £34.9m (2003, £31.8m).

RAC Auto Windscreens
Auto Windscreens experienced challenging trading conditions, reflected in a reduction in margins, when

a number of insurers opted for a single source of supply in 2003 and Auto Windscreens was unsuccessful in the tenders. The new management team took action to reduce costs and are introducing new, more flexible, working conditions into the business. Towards the end of the year there were encouraging signs of success in our sales activities, most notably with Co-operative Insurance Services where we have become the preferred supplier for all its automotive glass repair and replacement work.

Sales in 2004 were down by 2% at £95.2m (2003, £96.9m). The business continues to make an attractive return on sales, to cover its cost of capital, and to be cash generative.

Whilst 2004 was a mixed year for RAC Consumer Services, we nonetheless saw revenue growth and underlying profit momentum, and a vitally important strategic move into financial services. The major priorities for 2005 are to stimulate growth in our Roadside membership base and, through a £5m increase in marketing expenditure, maximise the opportunity presented by our Financial and Legal Services businesses. Success in these areas will help us move towards our goal of 20% of members buying more than one service, from the 13% level seen in 2004.

Nick Hughes has been appointed as Managing Director of RAC Consumer with effect from 1st May 2005. Nick joins RAC from American Express where he has been European Head of Marketing for the last three years. His previous experience includes McKinsey & Co and South African Breweries.

Jon Walden has resumed his role as Managing Director of Lex Vehicle Leasing.

Business Services

We have strong business to business credentials through our Lex and RAC brands, and provide extensive vehicle and customer services including roadside assistance, motor claims handling, contact centres, fleet management, vehicle finance, supply chain management and vehicle distribution and sales. Our customers include the Ministry of Defence, British Airways, Norwich Union, Ford and Audi. We provide support and service around the clock, 365 days a year.

As a Company our individual businesses work together to provide services across a number of sectors. In particular, we have identified five key areas: motor and vehicle manufacturers, defence, insurance, utilities, and airside operations, where customers benefit from our knowledge and expertise to bring operational and efficiency benefits. The opportunities within these sectors are considerable and we estimate that our current order book has a revenue value of approximately £2bn. Our sales to these sectors increased by 10% to £303m in 2004.

Highlights

- Lex Vehicle Leasing sales increased by 17%, and profits by 16%
- RAC Business Solutions sales up 6% and profits up 271%
- Record new car sales in Hyundai, topping 37,000 vehicles and taking market share to 1.5% (2003, 1.3%)
- LVL successfully integrated business acquired from Business Partner, the contract hire arm of Ford Financial in the UK
- Orderly disengagement from Leyland parts distribution negotiated with Paccar

Our Business Services' operations performed well in 2004, with revenues from continuing activities up 8% to £1,131.8m (2003, £1,045.1m) and profits, after absorbing the anticipated reduction in Paccar contribution, increasing by 3% to £54.7m (2003, £53.0m). We strengthened the range of RAC's services sold into the business to business market. In particular, the work we carry out in claims handling for the insurance market, and services to motor manufacturers, including an agreement to manage service bookings for a major UK motor manufacturer, have helped RAC Business Solutions grow revenues by 6%, and profit by 271%.

Lex Vehicle Leasing

Lex Vehicle Leasing, our joint venture with HBOS, had another excellent year. Our half share of profits grew 16% to £22.7m, (2003, £19.6m), on revenue up 17% to £241.8m (2003, £207.2m). Organic sales growth accounted for 4% of the increase, and the new business with Ford Financial the remaining 13%.

The company increased its fleet size by 21% to 123,600 vehicles (2003, 102,300 vehicles), reflecting both the successful integration of the Ford Financial outsourcing contract and organic sales growth, with particularly good performances with large fleet customers. Profit growth was further aided by good cost control and the continued delivery of benefits from the company's Six-Sigma quality programme which is now being adopted elsewhere in RAC.

The used car market was better than expected throughout the year, resulting in lower than anticipated disposal losses.

The business' market-leading service reputation was confirmed by the award, for the sixth year out of seven, of "UK's Best Contract Hire Company" by Fleet Week and Fleet Management, and additionally being named "UK Leasing Specialist of the year" by the Institute of Transport Management.

RAC Business Solutions

Revenues grew by 6% to £169.8m (2003, £160.8m), and profits increased by 271% to £5.2m (2003, £1.4m).

