

3 The Peninsular and Oriental Steam Navigation Company

3.1. P & O told us that it was a broadly based group with a wide range of activities:

- Service industries
- Road transport
- Cruises
- Ferries
- House-building and construction
- Property
- Bulk shipping
- Container shipping
- Off-shore supply boats and stevedoring (through P & O Australia Ltd).

History 3.2. P & O's first shipping service was established in 1837 from the United Kingdom to Spain, Portugal and the Mediterranean ports. P & O was incorporated by Royal Charter in 1840 when it established a shipping service to the Far East. Shipping routes were subsequently established throughout the Near and Far East and to Australasia, and the company's business expanded both organically and by acquisition over the ensuing century.

3.3. P & O told us that the increased demand for shipping, following the first closure of the Suez Canal, coupled with the encouragement various Governments had given to their shipping and shipping industries, had led to a world surplus of shipping; as a consequence by the late 1950s world freight rates had collapsed.

3.4. In these circumstances the policy of P & O had been to develop more profitable shipping activities rather than to make sudden large-scale withdrawals of capital from the industry. P & O told us that in pursuing this policy it had invested in new cargo trades in the 1960s including oil tankers, dry bulk carriers and, later, liquefied petroleum gas carriers. The company also set up Overseas Containers Ltd (OCL) with three other United Kingdom shipping companies to take over the company's cargo liner trades as they were converted to container shipping,

3.5. P & O began to diversify its activities in the 1970s. It phased out its scheduled passenger line services to the Far East and Australasia and developed the concept of ocean cruising as a leisure market. Its North Sea ferry services which had been established in the late 1960s were complemented by the acquisition of the Coast Lines Group which provided short sea ferry and road haulage activities and by the establishment of cross-Channel ferry services. This resulted in P & O serving routes to Orkney and Shetland, Northern Ireland, the Republic of Ireland, Sweden, the Netherlands, Belgium and France and led to the development of P & O's integrated road and sea through-transport freight haulage operators, Ferrymasters and Pandoro. P & O also acquired the house-building and property construction group, Bovis, and developed a subsidiary company in Australia engaged principally in materials handling, off-shore supplies services and cold storage and distribution. During this period P & O made investments in oil and gas-related activities mainly in the United States and in the North Sea.

3.6. During the latter half of the 1970s, faced with the continuing shipping recession which affected the oil and gas trades as well as more traditional shipping activities, the company embarked on a restructuring programme which included the sale of certain businesses and assets amongst which were the North Sea and United States oil businesses. In 1984 P & O Building and P & O Falco, the oil trading business, were disposed of and in January 1985 the company sold its cross-Channel ferry activities to European Ferries.

3.7. In February 1985 P & O merged with Sterling Guarantee Trust PLC (SGT) which brought into the group a number of service businesses, including the Earls Court and Olympia exhibition centres, the Arndale Shopping Centres and the Sutcliffe Industrial Catering Group as well as a substantial portfolio of office, shop and commercial properties located largely in the United Kingdom and the United States of America.

Recent acquisitions

3.8. In January 1986 P & O acquired a 50.01 per cent interest in European Financial Holdings Ltd (EFH) which holds 20.8 per cent of the ordinary shares and of the convertible preference shares in European Ferries (see Chapter 5). In April 1986 P & O reached agreement with the other shareholders of OCL to acquire their interest in that company and in June 1986 P & O acquired Stock Conversion PLC (Stock Conversion), a large United Kingdom property company in which an associate company of European Ferries, Stockley PLC (Stockley), had an interest.

P & O's business strategy

3.9. P & O told us that owing to the spread of its activities, the group's overall objectives were essentially financial relating primarily to return on investment, earnings growth and asset backing. Its basic strategy was to build by internal expansion or, if appropriate, by acquisition, on its successful businesses and to divest itself of those which did not meet its criteria. The group was prepared to make acquisitions outside its present sectors if they seemed likely to help it achieve its objectives but acquisitions were most likely to occur in areas of business with which the group was familiar.

