operating and financial review

The financial statements are presented in both euro and sterling. Euro is the main reporting currency for the Group due to the significance of Avis' continental European operations.

REVENUE OVERVIEW

Full year Group revenues grew by 4.2% to €1,255.4 million and were up 8.3% pre 11 September (or 11.2% excluding Germany, where we continue to pursue a strategy of focusing on higher yield business in preference to further volume growth).

Despite slower economic growth both in Europe and the US and the exceptional impact of the events of 11 September, volume for the full year grew by 2.3%. Our continued focus on pricing and yield strategies generated further pricing gains, with revenue per rental up 5.6%.

Revenue growth in all customer segments

We have continued to pursue a strategy of balanced growth, with increases in all major customer segments: Replacement up 6%, Corporate 3%, Leisure 3% and Premium 4%.

The strongest revenue growth was in Replacement, which accounted for 20% of our business and includes customers from breakdown and motor assistance organisations, insurance companies and vehicle leasing companies. Rentals increased by 9% with the successful development of new accounts gained during 2000 and growth in Centrus, which was up 33% in the second half of 2001. Sales initiatives to generate additional long term and replacement business post 11 September resulted in continued growth throughout 2001.

The Corporate sector accounted for 24% of our business and includes relationships with 75% of Europe's top 500 companies, as well as a growing share of the small and medium sized enterprise market. Revenues grew strongly by 9% prior to 11 September, with a significant increase in revenue per rental largely influenced by our successful yield strategy in Germany. Post 11 September, restrictions on corporate travel in Europe and the significant decline in transatlantic business caused revenues to fall to 9% below the equivalent prior year period.

The Leisure sector accounted for 37% of our business and includes customers from travel companies and airlines, as well as retail customers. Pre 11 September, intra-European volumes were increasing although there were fewer transatlantic leisure visitors due to the slowdown in the US economy and concerns about foot and mouth. During this period, overall volumes remained flat versus prior year although revenues were up 7%. After 11 September, pricing remained positive, so although volume was down 8%, we saw the net decline in revenues limited to 7% below the equivalent prior year period.

The Premium sector accounted for the remaining 19% of our business and includes rentals from customers who have not made an advance reservation. Volume increased by 7% prior to 11 September, with revenues up 10%. However, revenue reduced to 8% below prior year post 11 September.

Domestic and intra-European revenues ahead of 2000

The Group's customers originated from three geographic sources: domestic which was 59% of revenue, intra-Europe 25% of revenue and international 16% of revenue. Full year revenue was ahead of prior year by 5% in domestic and 7% in intra-Europe, with increases in both volume and revenue per rental.

MARK McCAFFERTY
CHIEF EXECUTIVE

CHRIS COWAN
GROUP FINANCE DIRECTOR

Full year international revenue was 4% lower than prior year, with revenue per rental increases more than offset by volume decline. US inbound revenue, the largest part of our international revenue, was 4% ahead of prior year pre 11 September, despite volumes being 11% down due to the slowdown in the US economy and foot and mouth. Post 11 September, US revenues fell to 26% below prior year, with volumes down 30%. However, prices remained strongly ahead throughout the year.

Approximately 50% of the Group's business is generated through airports with the balance through city, rail and resort locations. Airport business was the most affected by the events of 2001, although full year revenue through this channel was still ahead of prior year. Downtown revenue was much less affected post 11 September, less than 1% down, despite lower economic activity. Proactive sales initiatives and internet promotions stimulated demand for local and replacement business and the continued development of our rail partnerships resulted in an increase in rentals originating from rail locations.

Strong growth in France, Spain and Italy

The major markets of France, Spain, Italy, UK and Germany generated 82% of total revenue during 2001.

