

ANNUAL REPORT 2005

LEADING IN WORLD TRADE



P&O 

Company overview

P&O is an international logistics and transport company. P&O's businesses are focused on achieving world class operational and financial performance and on delivering excellent service to customers.

Ports



One of the world's pre-eminent container terminal operators and stevedores with operations, including 29 container terminals, in over 100 ports. P&O Ports has a presence in 19 countries around the world. Its main service is containerised cargo handling in ports which offer strong growth opportunities. Other services include general cargo, bulk cargo, roll on-roll off facilities and cruise passenger terminal management, as well as a range of maritime services.

Ferries



P&O is a household name in the UK for ferry travel. P&O Ferries and P&O Irish Sea carry freight and tourist traffic between the UK and France, Spain, Belgium, Holland, Northern Ireland and the Republic of Ireland. P&O has a fleet of 23 ships. P&O Ferrymasters, the European road haulage and freight management business, is part of the Ferries division.

Properties and other



P&O Estates is the property investment, development and asset management division of P&O in Europe and the US.

During the course of 2005, P&O sold its Cold Logistics division and its stake in the container shipping business, Royal P&O Nedlloyd.

Highlights 2005

Profit for the period £290.1 million (2004 £151.5 million loss)

Underlying earnings before net financing costs and tax
£252.0 million (2004 £282.4 million)

Strong cash inflow with net debt reduced to £604.6 million
(2004 £1,181.6 million)

Ports underlying profit up 14% and container throughput up
6% to 14.7 million teus

Ferries underlying profit £14.7 million (2004 £5.9 million loss)
demonstrating success of the Fundamental Business Review

Net property disposals of £395.0 million

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Chairman's statement



Sir John Parker
Chairman



The 2005 results reflect good growth in our major business, Ports, and a turnaround in the performance of our Ferries business. The Group achieved significant strategic progress in 2005 and we now look forward to the next chapter in the long history of P&O under the new ownership of DP World.

Results

Group operating profit from continuing operations before separately disclosable items was £186.9 million (2004 £190.6 million). Good growth was reported in our major business, Ports, and Ferries returned to profitability despite high fuel costs and the significant impact of berthing problems at Calais at the start of the year. The overall decline in profit was due to a much reduced contribution from the Property business, reflecting the strategic sell down of the portfolio.

Profit before tax and separately disclosable items increased to £128.2 million (2004 £107.1 million) benefiting from reduced finance costs. Separately disclosable items from continuing operations before tax were a charge of £27.6 million compared to charges of £294.3 million in the prior year primarily in relation to impairments and reorganisation. Consequently, profit before tax on continuing operations was £100.6 million (2004 loss £187.2 million). Profit from discontinued operations and profit on sale of discontinued operations net of tax was £213.5 million (2004 £56.5 million) including a gain of £188.0 million on disposal of the Group's interest in Royal P&O Nedlloyd. The resulting profit for the period was £290.1 million (2004 £151.5 million loss).

Earnings per share and dividend

Underlying earnings from continuing operations per £1 nominal of deferred stock were 12.3p (2004 10.2p). After separately disclosable items the basic earnings per £1 nominal of deferred stock were 37.4p

(2004 loss 22.6p). A final dividend of 6.0p per £1 nominal of deferred stock is recommended by the Board and hence the total dividend for 2005 is 9.0p (2004 9.0p).

Strategic progress

2005, in particular, was a significant year in P&O's development with a number of strategic objectives being achieved.

We sold our shareholding in Royal P&O Nedlloyd at a significant profit. We also exited the Cold Logistics business. Our strategy of selling down the property portfolio was largely completed and we achieved our increased target of sales of close to £400 million. P&O Estates will continue to manage the remaining assets together with the London Gateway business park and selected new projects.

Almost £170.0 million was invested in expanding the Ports portfolio worldwide and exciting projects have been announced in locations such as Vietnam and Russia. We were pleased to receive conditional approval for our proposals to develop a world class port and a major business park at London Gateway in the UK.

The proposals to change fundamentally the way we run our Ferries business have been implemented successfully and the benefits can be seen as the business has now returned to profitability.

Acquisition by DP World

In November 2005, an initial cash offer was announced for P&O by Thunder FZE, a private company wholly owned by the Ports, Customs and Free Zone Corporation of Dubai (DP World). Thunder FZE was ultimately successful in acquiring P&O, with the transaction becoming effective on 8 March 2006. P&O was de-listed on 9 March 2006 and this is therefore expected to be the last Annual Report for P&O in this format.

Our aim has been to create stockholder value. The de-merger of the cruises business in 2000 has subsequently crystallised approximately £4.9 billion in value for shareholders in that company. The recent takeover of P&O by DP World has resulted from the strategic progress that P&O has made over a number of years and continued to make in 2005. At the cruises de-merger in October 2000, our deferred stock was valued at 243.0p. The recommended offer from DP World, which was subsequently accepted by stockholders, was 520.0p. Consequently, approximately £1.9 billion of value has been created, and stockholders have also enjoyed dividends throughout that period. In total, P&O has created approximately £6.8 billion in value since the 2000 de-merger.

Employees

During this period of great change for the Company it is particularly appropriate to recognise the considerable contribution of our employees. Change brings uncertainty. Despite this, our employees have continued to give of their best. As a result our businesses have performed strongly. Our new owners, DP World, have recognised this and said that they regard the management and employees as key to the ongoing success of the combined entity. I am sure this confidence is well deserved.

Board

I was honoured to become the Chairman of P&O in succession to Lord Sterling at the AGM in May 2005. Lord Sterling stepped down after some 25 years of distinguished service to P&O and the wider shipping and business community. The Group and its stakeholders owe much to his business flair and leadership over these years. Together with P&O's Managing Director, Sir Bruce MacPhail, the Group diversified from its long history in shipping, into a strong broad based business. It has increasingly been focused on its international ports and ferries divisions. This, together with the merger of cruises, provided the significant value creating opportunities for stockholders that we have quantified above.

Our previous senior non-executive director, Rodney Galpin, stood down at the same time as Lord Sterling. I should like to record the Board's gratitude to Rodney for his service over nine eventful years.

Michael Everard, a non-executive director, stepped down from the Board at the end of 2005. He had served for five years and we benefited greatly from his extensive knowledge of the shipping industry.

In the autumn of 2005 we took important steps to significantly strengthen the Board with the recruitment of four new non-executive directors: Baroness Symons of Vernham Dean, (a former Government Minister), Richard Cousins, (former Group CEO of BPB plc), Mike Turner, (Group CEO of BAE Systems plc) and Richard Gillingwater, (Chief Executive of the Government Shareholder Executive).

Following the completion of the takeover by DP World these new directors together with Sir John Collins (Senior non-executive director), Sir David Brown and David Williams all stepped down from the Board. I want to pay tribute to an outstanding group of director colleagues who supported me as Chairman and collectively gave wise counsel and guidance to our Executive Management led by our Chief Executive, Robert Woods. I am delighted that DP World has requested Robert to remain as Chief Executive of P&O, particularly during the next six months of critical integration planning and implementation.

I also want to record my deep appreciation of the work of Nick Luff (CFO) who together with Michael Gradon (Executive Director, Commercial and Legal Affairs & Chief Executive, London Gateway), Russ Peters (Chief Executive Officer, Ferries) and Peter Smith (Executive Director, Communications & Strategy) have contributed much to the success of P&O and to the completion of the DP World transaction. Together with Robert Woods, our management and employees around the world, they have contributed to build a sound platform from which our new owners can take the combined group forward.

With the completion of the takeover, DP World has appointed five new members to the Board: Jamal Majid Bin Thaniah, Mohammed Sharaf, H. Edward Bilkey, Yuvraj Narayan and Anil Wats. My colleagues and I extend to them a very warm welcome and we wish them and our new owners all possible success as the Company and its people enter a new era.

Leading in world trade

This year has seen us make significant headway against our strategic goals, through the disposal of our Container Shipping interests and Cold Logistics, the continued sell-down of our property portfolio and good improvements in our Ferries business. As a result, the Group has been able to continue its increased focus on the fast-expanding Ports business, winning a number of high profile new projects and enjoying healthy organic volume and profit growth.

ROYAL P&O NEDLLOYD SALE

JUNE

Our entire 25% shareholding in Royal P&O Nedlloyd was sold following the takeover offer by AP Moeller-Maersk. Total proceeds from the disposal were £381.0 million. A gain of £188.0 million was recorded.

APPROVAL FOR LONDON GATEWAY SCHEMES

JULY

The UK Government announced it was 'minded to approve' P&O's plans for a world class port and a major business park to be developed at London Gateway.

SALE OF US PROPERTY

JULY

P&O exited its property business in Boston, following the sale for £53.0 million of its last remaining properties there.

RECOMMENDED CASH ACQUISITION OF P&O BY DP WORLD

NOVEMBER

The Boards of P&O and DP World announced a recommended cash offer for all of P&O's issued and to be issued Deferred Stock. The acquisition completed on 8 March 2006.

P&O COLD LOGISTICS SALE

NOVEMBER

Our Cold Logistics business, one of the leading operations of its kind in the world, was sold to Canada's Versacold Holdings Corp for £183.0 million.

MAJOR NEW PORT PROJECT IN VIETNAM

DECEMBER

P&O signed a joint venture agreement to develop and operate a new container terminal in Ho Chi Minh City. The first berths are scheduled to open in 2008 and eventual capacity at the terminal will be 1.5 million teus.

Leading in world trade



In one year P&O...

Ports

Handled nearly **15 million** twenty foot equivalent container units (teus)

Loaded and unloaded more than **1 million boxes** of fruit in the US

Moved more than **1.6 million** new vehicles on and off ships heading for markets around the world

Dealt with almost **4.5 million** passengers

Ferries

Welcomed more than **9.8 million** passengers on board

Carried **1.8 million** freight units

Transported **1.7 million** tourist vehicles

Operating and financial review

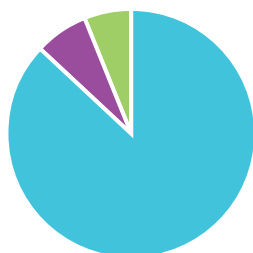
Robert Woods CBE
Chief Executive



2005 was a year of significant progress against our strategic goals. Ports now accounts for the great majority of our operating assets and operating profits, while our Ferries division has returned to profitability and continues to make further progress.

Strategic review

Operating profit from continuing operations before separately disclosable items
2005



■ Ports – 87%
■ Ferries – 7%
■ Property – 6%

In my review last year I commented on the sharpened investment strategy of the Group with a focus on reallocating capital to the businesses where P&O is a market leader. Significant progress continued to be made in 2005 and also in the implementation of the Fundamental Business Review of Ferries which was announced in September 2004. The key achievements for the year include:

- Property disposals were accelerated with net sales of £395 million compared to an initial target of £325 million
- We sold our 25% holding in Royal P&O Nedlloyd realising proceeds of £381.0 million
- The Cold Logistics business was sold for £183.0 million to Versacold Holdings Corp. of Canada
- Investment of approximately £170.0 million was made in the Ports business
- Net debt was reduced by £577.0 million
- An additional £100.0 million above normal contributions was paid into the main UK pension scheme
- The proposals of the Fundamental Business Review of Ferries have now been fully implemented and in 2005 the business was returned to profitability.

Ports

Ports now comprises over 70% of the net operating assets of the Group and contributes over 85% of continuing operating profit.

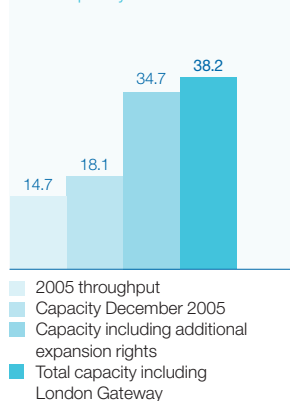
Ports is a highly attractive business because of our competitive strength in local markets and the high levels of international trade growth. This has been further supported by the increasing relocation of manufacturing into Asia and the resulting trade imbalances around the globe. We have approximately 50% of our Ports net operating asset base in Asia.

The particular strategic advantages we see in our Ports business are:

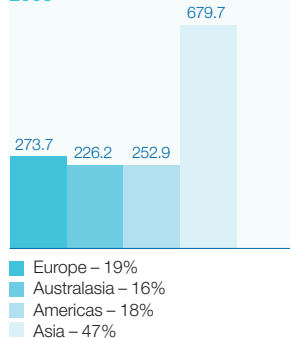
- Origin and destination cargoes – unlike trans-shipment ports, our focus on ports which service the regional or local economy means that there is less risk that cargo can be relocated to another port
- Common user terminals – we service a wide range of customers and do not have capacity dedicated to any particular customer
- Expansion opportunities – our current container terminal capacity is 18 million teus, but this can be ultimately expanded to approximately 38 million teus through adding equipment and exercising expansion rights that we hold at existing locations, including the 3.5 million teu capacity London Gateway project for which the government gave conditional approval in 2005.