3.10. P & O said that a common feature of most of its activities was the international span of the operations and therefore the international nature of competition. Its international markets were expanding and increasing financial strength was essential in order to compete successfully. It considered that with skills which were applicable internationally the group was too heavily concentrated in the United Kingdom and accordingly one of its objectives was to build up its overseas shore-based operations. Areas where expansion was proposed were the Far East where the group's well-known name could be exploited and the United States of America where the group was experienced. Australian investments would also be allowed to grow. P & O told us that it was difficult to plan overseas expansion precisely as much depended on the opportunities and the movement of exchange rates.

Organisation and management

3.11. P & O's major subsidiaries and associated companies are organised and managed on a divisional basis as follows:

- (a) *Service Industries*. This division comprises the Earls Court and Olympia exhibition centres and a number of other group subsidiaries supplying catering services, automatic vending equipment, tools and engineers' supplies and tools for the off-shore oil industries. It also includes POETS, a group of P & O subsidiaries operating, *inter alia*, integrated through transport services in the United Kingdom, the Republic of Ireland and other European countries. Pandoro provides door-to-door unit load freight services between England and Northern Ireland and between England and the Republic of Ireland. NITS provides similar services between Scotland and Northern Ireland, and Ferrymasters operates from the United Kingdom to Western Europe. Other specialised road transport services are supplied by P & O Roadtanks Ltd (bulk powder and bulk liquid transport)

and P & O Roadways Ltd (contract hire and transport of containers and demountable trucks). This division also operates warehousing and bond facilities.

- (b) *Passenger Shipping.* P & O Cruises Ltd provides holiday cruises world-wide. Its other activities include holiday tour interests, travel services and resort hotel management in California. The company operates seven cruise ships. P & O owns a 50 per cent interest in the North Sea Ferries consortium which operates six passenger and freight ferries between Hull and Rotterdam and between Hull and Zeebrugge as well as two freight-only ferries between Ipswich and Rotterdam. P & O Ferries Ltd (P & O Ferries) operates two passenger and freight ferries and two cargo ferries between Scotland and the Orkney and Shetland Islands.
- (c) *House-building, Construction and Development.* This division consists of Bovis Homes Ltd, which builds approximately 3,000 houses a year in Great Britain and approximately 250 in the United States of America. Its United Kingdom activities are concentrated in the home counties, the South-East, the Midlands and the West. Bovis Construction Ltd and Bovis International Ltd provide construction services in the United Kingdom and overseas. Town and City Properties (Development) Ltd develops retail and commercial properties for sale or investment.
- (d) *Container and Bulk Shipping.* This division comprises P & O Bulk Shipping Ltd which operates a fleet of 10 bulk carriers and OCL which is one of the world's largest container shipping companies with a fleet of 25 ships and over 70,000 containers. P & O Gas Carriers Ltd, a company owned 50 per cent each by P & O and Overseas Shipholding Company Group Inc, has recently been sold.
- (e) *Investment Property.* This division consists of Town and City Properties Management Ltd which manages the group's United Kingdom investment property portfolio comprising offices, shops and other premises, Arndale Shopping Centres Ltd which has interests in and manages shopping centres in the United Kingdom, and Town and City Properties (Overseas) Ltd which is responsible for P & O group's overseas property interests (excluding Australia). These are largely concentrated in Boston, United States of America.
- (f) *P & O Australia.* P & O Australia Ltd is a 75 per cent owned subsidiary of P & O. It has interests in materials handling, off-shore services, cold storage and distribution and leisure activities in Australia and the Pacific Basin. It runs container terminals and stevedoring businesses in most major Australian ports and is the largest operator of supply vessels to the Australian off-shore oil industry.

3.12. P & O told us that its main operating companies were expected to act independently in terms of day-to-day management. Group policy was reserved to matters such as senior management appointments, dividends, capital expenditure approval, treasury, financial control, employment policy and pensions. P & O has 15 directors of whom three are non-executive. The Board normally meets once a month with other meetings as necessary to consider specific matters. Committees of the Board meet as required to approve loans, guarantees and the sealing of documents etc. P & O told us that the presentation, review and agreement of strategic plans and annual budgets was an important facet of overall group control. Service companies had been set up where possible as profit centres and the operating companies could generally choose to utilise their services on an arm's length commercial basis except where there was an overriding benefit to the group.

