Financial review

Ian Bull considers the Group's performance over the past year and the improving balance sheet.

Ian A Bull FCMA

Chief Financial Officer

Continuing operations	Year ended 31 December 2012	Year ended 31 December 2011
Revenue	**1,084.4**	976.1
Profit before net finance expense, tax and exceptional items	**236.1**	187.7
Net finance expense	**(29.7)**	(32.8)
Profit before tax and exceptional items	**206.4**	154.9
Exceptional items before tax	**(5.7)**	(20.3)
Profit before tax	**200.7**	134.6
Income tax expense	**(10.4)**	(16.8)
Profit after tax – continuing	**190.3**	117.8
Profit after tax – discontinued	**–**	0.4
Profit for the year	**190.3**	118.2

Trading summary – Continuing operations

Revenue

Revenue from continuing operations increased by £108.3 million (11.1%) to £1,084.4 million (2011: £976.1 million). Excluding High Rollers, revenue increased by £73.0 million (7.4%) to £1,053.3 million (2011: £980.3 million). The increase is mainly attributable to improved machines and OTC performance in UK Retail, improved European Retail performance and growth in Digital sportsbook partially offset by a decline in Poker and Bingo in Digital.

Revenue recognition – reconciliation to gross win

The Group reports the gains and losses on all betting and gaming activities as revenue in accordance with IAS 39, which is measured at the fair value of the consideration received or receivable from customers less fair value adjustment for free bets, promotions and bonuses. Gross win includes free bets, promotions and bonuses, as well as VAT payable on machine income.

A reconciliation of gross win to revenue for continuing operations is shown below.

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Gross win	**1,203.6**	1,078.5
Adjustments[1]	**(49.5)**	(41.3)
VAT	**(69.7)**	(61.1)
Revenue	**1,084.4**	976.1

[1] Includes free bets, promotions, bonuses and other fair value adjustments.

The table below sets out the gross win and net revenue for each division.

	Year ended 31 December 2012		Year ended 31 December 2011	
	Gross win £m	Net revenue £m	Gross win £m	Net revenue £m
UK Retail	**820.5**	**739.5**	753.7	683.3
European Retail	**128.5**	**126.2**	126.3	124.1
Digital	**213.1**	**178.1**	192.7	163.4
Core Telephone Betting	**10.3**	**9.5**	9.9	9.5
High Rollers	**31.2**	**31.1**	(4.1)	(4.2)
Total	**1,203.6**	**1,084.4**	1,078.5	976.1

Profit before net finance expense, tax and exceptional items

Profit before net finance expense, tax and exceptional items increased by £48.4 million or 25.8% to £236.1 million (2011: £187.7 million).

Excluding High Rollers, profit before net finance expense, tax and exceptional items increased by £15.2 million or 8.0% to £206.1 million (2011: £190.9 million) reflecting increased profit in UK Retail and European Retail, decreased losses in Telephones, partially offset by decreased profit in Digital and higher Corporate costs.

Corporate costs

Before exceptional items, total Corporate costs increased by £1.9 million to £25.1 million (2011: £23.2 million) including an increase in share-based payments charge.

Finance expense

Before exceptional items, net finance expense of £29.7 million was £3.1 million lower than last year (2011: £32.8 million) mainly due to a lower average net debt.

Profit before tax

The increase in trading profits as well as a lower finance expense has resulted in a 33.2% increase in profit from continuing operations before taxation and exceptional items to £206.4 million (2011: £154.9 million).

Exceptional items before tax

£5.7 million of exceptional losses before tax include a £3.8 million loss on the closure of shops and disposal of assets within UK and European Retail, £2.2 million in respect of Spanish retrospective online gaming taxes and £0.3 million net gain on derivative financial instruments not in a hedging relationship.

Taxation

The Group has made further progress in the resolution of historical tax matters and has reached settlement with HMRC on all outstanding items in respect of tax years through to 31 December 2007. As a result, tax provisions no longer required have been released leading to a Group taxation charge for continuing operations before exceptional items of £10.7 million, representing an effective tax charge of 5.2% (2011: 11.9%). There was a tax credit of £0.3 million in relation to exceptional items in 2012 (2011: £1.6 million).

Dividend

The Board recommends a final dividend of 4.60 pence per share taking the full year dividend to 8.90 pence per share, an increase of 14.1% over last year.

The dividend will be payable on 9 May 2013 to shareholders on the register on 22 March 2013.

Earnings per share (EPS) – Group

Underlying

EPS (before exceptional items and High Rollers) increased by 20.3% to 18.4 pence (2011: 15.3 pence), reflecting the increased profit before tax and lower effective tax rate.

Total

EPS (before exceptional items) increased 40.0% to 21.6 pence (2011: 15.0 pence), reflecting the increased profit before tax and lower effective tax charge. EPS (including the impact of exceptional items) was 21.0 pence (2011: 13.0 pence). Fully diluted EPS (including the impact of exceptional items) was 20.6 pence (2011: 12.9 pence) after adjustment for outstanding share options and other potentially issuable shares.

Cash flow, capital expenditure, borrowings and banking facilities

Cash generated by operations was £283.2 million. After net finance expense paid of £32.7 million, income taxes paid of £5.2 million and £102.3 million on capital expenditure and intangible additions, cash inflow was £143.0 million. Post dividend payment of £74.0 million and other outflows of £2.0 million, free cash flow of £67.0 million was generated in the year.

At 31 December 2012, gross borrowings of £406.2 million less cash and cash equivalents of £19.3 million resulted in a reduction in net debt to £386.9 million (2011: £453.9 million).

On 11 July 2012, the Group repaid the remaining balance on the 7.125% bond of £131.4 million using existing facilities. The Group has a £225 million 7.625% sterling bond due in 2017.

Going concern

In assessing the going concern basis, the directors considered the Group's business activities, the financial position of the Group and the Group's financial risk management objectives and policies. The directors consider that the Group has adequate resources to continue in operational existence for the foreseeable future and that it is therefore appropriate to adopt the going concern basis in preparing its financial statements.