New port investments take time to reach optimum utilisation and can dilute returns for the overall portfolio in the short term. However, our established operations, i.e. those which we have operated for more than five years, have reported a return on average capital employed of 19% in 2005.

Ports capacity teus m



Ports net operating assets £m 2005



Our port concessions are long term, typically 25 years or more. This, together with our considerable expansion opportunity and inherent strategic advantages, demonstrates why we believe the business is highly attractive.

Ferries

In September 2004 we announced far reaching proposals concerning how our Ferries business was run. These proposals have been implemented quickly with a number of changes being made at the start of 2005.

Freight – The freight market continues to grow and, consequently, greater focus is now placed on it. Customer links have been improved and tariff structures simplified. Despite capacity reductions in our overall fleet we have retained freight capacity at peak times through vessel rescheduling.

Tourist – Our tourist product on the important Short Sea sector is focused on 'short break' and 'long stay' customers where volumes have been stable rather than on 'day trip' traffic which has been in decline. We have introduced an affordable, hassle free tourist offer which is delivered in a simple, more focused and flexible way. This includes improvements to our website and booking processes together with an on-board product more closely tailored to our customers' requirements.

A number of structural changes have been implemented. Four routes have been closed and nine ships redelivered to their owners or sold, reducing the fleet to 23 ships. Flexible manning has been introduced on ships and is working well. Extensive employee consultation has been helpful in implementing these changes.

As a result of these strategic changes, we have reduced the cost base of the business by approximately 20% and are ahead of schedule for our profit improvement target of £50.0 million (on an International Financial Reporting Standards basis – £55.0 million under UK GAAP) to be delivered by 2006. We have also concluded agreements to enable us to continue to operate the *Pride of Rotterdam* on the North Sea route after the current charter expires in November 2006.

Property

We made good progress in selling down our property assets. At 31 December 2005 we held approximately £190.0 million of assets (excluding London Gateway), compared to approximately £510.0 million a year earlier. In early 2006 we largely exited our US property via the sale of our Denver portfolio which had a book value of £67.0 million. In the 2005 Interim Results announcement we indicated that, in future, our European team responsible for property investment, development and management would be known as P&O Estates. P&O Estates is responsible for the management of the London Gateway Park, and our other European property assets and will also pursue selected new projects where our development skills can be utilised.

Looking ahead

DP World completed the takeover of P&O on 8 March 2006. The combined group will operate 51 container terminals with a gross capacity of 50 million teus, with a presence in 30 countries across the Middle East, Asia, Europe, Australasia and the Americas. In addition, the combined group will benefit from the opportunity for expansion from projects such as Vietnam and London Gateway. DP World recognises the good progress made with the implementation of the restructuring programme within Ferries and looks forward to restoring the business to strong profitability in 2006. It also believes that there will be significant opportunities for employees and customers of both companies going forward.

Operating and financial review

Ports

Performance review

Container throughput increased by 6% to 14.7 million teus (equity adjusted)

Operating profit grew to £176.3 million in 2005 (2004 £164.0 million)

Approximately £170.0 million invested in developing existing operations

Expansion of capacity across the portfolio, but notably in Canada, India, Pakistan, China, Russia, France and the UK

Opening of new Antwerp Gateway project

Market review

Global container traffic is estimated to have grown 11% during 2005 to 115.4 million teus. China continued to return impressive growth in port handling at over 20% year on year, considerably in excess of the rest of Asia (total annual Asian growth is estimated at 12%). With respect to the main markets outside of Asia in which P&O operates, North America maintained its prior year annual growth rate of 9%, with South America recording an impressive 16% annual volume increase. In Australia growth was approximately 4%, compared to 9% in 2004, reflecting a slowing of GDP/domestic demand. In Western Europe, despite weak Eurozone GDP growth of 1.1%, the region's export led recovery resulted in a 9% growth in container volumes (source: Economist Intelligence Unit).

P&O Ports maintained its global market position as the fourth largest container terminal operator in the world, based on annual volume throughput.

Customers

Ports operates common user terminals with the objective of providing the same high level of service to all customers. Customers include all the major container shipping lines as well as break bulk, passenger and car carriers. We also provide logistics activities dealing directly with transport companies and the ultimate cargo owners such as manufacturers, traders and importers.

We aim to provide excellent value to our customers, with a commitment to delivering industry leading levels of service in all locations.

Financial review

Ports total operating profit was £176.3 million (2004 £164.0 million). Excluding separately disclosable items, which were significant in the prior year (£7.9 million), and the Maritime Services business, Ports underlying profit increased 14% to £169.3 million (2004 £149.1 million) with the strong growth reported in the first half continuing throughout much of the year. Profit growth significantly exceeded annual volume growth of 6% to 14.7 million teus. Net operating assets increased to £1,457.6 million (2004 £1,223.8 million) with approximately £170.0 million of capital investment in the year. Return on average capital employed at ports P&O has operated for more than five years remained high and increased to 19% (2004 18%).

Asia

Our Asian terminals increased underlying profit by 17% to £95.6 million (2004 £81.4 million), with organic volume growth of 13%.

Port operations

Asia – Total throughput teus		6,524,000
Location	Country	Shareholding
Manila	Philippines	84%
Laem Chabang	Thailand	35%
Qingdao	China	29%
Shekou, Shenzhen	China	22%
Surabaya	Indonesia	49%
Vostochny	Russia	25%
Chennai	India	75%
Mundra	India	100%
Mumbai	India	100%
Karachi	Pakistan	55%
Colombo	Sri Lanka	16%
Americas – Total throughput teus		2,375,000
Location	Country	Shareholding
New Jersey	USA	50%
New Orleans	USA	100%
Miami	USA	50%
Baltimore	USA	100%
Various locations	USA	
Buenos Aires	Argentina	53%
Vancouver	Canada	100%
Europe – Total throughput teus		3,782,000
Location	Country	Shareholding
Le Havre	France	37%
Marseille	France	20%
Antwerp	Belgium	100%
Antwerp Gateway	Belgium	43%
Southampton	UK	51%
Tilbury	UK	34%
Maputo	Mozambique	67%
Australasia – Total throughput teus		1,988,000
Location	Country	Shareholding
Sydney	Australia	90%
Melbourne	Australia	100%
Brisbane	Australia	100%
Fremantle	Australia	100%
Total teus		14,669,000

In China, strong profit growth was achieved, driven by 18% growth in volume. Growth was particularly strong at Qingdao, which in total handled 4.6 million teus for the year (P&O has a 29% interest in Qingdao). The operations at Shekou (Phase I and II) in the port of Shenzhen handled over 2.2 million teus in total for the year, but volume growth was restricted by capacity constraints (P&O has a 22% interest in Shekou). Discussions continue for expansion into the Phase III terminal which is currently operated by one of the joint venture partners. Shenzhen is now estimated to be the fourth largest port in the world, based on volumes handled.



Port development

July 2005 saw the official opening of the new Antwerp Gateway terminal in Belgium, where Ports holds a 40 year joint venture concession. The port currently has a capacity of 1.4 million teus. The development is expected to be completed in 2010, with six berths, a quay line of 2,450 metres, a draft of 17 metres and an annual handling capacity in excess 3.5 million teus. Antwerp Gateway has already become a regular stop on several main shipping line services connecting Northern Europe and the Far East.

6%

organic growth
in volume 2005

In India, Nhava Sheva (Mumbai) achieved volume growth despite being capacity constrained and, as previously reported, the reduction in regulated tariff led to operating profit being approximately £3.0 million lower than 2004. Growth in both volume and profit was achieved at the operations in Chennai and Mundra. In Pakistan, good volume growth continued throughout the year and this combined with a significant contribution from ancillary services, such as storage, resulted in a notable increase in profit at Port Qasim. However, ancillary levels returned to normal towards the end of the year.

Elsewhere, in the Philippines, increases in the regulated tariff resulted in good profit growth despite container volumes remaining static. In Indonesia, container volumes and profit were unchanged at Surabaya compared to the prior year. During the year we reached agreement with our joint venture partner at Vostochny, Russia to double the size of our operations to an estimated 0.8 to 1.0 million teus of capacity when fully equipped. P&O's additional investment was £9.0 million. We also announced a joint venture agreement to own 80% of the Saigon Premier Container Terminal which is likely to be granted a 43 year concession to operate a new container terminal in Ho Chi Minh City, Vietnam. Total capacity is estimated to reach 1.5 million teus at an indicative investment of US\$224 million (£130 million). The initial berths are scheduled to commence operations in 2008.

Americas

Our ports in the Americas improved underlying profit 26% to £24.5 million (2004 £19.4 million) with organic volume growth of 9%. The non-containerised business performed well for the year despite disruption by hurricanes Katrina and Rita. The operations at New Orleans, Lake Charles and Houston were temporarily affected, although Gulfport sustained longer-term damage. Damage and business interruption costs have been largely covered by insurance. The operations at Miami performed particularly well and benefited from high ancillary revenue. Port Newark (New York) moved into profitability for the year benefiting from customer gains, improved volumes and enhanced utilisation following reconstruction of the main part of the terminal during 2004.

In Argentina, the market was competitive, with volumes at the TRP operations under pressure in the first half but market share improving during the second half of the year. Consequently, overall volume growth of 11% was achieved but profits were slightly down year on year. The terminal in Vancouver achieved higher volumes and increased tariffs but redevelopment of the terminal and a truckers' strike in the second half of the year held back profit growth. Redevelopment of our Centerm terminal is anticipated to be completed by the end of May 2006 to double its size.

14%

Underlying profit grew to £169.3 million in 2005 (2004 £149.1 million)

Operating and financial review



Investment

Ports' Centerm terminal in Vancouver has been the recipient of a significant amount of capital expenditure over the past year, aimed at increasing throughput and efficiency at the port. Two new quay cranes were delivered in July and 16 new rubber tyre gantries (RTG) were delivered in December. The RTGs will come into use by the end of March 2006, once employees have been trained. This new equipment is in addition to 250 new reefer points (for powering refrigerated containers), for a total of 550 reefers now operating. The new equipment will be complemented by dredge works, due to be completed by the end of April 2006, which will take the draft to 15.5 metres along the entire 640 metre quay.

£170m

Approximately £170 million invested in developing existing operations.

Australasia

Despite annual container volume growth of just 4%, underlying profit increased 11% to £31.4 million (2004 £28.4 million), with improved contributions from the logistics and transport business and the non-container operations. The results from the container terminals were also ahead of the prior year. Container volumes benefited from strong Asian trade volumes at the start of the year, however this was offset by weakening consumer demand through much of 2005. Ancillary revenue was particularly strong at the container terminals at the end of the year. A letter of intent has been signed to extend the existing lease at the container terminal in Sydney to September 2024.

Europe

Underlying profit was £17.8 million (2004 £19.9 million) and container volumes were down 3%. Volumes at Southampton were down 5% year on year following the loss of a service to another terminal at the end of 2004. Consequently, profits were reduced but were also impacted by an increase in local authority rates by approximately £2.0 million p.a. and higher labour costs in order to support increases in capacity to 1.9 million teus. Volumes were also down at Antwerp following the planned relocation of a low yielding customer, however, this

improved the business 'mix' and meant that profits were significantly ahead of the prior year. The new Antwerp Gateway terminal opened in the third quarter of the year and customers have commenced calls. The other European terminals reported improved profit and volumes.

On 20 July we obtained the government's 'minded to approve' decision for the London Gateway Port and London Gateway Park schemes in the UK. Considerable work is under way to prepare for the development of the site and, as requested by Government, P&O submitted its response to the 'minded to approve' letter by the 20 October 2005 deadline.

Maritime services

Underlying profit was £7.4 million (2004 £7.0 million) reflecting a good performance from the specialised shipping contracts operated for the Australian Government and Royal Australian Navy.

Ferries

Performance review

Business returned to profitability

Proposals of Fundamental Business Review implemented – profit improvements of £50 million (on an IFRS basis) per annum, ahead of schedule

Disruption at Calais had a significant impact on the Short Sea business and is estimated to have impacted net revenue by £12–13 million

High fuel prices throughout the year increased costs by £16 million

Market review

P&O is one of the leading ferry operators in the UK.

The freight market continues to grow. In the important Short Sea market, the Port of Dover reported 3% growth in freight and this was despite reduced berthing capacity at Calais at the start of the year.

Structural changes in the tourist market, such as the growth in 'low-cost' airlines has led to an overall decline in tourist volumes in recent periods. This was largely due to a reduction in 'day trip' traffic which was also impacted by factors such as the sterling: euro exchange rate and changes in French duty on retail goods. On the Short Sea, the Port of Dover actually reported 1% market growth in car traffic to almost 2.6 million cars in 2005, albeit this was stimulated by 'low-cost' ferry operators lowering prices in the summer period. Port of Dover coach volumes fell 16% as traffic moved to Eurotunnel during the year. The significant reduction in the coach market led to overall passenger volumes declining 7% to 13.3 million passengers in the Short Sea market.

Customers

Ferries is committed to offering a timely, frequent and competitively priced freight service and an affordable, hassle free tourist experience delivered in a simple and flexible way. Safety, as always, remains paramount.

