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04

## The express division



Sydney Opera House reflection

## Express business description

Our express division provides on-demand door-to-door express delivery services for customers sending documents, parcels and freight. We offer regional, national and world-wide express delivery services, primarily for business-to-business customers. The express services we provide and the prices we charge to customers are in the main classified by transit times, distances to be covered and sizes and weights of consignments.

### EXPRESS STRATEGY

In previous years we mainly focused on smaller and medium-sized customers. In 2004, we further refined our strategy to ensure a balance of customers of different sizes. We also increased our focus on controlling costs in all areas of our operations.

Our ambition is to be the leader in day- and time-certain, door-to-door transport for our business-to-business clients with the widest geographical coverage.

We are a global express player. Our strategic intent is to:

- be number one in Europe in national and intra-European express flows,
- build uplift capacity from China to fuel our European network and establish a domestic network in China,
- be number one in the Rest of the World emerging markets, and
- be number one in special services.

### Express operating revenues

	Year ended at 31 December			
	2004		2003	2002 <sup>1</sup>
	US\$	€	€	€
Express Europe	5,163	3,814	3,455	3,402
Express Rest of the World	1,194	882	796	773
<b>Total operating revenues</b>	<b>6,357</b>	<b>4,696</b>	<b>4,251</b>	<b>4,175</b>

(in millions)

1. Figures for 2002 have been restated to reflect the transfer of Innight services from express to logistics.

### EXPRESS DIVISION OVERVIEW

In 2004, despite a mixed world-wide economy, our express business produced a strong performance driven by our international businesses, offering the right products, disciplined pricing management and an efficient sales process.

The primary factors behind our profit improvements in 2004 were strong international volumes, which were supported by a more balanced customer portfolio, continued positive revenue quality yield and careful cost management. Revenue quality yield is one of our key measures and it is calculated as the average of the percentage change in revenue per consignment compared to the previous year, and the percentage change in revenue per kilogramme compared to the previous year. Our employees furthered our mission through strict adherence to our commercial policy, a focus on serving business-to-business customers, and consistent company-wide deployment of our uniform best practice processes.

To achieve this, our objectives are to:

- achieve profitable revenue growth through volume acquisitions at optimised pricing,
- maintain a balanced customer portfolio (global accounts, national major, large, medium, small and adhoc customers),
- focus on product performance,
- improve cost effectiveness,
- ensure quality in all key areas,
- provide high-quality and cost-effective intra-European services through connecting strong domestic businesses,
- secure outstanding levels of customer satisfaction,
- develop leading-edge support technologies that provide added-value for customers,
- strengthen the TNT brand and increase top-of-mind awareness of the comprehensive range of reliable on-demand express delivery services provided by the company, and
- recruit, develop and manage our employees towards the highest standard of customer care.

In 2004, our express division earned revenues of €4,696 million. Express accounted for 37.2% of our operating revenue, 27.4% of our operating income and 26.8% of our earnings from operations.

The following table sets forth operating revenues for the Europe and Rest of the World lines of business in our express division for each of the years in the three-year period ended 31 December 2004.

Technology continues to be an essential element to achieve our business strategy. We continue to standardise our processes throughout our global organisation and this is being supported by the development and implementation of common processes on a standard IT platform. We plan for our common sales and customer service systems to support a single “face” to the customer through harmonisation of our international and domestic processes. We continue to develop the common back office system using the integrated solutions from SAP.

In 2004 we continued to exploit the comprehensive range of cross-functional data available in our datawarehouse to provide consistent and timely management reporting and analysis of our key performance indicators. This has enabled in-depth measurement and analysis of our operational service performance and sales activities, which facilitates continuous improvement and adoption of best practice in our business.

A focus in 2004 was to maintain high quality technology for use by our customers. Our most recent regular customer survey demonstrated a high degree of satisfaction with the technology and functionality of the solutions provided. Key reasons for using the customer systems were stated as ease of use, speed of use and simplification of business activity. We also gained consistently high scores for customer technology in our regular customer loyalty surveys.

In 2004 we undertook a number of benchmarks of our technology effectiveness and efficiency. In all cases these showed excellent results, indicating that we remained effective in all aspects of information and communication systems.

We are actively looking into business opportunities and potential acquisitions to expand our express operations.