Turnover and employment

3.13. P & O had a revenue of £1,629 million and employed an average of 31,505 people in 1985. Table 3.1 shows the percentage of total revenue accounted for by P & O's main activities.

TABLE 3.1 Analysis of P & O's turnover by main activity 1985

	%
Industrial services	10
Road transport	10
Cruises	16
Ferries	2
House-building and construction	25
Property	3
Bulk shipping	3
Container shipping	26
P & O Australia	5
	100

Source: P & O.

P & O's ferry services

3.14. P & O operates a number of ferry services to Continental Europe and the Republic of Ireland and also within the United Kingdom. Its services (through the North Sea Ferries joint venture) from Hull to Rotterdam and to Zeebrugge cater for passengers and cars as well as freight. P & O's ferry services to Continental Europe from Ipswich and Middlesbrough are freight-only as are its services to Northern Ireland and the Republic. The group also operates car, passenger and freight ferry services from Scotland to the Orkney and Shetland Islands. All P & O's ferry services are operated by ro/ro ships.

North Sea ferry services

3.15. Since 1965 P & O has operated as a joint venture with Nedlloyd, a passenger, car and freight ferry service between the United Kingdom and Belgium and the Netherlands. The service, which operates overnight, is known as North Sea Ferries and runs from Hull to Rotterdam and to Zeebrugge. It is operated by a wholly-owned P & O subsidiary, North Sea Ferries Ltd, and by a Nedlloyd subsidiary using two P & O ships and two Nedlloyd ships. The service is supplemented by two freight-only ships chartered in by P & O on the Hull to Zeebrugge route.

3.16. North Sea Ferries also operates two freight-only ships between Ipswich and Rotterdam. One of these ships belongs to P & O and the other is chartered in by it. Ferrymasters, the P & O subsidiary which operates door-to-door haulage services between the United Kingdom and Continental Europe (see paragraph 3.24), is allocated 55 per cent of the space on these two ships with the remaining 45 per cent available for sale by North Sea Ferries to other users. This allocation is flexible depending upon the precise requirements of each operator on any particular sailing.

3.17. P & O told us that each partner in North Sea Ferries has a large cruise ferry on order for delivery in 1987 at which time the four smaller ships on the Hull to Zeebrugge route will be withdrawn. The cruise ferries will have large freight and passenger capacity.

3.18. Day-to-day management of North Sea Ferries is based in Rotterdam and the service has branch offices in Hull, Zeebrugge and Ipswich. P & O and Nedlloyd share equally all profits, losses, assets and decisions of North Sea Ferries and the business has its own management structure separate from that of both P & O and Nedlloyd.

3.19. Ferrymasters operates a freight ferry from Middlesbrough to Gothenburg and Helsingborg but this service is completely dedicated to the company's own door-to-door haulage operation.

Irish Sea services

3.20. P & O's Irish Sea routes are now freight-only and are operated by two P & O subsidiaries which also operate door-to-door haulage services. The ships on these routes carry a mixture of these subsidiaries' own haulage through traffic and quay-to-quay traffic for other customers. Until 1981 P & O operated a passenger, car and freight service between Liverpool and Belfast.

3.21. NITS operates one ship between Ardrossan and Belfast and Pandoro operates one ship between Liverpool and Larne and one ship between Fleetwood and Larne. Pandoro also operates a joint two-ship service between Fleetwood and Dublin with B & I. Pandoro's arrangements with B & I are limited to space and cost sharing and do not include the pooling of revenue.

Other ferry services

3.22. Another P & O subsidiary, P & O Ferries, operates passenger, car and freight ferry services from Aberdeen and Leith to Orkney and Shetland and from Scrabster to Orkney. These services are operated by two multi-purpose ships and two freight-only ships.