Ferries services the premium segment of the ferry tourist market but also satisfies 'low cost' customer needs via a lower cost product at off-peak periods on the Short Sea.

We believe that the results of the Fundamental Business Review are benefiting both freight and tourist customers. Customer links have been improved and tariff structures simplified. Despite capacity reductions in our overall fleet in 2005, we retained freight capacity at peak times via vessel rescheduling. Our tourist product is now focused on 'short break' and 'long stay' traffic. We have improved our website and booking processes plus refined our restaurant and retail outlets and services on-board.



On-board experience

As part of the Fundamental Business Review within Ferries, we carried out a major review of on-board shopping. During 2005, we invested extensively in our product ranges. Many of our shops have been completely redesigned to bring a brighter, fresher look, with more room to create the type of environment that customers will be used to seeing in the best airport and high street outlets. The range of goods sold on-board has also been updated to incorporate items such as designer sunglasses and the latest fragrances and skincare products, many of which are exclusive to P&O Ferries.

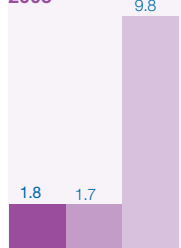
Operating and financial review

£50m

profit improvements ahead of schedule (IFRS basis)

Ferry carryings (millions)

2005



■ Freight units
■ Tourist vehicles
■ Passengers

Financial review

Ferries operating profit was £16.3 million (2004 £286.5 million loss). Excluding separately disclosable items, underlying profit was £14.7 million compared to a loss of £5.9 million in the prior year. The business has suffered from difficult market conditions in recent years but has now been returned to profitability, despite disruption at Calais and high fuel prices in 2005. This demonstrates the success of the Fundamental Business Review implemented during the year. The result includes the Ferrymasters business which reported an underlying profit of £2.2 million (2004 £1.9 million loss).

A number of changes to our product have now been completed. At the start of the year, greater focus was placed on the freight business. The tourist business was simplified, in line with customer needs, and is being managed to higher value/lower volume traffic. A number of structural changes were implemented. Four routes were closed and nine ships redelivered to their owners or sold. Flexible manning was introduced on ships at the start of the year and has worked well. Employee consultation has been successful in implementing these changes.

Trading for the year was significantly impacted by the disruption at Calais due to a lack of berthing capacity. This led to approximately 14% of sailings (approximately £12–13 million of net revenue) on the Dover-Calais route being lost in the first half. A claim has been lodged against the Calais Chamber of Commerce to recover the estimated net cost. Operations returned to normal for the peak summer period but there was some impact on bookings.

On a like for like basis, net revenue (turnover less direct variable costs) declined by £16 million compared to 2004. Total freight volumes were stable, with 4% volume growth on non-Short Sea routes offset by a 2% decline on the Short Sea. Average net freight rates were stable. Total tourist vehicle volumes were down 9% year on year, mainly attributable to a 14% volume decline on the Short Sea which was not offset by growth on other routes. Short Sea volumes were impacted by the Calais disruption and also reflected reduced capacity. Average net tourist vehicle rates were down 2% for the year reflecting a competitive market during the peak summer period. Passenger numbers decreased 13% but the net on-board spend per passenger improved, reflecting a change in mix towards the higher margins on non-Short Sea routes and also a good performance from food and beverage outlets. As a result, net revenue generated from on-board sales was down by 4%.

Our target for the Fundamental Business Review was to reduce the cost base of the business by approximately 20% and we are ahead of schedule. Excluding the impact of high fuel prices which cost approximately £16 million, cost savings and profit improvements of £48 million have already been delivered compared to the target of £50 million (on an IFRS basis) by the end of 2006. Consequently, despite a decline in net revenue, and including the Ferrymasters result, the Ferries business reported a total underlying profit of £14.7 million.

Property

Property

Property total operating profit was £12.0 million (2004 £nil). Excluding separately disclosable items, underlying profit was £12.7 million (2004 £54.0 million). In the half year results we reported that we had exceeded our full year target of £325 million of net sales and estimated that net sales would be close to £400 million for 2005. We ended the year with net sales of £395 million.

In the US, we exited all our property at Boston with the final sale achieved in July, resulting in proceeds of £53.0 million and a gain of £8.0 million against book value. Smaller sales also progressed in our business parks in Denver and Houston. At year end, the US net operating assets were US\$182.7 million (£106.4 million). In January 2006 we sold our Denver portfolio which had a book value of US\$120.0 million (£67.0 million)

and realised a gain of US\$15.0 million (£8.0 million). Consequently P&O has now largely exited its US property interests.

In the UK and Continental Europe, a number of sales were reported during 2005 including the sale of the Hanseatic Trade Center in Hamburg, Drake Circus shopping centre at Plymouth, the Regent Quarter development at Kings Cross and the Elizabeth House development at Waterloo. Consequently, at year end, excluding London Gateway Park, P&O has approximately £84.5 million of net operating assets in the UK and Continental Europe. P&O Estates will continue to manage these assets, together with London Gateway Park, and will pursue selected new projects.



Drake Circus

Drake Circus is a fully enclosed, 49,200 m² (530,000 ft²) two level shopping centre in the heart of Plymouth in the UK which is due for completion in October 2006. The centre is being built on the site of a former 1970s precinct scheme, most of which was owned by P&O initially. In excess of 70% of the 48 shops, including nine major stores, have been let to names such as Boots, Zara, Next and Primark. In addition, P&O Estates negotiated a key deal with M&S to extend and refurbish their store. The investment, with a likely end value in excess of £200.0m, has been pre-sold to Morgan Stanley Real Estate Fund with P&O Estates retaining the development and asset management roles.

Discontinued businesses

Cold logistics

P&O announced the sale of the Cold Logistics business to Versacold Holdings Corp. of Canada for £183.0 million on 2 November 2005. The sale completed and proceeds were received in mid-December. The proceeds comprised £140.2 million cash, C\$69.0 million (£33.0 million) of convertible debentures issued by Versacold Income Fund and the balance settled via the transfer of third party debt. Following transaction costs, stamp duty and working capital adjustments, P&O recorded a loss of £15.0 million on the sale.

P&O's share of the total operating profit to mid-December 2005 was £23.1 million (2004 £9.2 million). P&O's share of underlying profit, excluding separately disclosable items, was £21.0 million (2004 £18.4 million). The US business had a good year reflecting the full year benefit of rationalising some small, low yielding facilities, together with an ongoing focus on productivity. Good volume growth was achieved, particularly from retail customers. The business in Argentina traded consistently with the prior period, supported by a strong export market and high domestic volume.

In Australia, good retail volume growth was also achieved and operating profit ended the year ahead of 2004. The labour productivity issues and contract start up costs which impacted the first half were resolved in the second half of the year. The New Zealand business continued to produce stable results.

Container shipping

P&O sold its 25% interest in Royal P&O Nedlloyd to two financial institutions acting on behalf of A.P. Moeller-Maersk on 29 June. Total proceeds of £381.0 million (€56.25 per share) were received on 30 June 2005 and resulted in a gain of £188.0 million. P&O's share of the operating result of Royal P&O Nedlloyd up to its disposal and before separately disclosable items was a profit of £26.9 million (2004 full year £59.8 million).

Operating and financial review

Community

Social responsibility

P&O's approach to social responsibility is based on the simple principle that our activities should be conducted in a way which is economically, environmentally and socially sustainable. Since 2002, this principle has been enshrined within our policy on social responsibility and this policy and the values it establishes remain at the heart of all P&O's undertakings, whether providing services to the public, to our business customers or when evaluating and establishing new projects around the world.

In 2005, P&O established a new Social Responsibility and Policy Committee, overseen by the Chairman to review how and where P&O channelled its charitable contributions. The first output of the committee was a new Donations Policy which is now being implemented across the Group. The policy increases the emphasis on funding with a clear link to P&O's businesses whether through local communities, historical association or other cultural or commercial relationships. Projects which also allow for direct involvement from P&O are also favoured.

Workplace

P&O has long maintained an absolute commitment to achieving the highest standards of safety and environmental (S&E) management in every one of its operations. Our health and safety aspiration is to cause no harm to people and the environment. In pursuit of this objective, considerable resources are applied to improve our S&E performance across the globe. Our management teams are working to achieve S&E excellence with a worldwide workforce equivalent of over 35,000 employees (including contractors). This work involves meeting and dealing with the many challenges that operating in a dynamic, diverse and complex industry present.

Ports represents the largest and most rapidly growing of the P&O businesses, now operating in over 100 locations in 19 countries and as such it has been the focus of recent S&E initiatives. While Ports has been the focus for these S&E programmes, we have maintained the highest industry standards in Ferries and other operations.

In 2004 the Ports Senior Management Board endorsed a 'Safety & Environment Breakthrough Strategy' that committed the business to working towards world-class safety performance. The strategy has two key safety goals: achieving a fatality free year and reducing the Lost Time Injury Frequency Rate (LTIFR) by 20% year on year for each of the next five years. This strategy is being implemented on the basis of four key concepts – Leadership, The Fatal 5, Behaviour and Supervision, and Professional Support and Services.

Progress to date has been encouraging. The Ports 2005 LTIFR was 27% lower than it was in 2004, a result that exceeds the target set. This injury rate reduction is a positive sign that the strategy is beginning to take effect. Workplace fatalities however have not yet been eliminated from our businesses, highlighting that further work and effort is required. Fatality prevention will continue to be the key feature of safety initiatives and programmes.

During 2005, the Company also established a range of major new programmes at the P&O Institute. The Institute is not a traditional 'bricks and mortar' entity but a learning and development initiative that brings together people at different levels and locations to develop their knowledge and skills.



Building communities

Our terminal at Mundra is strategically positioned for container handling being the closest deep water port to Delhi, but its location in the industrial hinterland meant an acute shortage of suitable accommodation for the growing number of port employees and their families. The solution was for P&O to build a self-sufficient township. The project was completed in 2005 and now houses 300 employee residents rent-free. As well as fully equipped apartments, the township includes a library, restaurant, children's areas, leisure spaces, shops and a medical centre. A local school is just nearby. The development has its own on-site boreholes for water and waste water is treated and used for watering the extensive public gardens and sports fields.



Focus on safety

2005 saw the introduction of the Chairman's Safety and Environment Awards. The submissions demonstrated a widespread commitment across our businesses to reach ever higher standards in the areas of safety and environmental protection. Our port in Manila was singled out for its work over the past decade to establish a culture of safety in the terminal. Centerm, our terminal in Canada was rewarded for a programme to improve lashing and de-lashing practices, one of the most dangerous activities for stevedores. Finally, Larne Harbour was recognised for its introduction of an impressive Environmental Review System.

The Institute has been very well received by our employees who have been quick to acknowledge the value of the additional insights it brings to their day to day jobs and the benefits of sharing experiences with their peers from other operations within the Group.

Giving employees the opportunity to participate in the value we are creating has proved popular. Some 30% of eligible staff participated in our Global Sharesave Plan and will see a significant financial benefit from DP World's acquisition of P&O's deferred stock.

Environment

Environment

P&O established its first Group environmental policy in 1990, and since 1996 it has publicly reported every two years upon the key environmental aspects, impacts and performance of the operating companies that make up the Group. Quantified environmental improvement targets were first established in 1998, and these have proved to be a useful mechanism for initiating progressive change within the diverse range of P&O operating companies.

In 2004, the latest set of two year environmental and community targets were published for the period 2004/05. Final data is still being collated, but from an analysis of provisional figures it is possible to confirm that of the 37 targets established by Ferries, Ports, Maritime Services and Ferrymasters, 18 have been achieved in full, 12 achieved in part, two were deferred and five have not been achieved.

We are pleased to record that there were no major environmental incidents recorded in 2005.

A wide range of progressive new targets have been set for the next reporting period.

To complement this activity, Ports has recruited a Global Environment Manager who will, initially, focus particularly on two key environmental pilot projects that underpin our aim to 'Reduce, Reuse and

Recycle'. The first of these looks at improvements in efficient energy use, specifically in relation to diesel and electricity, energy resources we rely on heavily in our business. The second addresses the area of spills of oil, fuel and hazardous substances, investigating a range of systems to help prevent spills as well as to improve spill response and control.

Assurance

Each operating company is required to manage and internally verify the performance of their safety, environmental, and other social responsibility related management systems. Various key performance indicators are measured and reported by operating companies to Group on a monthly or annual basis. Many of these operating companies have also implemented externally certified management systems such as ISO14001 (environmental), ISO18001 (safety) or participated in wider benchmarking schemes such as the Business in the Community Corporate Responsibility index.

Over and above these processes, the P&O Group Safety & Environment Directorate undertook a series of independent safety and environmental audits on behalf of the Main Board during 2005. A total of 39 audits were made of both land based and marine activities, the selection of which was designed to ensure that attention remains focused upon key risk areas.

Operating and financial review

The Group achieved a good set of results in 2005 and strong cash flow significantly strengthened our financial position.

