

BUSES IN TRANSITION: ALL ABOARD!

The humble omnibus makes a significant contribution to social mobility, access to basic services and to environmental sustainability. As the 200th anniversary of the first public omnibus service fast approaches in 2029, we take a look at the exciting prospects in place for the UK bus industry, and in particular through the lens of one EdenTree investment: National Express Group.

FIRST THINGS – A RECENT HISTORY OF UK BUS

The UK bus and coach sector is a vibrant one but it is hugely fragmented with over 1,000 operators that range from the 'Big Five' to single-vehicle family operators. Following the break-up of the nationalised National Bus Company in 1988 into smaller management buy-outs, there was rapid consolidation that led to the emergence of five national players – Arriva, FirstGroup, Go-Ahead, National Express and Stagecoach. Except in the capital where TfL (previously London Transport) operates a regulated route model, operators were free to operate services for which there was local authority subsidy or where the

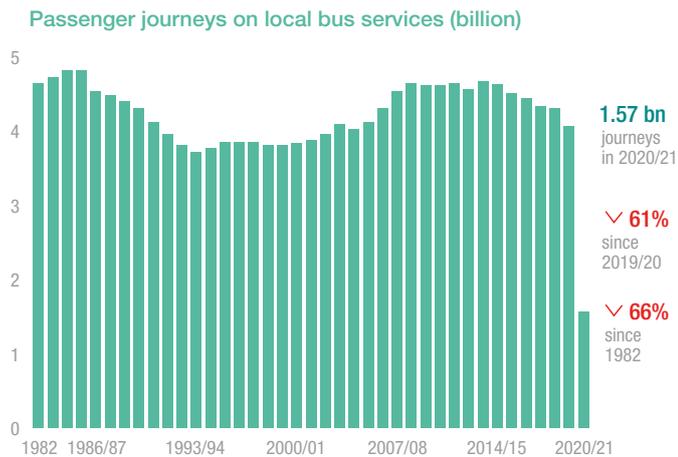
route was economically viable. Over time the industry leaders expanded into rail, logistics, airports and overseas operations to become integrated transport groups. Apart from Arriva, which was acquired by Deutsche Bahn in 2010, the four largest operators remain UK owned and listed; however this may be about to change with bids for Stagecoach and Go Ahead Group now in play, and a bid for FirstGroup rejected by the Board. If these bids were to proceed the Big 5 would be reduced to just one UK owned transport champion – National Express Group.



SOME QUICK FACTS ABOUT THE BUS SECTOR IN ENGLAND

The bus fleet in England totals around 32,600 vehicles in 2020/21 of which 29% were in London, 28% metropolitan, and 43% rural and non-metropolitan.

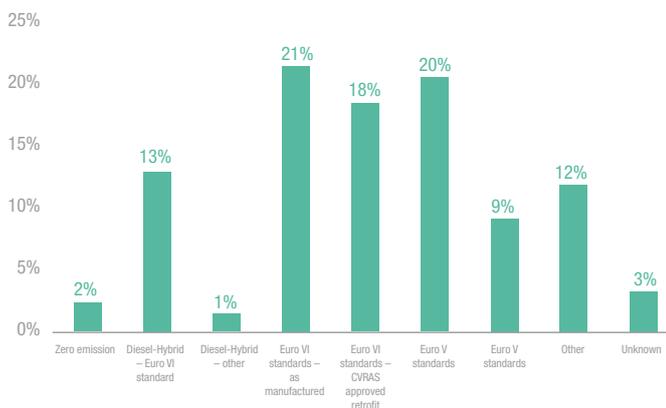
There were 1.57 billion bus journeys in 2020/21 and 0.96bn vehicle miles.



54% of all bus journeys taken were in London playing to its high frequency service model that operates across the capital.

79% of all vehicles were diesel powered, with just 2% zero emission, with 52% meeting the strictest EURO VI emission standards (29% met older EURO IV and V standards).

Percentage of local buses by emission standards in England 2020/21



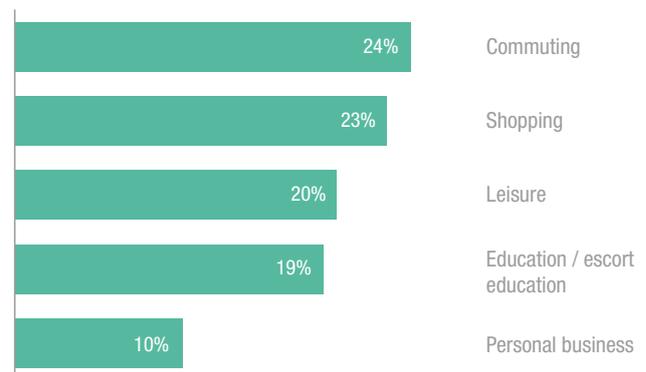
The average age of the bus fleet in England is now just 8.5 years. Investment by the five big players has substantially reduced the average age of the fleet since the 1990s.