### Express Europe

The Express Europe line of our express division provides regional, national and pan-European express services as well as time-sensitive door-to-door products that deliver consignments between Europe and the rest of the world. Our extensive integrated road and air networks have given us a strong position in the European market and are an important strategic asset with dense coverage in 33 European countries. We expanded our European network in 2004 and continued to introduce uniform best practice approaches throughout the organisation.

In Europe, we provide on-demand expedited door-to-door delivery services that involve carrying documents, parcels and freight for our European customers. The shipments are collected by a fleet of vehicles that make either scheduled stops or on-demand collections upon receipt of customer telephone or Internet requests. Shipment and consignment details are sent to the nearest depot in our network. Details of each shipment are entered into our track-and-trace systems either through scanning, data entry or electronic data interchange methods. The customer can then access the information through the Internet or proprietary customer interface technology. Each shipment is then sorted by destination and consolidated with other customers' consignments. Depending on its destination, each shipment is then line-hauled to a domestic road hub, an international road hub or one of our airports, generally within two hours of arrival at the depot.

We transport intra European shipments from the collecting depot by road or on one of the aircraft owned or leased by us from an origin airport to our main air express sorting hub in Liège, Belgium. Where transit times allow, shipments that do not travel by air are carried by truck to one of our 10 main European road hubs. We then unload and sort the shipments and consolidate them with other consignments for each destination and then put them on outbound line-hauls for movement to the delivery depot. We move domestic consignments within major European countries from the collection to the delivery depot, either directly or via a domestic hub.

At the delivery depot we sort the shipments and then load them on the appropriate delivery vehicle. Proof of delivery is entered into the Global Link or other appropriate computer system that is updated at every point in the process. This enables us to notify the customer when the consignee has received the shipment. Through these integrated road and air networks we are able to

offer a range of fast and reliable express delivery services in most European countries. Our track-and-trace systems, including the Global Link system, enable us to offer an automated proof-of-delivery service, and customers can access the information through the Internet or proprietary customer interface technology.

In the pan-European segment of the market, our competition comes from global providers with international networks. Parcel alliances and public postal operators are trying to penetrate the pan-European market by buying into parcel and express companies to create international air and road express networks. Trends in the industry indicate that express companies are seeking to extend their services further into the conventional freight markets in an effort to exploit the capacity of their networks. For these reasons, it is likely that the major express operators will increasingly look for opportunities in liberalised post markets and in the wider freight markets. Growth rates in the express market in Europe have been higher than those in the United States, indicating ongoing market penetration of dedicated parcel and time-sensitive delivery services.

We expect that the overall international market, particularly the Pacific routes, should grow at faster rates than European domestic markets. The market in Europe has undergone a period of intense consolidation in recent years and now has four other major players: Deutsche Post (DHL), FedEx Corp., Geopost-Groupe (La Poste) and United Parcel Service Inc. (UPS). However, the market is still much more fragmented than that of the United States and there are still several large regional operators. Growth for the private courier companies in Europe has been consistently higher than for their more mature United States counterparts.

We already have a more extensive express delivery road network in Europe than any of its competitors. Based on this robust infrastructure and on the disappearance of customs border controls resulting from the enlargement of the European Union, we launched 16 new road linehaul connections between eight new acceding European Union member states on 17 May 2004. With 1,800 staff, 900 vehicles and 67 depots in these eight accession countries, we have well-established profitable operations in this high-growth region, and a relatively modest expenditure was sufficient to provide customers with new and better services in the enlarged European Union.

With the removal of the time consuming customs clearances resulting from the enlarged European Union, we now offer much improved international road transit times. The new road linehails in response to the enlargement of the European Union were launched on 17 May 2004 and have resulted in an improvement in road transit times, by between one and five working days. We have seen a substantial improvement in our ability to deliver consignments originating from the European Union. Examples include:

- from Ostrava, Czech Republic to Vilnius, Lithuania, journey times were cut from six days to two days,
- from Tallinn, Estonia to Warsaw, Poland, journey times were cut from six days to two days, and
- from Budapest, Hungary to Prague, Czech Republic, journey times were cut from four days to one day.

In addition to offering customers shorter overall transit times between European Union countries, we have capitalised on reduced delays at country borders to provide customers in the accession countries with later collections for exports and earlier deliveries of imports. We have added additional sorting capabilities at 10 of our existing sites to process the increased flow of consignments travelling through our network.