Group financial review

Earnings per share

Our core businesses performed well in 2005. Ports operating profit increased by 8% to £176.3 million and Ferries returned to profitability achieving an operating profit of £16.3 million (2004 £286.5 million loss). The contribution from property was much reduced following the strategic sell-down of the portfolio. Underlying earnings from continuing operations per £1 nominal of deferred stock were 12.3p (2004 10.2p). After separately disclosable items the basic earnings per £1 nominal of deferred stock were 37.4p (2004 22.6p loss).

Separately disclosable items included a profit on discontinued operations net of tax of £179.9 million which largely reflected the £188.0 million profit on the sale of our interest in Royal P&O Nedlloyd. This led to the significant increase in basic earnings as in the prior year, the separately disclosable items comprised significant reorganisation and impairment charges.

Cash flow and financial position

Net cash inflow from operating activities reduced to £408.8 million (2004 £483.9 million), due to a significant outflow from changes in working capital, provisions and a £100 million payment into the UK pension fund. Net investing activities was an inflow of £347.1 million (2004 £243.8 million) with capital expenditure in Ports offset by cash inflows of £381.0 million on the disposal of the Group's interest in Royal P&O Nedlloyd and £140.2 million on disposal of the Cold Logistics business. Consequently, after interest, dividend payments, exchange and other items, Group net debt reduced by £577.0 million to £604.6 million (2004 £1,181.6 million).

Total equity increased to £871.2 million (2004 £737.7 million), benefiting from the significant gain on disposal of Royal P&O Nedlloyd. The debt to capital ratio was 41.0% (2004 61.6%).

Acquisitions and disposals

A number of significant strategic disposals occurred during the year together with further investment in the Ports portfolio.

We exited our interest in container shipping via the sale of our 25% shareholding in Royal P&O Nedlloyd to two financial institutions acting on behalf of AP Moeller-Maersk. Settlement occurred on 30 June 2005 and realised proceeds of €571.0 million (£381.0 million).

The Group disposed of a number of development properties during the year with net sale proceeds totalling £395.0 million. This included the sale of our remaining property at the Hanseatic Trade Center in Germany, the sale of the Drake Circus, Regent Quarter and Elizabeth House developments in the UK and the sale of our Boston Wharf property in the US. Subsequent to year end we also sold our property portfolio in Denver and so have largely exited all our property interests in the US.

We sold our Cold Logistics business to Versacold Holdings Corp. of Canada for £183.0 million. Completion occurred on 19 December 2005 and we realised £140.2 million of cash proceeds, C\$69.0 million (£33.0 million) of convertible debentures in Versacold Income Fund with the balance of the proceeds settled via transfer of third party debt.

We entered into agreements to enable Ferries to continue to operate the *Pride of Rotterdam* after the current charter expires in November 2006. The agreements involve Ferries exercising an option to acquire the vessel for €111.0 million (£75.0 million) in November 2006. Detailed terms, subject to contract, have been agreed with a third party who will buy the ship and charter it back to Ferries for up to 10 years.

Approximately £170 million has been invested in the Ports division during the year. This included £40 million on the expansion of our container terminal in Canada which is being doubled in size to almost 800,000 teus, £24 million on further equipment and civil works at our growing port at Mundra, India plus approximately £40 million invested at the terminals at Chennai in India, Port Qasim in Pakistan and Southampton in the UK. We also invested £9 million to double the size of our port operations in Vostochny, Russia to a total gross capacity of 0.8 to 1.0 million teus. Significant investment was also made by our joint venture and associate interests including the new project at Antwerp Gateway as well as expansion at Shekou, China and also the terminals in France.

Tax charge

The underlying tax charge for 2005 was £40.0 million (2004 £33.9 million) excluding the impact of separately disclosable items. This represents an effective tax rate of 22% (2004 19%) on underlying pre-tax profit of the Group of £179.3 million (2004 £176.3 million).

Pensions

The two pension schemes of most relevance to the Group's financial position are the P&O UK Scheme and the New Section of the industry wide Merchant Navy Officers' Pension Fund ('MNOPF').

Previously, the UK scheme was a joint scheme for both P&O and Royal P&O Nedlloyd employees. During the year, the scheme was separated with 25% of the assets and liabilities being transferred into a Royal P&O Nedlloyd scheme. Royal P&O Nedlloyd also made a £70.0 million exit payment into the remaining P&O UK Scheme. In December the Group made a £100.0 million special contribution into the scheme and consequently at 31 December 2005 the scheme deficit had reduced to £117.4 million on an IAS 19 basis. DP World has reached an agreement in principle with the trustees of the P&O UK Scheme about its future operation and funding. A special contribution of £25.0 million (being £125.0 million less the £100.0 million special contribution paid by P&O in December) was paid into the UK scheme when the DP World takeover of P&O became effective in March 2006. Further deficit contributions of £75.0 million will be paid into the scheme over a five year period.

With respect to the MNOPF, a court case in March 2005 established which employers will be liable for deficit payments. Based on the judgement and confirmation as to the allocation basis adopted, P&O's share of the deficit is approximately 18% and P&O is exposed on a proportional basis to movements in the total assets and liabilities of the fund. Consequently, P&O is accounting for its share of the MNOPF as a defined benefit scheme with 18% of the net deficit included in the balance sheet. On this basis, at 31 December 2005 a net deficit of £129.8 million is included in the Group balance sheet.

International Financial Reporting Standards (IFRS)

These are the Group's first annual IFRS consolidated financial statements prepared in accordance with IFRS. Details of the transition to IFRS are included in note 36 to the financial statements.

Board of directors

Sir John Parker

63; Appointed Chairman 13 May 2005; Non-executive director and Deputy Chairman on 1 February 2005; Chairman of National Grid Transco plc; Senior non-executive director of the Bank of England; Non-executive director of Carnival Corporation and Carnival plc. Chairman of RMC Group 2001 to 2005; Chief Executive of Babcock International Group plc 1993 to 2000 and Chairman 1994 to 2000; Chairman and Chief Executive of Harland and Wolff Plc 1983 to 1993; Fellow of the Royal Academy of Engineering and Past President of the Royal Institution of Naval Architects.

Robert Woods, CBE

59; Appointed to the Board 18 January 1996; Chief Executive since 1 January 2004 and Executive Chairman of Ports since May 2002; Group Managing Director of Royal P&O Nedlloyd Container Line Ltd from 2000 to 2003; joined P&O in 1971; past President of the Chamber of Shipping; Non-executive director of John Swire & Sons.

H. Edward Bilkey

71; Appointed to the Board 8 March 2006; Chief Operating Officer DP World. Formerly Executive Director Dubai Ports Authority and Jebel Ali Free Zone; Vice President Maher Terminals, Port of New York; President Norton Lilly & Co.

Jamal Majid Bin Thaniah

47; Appointed to the Board 8 March 2006; Director of the Board of the Ports&Free Zone World FZW, Dubai; Chief Executive Officer Ports&Free Zone World FZW; formerly Chief Executive Officer Dubai Ports Authority from 2001; Executive Member of the Dubai E-Government Committee.

Michael Gradon

46; Appointed to the Board on 10 June 1998; Executive Director, Commercial and Legal Affairs, and Chief Executive, London Gateway; joined the Company in 1986 becoming Group Legal Director in 1994 and Company Secretary from 1996 to 2005.

Yuvraj Narayan

49; Appointed to the Board 8 March 2006; Senior Vice President, Corporate Strategy, DP World. Formerly, Director-Finance for Dubai Ports International and Chief Financial Officer Salalah Port Services Co. SAOG; Head of Corporate and Project Finance for South Asia, ANZ Group.

Mohammed Sharaf

44; Appointed to the Board 8 March 2006; Chief Executive Officer DP World; former Managing Director Dubai Ports Authority and Managing Director DPI Terminals after joining in 1992.

Anil Wats

48; Appointed to the Board 8 March 2006; Executive Vice President DP World; previously Senior Vice President and Managing Director, Asia Pacific and Australia. Formerly, Chief Executive Officer AP Moeller for Indonesia; Vice President and Chief Executive Officer for the Mediterranean and then for the Middle East and Subcontinent of Sea Land Service, Inc.

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Report of the directors

The directors present their report and accounts for the year ended 31 December 2005.

Principal group activities, review of operations and results

The operating and financial review on pages 6 to 17 describes the principal activities, operations, performance and financial position of the Group. The results of the Group are set out in detail on pages 38 to 41 and in the accompanying notes. The results of the Company are set out in detail on page 97 and in the accompanying notes. Further information is given in the Chairman's statement on pages 2 and 3. The principal subsidiaries, joint ventures and associates are listed on page 115.

Takeover by DP World

On 29 November 2005, the P&O Board recommended the cash acquisition of P&O by Thunder FZE (a wholly owned subsidiary of Ports, Customs and Free Zone Corporation, Dubai ("DP World")) by way of schemes of arrangement. Following the announcement of an offer by PSA Venture (UK) Limited (a wholly owned subsidiary of PSA International Pte Ltd ("PSA") of Singapore) (also recommended by the Board) on the morning of 26 January 2006, the Board recommended revised proposals from Thunder FZE on the evening of 26 January 2006. These proposals were approved by the stockholders at meetings held on 13 February 2006, and following approval of the schemes by the High Court the schemes became effective on 8 March 2006. The P&O stock was de-listed on 9 March 2006. Under the terms of the schemes, holders of Deferred Stock received, at their option, 520 pence per unit in cash or loan notes of equivalent value, and holders of Concessionary Stock received, at their option, either 120 pence per unit, or 100 pence per unit plus a Concessionary Unit providing continued rights to discounted ferry fares. Holders of Preferred Stock received £1 per unit of stock.

Principal changes in the Group

On 24 January 2005, the Group announced that the HTC Hanseatic Trade Center GmbH & Co. Grundbesitz partnership had sold the remaining four buildings of its office development in Hamburg for €200 million (£140 million) in cash to a consortium comprising affiliates of Lehman Brothers Real Estate Partners, L.P., Tishman Speyer Properties and Quantum Immobilien AG.

On 31 January 2005, the Group announced that it had realised £55 million in cash from its 600,000 sq ft shopping centre development in Plymouth through a sale to Morgan Stanley Real Estate Fund.

On 8 March 2005, the Group announced that it had sold one of the main blocks of the Regent Quarter development at King's Cross to LaSalle London Office Fund for £47 million.

On 29 June 2005, the Group announced that it had entered into an agreement to sell its entire 25 per cent shareholding in Royal P&O Nedlloyd N.V. to two financial institutions, which were acting on behalf of AP Moeller-Maersk, for total proceeds of £381 million (€56.25 per share) in cash before costs.

On 20 July 2005, the UK Government announced that it was 'minded to approve' P&O's proposals to develop a world class port and a logistics and business park at London Gateway in Thurrock, Essex.

On 27 July 2005, the Group announced that it had reached agreement with its joint venture partner to double the size of its port operations at Vostochny in Russia. Following the transaction, P&O holds 25 per cent of a new joint venture, RailFleet Holdings Limited. The cash consideration paid was £9 million (US\$16 million).

On 29 July 2005, the Group announced that Boston Wharf Company, a wholly owned subsidiary of P&O, had sold the remainder of its property portfolio in Boston for £53 million (US\$92 million) to W2005 BWH Realty L.L.C., an affiliate of Archon Group L.P. This was the last of the Group's property interests in Boston.

On 25 August 2005, the Group announced that it had agreed the sale of the second of the two main blocks of its Regent Quarter property development to LaSalle London Office Fund for £46 million.

On 2 November 2005, the Group announced that it had agreed to sell its Cold Logistics business to Versacold Holdings Corp. of Canada for £183 million. This transaction was completed on 19 December 2005.

On 11 November 2005, the Group announced that it had reached agreements that will enable it to continue to operate the *Pride of Rotterdam*. The vessel is currently owned by Norships II CV, a Dutch partnership, which has chartered the vessel to P&O Ferries since the ship first entered service in 2001. P&O Ferries has exercised its option under the charter to acquire the vessel from the Dutch partnership for €111 million (£75 million) at the end of the charter period in November 2006. The Group has agreed with a third party, who will buy the ship, to charter it back to P&O Ferries for up to ten years.

On 6 December 2005, the Group announced that it had signed a joint venture agreement with the Tan Thuan Industrial Promotion Company (IPC) to develop and operate a new container terminal in Ho Chi Minh City, Vietnam. The Group will own 80 per cent of the Saigon Premier Container Terminal, to which IPC (holding the remaining 20 per cent) will grant 43 year concession rights.

On 1 February 2006, the Group announced it had sold its entire property portfolio in Denver to Shea Homes Limited Partnership. The portfolio had a book value of approximately US\$120 million (£67 million) and as a result of the sale, the Group had largely exited its property interests in the US.

On 1 February 2006, the Group announced it had completed a transaction with Morgan Stanley Real Estate Fund realising £61 million in cash from a sell-down of its interest in the Elizabeth House development site at Waterloo in London.