Traffic

3.23. Traffic carried by P & O's freight ferry services to Belgium and the Netherlands and to Northern Ireland in 1985 is set out in Table 3.2.

TABLE 3.2 Freight traffic carried by P & O between the United Kingdom and Belgium and the Netherlands and between Great Britain and Northern Ireland, 1985

<i>North Sea Ferries</i>		<i>Running metres</i>
		'000
Hull-Rotterdam		617
Hull-Zeebrugge		559
Ipswich-Rotterdam		831
<i>Irish Sea</i>		<i>Trailer loads</i>
Fleetwood-Larne	}	74,000
Liverpool-Larne		
Ardrossan-Belfast		18,000

Source: P & O.

Note: North Sea Ferries' basis of charging is in running metres.

P & O's door-to-door transport services

3.24. P & O's integrated door-to-door transport services are operated from the United Kingdom to Continental Europe by Ferrymasters, to Northern Ireland and the Republic of Ireland by Pandoro and from Scotland to Northern Ireland by NITS. P & O told us that its integrated haulage operations had developed from the establishment in the 1960s and 1970s of its North Sea and cross-Channel ferry services and had been complemented by the group's acquisition of the Coast Lines Group which had included road haulage in its activities.

3.25. The P & O subsidiaries operating door-to-door transport services now have a fleet of 6,000 trailers, 1,440 tractor units and six ro/ro freight ferries. As indicated in paragraphs 3.16, 3.19 and 3.20, P & O's door-to-door haulage companies use their own or North Sea Ferries' ships on some routes but on other routes they use shipping services provided by other operators. Most of P & O's own trailer traffic is sent unaccompanied on shipping services.

P & O's United States property interests

3.26. P & O told us that it had considerable investments in property in the United States. These are held through a subsidiary company, Town and City Properties (Overseas) Ltd, which also holds the group's property interest in Europe. P & O's property interests in the United States consist mainly of offices and office, residential and light industrial development in Boston.

Financial information

3.27. P & O's accounts are prepared on the historical cost basis modified by the inclusion of substantially all properties at their latest valuations. Since the company merged with SGT in February 1985 group accounts have been prepared in accordance with the provisions of merger accounting. Consequently the results of SGT are consolidated with the P & O profit and loss accounts and balance sheets to form group accounts. Group results for each of the last five years¹ are shown in Tables 3.3 and 3.4.

¹ The group profit and loss accounts include additionally the interim result for the six months ended 30 June 1986.

TABLE 3.3 P & O: summarised group balance sheets at 31 December for each of the last five years*

	<i>£ million</i>				
	<i>1981</i>	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Assets employed					
Fixed assets					
Tangible assets					
Ships	301.8	280.5	227.1	309.4	261.7
Properties	541.3	531.8	522.9	513.9	532.0
Other fixed assets	77.2	99.9	134.7	62.5	56.1
	<u>920.3</u>	<u>912.2</u>	<u>884.7</u>	<u>885.8</u>	<u>849.8</u>
Interest in leased assets	20.6	24.1	18.5	13.0	16.5
Other investments	138.0	144.9	137.7	151.9	178.9
Net current assets (excluding cash and current borrowings)	42.7	142.0	7.4	17.9	8.8
	<u>1,121.6</u>	<u>1,223.2</u>	<u>1,048.3</u>	<u>1,068.6</u>	<u>1,054.0</u>
Deduct borrowings (net of cash)	(378.0)	(486.0)	(284.8)	(320.8)	(280.7)
Net assets	<u>743.6</u>	<u>737.2</u>	<u>763.5</u>	<u>747.8</u>	<u>773.3</u>
Financed by					
Deferred stock	141.9	142.1	142.4	243.7	244.6
6.3% (net) convertible stock	—	—	—	56.2	54.5
Preferred stock	3.3	3.3	3.3	3.3	3.3
Reserves	577.0	566.9	598.4	420.9	444.4
	<u>722.2</u>	<u>712.3</u>	<u>744.1</u>	<u>724.1</u>	<u>746.8</u>
Stockholders' funds	722.2	712.3	744.1	724.1	746.8
Minority interests	16.1	16.0	17.1	21.1	24.5
Insurance funds	5.3	8.9	2.3	2.6	2.0
	<u>743.6</u>	<u>737.2</u>	<u>763.5</u>	<u>747.8</u>	<u>773.3</u>
Capital gearing (%)	50.8	65.9	37.3	42.9	36.3

Source: P & O.