We continue to enhance our European air and road networks to be able to offer the most reliable service to our customers. With respect to our European network, we added a road service to Bosnia in 2004, making it the 33rd country in our express road network. We introduced Turku in Finland as a new airport connection in March 2004 and in October 2004 further expanded our already dense network coverage by introducing Malta and Cluj in Romania. We intend to make further investments to improve the sorting facilities at our hub at Arnhem.

On 8 January 2004, we announced plans to introduce a further five Boeing 737-300 aircraft to our European air network. The five aircraft, leased for five years from GE Capital Aviation Services, will replace chartered aircraft currently operating in our express air network. The new B-737s will be phased in over the next four years. Two aircraft joined the fleet in 2004, with further aircraft to be added in 2005, 2006 and 2007.

#### **Liège Investment**

On 25 May 2004, we announced a €36 million investment plan for our Liège air hub, to be completed by the end of 2005. This investment confirms our growth prospects and our strong commitment to the region. Our investment is intended to improve transit times for our customer base and increase the percentage of consignments delivered on time and in perfect condition.

The planned investment is intended to:

- accommodate growth in number of airport destinations and sorting splits,
- remove time consuming, non-ergonomic manual processes,
- provide extra capacity,
- reduce damaged shipments,
- allow later departures and earlier arrivals, and
- increase staff productivity.

A number of initiatives were taken and launched aiming at reducing noise, either on the ground or in-flight, of our fleet. These include the implementation of new aircraft procedures to reduce lateral tolerance and optimise the climb profile during take-off, introduction of Boeing 737 aircraft, ground power units replacing noisier auxiliary power units and commencing to recertify the A300 aircraft at a lower maximum take off weight. See chapter 12, note 14.

#### **Express Rest of the World**

The Express Rest of the World business line provides door-to-door express delivery of documents, parcels and freight worldwide in all areas outside Europe and from these areas to Europe. Our worldwide coverage extends to more than 200 countries. In many of these countries our global express services are augmented by domestic and regional express delivery services. We also are building our position in Asia and have further improved service levels between Europe and Asia. Our business in Asia has expanded through a mix of organic growth, acquisitions and co-operative ventures such as our alliance with China Post.

In China, we have 25 company-owned locations supported by an extensive agency and associate network that allows us to serve some 500 cities. We aim to have 35 of our own locations by the end of 2005.

Express Rest of the World operates in a similar way to that of our Express Europe business line, but relies primarily on airlift by commercial passenger airlines for linehaul transportation links.

In Australia our business was brought back to profitability in 2003, and further earnings improvements were achieved in 2004, through:

- yield improvements through appropriate pricing actions,
- increased customer loyalty through improved delivery of customer services, and
- strong cost management.

In North America, we carry international express shipments primarily to and from the Northeast and West Coast regions. Building on our own delivery network in the Northeast business corridor, we have introduced improved next-day delivery services to nine major business centres, including New York, Washington D.C., Chicago and Toronto.

Express Rest of the World primarily competes with the three major carriers, which are UPS, FedEx and Deutsche Post (DHL). See chapter 10 – “Risk factors”. All of these carriers are pursuing aggressive expansion strategies in China and other emerging markets.

## Express financial review

### Express operating revenues

	Year ended at 31 December					
	2004		% VARIANCE	2003	% VARIANCE	2002 <sup>1</sup>
	US\$	€		€		€
Express Europe	5,163	3,814	10.4	3,455	1.6	3,402
Express Rest of the World	1,194	882	10.8	796	3.0	773
<b>Total operating revenues</b>	<b>6,357</b>	<b>4,696</b>	<b>10.5</b>	<b>4,251</b>	<b>1.8</b>	<b>4,175</b>

(in millions, except percentages)

1. Figures for 2002 have been restated to reflect the transfer of Innight services from express to logistics.

### Express operating expenses

	Year ended at 31 December					
	2004		% VARIANCE	2003	% VARIANCE	2002 <sup>1</sup>
	US\$	€		€		€
Cost of materials	202	149	18.3	126	(6.0)	134
Work contracted out and other external expenses	3,047	2,251	9.4	2,057	0.6	2,044
Salaries and social security contributions	2,070	1,529	7.8	1,418	2.8	1,379
Depreciation, amortisation and impairments	283	209	5.6	198	3.7	191
Other operating expenses	319	236	3.1	229	(2.6)	235
<b>Total operating expenses</b>	<b>5,921</b>	<b>4,374</b>	<b>8.6</b>	<b>4,028</b>	<b>1.1</b>	<b>3,983</b>