On 15 March 2006, DP World announced that it intends to sell P&O Ports North America, which has operations in a number of US east coast ports. It is expected that a sale will be completed later in 2006.

Directors

A list of the current directors of the Company is given on page 18, including the dates of their appointment. Lord Sterling and Rodney Galpin retired from the Board on 13 May 2005, and Michael Everard retired from the Board on 31 December 2005. David Williams and Sir John Parker were appointed to the Board with effect from 1 January and 1 February 2005 respectively and were re-elected by the stockholders at the 2005 annual general meeting. Baroness Symons and Mike Turner were appointed to the Board with effect from 1 December 2005, Richard Cousins was appointed to the Board with effect from 7 December 2005 and Richard Gillingwater was appointed to the Board with effect from 1 January 2006. The non-executive directors, Sir David Brown, Sir John Collins, David Williams, Baroness Symons, Mike Turner, Richard Cousins and Richard Gillingwater all resigned from the Board on 8 March 2006 (the effective date of the takeover by DP World) and Jamal Majid Bin Thaniah, Mohammed Sharaf, H. Edward Bilkey, Yuvraj Narayan and Anil Wats were appointed to the Board on that date. Nick Luff, Russ Peters and Peter Smith all stepped down from the Board on 30 April 2006.

Details of the directors' remuneration and their interests in the shares of the Company are set out in the directors' remuneration report on pages 28 to 35.

Dividends

The directors recommend a final dividend in respect of the year ended 31 December 2005 of 6.0p per £1 nominal of deferred stock. This would bring the total cash dividend for the year to 9.0p per £1 nominal of deferred stock.

Employees

The Company is committed to keeping employees throughout the Group informed of performance, development and progress through its established system of briefings by management, the Group's bi-monthly newspaper, Wavelength, and widely distributed news and information bulletins. There is a European Works Council, known as the P&O European Forum, the purpose of which is to inform and consult with employee representatives on transnational issues. Members are elected in the UK and Ireland and either elected or appointed, in accordance with national laws, in other countries. The P&O European Forum meets twice a year.

DP World is strongly committed to employee communication. There are no plans for any changes to the present arrangements although over time they will continue to develop.

The Company's aim is to meet the objectives of the code of good practice on the employment of disabled people. Full and fair consideration is given to disabled applicants for employment and training, and career development is encouraged on the basis of aptitude and abilities. It remains Company policy to retain employees who become disabled whilst in its service and to provide specialised training where appropriate.

Employees are able to share in the Group's results through performance related bonus schemes which are widely applied in the Group.

During the year employees were able to participate in a number of share related plans. All awards under these plans became exercisable upon acquisition of the Group by DP World.

The P&O 2004 UK Sharesave plan (the "2004 Plan") was approved by stockholders on 14 May 2004 and was to expire on 14 May 2014. Under this plan, which was a UK Inland Revenue approved plan, eligible employees were invited to apply for options during the six weeks after announcement of the interim or final results or at such other times as the directors considered were warranted by special circumstances. The option granted to each individual was related to the monthly sum the individual agreed to save under a contract, not exceeding £250 per month for a period of three or five years, with a financial institution nominated by the directors. Options were granted with an exercise price which is discounted by up to 20 per cent by reference to the market value of the deferred stock at the time the options were offered to eligible employees. Options were normally exercisable within six months following the end of the related savings contract, but earlier exercise was permitted in certain circumstances, for example, if an individual left employment for specific "good leaver" reasons or if there was a change in control of the Company.

In view of the global nature of the P&O Group and the benefits of encouraging wide employee share ownership, the Company operated plans, based on the 2004 Plan, for the benefit of overseas employees. All such plans operated within the individual and plan limits applicable to the 2004 Plan. The overseas plans were also due to expire on 14 May 2014.

The P&O 2000 Executive Stock Option Plan (the "P&O Option Plan") was approved by stockholders on 20 October 2000. Under the P&O Option Plan, options could be granted twice a year, during the six weeks after the release of the interim or final results. The life of options was ten years and the price at which options could be granted was governed by the market price of deferred stock at the time of grant. There were restrictions on the total number of options that could be granted in normal circumstances to any one executive and the scheme also contained limits on the total amount of stock over which options could be granted.

The rules of the P&O Option Plan reflected current institutional investor guidelines by requiring that options granted under the plan could normally be exercised only if a performance target had been met. Options granted under this scheme would not normally be exercisable unless the growth in P&O's headline earnings per £1 nominal of deferred stock ("Headline EPS") over a period of at least three years from grant exceeded the percentage increase in the UK Index of Retail Prices by an average of at least three per cent per annum. The rules permitted the adoption of a different basis if at the time of a grant of options it was thought appropriate to do so, provided that the replacement conditions were no less demanding. The Company reported negative Headline EPS for 2002 and accordingly application of the formula for Headline EPS growth would have resulted in a less stretching hurdle. Therefore, the remuneration committee resolved that options granted during 2003 would not normally be exercisable unless the growth in P&O's profit before tax and separately disclosable items profit per £1 nominal of deferred stock over a period of at least three years from grant exceeded the percentage increase in the UK Index of Retail Prices by an average of at least three per cent per annum. In 2004 the remuneration committee decided to revert to the earlier, Headline EPS, performance target.

On 14 May 2004 the stockholders approved an amendment to the rules of the P&O Option Plan to enable the Company to satisfy the exercise of both existing and future options by the issue of only that amount of stock which had a value, at the time of exercise, equal to the net gain resulting

from the exercise, that is, the difference between the market price on the day of exercise of the amount of stock under the option and the total exercise price payable.

Pursuant to the Board remuneration structures set out in the directors' remuneration report on pages 28 to 35, no further grants of options were made under the P&O Option Plan in 2005.

Corporate responsibility, safety and the environment

There are Group policies for health, safety, welfare, the environment and social responsibility, which are communicated to all staff. More information on these policies is given on pages 14 and 15. Each operating company is required to produce its own policies and management systems to reflect Group policies and best industry practice in its sector of business. The Company also encourages the adoption of similar policies by its significant joint ventures and associates.

Monitoring of compliance with Group policies is maintained by periodic assessment under the direction of the Head of Group Safety and Environment. Reports are reviewed by Peter Smith, the Board director responsible for safety, environmental and social responsibility issues. In addition, a monthly report on these matters is submitted to the Board.

Ultimate holding company

The Company's immediate controlling party is Thunder FZE, a wholly owned subsidiary of Ports, Customs and Free Zone Corporation, Dubai ("DP World"). No other group financial statements include the results of the Group.

Going concern

The directors, having made enquiries, consider that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future and therefore they consider it appropriate to adopt the going concern basis in preparing the accounts. The parent company has undertaken to provide the Company and the Group with sufficient funds as are necessary for it to meet its liabilities as they fall due, for at least the next 12 months.

Creditor payment policy

The Company's policy is to pay suppliers in accordance with terms and conditions agreed when the orders are placed. Although the Company does not follow any code or standard on payment policy, where payment terms have not been specifically agreed invoices dated in one calendar month are paid close to the end of the following month. These policies are understood by the purchasing and finance departments. The Company has procedures for dealing promptly with complaints and disputes. The Company had 30 days (2004 27 days) purchases outstanding at 31 December 2005.

Donations

During the year ended 31 December 2005 the Group contributed £158,000 (2004 £141,000) for UK charitable purposes. Further significant charitable donations were made in 2005 and in previous years to overseas causes. As mentioned in the 2004 annual report, an additional £200,000 was given, via the Company's ports in South Asia, to support relief operations following the tsunami disaster on 26 December 2004. The Group made no contributions to political parties during the year (2004 £nil).

Indemnity

All directors are entitled to contractual indemnification from the Company to the extent permitted by law against claims and legal expenses incurred in the course of their duties.

Auditors

Following DP World's acquisition of the Company the directors have decided to appoint Ernst & Young LLP as independent auditors of the Company. Accordingly KPMG Audit Plc have indicated that they will resign as auditors of the Company. The appointment of Ernst & Young LLP as independent auditors of the Company is to be proposed at the forthcoming annual general meeting.

By order of the Board

D J Leonard

Secretary

1 June 2006

Corporate governance

The revised Combined Code on corporate governance ("the Combined Code"), which implements the recommendations made in the "Higgs Review of the role and effectiveness of non-executive directors" and Sir Robert Smith's guidance for audit committees, came into effect for the Company for the financial year commencing 1 January 2004. During 2005 the Company complied in all material respects with the Combined Code apart from the balance between the non-executive and executive directors: during the period from 13 May to 1 December, non-executive directors constituted less than half of the Board, excluding the Chairman. However, in light of the high calibre and wide experience of the non-executive directors, this was not considered a significant departure from the principles of the Combined Code. With the appointment of four new non-executive directors in December 2005 and January 2006, non-executive directors once again constituted at least half of the Board, excluding the Chairman. Since the resignation of seven non-executive directors and the appointment of five executive directors on 8 March 2006, non-executive directors have no longer constituted half of the Board.

The following is an explanation of the Company's corporate governance policies in the light of the Combined Code.

Directors

The full Board meets at least nine times each year. Although there is a prescribed pattern of presentation to the Board, including matters specifically reserved for the Board's decision (which include strategy; the annual budget; major transactions; key appointments and divisional structure; personnel, health, safety and environmental policies; insurance and risk management; and internal controls), all Board meetings tend to have further subjects for discussion and decision taking. Board papers, including an agenda, are sent out in advance of the meetings. Board meetings are discursive in style and directors are encouraged to offer their opinions.

The Board has delegated the following responsibilities to the management: the development and recommendation of strategic plans for consideration by the Board that reflect the longer term objectives and priorities established by the Board; implementation of the strategies and policies of the Group as determined by the Board; monitoring of the operating and financial results against plans and budgets; monitoring the quality of the investment process against objectives, prioritising the allocation of capital, technical and human resources; and developing and implementing risk management systems subject to the continuing oversight of the Board and the audit committee as set out below.

A list of the directors of the Company is given on page 18. Prior to the DP World takeover there was a Chairman, a Chief Executive and a senior non-executive director. The non-executive directors were independent of management and had no relationship which could materially interfere with the exercise of their independent judgement. Sir John Collins is a director of N M Rothschild & Sons ("NMR") which provided financial advice to the Company, but since Sir John's role is solely as a non-executive director of NMR on a fixed remuneration with no relationship to the income or profits of NMR, the Board regarded him as independent. Sir John Parker is a non-executive director of Carnival plc which benefits from a trade mark licence in respect of the P&O name and flag. The company receives no fee for this licence. The Company has various other business relationships with Carnival plc, but these are considered to be immaterial both individually and in aggregate. Given the limited nature of the contractual relationships between P&O and Carnival plc and Sir John's role solely as a non-executive director of Carnival plc, the Board regarded him as independent at the time of his appointment.

During the year the Board carried out a formal evaluation of its performance and that of its committees and individual directors, at the same time reviewing progress against the 2004 evaluation. The procedure adopted was for each director to complete a detailed questionnaire, on a non-attributable basis, on his perception of the composition, operation and effectiveness of the Board (and any of its committees on which he served), and on the performance of the Chairman and each of his fellow directors. A final report, setting out the findings and suggesting avenues for further work, was then presented to the Board towards the end of the year.

During the year the Board began a programme of visits to P&O's operating sites, which was consistent with the policy (mentioned in the 2004 report) of addressing certain operational issues at Group, rather than divisional, level.

All directors have access to the Company Secretary and independent professional advice at the Company's expense if necessary.

The following table sets out the number of meetings of the Board, and of the principal committees of the Board, during 2005 together with details of attendance.

	Board	Audit	Remuneration	Nomination
Number of meetings	11	4	5	3
Attendance:				
Sir John Parker (appointed 1 February 2005)	10	n/a	n/a	3
Lord Sterling (retired 13 May 2005)	3	n/a	n/a	n/a
Robert Woods	11	n/a	n/a	3
Sir David Brown	11	4	5	3
Sir John Collins	10	4	5	3
Michael Everard (retired 31 December 2005)	10	2	4	2
Rodney Galpin (retired 13 May 2005)	3	2	3	n/a
Michael Gradon	11	n/a	n/a	n/a
Nick Luff	11	n/a	n/a	n/a
Russ Peters	11	n/a	n/a	n/a
Peter Smith	11	n/a	n/a	n/a
David Williams (appointed 1 January 2005)	8	4	3	n/a
The Rt Hon the Baroness Symons of Vernham Dean (appointed 1 December 2005)	1	n/a	n/a	n/a
Mike Turner (appointed 1 December 2005)	1	n/a	n/a	n/a
Richard Cousins (appointed 7 December 2005)	n/a	n/a	n/a	n/a

Directors' remuneration

The directors' remuneration report is set out on pages 28 to 35.

Accountability and audit

The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. The internal control system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss.

The system of internal control described below has been in place throughout the year and until the effective date of the takeover.

Until the takeover, the Board delegated certain powers and duties to Board committees, all of which operated within defined terms of reference.