In France, full year revenue grew by 10% and was unchanged year on year post September. Spain also achieved double-digit revenue growth for the full year, with domestic business growing strongly throughout the year, as well as continued strength in the intra-European sector. Post September revenue in Spain was also unchanged from the same period in prior year. Full year revenues in Italy were up 7%, although this market was more severely impacted post September by the sharp reduction in transatlantic travel. In the UK, revenues grew by 3% with positive gains in Replacement and Corporate being offset by the particular impact on Leisure of the slower US economic environment coupled with a significant reduction in peak season customers due to foot and mouth. Against the background of a rapid economic slowdown in Germany and further significant increases in fleet costs, we continued our strategy of emphasising yield in preference to further significant volume growth, successfully achieving rate per day increases of 10%. Full year revenue was down 8%.

Centrus developments

The Centrus business was repositioned early in 2001 to operate within the Association of British Insurers third party hire initiative, which provides a framework for credit hire services. Underpinned by some major new account wins and consolidation in the market, revenues grew strongly, up 18% in 2001 to €35.4 million. Trends in monthly hire starts have continued to accelerate, with a 30% increase in the last quarter and the business returned to profit in the second half of the year. The detailed process of settlement of past claims continues to progress steadily but slowly with the insurance companies.

PROFIT OVERVIEW

Operating profit before exceptional items and goodwill amortisation was 12.5% lower than prior year at €215.6 million, impacted by the fall in revenue post 11 September.

Operating margin of 17.2% was 3.3% points lower than prior year (see table below). The impact of 11 September was 2.1%

points. A further 0.6% points was due to the one-off impact from euro conversion and the change in Centrus' margin.

Continued initiatives to contain the increase in fleet costs were successful, with the full year increase for 2001 limited to 1.0% of revenue versus 3.1% of revenue in 2000.

Operating margin analysis	2001 %	2000 %	Margin Movement
Selling costs	6.6	6.8	0.2
Revenue related	8.2	8.0	(0.2)
Rental related	2.1	1.6	(0.5)
Fleet costs	33.1	32.1	(1.0)
Staff costs	20.5	20.1	(0.4)
Overheads	12.3	10.9	(1.4)
Operating margin (%)	17.2	20.5	(3.3)

Rapid adjustment to changed market conditions post 11 September

One of the Group's inherent strengths is its proven ability to rapidly adjust capacity to reduced demand with minimal one-off costs. Through a combination of actions such as accelerating the return of vehicles due for sale, delaying the purchase of vehicles, extending contract periods and redistributing fleet to less affected rental locations, the Group's average fleet for the period was 5% less than planned prior to September. These actions meant that our key fleet efficiency measure of vehicle utilisation was at prior year level during the last quarter of 2001 and enabled us to maintain full year utilisation at 0.7% above prior year.

Our other key operational efficiency measure is staff productivity, measured by the number of rentals per full time equivalent staff member (FTE). The flexibility of our operational staffing arrangements also enabled timely adjustment with no one-off costs. This was achieved through a number of initiatives including the early cancellation of casual and temporary contracts and the reassignment of permanent staff to alternative duties and to locations less affected post 11 September. With these actions, the Group exited the year with FTE 4% less than planned prior to September. As a result, we maintained underlying productivity at prior year level during the last quarter and full year productivity was just 0.8% lower than prior year, despite the disruption of September.

Whilst utilisation and productivity actions minimised the margin impact of 11 September, the Group incurred higher transportation costs during this period in the redistribution of fleet and the transfer of sale vehicles to disposal outlets which contributed to the 0.5% points increase in rental related costs.

Fleet strategies limit fleet cost increase

We have continued to develop a series of initiatives to limit the increase in fleet costs which from the period 1998 to 2001 have risen at a rate of around 3% of revenue per annum. These initiatives delivered benefit in 2001 with the cost increase limited to 1% of revenue, despite the impact of 11 September.

Our continuing focus on fleet procurement and disposal strategies as well as optimising holding periods on vehicles (up to seven months in 2001) has enabled us to contain the size of fleet required to service our business. These strategies have contributed to continued improvement in vehicle utilisation which was up 0.7% to 68.5% in 2001.

We have also improved damage recovery through process enhancements and investment in additional staff in Italy, Spain and France generating savings of €4 million during 2001.