During 2004 we were successful with both existing and new customers, strengthening our relationships with motor manufacturers, fleet operators and insurance companies. We renewed important contracts with Motability, for roadside assistance and vehicle inspection, and Norwich Union, for claims handling.

We broadened the range of products we offer to our customers, helped by the successful implementation of new claims handling and customer management systems, and now have a comprehensive range of services, including outsourcing of customer and dealer contact centres, vehicle inspections, automotive technical support and third party care for insurers. Our new products include service booking solutions for both motor manufacturers and fleet operators, automated vehicle license checking, and a new accident management service for fleets and insurers, at our operation in France.

Manufacturing Support Services

Included in this division are: Lex Defence; Hyundai, our car importership; Lex Auto Logistics, our supply chain management business; Lex Commercials, our truck dealership group and Lex Transfleet, our commercial vehicle contract hire, rental and fleet management business, (jointly owned with Lombard - part of the Royal Bank of Scotland Group).

We are the preferred bidder, in partnership with Amey, for the Ministry of Defence "C" Vehicle contract to supply and maintain construction vehicles, plant equipment and rough terrain mechanical handling equipment operated by the British armed forces world-wide. We anticipate the contract will be awarded in the Spring of 2005, with full implementation by April 2006. This will extend our long-standing relationship with the Ministry of Defence, our biggest vehicle services client.

Hyundai had an excellent year with strong growth in sales, outperforming a buoyant new car market. The model range continued to strengthen, with the award winning Getz and highly regarded Coupe supported by the successful launch of the Tucson, Hyundai's mid-range 4x4. Registrations were up 17% to 37,600, and market share increased to 1.5% (2003, 1.3%).

Lex Auto Logistics concluded negotiations with Paccar for the cessation of our Leyland parts distribution activities, which will now revert to Paccar towards the end of 2005. As a result of the negotiation, Lex Auto Logistics will continue to benefit from the contract until September 2005, but additionally will receive an exceptional profit of £18.0m, with £4.5m reported in 2004 and the remaining £13.5m in 2005. Management have initiated a restructuring plan to minimise the effect of the lost contribution from the contract, including a move to smaller premises planned for early 2006.

Lex Commercials had a good year with revenues up by 3% to £162.8m (2003 £158.6m) aided by strong demand for new vans and trucks. During 2004, Lex Commercials signed additional franchises for Foden and Isuzu trucks, acquired a further DAF/LDV outlet and a specialist commercial workshop. This business continues to support a number of Group companies in the delivery of complex bids.

During the year we completed the exit from our mechanical handling businesses, through the disposal of Lex Komatsu South, Lex Havelange in Belgium, and Lex Manutention in France. We also negotiated the management buy-out of Isuzu Truck and disposed of Multipart Universal.

Our people

Core to our business success is the service we deliver to our customers, and we have a strong belief in the role that our colleagues play in achieving service excellence. In 2004 we were pleased to receive further recognition of the positive steps we are taking towards our aim of delivering inspirational service - internally, we achieved an increase in overall colleague satisfaction, and externally received a record number of customer service awards across our consumer and business services. We are grateful to all our colleagues who have delivered outstanding service to our customers throughout the year.

Public policy

RAC has been synonymous with motoring for over a century and continues to provide comment on the key issues of the day – from congestion and road safety, to driving standards and transport investment. In conjunction with our partners at the RAC Foundation, we engage at all levels of government and through the media to promote the interests of motorists.

Our annual 'Report on Motoring' is now in its 16th year. Our 2005 report looks at the various agonies and ecstasies of motoring today. The report investigates the major factors impacting negatively on the motorist, focusing particularly on those representing the biggest challenges to policy makers looking to make our roads safer. By focusing on these major road safety factors, the RAC Report on Motoring supports the current legislative agenda which aims to reduce the 38,000 deaths and serious injuries that are suffered on our roads every year, and so make them a safer and more enjoyable place to be.

Outlook

Over the past three years our continuing operating profits, excluding the discontinuing Paccar income, have grown by 12% pa. In 2004 we delivered good revenue growth in both Consumer and Business Services driven by the strength of our brands, our customer base, and improvements in customer service. We have started the new financial year well and remain confident in our future prospects.