Audit committee

The audit committee was made up entirely of independent non-executive directors. Until 13 May 2005 the audit committee was chaired by Rodney Galpin whom the Board considered to have the appropriate financial experience to fulfil this role. David Williams succeeded Rodney Galpin as Chairman of the committee on 13 May 2005. David Williams was until 31 January 2006 Finance Director of Bunzl plc. The other members of the committee were Sir John Collins, Sir David Brown and Michael Everard. The Chief Executive, Chief Financial Officer, external auditors and internal auditors were invited to attend audit committee meetings, along with any other director or member of staff considered necessary by the committee to complete its work. The committee met with external auditors and internal auditors without executive directors or members of staff present, as it considered appropriate (and at least once a year).

The committee met at least three times each year.

The committee's remit included the following:

- to review the form and content of the financial statements to be presented to stockholders of the Company at the half year and at the year end, and, if necessary, to challenge the actions and judgements of management in relation to them;
- to keep under review the scope and results of the external audit and the independence, effectiveness, resources and objectivity of the auditors;
- to review the effectiveness of the system of risk management and at least annually to carry out a review of the effectiveness of the system of internal controls and the process of risk management;
- to review management and internal audit reports on the effectiveness of the system of internal financial control, including the year end financial reporting process and the Company's procedures for investigating concerns raised by members of staff, and to report its findings to the Board. A whistle-blowing policy was in place throughout the year;
- to monitor the integrity of the Company's financial controls; and
- to receive reports from the internal audit department and to monitor the quality of the department's work, ensuring that it was adequately resourced.

Independence of external auditors

The audit committee was responsible for recommending a firm of auditors of appropriate independence and experience and for the approval of all audit fees and terms of engagement. The committee's policy was to undertake a formal assessment of the auditors' independence each year which included:

- a review of non-audit services provided to the Group and related fees;
- discussion with the auditors of a written report detailing any relationships with the Company and any other parties that could affect independence or the perception of independence;
- a review of the auditors' own procedures for ensuring the independence of the audit firm and partners and staff involved in the audit, including the regular rotation of the audit partner; and
- obtaining written confirmation from the auditors that, in their professional judgement, they were independent.

The audit committee implemented procedures relating to the provision of non-audit services by the Company's auditors. These included:

- the maintenance of a schedule of certain non-audit services, including consultancy, investment banking and legal services, which the Company is specifically prohibited from obtaining from the audit firm;
- requiring the selection of providers of permitted non-audit services to be subject to a tender process, where appropriate; and
- requiring non-audit work and the fees involved to be approved in advance by the audit committee.

An analysis of the fees payable to the external audit firm in respect of both audit and non-audit services during the year is set out in note 3 to the accounts.

Risk management process

The Group risk management process, on which the review of effectiveness of the system of internal control and risk management is based, has the following key features:

- Through a series of interviews, management discussions and risk assessment workshops, all major businesses within the Group determine the most significant risks to the achievement of their business objectives. Appropriate risk management activity is then determined and any required action plans are implemented. This is a continual process, and may be associated with a variety of financial, operational and compliance matters including organisation structures, business strategies, disruption in information technology systems, competition, natural catastrophe and regulatory requirements.
- The risks and associated controls are summarised in risk portfolios and are presented to the Board for review.
- At each year end, divisional management certify that the risk management process is in place and an assessment has been conducted throughout their businesses and that appropriate internal control procedures are in place or in hand to manage the risks identified. These self-certifications were made available to the audit committee.
- The self certification statements referred to above include a section where divisional management state that they are not aware of any irregularities involving actual or suspected fraud or breach of regulation, legislation or contract that may cause significant loss to the Company.

Internal control

The Board has complied with the guidance of the Turnbull committee by establishing a strong control framework within which the Group operates and the audit committee undertook a review of the effectiveness of internal controls and process of risk management in accordance with its remit. The principal features and key high level control procedures include:

- An organisation structure which supports clear lines of communication and accountability and delegation of authority rules which specify responsibility.
- Business strategies are prepared at divisional level and are approved by the Board. In addition, there are annual budgeting and strategic planning processes. Financial forecasts are prepared every quarter. Actual performance is compared to budget, latest forecast and prior year on a monthly basis. Significant variances are investigated and explained through normal monthly reporting channels.
- Key performance indicators are produced to summarise and monitor business activity.
- Evaluation and approval procedures for major capital expenditure and significant treasury transactions.
- Regular reviews of the effectiveness of the Group's health, safety, welfare and environment processes.
- The internal audit department provides additional assurance to the Board, and previously to the audit committee, that key controls are operating as intended. During 2005, the resources available to undertake internal audit fieldwork were increased.

The risk management process and the system of internal control are subject to continuous improvement.

Nomination committee

The nomination committee kept under review the structure, size and composition of the Board, giving consideration to succession planning. During 2005 the committee, with assistance from external search consultants, devised a candidate specification for additional non-executive directors. A full external search was then conducted which led to the appointment of Baroness Symons, Mike Turner, Richard Cousins and Richard Gillingwater as non-executive directors. They were selected for their strong records and experience, which complemented the range of expertise already represented on the Board.

Remuneration committee

The remuneration committee determined and agreed with the Board the framework and broad policy for the remuneration of the Company's Chairman, Chief Executive, executive directors and other members of the executive management in the tier immediately below Board level. The remuneration of non-executive directors was a matter for the executive members of the Board. No director or executive was involved in any decisions as to their own remuneration. The remuneration committee:

- approved the design of, and determined the targets for, any performance-related pay schemes operated by the Company for the executive directors and other relevant executive management and approved the total annual payments made under such schemes;
- reviewed the design of all share incentive plans for approval by the Board and stockholders and for any such plans determined each year whether awards would be made and, if so, the overall amount of such awards, the individual awards to executive directors and other senior executives and the performance targets to be used;
- determined the policy for, and scope of, pension arrangements for each executive director;
- determined, within the terms of the agreed policy and in consultation with the Chairman and/or Chief Executive as appropriate, the total individual remuneration package of each executive director and other relevant senior executives;
- ensured that contractual terms on termination, and any payments made, were fair to the individual and the Company;
- reviewed and noted annually the remuneration trends across the P&O Group; and
- was responsible for appointing external remuneration consultants who advised the committee by providing reliable up to date information about remuneration in other companies.

Directors' remuneration report

This report complies with the Directors' Remuneration Report Regulations 2002 (the "Regulations"), and has been approved by the directors.

Remuneration committee

The remuneration committee consisted entirely of independent non-executive directors and was chaired by Sir John Collins. The other members of the committee during 2005 were Rodney Galpin (until 13 May 2005), Michael Everard, Sir David Brown and David Williams. It should be noted that as at the date of this report the remuneration committee no longer exists as a result of the takeover by DP World. The consultants Deloitte were appointed by the committee to conduct a base salary benchmarking analysis in respect of the executive directors. During 2005, other parts of the Deloitte group carried out certain work for subsidiaries and associates of the Company including provision of tax calculation software, but in view of the limited scope and scale of this other work this is not considered to affect their independence. In addition, the committee consulted with the Chairman and Chief Executive as appropriate with regard to its proposals relating to the remuneration of the executive directors.

Policy

The policy of the committee was to review executive directors' remuneration based on an independent assessment of market practice. The total remuneration package of the executive directors was structured to attract, retain and motivate executive directors. The committee, in consultation with its advisers, conducted an annual review of executive directors' remuneration, including bonuses and long term incentives, to ensure consistency with market practice, local conditions and business objectives. The major proportion of the remuneration package for executive directors was performance-related assuming maximum performance in respect of the performance-related elements. This included participation in the Company's long term incentive plans, which consisted of the P&O Performance Share Plan (the "Performance Share Plan") and the P&O 2005 Matching Share Plan (the "2005 Matching Share Plan"), which are described in more detail below. The Company also operated a Deferred Bonus and Co-Investment Matching Plan (the "Matching Plan") and an Executive Stock Option Plan (the "P&O Option Plan"), although no general grants were made under the P&O Option Plan in 2005. Awards and options made in previous years under the Matching Plan and the P&O Option Plan remained outstanding during 2005. The performance conditions and policies relating to long term incentives and directors' remuneration packages were approved by stockholders in October 2000 (and May 2005 in the case of the Performance Share Plan and the 2005 Matching Share Plan) and have not been materially altered since. The total remuneration package was designed to align the interests of executive directors with those of stockholders. In 2004 the rules of the P&O Option Plan were amended, with stockholder approval, so as to allow the exercise of options to be satisfied by issuing or transferring a smaller amount of stock than that over which the option was originally granted. The Company had a Directors' Shareholding Guideline as described on page 34.

Following the takeover by DP World, the Company no longer has listed shares. As a consequence existing awards under the share plans described above have crystallised and no further grants or awards will be made under these plans. It is expected that alternative long term incentive arrangements will be implemented although not linked to listed shares.

Components of remuneration

The remuneration package of executive directors comprises base salary, an annual performance bonus scheme, long term incentive plans, pension arrangements and certain benefits in kind (for example health cover, car benefits and accommodation where relevant to their role). In some cases directors take their pension and other benefits in the form of a cash equivalent payment. In addition executive directors are entitled to participate in any all-employee share scheme of the Company.

Base salary

Base salaries of executive directors are reviewed annually and are set at levels which reflect the level of responsibility of the executive directors concerned and ensure that they are competitive with pay for executive directors holding equivalent positions in comparable companies. The benchmark levels represent remuneration data across industries and reflect factors including company size, reporting level and international accountability.

Annual performance bonus

Executive directors participate in a non-pensionable bonus scheme which is linked to the achievement of demanding business and corporate objectives including profitability and other key performance indicators.

Bonus targets for 2005 were based on headline profit and other financial targets for the Group and the main operating divisions, and the requirement to achieve key strategic objectives. The Group elements of the 2005 targets (financial and strategic) were achieved in a range of 80 to 100 per cent of maximum.

All incentive targets were set by the committee and were designed to be demanding. Financial targets were normally set above those for the prior year, but having regard to the anticipated trading environment.

The maximum annual bonus that can be earned is generally 75 per cent of salary. The committee had over-riding discretion in determining the payment of bonuses.

Long term incentives

As stated above, during the year the Company's long term incentive plans comprised the Performance Share Plan, 2005 Matching Share Plan, the Matching Plan and the P&O Option Plan.

A summary of the rules of each of these plans is given below: however, upon the change of control of the Company in March 2006 awards under these plans vested according to the provisions of the relevant plan rules.

The Performance Share Plan

Under the Performance Share Plan, executive directors and a limited number of other senior employees who had significant influence over the Group's ability to meet its strategic objectives were eligible to receive annual awards, in the form of deferred stock, worth up to 120 per cent of salary for directors and a lesser amount for executives below Board level. In order to provide flexibility, the scheme rules allowed annual awards of up to a maximum of 200 per cent of salary.

Awards would vest after three years subject to the Company's TSR performance against the constituents of the FTSE 350 (excluding investment trusts) at the date of award. 25 per cent of the award would vest if the Company was ranked at the median. The full award would vest if the Company was ranked at, or above, the upper quartile. Between these two points, the award would vest on a straight line basis. No portion of the award would vest if the Company was ranked below the median, and any unvested award at the end of the three year period would automatically lapse.

Awards would only vest subject to the remuneration committee determining that the TSR performance was a genuine reflection of the Company's underlying financial performance over the three year period.

Awards made to executives with responsibility solely for a specific business unit were made to vest subject to the performance of their business unit, as opposed to relative TSR. However, executive directors with such business unit responsibility had at least one third of the award subject to the TSR performance condition. Awards made to executive directors with Group-wide responsibility were subject solely to the TSR performance condition.

Awards could be satisfied by the use of stock purchased in the market or newly issued stock and to the extent that new issue stock was used this was subject to the normal dilution limits (i.e. options/awards over stock in the Company did not exceed 5 per cent of the Company's issued deferred stock in any rolling 10 year period in respect of executive schemes, or 10 per cent in any 10 year period in respect of all schemes).

Upon the change of control, awards vested based on the Company's performance to date and the time elapsed in the three year performance period. However, the remuneration committee exercised its discretion to allow full vesting in respect of all awards that had not been subject to a business unit performance condition, based on the Company's financial performance to the date of change of control.

The 2005 Matching Share Plan

Executive directors were able to invest their own cash resources up to a limit of 50 per cent of their maximum bonus opportunity into stock in the Company ("Invested Stock"). Participants who made such investment received a performance based matching award equal in value to the Invested Stock (valuing the Invested Stock on a pre-tax basis).

The first 2005 Matching Share Plan awards were made in 2005 and were designed to vest after three years, subject in normal circumstances to the participant continuing to hold the Invested Stock for the three year period and would vest based on the same TSR performance conditions as under the Performance Share Plan.

Upon the change of control, awards vested based on the Company's performance to date and the time elapsed in the three year performance period. However, the remuneration committee exercised its discretion to allow full vesting of all awards, based on the Company's financial performance to the date of change of control.

The Matching Plan

The Matching Plan provided participants with the opportunity to receive matching awards of deferred stock depending upon the performance of the Company over a two year retention period following the year in which an original bonus-related award was earned.