The bus industry supports 95,000 full time equivalent jobs.

¹ Annual Bus Statistics England 2020/21

Despite perceptions to the contrary the overwhelming number of buses do run on time (87.9%) and is as high as 91.6% in regions such as the North-East. Passenger satisfaction is fairly constant across England at around 72-76%.

On average, people make 22 trips by bus a year, but this represents just 3% of trips across all modes of travel.



Buses are by far the safest form of road transport by type with the fewest fatalities of any transport mode (35 in 2020) compared to 146 cycle fatalities and 1,116 by car. Buses are more likely to adhere to speed compliance than any other mode or road transport.¹



THE UK NATIONAL BUS STRATEGY – ‘BUS BACK BETTER’

In 2019 the UK Government set out its plans for a ‘revolution’ in bus travel, including simpler fares, improved access and frequency and investment in new vehicles. The Strategy sets out a vision in which the often maligned and ignored motor-bus is seen as a vital tool of inclusion and choice. Impediments were identified as poor frequency and reliability, complex ticketing, services that compete without reference to the customer, under and over-capacity, and poor interchange facilities with other transport hubs.

Devolution to new mayoral authorities under the Bus Services Act 2017 also sets the scene for a potential renaissance in local bus services as elected Mayors become empowered to



operate London style regulation in which routes are tendered. Greater Manchester is likely to be one such metropolitan area outside London to run this kind of integrated transport service as part of a 10 year plan to reshape Greater Manchester’s public transport needs.

As ambitious, the National Bus Strategy sets out the aspiration for a green revolution in which the bus is at the heart of the UK’s Net Zero ambitions. The transition is at an early stage, but UK bus operators have already invested over £1.3bn in cleaner vehicles. At present just 2% of UK buses are zero emission – the figure is higher in London at 4%. This is important as it is estimated that 3% of transport GHGs are produced by buses and coaches, but a fully loaded double deck bus can remove 75 cars from the road, thereby reducing congestion and improving air quality. Each zero emission bus saves 46 tonnes of CO₂ and removes 100% of equivalent NO_x.

As part of the ‘Bus Back Better’ strategy, the Government has set out a roadmap for Net Zero Bus Services whereby a phase out of the sale of diesel buses has been announced similar to that affecting internal combustion engine autos. Low or ultra-low emission vehicles will only be acceptable if a zero-emission vehicle is not viable. In addition to diesel phase-out, the Government is to announce an expectation by which time the UK fleet should be fully zero-emission.²

THE FUTURE OF FUEL

Despite 79% of the fleet being diesel powered, the image of a seven tonne bus belching black fumes is very much a thing of the past. The first Europe wide emissions standards were introduced as long ago as 1992, and have been supplemented by ever more rigorous low emission standards since then. For instance Euro I engines (1992) imposed a limit of 2.7g/Km of CO₂ and 0.97g/KM for NO_x for diesel engines; Euro VI (2014/15) has lowered this to 0.50g/Km of CO₂ and just 0.08g/KM for NO_x. In 2009 Euro V introduced the requirement to retrofit particulate filters. It could therefore be argued that the century old diesel bus has never been cleaner.³

The winning technology that will prevail in succession to diesel is as yet unclear; operators are incubating a number of options

including battery-electric and hydrogen. Bus makers such as BYD and Alexander Dennis are developing the former, whilst JCB owned Wrightbus and INEOS are developing hydrogen power. Both technologies are zero emission (assuming green hydrogen is the source) and critical mass may come down to price, economies of scale and ease of use. This latter point is critical; conventional diesel means vehicles can be refuelled with ease and parked randomly. However, battery power will need substantial new infrastructure, and buses will need to be parked in the right order so that the one in the front is ready to head out in the morning fully charged. It could mean the end of the conventional operator-owned local bus garage in favour of shared charging hubs.