Financial Review 2004

Segmental analysis

The segmental analysis of turnover, profit and loss and net assets, showing continuing and discontinued activities, before goodwill amortisation, exceptional items and tax is detailed in note 1 to the accounts. A summary of the segmental profit analysis is shown in the following table:

	Continuing Operations 2004	Discont-inued Operations 2004	Total 2004	Continuing Operations 2003	Discont-inued Operations 2003	Total 2003
	£m	£m	£m	£m	£m	£m
RAC Consumer Services	47.5	-	47.5	51.3	-	51.3
RAC Business Solutions	5.2	-	5.2	1.4	-	1.4
Lex Vehicle Leasing	22.7	-	22.7	19.6	-	19.6
Lex Industrial Solutions	-	0.1	0.1	-	(2.4)	(2.4)
- Leyland parts distribution and related activities	17.4	-	17.4	25.6	-	25.6
- All other activities	9.4	(0.1)	9.3	6.4	(0.1)	6.3

Manufacturer Support Services	26.8	(0.1)	26.7	32.0	(0.1)	31.9
Other	(4.7)	-	(4.7)	(5.7)	-	(5.7)
Profit before interest, goodwill amortisation, exceptionals and taxation	97.5	-	97.5	98.6	(2.5)	96.1
Interest	(8.9)	-	(8.9)	(9.4)	-	(9.4)
Profit before goodwill amortisation, exceptionals and taxation	88.6	-	88.6	89.2	(2.5)	86.7

The RAC Consumer Services result is after:

- £1.9 million of integration costs relating to the buy out of AXA's interest in RAC Financial Services and the acquisition of the renewal rights of AXA Direct.
- £2.0 million of costs in relation to preparation for regulation under the Insurance Mediation Directive, which are expected to continue through 2005,
- and £2.5 million of restructuring costs relating primarily to the outsourcing of IT support and the reshaping of our car inspections activities.

Lex Vehicle Leasing's result included a first-time contribution from the contract to supply vehicles for Ford Financial, which began in 2004.

The contribution to Manufacturer Support Services profits of the Leyland parts distribution activity, which will transfer to Paccar in September 2005, has been disclosed in a separate line to give clarity. A receipt of £4.5 million in 2004 has been treated separately as an exceptional item.

Profit from continuing operations before goodwill, exceptional items and tax fell by £0.6 million to £88.6 million, but excluding the non-recurring costs referred to above, it grew by £3.8 million (4.3%). Profit before tax for the year was £77.7 million (2003 - £25.7 million). The large increase reflects operating exceptional income in 2004 compared with operating exceptional charges in the prior year as described below. Additionally the comparative period had a significantly higher level of exceptional charges from asset disposals and impairments principally relating to our divestment of mechanical handling businesses. Whilst the last disposals were completed in the first half of 2004, the material impairments were taken in 2003.

Interest

Average net non-contract hire debt in 2004 was virtually unchanged on the 2003 level as a result of the investments referred to in the Cash flow and debt section below. The Group's exposure to interest rate rises was limited by outstanding interest rate swaps which had been established in previous years. Overall, the interest charge fell by £0.5 million to £8.9 million, giving a reduced interest rate of 6.9%. The falling average rate reflects a number of factors including reduced average margins and commitment fees paid to lenders and the maintenance of slightly lower levels of cash and investments (held mainly in the insurance related businesses for regulatory reasons).

Goodwill amortisation Goodwill amortisation totalled £7.8 million (2003 - £5.6 million). The £2.2 million increase relates to the part-year amortisation of goodwill on the acquisition of insurance assets from AXA (£1.5 million) and on our share of the Lex Vehicle Leasing contract with Ford Financial (£0.7 million).

Exceptional items

The Group recorded a net exceptional loss (operating, non-operating and VAT interest income) of £3.1 million.

Exceptional items	2004 £m
Operating exceptional items (including VAT interest income):	
Leyland transfer fee (first receipt)	4.5
VAT recovery:	
- principal amount	3.0
- interest income (credited to net interest payable and similar charges)	3.3
	10.8
Non-operating exceptional items: Manufacturer Support Services and Lex Industrial Solutions: - loss on disposal	(5.7)
- goodwill previously written off to reserves	(9.4)
Total loss on disposal of discontinued operations	(15.1)
Profit on sale of fixed assets	1.2
	(13.9)
Net exceptional items	**(3.1)**

There were operating exceptional credits, including VAT interest income, of £10.8 million (2003 – charge of £30.2 million). These were made up of the £4.5 million first payment on transfer of the Leyland parts distribution contract, and £6.3 million of VAT and interest recovered as a result of claims in relation to past VAT payments. These items are disclosed separately in order to present a more accurate view of the Group's underlying trading performance.