One third of any annual bonus awarded to directors and other executives who were participants in the Matching Plan was in the form of a Stock Award which was automatically invested in the Matching Plan. The Board believed that, in order to further align participants' interests with those of stockholders, participants should be invited to commit their own resources to the Matching Plan. Therefore participants also had a choice of investing their own funds in further deferred stock in the Company (described as Invested Stock) subject to an overall limit for directors on the amount invested in the Matching Plan in any one year of 75 per cent of base salary. Subject to the discretion of the Matching Plan Trustee, Matching Plan participants received Matching Awards. Matching Awards entitled the participants to acquire a maximum amount of deferred stock which, at the date of grant, had a value equal to the aggregate value of the executive's Stock Award and Invested Stock (valuing Invested Stock on a gross of tax basis).

The amount of deferred stock over which a Matching Award might be exercised was dependent on the Company's total shareholder return ("TSR") over the retention period compared to that of the other companies in the FTSE 350 index. TSR was used as a performance measure because it was considered to be effective in aligning the interests of executives and stockholders. If the Company achieved median performance a participant was entitled to exercise 25 per cent of his Matching Award and if the Company achieves upper quartile performance, a participant was entitled to exercise 100 per cent of his Matching Award. For performance between median and upper quartile, entitlement was calculated on a straight line basis. These targets were subject to review by the committee.

Matching Awards were only exercisable if a secondary validating performance condition was also met. This required earnings per share ("EPS") growth (after appropriate adjustments to ensure consistency throughout the period) over the retention period to exceed the growth in the UK Index of Retail Prices by an average of at least 3 per cent per annum. The rules of the Matching Plan permitted the adoption of a different performance condition if at the time of a grant of awards under the Matching Plan it was thought appropriate to do so, provided that the replacement conditions were no less demanding. For 2002 and 2004, the Company reported a negative EPS and accordingly application of the formula for EPS growth would result in a less stretching hurdle. Therefore, the remuneration committee resolved that the secondary validating performance condition for the 2003 awards (in respect of 2002) and 2005 awards (in respect of 2004) under the Matching Plan would be that the growth in P&O's profit before

tax and separately disclosable items per £1 nominal of deferred stock over the retention period must exceed the growth in the UK Index of Retail Prices by an average of at least 3 per cent per annum.

The TSR and EPS performance conditions were chosen since they were considered the most appropriate for determining the Company's performance. They were established after consultation with the Association of British Insurers and the Company's largest stockholders.

Upon the change of control, all awards vested in full in accordance with the rules of the plan.

Other share related benefits

In 2005 no general grant of stock options was made to the executive directors or senior executives under the P&O Option Plan. Options under this plan were generally exercisable three years after the date of grant subject to the achievement of performance conditions and remained exercisable until the tenth anniversary of grant. Performance conditions were generally based on the achievement of EPS growth (after appropriate adjustments to ensure consistency throughout the period) of an average of at least 3 per cent per annum in excess of the growth in the UK Retail Prices Index over a period of at least three years from grant. This was considered to be an appropriate hurdle and consistent with market practice at the time the P&O Option Plan was adopted. The Company reported negative EPS for 2002 and accordingly application of the formula for EPS growth would have resulted in a less stretching hurdle. Therefore, the remuneration committee resolved that options granted during 2003 would not normally be exercisable unless the growth in P&O's profit before tax and separately disclosable items per £1 nominal of deferred stock over a period of at least three years from grant exceeded the percentage increase in the UK Index of Retail Prices by an average of at least 3 per cent per annum.

There was a facility for the Company to require optionholders to assume the Company's liability for employer's national insurance contributions due on the exercise of unapproved stock options. The Company was able to grant additional options in recognition of the liability that optionholders assumed.

At the 2004 annual general meeting the stockholders approved an amendment to the rules of the P&O Option Plan to enable the Company to satisfy the exercise of both existing and future options by the issue of only that amount of stock which had a value, at the time of exercise, equal to the net gain resulting from the exercise, that is, the difference between the market price on the day of exercise of the amount of stock under the option and the total exercise price payable.

Executive directors were able to participate, subject to the usual limits, in the P&O 2004 UK Sharesave Plan (the "2004 Plan"), and previously the P&O Save As You Earn Stock Option Scheme (the "P&O SAYE Scheme"), on the same terms as other employees. The 2004 Plan operated within specific tax legislation (including a requirement to finance the exercise of the option using the proceeds of a monthly savings contract) and exercise of the option was not subject to satisfaction of a performance target since this was an all-employee share scheme.

Service contracts and Board changes

No executive director has a service contract of more than twelve months with the Company or any of its subsidiaries. All executive directors' service contracts were until 2006 re-issued with effect from 1 January in each year. As a result of the takeover process, in 2006 existing executive directors' service contracts were left in place (save as amended to reflect the annual salary review) and are terminable upon twelve months' notice by either party. The service contracts provide for payment in lieu of notice equivalent to twelve months' base salary and benefits, including bonus. Compensation payable upon early termination (other than under the payment in lieu of notice provisions) would be based on the contractual entitlement to salary and benefits subject to mitigation. Sir John Parker joined the Board as Deputy Chairman on 1 February 2005 on a salary of £200,000 p.a. and became Chairman on 13 May 2005 on a salary of £400,000 p.a. He was not entitled to participate in any of the Company's incentive or pension schemes. His contract was terminable on six months' notice but subject thereto was for a fixed term until 31 January 2008.

Robert Woods and Nick Luff were until 11 May 2005 non-executive directors of Royal P&O Nedlloyd N.V., as representatives of the Company, which retained their fees for this service. Robert Woods is a non-executive director of John Swire & Sons, for which he receives an annual fee of £32,500. Nick Luff is a non-executive director of QinetiQ Group plc for which he receives an annual fee of £35,000.

Non-executive directors

The non-executive directors had letters of appointment.

The remuneration of non-executive directors was decided by the Board. Non-executive directors received a base fee and they also received fees for additional services such as being a member of, or chairing a Board committee as set out below. Non-executive directors were not eligible for incentive schemes or other benefits.

Base fee — £30,000 per annum

Committee membership fee* — £5,000 per annum (per committee)

Committee chairmanship fee* — £5,000 per annum

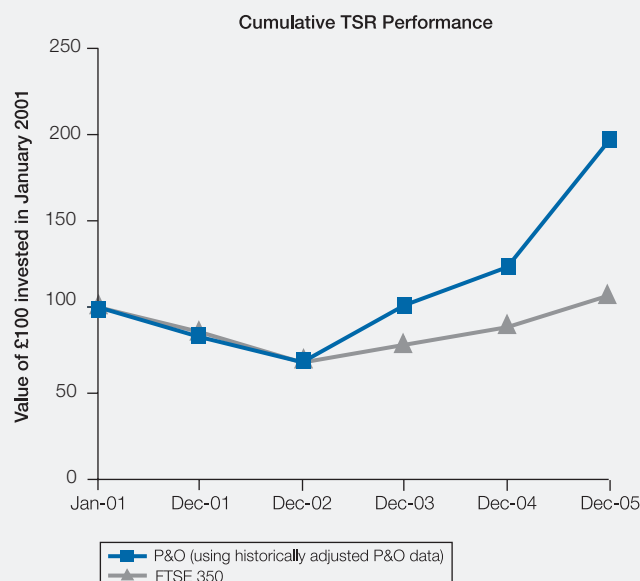
Senior non-executive director — £5,000 per annum

*Remuneration and audit committees only

Performance graph

In line with the Regulations, the following graph compares the performance of the Company's deferred stock on a TSR basis for the past five years against the FTSE 350 Index. This index has been selected as P&O was for most of that period a constituent of the FTSE 350 and uses this index for its comparator group for the Performance Share Plan and the 2005 Matching Share Plan. However, the line representing the FTSE 350 on the graph is based on the market index weighted by market capitalisation whereas the Performance Share Plan and the 2005 Matching Share Plan are based on the performance of the companies constituting the FTSE 350 at the commencement of the relevant performance period. TSR is shown as the value of £100 invested in P&O and in the FTSE 350 index over the five year period.

TSR is calculated for each year relative to the base date of 1 January 2001 and taking the percentage change of the market price over the relevant period, reinvesting any dividends at the ex-dividend date.



Details of directors' remuneration

With the exception of the deferred stock and the total interests columns in the table of executive directors' interests in shares and the non-executive directors' interests in shares, the following sections of the remuneration report have been audited.

Directors' emoluments

	Salary and fees 2005 £000	Bonus 2005 £000	Benefits in kind 2005 £000	Cash in lieu of benefits 2005 £000	Total 2005 £000	Total 2004 £000
Executive directors						
Robert Woods	500	338	21	–	859	767
Michael Gradon	325	219	20	–	564	480
Nick Luff	375	253	7	109	744	693
Russ Peters	265	186	18	–	469	320
Peter Smith	245	165	41	–	451	422
Lord Sterling #	135	91	31	–	257	660
Non-executive directors						
Sir John Parker †	310	–	–	–	310	–
Sir David Brown	40	–	–	–	40	33
Sir John Collins	48	–	–	–	48	39
David Williams	43	–	–	–	43	–
The Rt Hon the Baroness Symons of Vernham Dean †	3	–	–	–	3	–
Mike Turner †	3	–	–	–	3	–
Richard Cousins †	2	–	–	–	2	–
Michael Everard	40	–	–	–	40	33
Rodney Galpin #	19	–	–	–	19	44
	2,353	1,252	138	109	3,852	3,491

† from date of appointment

up to date of cessation of directorship

Aggregate emoluments in respect of qualifying services amounted to £3,852,000 (2004 £3,491,000) and the aggregate amount paid to pension schemes in respect of qualifying services amounted to £433,000 (2004 £374,000).

Nick Luff received a cash equivalent payment in place of certain benefits in kind and pension benefits.

Lord Sterling purchased a property (with related fixtures and fittings) on 18 October 2005 from the Group for £1,035,000 being the open market value as determined by independent valuers. The Group's profit on disposal was £418,000.

Sir Bruce MacPhail who retired as a director of the Company on 31 December 2003 worked on a part-time basis for the Company until 31 December 2005 managing the disposal of the development property portfolio for which he received a salary of £137,500, benefits in kind of £72,816 and a bonus of £206,250.

Richard Hein who retired as a director of the Company on 17 May 2002 was Chairman of P&O Australia Limited throughout 2005 for which he received a salary of £67,846, benefits in kind of £12,614 and a bonus of £20,956.

Directors' remuneration report

Directors' interests in shares

The following is a table of the executive directors' deferred stock, long term incentive awards and option grants (in units of £1 nominal of deferred stock) under the Matching Plan, Performance Share Plan, 2005 Matching Share Plan, P&O Option Plan, P&O SAYE Scheme and the 2004 Plan. The terms of these plans are set out under the heading "Long term incentives" on page 28. Further details of the stock option grants are set out on page 33.

	Deferred stock (unaudited)	Matching Plan Stock Awards	Matching Plan Invested Stock	Maximum Matching Plan Matching Awards	Maximum Performance Share Plan Awards	Maximum 2005 Matching Share Plan Awards	Stock Options	Total interests (unaudited)
Lord Sterling								
At 1 January 2005	1,757,822	16,114	154,638	273,036	–	–	1,110,025	3,311,635
Dividend stock*	–	–	–	–	–	–	–	–
Vested, exercised and sold ^{#(1,2)}	–	–	(91,360)	(152,266)	–	–	–	(243,626)
Own stock invested	91,360	–	–	–	–	–	–	91,360
At 13 May 2005	1,849,182	16,114	63,278	120,770	–	–	1,110,025	3,159,369
Robert Woods								
At 1 January 2005	72,000	18,533	124,573	225,225	–	–	1,192,747	1,633,078
Dividend stock*	9	1,252	–	–	1,450	453	–	3,164
Vested, exercised and sold ^{#(1,2)}	–	–	(89,690)	(149,483)	–	–	–	(239,173)
Own stock invested	1,243	–	88,447	–	–	–	–	89,690
Granted ^(3,4,5)	–	29,907	–	111,939	212,765	66,488	–	421,099
At 31 December 2005	73,252	49,692	123,330	187,681	214,215	66,941	1,192,747	1,907,858
Michael Gradon								
At 1 January 2005	144,434	10,635	84,365	150,711	–	–	818,198	1,208,343
Dividend stock*	179	776	–	–	870	206	–	2,031
Vested, exercised and sold ^{#(1,2)}	(121,385)	–	(45,526)	(75,876)	–	–	–	(242,787)
Own stock invested	(2,952)	–	48,478	–	–	–	–	45,526
Granted ^(3,4,5)	–	19,417	–	70,397	127,659	30,322	–	247,795
At 31 December 2005	20,276	30,828	87,317	145,232	128,529	30,528	818,198	1,260,908
Nick Luff								
At 1 January 2005	5,663	10,475	179,987	309,928	–	–	689,660	1,195,713
Dividend stock*	148	905	–	–	1,088	339	–	2,480
Vested, exercised and sold ^(1,2)	–	–	(67,500)	(112,500)	–	–	–	(180,000)
Own stock invested	(722)	–	68,222	–	–	–	–	67,500
Granted ^(3,4,5)	–	24,571	–	89,239	159,574	49,866	–	323,250
At 31 December 2005	5,089	35,951	180,709	286,667	160,662	50,205	689,660	1,408,943
Russ Peters								
At 1 January 2005	5,758	2,013	16,195	28,905	–	–	386,858	439,729
Dividend stock*	149	183	–	–	768	–	–	1,100
Own stock invested	–	–	–	–	–	–	–	–
Granted ^(3,4,5)	–	5,156	–	5,156	112,765	–	–	123,077
At 31 December 2005	5,907	7,352	16,195	34,061	113,533	–	386,858	563,906
Peter Smith								
At 1 January 2005	83,548	8,863	91,230	160,469	–	–	671,630	1,015,740
Dividend stock*	–	647	–	–	710	222	–	1,579
Vested, exercised and sold ^{#(1,2)}	(33,658)	–	(59,210)	(98,683)	–	–	–	(191,551)
Own stock invested	14,437	–	44,773	–	–	–	–	59,210
Granted ^(3,4,5)	–	16,181	–	58,768	104,255	32,577	–	211,781
At 31 December 2005	64,327	25,691	76,793	120,554	104,965	32,799	671,630	1,096,759

*The figures for vested, exercised and sold include the exercise of Matching Plan awards and the release of Matching Plan Invested Stock and are stated to show the amount of stock retained (being the increase in the deferred stock column) and the amount sold (being the decrease in the total interests column) after exercise.