We have continued to develop strategies for the effective disposal of vehicles in partnership with dealers and manufacturers.

In September 2001, the Group launched AutoCascade in a 50:50 B2B joint venture with Inchcape plc, offering internet-based re-marketing systems and services to fleet owners to maximise yield on vehicle disposals. In December it entered an exclusive arrangement with Fiat Auto UK for the electronic re-marketing of used vehicles.

In addition to this joint venture, yourautochoice.com, the Group's car sales service, was merged with Autobytel UK, an Inchcape subsidiary, in return for a 10% shareholding in that company. The exceptional charge of €3.9 million relates to yourautochoice.com and the restructuring of our interests.

Other operating costs

Despite the fall-off in demand post 11 September, selling costs and revenue related costs were reduced in line with revenue and therefore did not impact margins as operating commissions at most airports and referral commissions vary largely with revenue. Overheads increased by 1.4% points of revenues as these are mainly fixed and were not adjusted to the lower levels of demand post 11 September. Although immediate actions were taken to restrict non-strategic spend, we continued with our programme of investment in projects key to our future development.

STRATEGIC DEVELOPMENT

Continued investment in network development with joint venture for China

Avis Europe is the first international car rental company to enter into an equity joint venture for the Chinese market.

In January 2002 we signed a joint venture agreement with a subsidiary of Shanghai Automotive Industry Corporation, one of China's largest automotive groups. Its current car rental business, which forms the basis of the new joint venture, will be re-branded Avis and there are plans to expand throughout China. Avis will contribute cash of US$11 million over a period of three years to the 50:50 joint venture.

Asia is a key long term growth region for the Group and with this joint venture we now operate in 20 markets across the region. Since floatation in 1997 we have invested in the development of the brand in Japan, India and now China. Industry research predicts that these three markets will rank in the top four in the world for car sales by 2020.

Development for 2002

The Group exited 2001 with revenues since September approximately 5% below prior year and we anticipate a gradual return to more normalised levels of growth in the second half of 2002. We continue to invest in further joint initiatives within our extensive partnership base and we are further enhancing our product offering to rebuild Leisure business, particularly in the long haul market. In addition, we are putting more resources into countries less affected by recent events, and the further development of downtown business. This will be enhanced by a greater penetration of the small and medium sized enterprise market and targeted initiatives to significantly increase internet bookings. We are also enhancing our environmental initiatives and during 2002 will become the first company in the global travel industry to fully offset the carbon emissions produced by our corporate operations throughout Europe. In anticipation of gradual business recovery during 2002, we are retaining our current operating network and continuing to pursue selective investment for future growth.

TAX, TREASURY AND ACCOUNTING POLICIES

Tax rate reduced from 25% to 22%

The effective tax rate for 2001 was 22%, down 3% points from 2000 benefiting from recent falls in tax rates in a number of European countries and the utilisation of UK tax losses relating to the pre-floatation period.

Year end debt levels reduced

Net interest expense increased 5.5% to €71million, reflecting an increase in average debt to fund higher fleet levels and an increase in the proportion of debt which is at fixed interest rates. Year end debt levels are €100 million lower than prior year following the reduction in fleet post 11 September.

Free cash flow was an inflow of €50.9 million compared to an outflow of €202.6 million in 2000. The free cash flow can be analysed as follows:

Cash flow analysis	2001 € million	2000 € million
Net cash flow from operating activities	562.4	371.4
Interest, tax and dividends	(151.7)	(158.3)
Net fleet purchases	(349.8)	(396.8)
Other capital expenditure on other assets	(10.0)	(18.9)
Free cash flow	50.9	(202.6)
Net finance lease movement	36.7	(32.1)
Acquisitions and other	12.7	(49.6)
Movement in net debt	100.3	(284.3)

The net cash inflow from operating activities at €562.4 million was €191.0 million favourable to the prior year, the timing of fleet purchases and sales having impacted the prior year. Net fleet purchases at €349.8 million and the decrease in finance leases of €36.7 million, totalling €313.1 million, was €115.8 million less than the prior year, reflecting a lower level of year end fleet in line with reduced business activity. These factors, together with reduced acquisition costs in the current year, accounted for the decrease in net debt of €100.3 million.