In addition to the operating exceptional credits, there were exceptional losses of £13.9 million. The most significant items were a £9.4 million write off of goodwill which had previously been charged to reserves in relation to disposal of the mechanical handling businesses, and £5.7 million loss on disposal of those remaining mechanical handling businesses together with two Manufacturer Support Services businesses, Isuzu Truck and Multipart Universal. These losses have been partially offset by £1.2 million profit on fixed asset disposals.

The net loss on the disposal and closure of these operations reduced the current year tax charge by £2.5 million.

Group tax rate
The underlying group tax rate was 28% (2003 - 28%).

Earnings per share
Earnings per share on an FRS14 basis were 45.8 p (2003 - 8.3p) after exceptional items and goodwill amortisation. The rise in profits before goodwill amortisation and exceptional items has resulted in a modest increase in earnings per share on this basis to 55.7 p (2003 – 54.4p), up 2% on last year.

Dividends
The proposed final dividend of 15.6p per share would bring the total dividend for the year to 25.8p (2003 – 24.3p). The increase of 6.2% on last year (2003 – 5.7% increase) underlines our confidence in the prospects for growth in both profits and cash generation, as does our intention to effect a modest £20

million share buyback programme, announced in December. Dividend cover on profit before goodwill amortisation and exceptional items, after tax is 2.2 times (2003 – 2.2 times)

Shareholders funds

Shareholders funds have increased by £28.5 million to £427.7 million. The key factors were the retained profit for the year of £23.0 million and the add back of £9.4 million of goodwill on disposals previously written off to reserves. This increase is partially offset by a £7.7 million increase in own shares held in relation to share option schemes.

Capital expenditure

Gross capital expenditure was £70.9 million (2003 - £89.7 million), a reduction of £18.8 million compared with the high levels of 2003. This reflects the change in structure of the Group following the disposal of the last mechanical handling businesses (which were capital intensive), and the large systems investments which took place in 2003. Our total net capital expenditure, including disposals, fell by £15.8 million to £25.5 million. The level of gross capital expenditure and disposals is affected by BSM driver training vehicles which we retain for approximately six months before selling them back to the manufacturer.

Cash flow and debt

Net cash inflow from operating activities was £110.0 million (2003 - £117.9 million). We invested £25.5 million net (2003 - £41.3 million) in capital expenditure and £30.8 million in acquiring insurance assets from AXA. The disposal of the last mechanical handling businesses generated £10.6 million, excluding disposal expenses. Additionally, the financing of the Ford Financial transaction in Lex Vehicle Leasing was funded through a small capital injection of £7.5 million and the foregoing of our first half dividend from that joint venture, which would have been £6.5 million.

Despite the investment activity described above, total net debt decreased by £14.5 million to £139.8 million.

The financial ratios of the group have remained strong with interest cover at 11.0 times (2003 – 10.2 times) and a net debt to EBITDA ratio of 1.1 times (2003 – 1.3 times).

Pensions

In common with many other companies, our pension fund continued to be in deficit. Under FRS17 the total deficit at the end of the year, net of deferred tax, was estimated at £148 million (2003 - £123 million). To begin to address this shortfall additional contributions of over £5 million were made in 2004 and are ongoing. In addition a number of changes have been made to reduce the normal annual cost of the scheme by approximately £5 million. An improvement of £62 million in the market value of fund assets to £529 million (2003 - £467 million) was insufficient to offset the increase of £98 million in the valuation of pension liabilities to £740 million (2003 - £642 million) primarily caused by falling bond yields, an increase in our future inflation assumptions, and better estimates of actuarial experience.

Unlike many defined benefit schemes, the trustees of the Group pension scheme are entitled to set the contribution rate required from the Group. As set out in Note 33, an actuarial valuation took place on 5 April 2004. In the light of this valuation, it was agreed by the trustees that no change in contribution rates would be demanded for 2005, but it was noted that actuarial assumptions regarding life expectancy are under review by the pensions industry and that conclusions may start to be drawn during 2005. The trustees and Group management have therefore agreed that a further review of Group pensions provision will be undertaken during the course of 2005.

Risks

The group’s financial risk policy identifies risks and sets out a control framework for managing exposures. This policy is approved by the Board and covers financial risks as follows:

Liquidity risks

Committed facilities are maintained at levels which are in excess of current funding requirements. In addition the availability of facilities over the next five years is managed in accordance with policies which link the required minimum level of committed lines to planned needs. Compliance with the policies is monitored regularly throughout the year.