² Bus Back Better: National Bus Strategy for England

³ www.dieselnet.com/standards/eu/hd.php

NATIONAL EXPRESS GROUP – AN EDENTREE INVESTMENT



National Express Group is one of five dominant bus operators in the UK. Its origins go back to the state-owned National Bus Company in 1972 which

brought together scheduled national coach services with its bus operating companies in one entity. With privatisation in 1988 came a management buyout, and then floatation in 1992. The company today is a diversified global operator of road and rail transport systems in 11 countries; 80% of revenues arise outside of the UK, making it the least reliant of the five on regulated bus fares. The company's main markets are the US (student transportation), Spain (bus and coach), and the UK (coach, bus and student transportation). Other, smaller markets are Bahrain, Switzerland, Morocco, Germany and Canada. The company has withdrawn entirely from UK rail, but operates the Rhine-Munster Express in Germany and several other routes in Rhine-Westphalia.

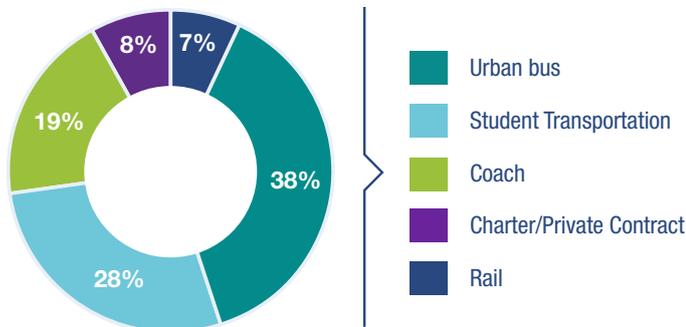
National Express's 32,000 vehicles covered 939 million miles in 2021 with a workforce of 51,000 people.

In the UK, National Express operates the eponymous and mostly franchised long-distance coach network serving over 500 locations via 1,800 daily services. National Express is also the dominant urban bus operator in the West Midlands, the largest urban bus network outside London, covering the conurbations of Birmingham, Wolverhampton and Coventry.

Our operating area



National Express - % Revenue by Business Type



The West Midlands region is likely to be among the first to adopt 'London style' regulation under a single local identity, the West Midlands Bus Alliance. National Express as the long-term incumbent operator stands well placed to maximise new opportunities under a revitalised local bus plan, which has already delivered over £100m of investment improvements.

WHAT ARE THE MAIN INTERESTS OUTSIDE OF THE UK?

The largest revenues are generated in North America and Spain. In the former, National Express is among the largest providers of student transportation (yellow school buses) in 33 States and three Canadian provinces. The company also offers commuter transit routes in the US. In Spain, National Express operates the century-old ALSA brand and is the leading road and long-distance travel operator.⁴



⁴ National Express Group www.nationalexpressgroup.com

WHAT IS THE INVESTMENT CASE FOR NATIONAL EXPRESS?

COVID-19 has been a headwind for public transport generally despite National Express being a high quality business. The shares fell by 80% from a decade long high in March 2020, but have since recovered as the world emerges from the pandemic. The Group's largest exposure is North America followed by continental Europe with over 80% of revenues coming from outside the UK. The Group has a strong track record of developing franchises in new geographies, including German rail services in 2019 on five routes in North Rhine-Westphalia, Bahrain in 2015 and Spain in 2005.

This diversification and withdrawal from complex UK rail franchising is seen as a strong positive compared to its peers. A long-term modal shift towards public transport and away from the private car augurs well for National Express with zero emission buses providing the backbone of clean, reliable, safe transport networks. The shares trade on an inexpensive forward valuation (PE of 8x) and remains well placed to deliver for long-term investors. Its 'Evolve Strategy' aims to add £1bn of revenue by 2027 and £100m of additional profit.



WHAT IS THE SUSTAINABILITY CASE FOR NATIONAL EXPRESS?

National Express supports our investment themes of social mobility, access to basic services and inclusion. The company is increasingly presenting itself as an ESG play where buses play a key role in reducing emissions and improving air quality. Shared travel which is increasingly customer focused (comfort, safety, free Wi-Fi and real-time digital information systems) is environmentally more sustainable.



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It is seeking to end diesel operated coaches by 2035 in the UK and by 2040 in Spain, the US and Morocco. Its Spanish buses are expected to be zero emission by 2035.