Treasury policy

The Group's treasury policy is structured to reduce the financial risks and exposures facing the business from changes in interest and foreign exchange rates. To achieve this, the Group undertakes an active hedging policy, including the use of a variety of derivatives (interest rate and foreign exchange swaps, forward rate agreements and caps) which are used under policies approved and monitored by a sub-committee of the Board, chaired by the Group Finance Director. These transactions are undertaken to reduce exposures arising from underlying commercial activities, and at no time are any transactions undertaken for speculative reasons. The Group controls credit risk by entering into transactions involving financial instruments only with authorised counter-parties of strong credit quality. Counter-party positions are monitored regularly.

Exchange rate hedging

The nature of our operations provides a natural currency hedge as each country's operations generate revenue and incur costs in local currency. In support, Group policy is to match the proportion of average liabilities of the Group in each major currency to the equivalent proportion of average assets (including goodwill), and thus minimise the effect of the

translation exposure on the results of the Group. The Group also operates a centralised netting system to settle on a monthly basis all intercompany transactions, thereby eliminating the majority of transactional foreign exchange exposures.

Currency analysis at 31 December 2001	Assets %	Liabilities %
Euro	77	77
Sterling	21	22
Other	2	1
Total	100	100

Interest rate hedging

The Group finances its operations through fixed and floating rate facilities and uses derivatives to fix a proportion of its debt so as to reduce exposure to rising interest rates. The policy targets the Group to have between 40% and 60% of its forecast debt in 12 months' time at fixed or capped rates. In assessing this measure the Group includes the notional principal amount of operating leases expected to be in place in the future as the pricing on such leases is in part a function of floating interest rates. As at 31 December 2001, the Group had in place interest rate swaps and caps providing cover on 56% of forecast debt at 31 December 2002.

Analysis of fixed debt at 31 December 2001

	Gross debt € million	Floating € million	Fixed € million	Fixed %	Weighted average fixed interest rate %	Weighted average period for which rate is fixed (years)
Euro	1,049.3	451.5	597.8	57	5.8	3.4
Sterling	109.7	77.4	32.3	29	7.0	1.6
Other	(6.7)	(6.7)	–	–	–	–
Total	1,152.3	522.2	630.1	55	5.9	3.3

Borrowing facilities

The Group is funded through a combination of a multi-currency Group banking facility of £330 million (€530 million equivalent), local bilateral banking and leasing facilities, a domestic Belgian commercial paper programme, and US$300 million of senior unsecured notes. In addition, during the year, an issue of €25 million of unsecured notes was completed, maturing in 2006. The Group also agreed with its principal banks to extend a £200 million tranche of its multi-currency banking facility from March 2002 to May 2003. The remaining £130 million tranche, which currently matures in May 2002, is structured as a 364-day facility with a two year term-out option. There have been no other changes to the principal facilities during the year and, in total, the Group has available to it financing amounting to approximately €2.5 billion.

Accounting standards and policies

The Group's accounting policies are set out in the financial statements and are consistent with prior year, except for a change to the policy on the recognition of credit repair revenue at Centrus as described in note 1. The new accounting standards implemented in 2001 have not had a material impact on the financial statements.

Shareholder return

Equity markets in 2001 continued to experience the high volatility of 2000, falling on the back of the deteriorating global economy. The terrorist attacks of 11 September had a larger impact on the FTSE Transport sector than most, falling by 29.5% by the year end, with a low of 37%. Our total shareholder return is down 19.4% sterling. However, since floatation in April 1997, the Company has provided shareholders with a 47.8% return, based on reinvestment of dividends and the increase in the share price. On an annualised basis shareholder return since floatation is 8.6% to 31 December 2001 compared with the FTSE Transport sector of (3.2)% and FTSE 250 of 8.9% over the same period.