* The 1981, 1982 and 1983 figures are aggregations of the P & O group balance sheet at 31 December and the SGT group balance sheet at the following 24 March. The 1984 and 1985 figures are as published in P & O's 1985 group accounts.

TABLE 3.4 P & O: summary of group profit and loss accounts for the years ended 31 December* (Showing divisional operating results)

	£ million																	
	Six months to 30 June																	
	1981			1982			1983			1984			1985			1986		
	Turnover	Operating result	%	Turnover	Operating result	%	Turnover	Operating result	%	Turnover	Operating result	%	Turnover	Operating result	%	Turnover	Operating result	%
Service industries	285.5	12.2	13.5	325.5	17.3	18.7	344.6	23.9	21.3	374.4	26.6	21.7	430.7	34.4	22.3	227.2	22.0	27.5
Passenger shipping	200.1	7.9	8.7	226.0	5.7	6.1	289.1	6.2	5.5	324.4	4.8	3.9	385.7	13.1	8.5	160.1	9.1	11.4
House-building, construction and development	249.1	11.9	13.2	288.4	10.1	10.9	362.1	21.8	19.5	455.8	26.5	21.6	539.3	30.0	19.5	237.3	20.6	25.7
Container and bulk shipping	75.5	22.7	25.1	60.3	15.7	16.9	57.8	12.8	11.4	59.6	22.0	18.0	68.9	34.4	22.3	28.4	9.8	12.2
P & O Australia	96.4	4.1	4.5	150.3	8.3	9.0	147.3	8.7	7.8	166.4	12.2	9.9	112.5	9.4	6.1	38.8	2.6	3.3
Banking	14.2	3.7	4.1	21.8	5.0	5.4	22.6	6.4	5.7	32.1	7.5	6.1	36.6	7.7	5.0	—	—	—
Investment property income	38.5	13.6	15.1	43.7	19.3	20.8	48.1	20.1	17.9	54.4	23.0	18.8	55.6	25.2	16.3	29.5	15.9	19.9
Discontinued activities	238.6	14.2	15.8	271.8	11.3	12.2	230.6	12.1	10.9	177.0	(0.3)	—	—	—	—	—	—	—
	<u>1,197.9</u>	<u>90.3</u>	<u>100.0</u>	<u>1,387.8</u>	<u>92.7</u>	<u>100.0</u>	<u>1,502.2</u>	<u>112.0</u>	<u>100.0</u>	<u>1,644.1</u>	<u>122.3</u>	<u>100.0</u>	<u>1,629.3</u>	<u>154.2</u>	<u>100.0</u>	<u>721.3</u>	<u>80.0</u>	<u>100.0</u>
Interest payable, less receivable		(55.3)			(53.2)			(40.1)			(31.4)			(25.6)			(10.2)	
Employee profit share		—			(0.3)			(0.5)			(0.7)			(3.0)			—	
Profit before taxation		<u>35.0</u>			<u>39.2</u>			<u>71.4</u>			<u>90.2</u>			<u>125.6</u>			<u>69.8</u>	
Taxation		(5.4)			(13.6)			(17.3)			(30.0)			(34.9)			(21.0)	
Profit after taxation		<u>29.6</u>			<u>25.6</u>			<u>54.1</u>			<u>60.2</u>			<u>90.7</u>			<u>48.8</u>	
Minority interests		(0.5)			(1.4)			(1.3)			(2.6)			(2.4)			(0.7)	
Extraordinary and capital items		(2.6)			(13.2)			(1.0)			(57.4)†			0.1			7.0	
Profit for financial year attributable to stockholders		<u>26.5</u>			<u>11.0</u>			<u>51.8</u>			<u>0.2</u>			<u>88.4</u>			<u>55.1</u>	

Source: P & O.