(in millions, except percentages)

1. Figures for 2002 have been restated to reflect the transfer of Innight services from express to logistics.

### Express operating income

	Year ended at 31 December					
	2004		% VARIANCE	2003	% VARIANCE	2002 <sup>1</sup>
	US\$	€		€		€
Earnings from operations	505	373	35.1	276	12.2	246
% of express operating revenues	7.9%	7.9%		6.5%		5.9%
Amortisation and impairment of goodwill	(69)	(51)	3.8	(53)	1.9	(54)
<b>Total operating income</b>	<b>436</b>	<b>322</b>	<b>44.4</b>	<b>223</b>	<b>16.1</b>	<b>192</b>

(in millions, except percentages)

1. Figures for 2002 have been restated to reflect the transfer of Innight services from express to logistics.

### Express operating statistics

	Year ended at 31 December		
	2004	2003	2002 <sup>1</sup>
Number of consignments (in thousands)	176,429	170,782	170,310
Total number of tons carried	3,378,863	3,203,138	3,149,161
Average of number of working days	260	250	250
Number of depots / hubs	857	836	854
Number of vehicles <sup>2</sup>	19,023	18,308	18,008
Number of aircraft <sup>2</sup>	42	43	43

1. Figures for 2002 have been restated to reflect the transfer of Innight services from express to logistics.

2. A substantial number of vehicles and aircraft are not owned by us but are leased or subcontracted.

During 2004, our express division realised higher operating revenues and improved earnings as a percentage of operating revenues due to a strong performance in our international business (attributable to offering the right products, disciplined pricing management and an efficient sales process) and a higher average number of working days.

We continued to grow our profit margin, which was achieved through the implementation of standard commercial policies, cost control whilst maintaining service levels and the ongoing review of our revenue quality yield against cost inflation.

Some of the other key performance indicators used to monitor our express business include on-time delivery, customer satisfaction and employee satisfaction.

### Express operating revenues

2004

Operating revenues of our express division for 2004 increased by €445 million (10.5%) compared to the prior year. The organic growth in operating revenues of our business was €454 million (10.7%). The 2003 acquisition of Archive and Data Storage had a positive effect on operating revenue of €1 million but negative foreign exchange effects had a negative effect of €10 million (-0.2%), mainly due to the weakening of the US dollar and various Asian currencies against the euro.

The increase in operating revenues was due primarily to strong volume growth and an increased number of working days, with European air volumes increasing over last year by 4.9% and road volumes by 9.7%, as well as a positive European revenue quality yield of 3.9%.

Express Europe operating revenues for 2004 increased by €359 million (10.4%) compared to the prior year. The organic growth in operating revenues was €347 million (10.1%). Most business units contributed to the increase in operating revenue despite the mixed economic conditions. In particular, the UK, Benelux, Italy, Spain and the Eastern European countries contributed to the majority of the growth in operating revenue. The 2003 acquisition of Archive and Data Storage had a positive effect on operating revenue of €1 million and foreign exchange had a positive effect of €11 million (0.3%).

Express Rest of the World operating revenues for 2004 increased by €86 million (10.8%) compared to the prior year. This was achieved through the €107 million (13.4%) organic growth in operating revenues from operations primarily in China, Taiwan and the Middle East. This was partly offset by negative foreign exchange effects of €21 million (-2.6%) mainly due to the weakening of the US dollar and various Asian currencies against the euro.

2003

Operating revenues of our express division for 2003 increased by €76 million (1.8%) compared to 2002. The organic growth in operating revenues of our business was €265 million (6.3%). The combination of the 2002 disposal of our Mistral Air Srl. business and the 2003 acquisition of Archive and Data Storage, had a net negative effect on operating revenue of €5 million (-0.1%) and negative foreign exchange effects accounted for a €184 million

(-4.4%) decline mainly due to the weakening of the UK pound, the US dollar and various Asian currencies against the euro.