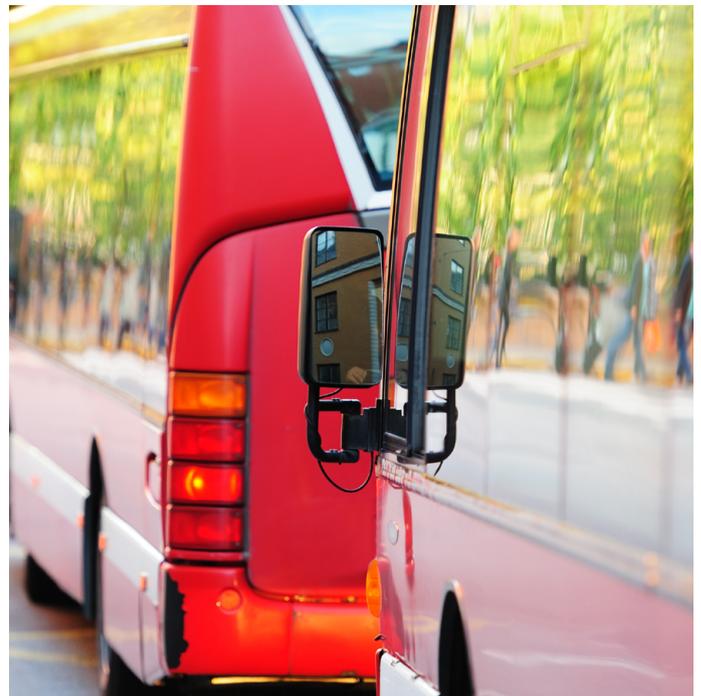
National Express is at the heart of plans to make Coventry the UK's first all-electric bus city with plans to replace 300 buses with zero-emission electric battery vehicles. National Express is also trialling 20 hydrogen-powered buses in partnership with Birmingham City Council.

Absolute emissions declined by 33% in 2020 and Scope I emissions from fuel combustion have fallen by 38% since 2015. This reflects a greening of the fleet, but also the impact of reduced travel due to COVID.

WHAT ABOUT SAFETY?

Unsurprisingly safety is a key priority and bus and coach travel remains very safe when compared to other road users. The company uses a benchmark (Fatalities and Weighted Injuries) index based on UK rail, with a score of 1.824 or 0.004 per million miles travelled. This increased slightly on 2019, but is significantly better than historical performance. As part of its drive to reduce incidents, National Express has fitted over 20,000 vehicles with a DriveCam safety system, and more than 400 digital fatigue alerts on long-distance coaches, which has led to a 50% fall in fatigue related safety events.

National Express has among the youngest fleets among UK bus operators which also supports higher safety standards, and the company fully supports the campaign to ban tyres that are over 10 years old – but has gone further than proposed legislation by suggesting this should extend to twin axle configurations. The company has committed to targets around safety including zero responsible fatalities and annual reduction in FWI/million miles travelled.



WHAT ABOUT EMPLOYMENT ISSUES?

National Express employs over 50,000 people in 11 countries. As a people-centric business, the company places high regard on 'being the place to work in mass transit'. This is delivered via industry leading employee satisfaction scores; being a Living Wage employer and achieving Investor in People status.⁵

WHAT IS EDENTREE'S POSITION?

The humble omnibus has been long overlooked as the work-horse of public transportation, and has long been subject to uneconomic routes and unsustainable fare increases that drive out the most vulnerable users such as the elderly, children and students. As we take on the challenge of climate change and poor urban air quality the bus is finally at an inflection point where its contribution to healthy cities and social inclusion is being recognised. Led by elected Mayors, the bus is now at the heart of a renaissance in thinking. New clean, comfortable and low emission vehicles also make the customer experience the best it has ever been; the decades old black-smoke emitting diesel bus is a thing of the past.

EdenTree has invested in National Express as an industry leader in public mass transportation that is well diversified and a long-standing quality business. Long-distance coach is an attractive competitor to rail – especially on cost grounds, whilst its operations overseas provide diversification away from the regulated UK bus market. Its dominant position in the West Midlands is a 'shop window' on what can be achieved as the wider UK fleet looks to transition. The holding complements our positive view on social inclusion, social mobility and access to basic services.

⁵ National Express ibid



THE RESPONSIBLE INVESTMENT TEAM

We have a specialist in-house Responsible Investment (RI) team who carry out thematic and stock-specific research to identify ethically responsible investment ideas for our range of screened Funds. Headed up by Neville White, Head of RI Policy & Research, and supported by Responsible Investment Analysts Carlota Esguevillas and Rita Wysheslesky, the team is also responsible for creating an on-going dialogue with companies, allowing us to engage on a wide variety of ethical and socially responsible investment concerns. For investors, it's an added layer of assurance that our client's money is being invested in companies that are operating in a responsible and sustainable way. Our ethical and responsible investment process is overseen by an independent Advisory Panel that meets three times a year, and comprises industry and business experts, appointed for their specialist knowledge.



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