* All the comparative figures have been restated to reflect the merger in February 1985 with Sterling Guarantee Trust PLC.

† Extraordinary items in 1984 included £78.3 million losses on ship sales, £14.5 million losses on sale and closure of businesses and a capital profit of £47.9 million on sale of properties.

3.28. The main contribution increases during the period to 31 December 1985 arise from the Service Industry Division (13.5 per cent to 22.3 per cent) and House-building, Construction and Development Division (13.2 per cent to 19.5 per cent)

3.29. Table 3.5 summarises details of P & O's group source and application of funds for the three years ended 31 December 1985.

TABLE 3.5 P & O: group source and application of funds for the years ended 31 December*

	<i>£ million</i>		
	1983	1984	1985
Source of funds			
Profit on ordinary activities before tax	71.4	90.2	125.6
Items not affecting movement of funds			
Depreciation	52.2	45.0	43.7
Shares of profits of associated companies	(9.1)	(28.7)	(37.9)
Unrealised exchange movements	(10.1)	9.2	9.6
	<u>104.4</u>	<u>99.4</u>	<u>141.0</u>
Sale of ships	45.5	10.5	44.8
Sale of properties	43.8	105.8	29.0
Sale of investments and other fixed assets	43.5	66.8	17.3
Issue of stock	0.3	0.3	0.6
Dividends from associated companies	6.3	12.3	11.8
	<u>243.8</u>	<u>295.1</u>	<u>244.5</u>
Application of funds			
Purchase of ships	26.9	127.5	48.4
Purchase of properties	23.4	39.4	37.6
Purchase of investment and other fixed assets	71.3	50.9	67.8
Other capital items	18.4	8.1	16.2
Tax paid	14.3	12.7	25.0
Dividends paid	19.7	32.2	31.6
	<u>174.0</u>	<u>270.8</u>	<u>226.6</u>
Movement in working capital			
Stocks	19.4	(11.1)	12.7
Debtors and current investments	(8.8)	(303.3)	(44.7)
Creditors and provisions	(147.3)	327.7	30.0
Trading assets of banking subs	5.3	4.6	1.2
	<u>42.6</u>	<u>288.7</u>	<u>227.8</u>
Net increase in funds	<u>201.2</u>	<u>6.4</u>	<u>16.7</u>
Represented by			
(Decrease)/increase in short-term deposits and bank balances	(2.5)	2.1	(0.2)
Decrease in loans and bank overdraft	203.7	4.3	16.9
	<u>201.2</u>	<u>6.4</u>	<u>16.7</u>

Source: P & O.

* The 1983 figures are aggregations of the P & O group at 31 December and the SGT group at the following 24 March, with minor adjustments to achieve consistency. The 1984 and 1985 figures are as published in the 1985 group accounts.

3.30. P & O's size relative to European Ferries based upon the published accounts for the financial year ended 31 December 1985, adjusted for the subsequent acquisition of OCL and Stock Conversion is set out in Table 3.6. Table 3.7 sets out P & O's returns on average capital employed and net assets for the four years to 31 December 1985.

TABLE 3.6 P & O's size relative to European Ferries

	<i>Number of times</i>
Capital employed	3.3
Net trading assets	3.3
Profit before tax and extraordinary items	3.6
Turnover	5.4

Source: MMC from P & O data.

TABLE 3.7 P & O: returns on average capital employed and net assets (including consolidated SGT figures)

	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Average capital employed (£m)	1,172.4	1,135.7	1,058.4	1,061.3
Profit before interest payable, extra-ordinary items and tax (£m)	92.4	111.5	121.6	151.2
Returns on average capital employed (%)	7.9	9.8	11.5	14.2
Average net assets (£m)	740.4	750.3	755.6	760.5
Profit before extraordinary items and tax (£m)	39.2	71.4	90.2	125.6
Returns on average net assets (%)	5.3	9.5	11.9	16.5

Source: MMC.