The increase in operating revenues was due primarily to improvements in the revenue quality yield and modest volume improvements that resulted from the continued focus on the division's standard commercial policies that concentrate on providing simplified, no-discount tariffs to all new small and medium-sized business-to-business customers.

Express Europe operating revenues for 2003 increased by €53 million (1.6%) compared to the prior year. The organic growth in operating revenues was €168 million (4.9%). Most business units contributed to the increase in operating revenue despite the difficult economic conditions. In particular, Germany, France, Austria, Spain and the Eastern European countries contributed to the majority of the growth in operating revenue. The negative effect on operating revenue in 2003 from acquisitions of €5 million (-0.1%) mainly related to a €6 million decrease in revenues through the sale of our Mistral Air business in 2002, offset by €1 million in additional revenues from Archive and Data Storage. The negative foreign exchange effects of €110 million (-3.2%) related mainly to the weakening of the UK pound against the euro.

Express Rest of the World operating revenues for 2003 increased by €23 million (3.0%) compared to the prior year. This was achieved through the €97 million (12.6%) organic growth in operating revenues from operations primarily in Australia, Asia and the Middle East. This was partly offset by foreign exchange effects of €74 million (-9.6%) mainly due to the weakening of various Asian currencies against the euro.

### Express operating income

2004

The express division's operating income for 2004 increased by €99 million (44.4%) compared to 2003. Amortisation of goodwill during 2004 decreased by €2 million to €51 million compared to 2003 and the express division's earnings from operations for 2004 increased by €97 million (35.1%) compared to 2003.

Operating expenses of our express division for 2004 increased by €346 million (8.6%) compared to the prior year. This was driven mainly by the strong international volume growth, additional full time equivalent employees required to process these volumes, the expansion of our business in China and Eastern Europe and the high costs of fuel for our aircraft, linehaul and pick up and delivery vehicles. Cost of materials increased by €23 million (18.3%) due to the higher fuel costs incurred in all business units. Work contracted out and other external expenses increased by €194 million (9.4%). This included the cost of linehaul and pick up and delivery, which have increased to service the higher volumes and to improve the service quality. This also included the higher fuel costs from commercial linehaul and subcontractors as well as the increased number of depots in China. Salaries and social security contributions increased by €111 million (7.8%) due to the additional number of full time equivalents, salary increases for existing employees, severance and redundancy payments and the higher number of working days in 2004. Depreciation, amortisation and impairments increased by €11 million (5.6%) due to the costs of asset impairments

on buildings in Australia and Germany. In Australia we had an impaired depot due to construction faults. The impairment amount was offset against a compensation received from the company that constructed the depot. Other operating expenses increased by €7 million (3.1%) due to increased advertising and consultants costs.

The improvement in operating income was due primarily to continued focus on the division's standard commercial policies and achieving further operating efficiencies by continuing to share best operating practices throughout our business and investing in operations and information systems aimed at further improving our service quality. Almost all our express business units achieved improvements in their earnings from operations. Improvements were most significant in the Benelux countries, the UK, Ireland, Germany, Eastern Europe, Spain, Austria and Scandinavia. The organic growth in earnings from operations for 2004 increased by €96 million (34.8%) compared to 2003. The positive foreign exchange fluctuations amounted to €1 million (0.3%).

Overall earnings from operations as a percentage of express operating revenues increased to 7.9% for 2004 compared to 6.5% in the prior year.

#### 2003

The express division's operating income for 2003 increased by €31 million (16.1%) compared to 2002. Amortisation of goodwill during 2003 decreased by €1 million to €53 million compared to 2002 and the express division's earnings from operations for 2003 increased by €30 million (12.2%) compared to 2002. The improvement was due primarily to continued focus on the division's standard commercial policies that concentrate on providing simplified, no-discount tariffs to all new small- and medium-sized business-to-business customers and achieving further operating efficiencies by continuing to share best operating practices throughout our business and investing in operation and information systems aimed at further improving our service quality. The organic growth in earnings from operations for 2003 increased by €57 million (23.1%) compared to 2002. This was partly offset by acquisitions that resulted in a €5 million (-2.0%) decrease in earnings from operations and foreign exchange fluctuations that amounted to €22 million (-8.9%) mainly due to the weakening of the UK pound, the US dollar and various Asian currencies against the euro.

Overall earnings from operations as a percentage of express operating revenues increased to 6.5% for 2003 compared to 5.9% in the prior year.