The businesses are able to access liquidity through overdraft accounts which, as they are subject to netting arrangements, ensure that short-term cash balances are directly offset against overdrafts.

Interest rate risks
Board policies dictate a range for the amount of debt upon which interest rates must be fixed. The policies cover the next five years, and ensure that interest rate exposure management is linked to the interest cover covenants contained within our various funding agreements.

A key part of the activities of our joint venture contract hire companies is the management of funding. Substantially all of the interest rate exposures of these companies are managed through term borrowings or the use of derivatives. The companies aim to eliminate their exposures rather than seek to make any gain from the future movement in interest rates.

Exchange rate risks
The Group has very limited currency denominated transactions. Where transaction exposures do arise they are largely hedged. Similarly as the Group's overseas activities are small there are few translation exposures. Currently no translation exposures are hedged. Should exposures increase beyond a specified de minimis current policies dictate that appropriate hedging will be initiated.

International Financial Reporting Standards (IFRS)
RAC plc will report 2005 interim and full year results under IFRS, including comparative information for 2004. We will also communicate the 2004 results restated for IFRS, and the opening balance sheet, to shareholders and the wider financial community in the first half of 2005. We consider ourselves to be well prepared for these changes.

The following new accounting standards will have most effect on RAC:

Share-based payments (IFRS 2)
Share option awards are not currently charged to earnings, on the basis that such awards have been granted either at the market value of the underlying share or under an approved SAYE scheme. Under IFRS the fair value of the option grant will be measured and charged to earnings over the vesting period.

Goodwill amortisation and Intangibles (IFRS 3 and IAS 36 & 38)
Current policy is either to amortise goodwill over its estimated useful life, or to perform an annual review for impairment. Under IFRS we will cease to amortise goodwill, but will continue with the annual impairment reviews. At the same time, a wider range of intangible assets will be recognised than under UK GAAP for acquisitions occurring after 1 January 2004, and these will continue to be amortised. The acquisition of renewal rights in relation to the AXA Direct business undertaken in 2004 will be treated accordingly.

Pensions (IAS 19)
Under IAS 19, in addition to the service cost for pensions, which is charged to payroll costs (and is broadly comparable to SSAP 24) there will be a financing charge on the scheme deficit which will appear within net financing charges. Also, under IFRS, pension scheme assets and liabilities will be carried on the balance sheet at fair value. Actuarial gains and losses will be recognised immediately in the statement of recognised income and expenditure.

Leases (IAS 16,17 & 18)
IFRS require depreciation to be charged on a straight line basis, rather than on the actuarial after tax (AAT) basis used in Lex Vehicle Leasing. IFRS also require changes in the basis for maintenance cost accounting which will affect both Lex Vehicle Leasing and Lex Transfleet. These changes have no pre-tax cash impact on our contract-hire businesses, and no impact on profits over the life of an individual lease. However, they will tend to change the profile of profits during the life of the vehicle lease, and in a growing business will have the effect of deferring profit recognition in comparison with our current UK GAAP treatment.

Legal revenue recognition (IAS 18)
Under IFRS, revenue in our legal practice will be recognised based on an assessment of the proportion of the case which has been completed, rather than on the current basis of payments received. Given that payments are typically made only on case completion, this will have the effect of bringing forward revenue recognition.

The first three areas will affect RAC in common with many UK public companies, The final two (leases and legal revenue recognition) are more specific to RAC and, taken together, are not expected to be material to RAC’s operating profitability).

Insurance Mediation Directive

Parts of RAC plc, particularly the Consumer business, have become regulated by the FSA under the General Insurance Regulation provisions with effect from 14 January 2005. The Regulation covers, amongst other things, the conduct of business, risk assessment procedures and capital adequacy considerations in respect of the Group's roadside breakdown, motor insurance and other general insurance activities.

Ends

Profit and loss account, balance sheet, cash flow and notes follow.

The financial information set out below does not constitute the company's statutory accounts for years ended 31 December 2004 or 2003 but is derived from those accounts. Statutory accounts for the year ended 31 December 2003 have been delivered to the registrar of companies, and those for the year ended 31 December 2003 will be delivered following the company's annual general meeting. The auditors have reported on those accounts; their reports were unqualified and did not contain statements under section 237 (2) or (3) of the Companies Act 1985.