#Dividend stock includes stock purchased in lieu of dividends for the stock held in the Employee Benefit Trust and stock purchased with dividends for stock in PEPs and ISAs.

- (1) The Matching Plan Stock Awards, which had been granted on 21 March 2003, vested on 9 March 2005. The market value of the deferred stock constituting these awards on the day of grant was 184p and on the day of vesting was 303p.
- (2) The date of exercise of the Matching Plan Stock Award was 9 March 2005. The market value of the deferred stock constituting these awards on the day of exercise was 303p.
- (3) The 2005 Matching Plan Awards were granted on 9 March 2005 and the market value of the deferred stock constituting these awards on the day of the grant was 303p. The performance conditions and performance period for these awards are described on page 29.
- (4) The 2005 Performance Share Plan awards were granted on 13 May 2005 and the market value of the deferred stock constituting these awards on the day of the grant was 282p. The performance conditions and performance period for these awards are described on page 29.
- (5) The 2005 Matching Share Plan awards were granted on 13 May 2005 and the market value of the deferred stock constituting these awards on the day of the grant was 282p. The performance conditions and performance period for these awards are described on page 29.

"Invested stock" includes invested stock under both the Matching Plan and the 2005 Matching share Plan.

The aggregate net value of assets received or receivable by directors during the year under long term incentive plans was £3,826,138 (2004 £1,544,555).

No director had interests, whether beneficial or non-beneficial, in the Company's preferred stock or debenture stocks or in the share capital, loan stocks or debenture stocks of the Company's subsidiaries at the beginning or end of the year or at the date of this report. No director had a material interest in any contract of significance with the Company or any subsidiary, joint venture or associate during the year.

As potential beneficiaries of the P&O Employee Benefit Trust (the "Trust"), the executive directors are technically deemed to be interested in deferred stock of the Company held by the Trust. At 31 December 2005, the Trust held £12,207,682 nominal of deferred stock.

Stock Awards

The Trustee waives its right to receive dividends on stock held in the Trust and the amount of stock to which Stock Awards relate increased during the year, due to additional P&O deferred stock purchased by the Trustee which had a value equivalent to the value of the dividend forgone. Stock Awards are eligible for Matching Awards in accordance with the rules of the Matching Plan as described above. The terms of the Matching Plan (including the performance conditions) are summarised on page 29. Stock Awards are subject to a retention period of two years from the date of grant. Stock Awards granted in 2004 and 2005 would normally have become exercisable from the announcement of the 2005 and 2006 preliminary results respectively. However, upon the change of control of P&O on 8 March 2006, Stock Awards under the Matching Plan, performance awards under the Performance Share Plan and Matching Awards under the Matching Plan and 2005 Matching Share Plan became exercisable in accordance with the rules of the plans. Under the Matching Plan, Stock Awards vested in full. Under all plans, Matching and Performance Awards vested in full (subject to pro-rating to the date of departure for those who had left the Company before the end of the relevant performance period).

Non-executive directors' interests in shares (unaudited)

The non-executive directors and their families had the following beneficial interests in units of £1 nominal of deferred stock of the Company at 31 December 2005:

	2005	2004
Sir John Parker	20,000	n/a
Sir David Brown	1,000	1,000
Sir John Collins	4,414	4,414
Michael Everard	3,500	3,500

Stock options

Further details of the stock options granted to directors under the P&O Option Plan and the P&O SAYE Scheme are set out below:

	Outstanding at 1 January and 31 December 2005	Exercisable	
		From	To
Lord Sterling*	229,533	23/10/03	23/10/10
	282,615	17/9/04	17/9/11
	355,673	24/9/05	24/9/12
	242,204	29/9/06	29/9/13
	1,110,025		
Robert Woods	226,014	23/10/03	23/10/10
	277,962	17/9/04	17/9/11
	409,755	24/9/05	24/9/12
	279,016	29/9/06	29/9/13
	1,192,747		
Michael Gradon	162,908	23/10/03	23/10/10
	207,592	17/9/04	17/9/11
	261,228	24/9/05	24/9/12
	186,470	29/9/06	29/9/13
	818,198		
Nick Luff	447,915	18/6/06	18/6/13
	241,745	29/9/06	29/9/13
	689,660		
Russ Peters	206,768	24/9/05	24/9/12
	7,382 [#]	1/6/06	1/11/06
	172,708	29/9/06	29/9/13
	386,858		
Peter Smith	124,432	23/10/03	23/10/10
	170,250	17/9/04	17/9/11
	214,175	24/9/05	24/9/12
	7,382 [#]	1/6/06	1/11/06
	155,391	29/9/06	29/9/13
	671,630		

*Lord Sterling retired from the Board on 13 May 2005 and the stock options listed above are at that date.

[#] P&O SAYE Plan options.

The performance conditions for each of the above stock options are described on page 30. The performance conditions for all options are based on EPS growth, except for the options exercisable from 29 September 2006.

The Company had a Directors' Shareholding Guideline whereby executive directors were expected to build up over a three year period, and maintain thereafter, a holding of deferred stock in the Company (including Stock Awards and Invested Stock) with a value broadly equivalent to at least 100 per cent of salary. This guideline was applied flexibly, where appropriate, for example to recognise the possibility of directors wishing to reduce their holding as they neared retirement or to take account of other special circumstances.

The aggregate gains made by directors on the exercise of deferred stock under option were £nil (2004 £137,743).

The mid-market price of the deferred stock at 30 December 2005 was 466.0p (2004 297.5p). The highest mid-market price during the year was 494.0p and the lowest mid-market price was 265.0p.

Pensions

	Current age	Increase in accrued pension (net of inflation/revaluation) during the year (A) £000 p.a.	Transfer value of the increase in accrued pension (net of inflation/revaluation) less director's contribution 31 December 2005 (B) £000	Accrued pension at 31 December 2005 (C) £000 p.a.	Increase in accrued pension during the year (D) £000 p.a.	Transfer value of accrued pension at 31 December 2005 (E) £000	Transfer value of accrued pension at 31 December 2004 (F) £000	Increase/(decrease) in transfer value over the year, less director's contribution (G) £000
Lord Sterling	71	–	–	586	37	12,096	11,201	896
Robert Woods	59	21	435	345	45	7,842	6,828	981
Michael Gradon	46	18	144	130	21	1,183	920	241
Russ Peters	57	10	156	156	13	2,790	2,281	492
Peter Smith	54	3	32	69	4	947	795	145

Notes:

- All executive directors during the year, except Nick Luff, were members of the P&O Pension Scheme (the "P&O UK Scheme").
- The accrued pensions indicated in column (C) are the pensions payable on reaching age 60, except for Lord Sterling whose pension is now in payment and Robert Woods whose pension could be payable immediately.
- Where applicable the rate of inflation used in columns (A) and (B) is 2.7 per cent.
- The pensions and transfer values indicated in columns (A) to (G) above, exclude the effect of any Additional Voluntary Contributions paid by the directors.

Lord Sterling has ceased to accrue further pension rights and his pension is in payment from 31 May 2005. The pension in columns (C) and (D) above, reflect the P&O UK Scheme's late retirement provisions. The transfer values indicated in columns (E), (F) and (G) demonstrate the change in cost to the P&O UK Scheme of providing the late retirement benefits, given prevailing market conditions. In accordance with Inland Revenue Regulations he is not entitled to transfer his benefits out of the P&O UK Scheme. For column (E) the pension has been valued when it came into payment, based on market conditions as at 31 December 2005.

Robert Woods' accrued pension in column (C) is the total pension earned, which could be paid immediately in the event of retirement. For the purpose of the UK Listing Authority's Listing Rules the figure in column (A) is consistent with him being entitled to an immediate pension last year.

Michael Gradon's pension rights in the event of early retirement would be affected by various historical provisions, which have not been available to new directors for some years. The actual pension payable would depend on his age and service and whether his retirement was voluntary or compulsory. The various provisions would start to apply from age 47 and begin to fall away gradually after age 55. The maximum effect of these provisions would be on retirement from service at age 55, where the value of the standard provisions reflected above could be enhanced by up to 40 per cent.

Peter Smith's pension rights are restricted by the current earnings cap, which was introduced by the government in 1989. The Company has therefore established a Funded Unapproved Retirement Benefits Scheme ("FURBS") which operates on a defined contribution basis. The Company's contribution to the FURBS is paid quarterly in arrears and it amounted to £45,567 in 2005 (2004 £43,741).

Nick Luff receives no pension benefit from the Company. The Company provides life insurance for which an insurance policy is in place, the cost of which is included within the directors' emoluments table on page 31.

General provisions of the P&O UK Scheme

The Normal Retirement Age for Senior Executives is 60. The maximum pension is normally two thirds of pensionable salary. Only basic salary is pensionable. Early retirement pensions are normally reduced to take account of the longer period over which they will be paid. However in certain circumstances the Scheme rules will allow unreduced pensions to be paid, providing they are funded by the employer at the time of retirement.

The P&O UK Scheme's rules guarantee pension increases during retirement fully in line with RPI increases up to 3 per cent, subject to the minimum introduced in the Pensions Act 1995. Increases above 3 per cent are not guaranteed but the trustee has the power to grant them, if circumstances permit, without referring to the Company. Increases greater than 80 per cent of the increase in RPI may only be given with the agreement of the Company. The current policy of the Company and the trustee is to fund the P&O UK Scheme for increases up to 80 per cent of the increase in RPI, subject to the above guarantees, allowance for which is made in transfer value calculations.

In the event of death before retirement, the P&O UK Scheme provides a capital sum equal to four times basic salary (or four times the earnings cap for those joining after 1989) plus spouse pensions or, at the trustee's discretion, a dependents pension of up to 66 per cent of the member's pension. Children's allowances are also payable at the rate of 25 per cent of the spouse/dependents pension.

By order of the Board

D J Leonard

Secretary

1 June 2006

Statement of directors' responsibilities in respect of the Annual Report and the financial statements

The directors are responsible for preparing the Annual Report and the Group and parent company financial statements, in accordance with applicable law and regulations.

Company law requires the directors to prepare Group and parent company financial statements for each financial year. Under that law the directors are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and have elected to prepare the parent company financial statements in accordance with UK Accounting Standards.

The Group financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and performance of the Group; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

The parent company financial statements are required by law to give a true and fair view of the state of affairs of the parent company.

In preparing each of the Group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- for the Group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Directors' Report and Directors' Remuneration Report that comply with that law and those regulations.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Report of the independent auditors

Independent auditors' report to the members of The Peninsular and Oriental Steam Navigation Company

We have audited the Group and Parent company financial statements (the "financial statements") of The Peninsular and Oriental Steam Navigation Company for the year ended 31 December 2005 which comprise the Consolidated income statement, the Consolidated and Parent company balance sheets, the Consolidated statement of cash flows, the Consolidated statement of recognised income and expense and the related notes. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the Annual Report and the Group financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU, and for preparing the parent company financial statements and the Directors' Remuneration Report in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 36.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and whether, in addition, the Group financial statements have been properly prepared in accordance with Article 4 of the IAS Regulation. We also report to you if, in our opinion, the Directors' Report is not consistent with the financial statements, if the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the Group financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Group's affairs as at 31 December 2005 and of its profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation;
- the Parent company financial statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the Parent company's affairs as at 31 December 2005; and
- the Parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc

Chartered Accountants
Registered Auditor

8 Salisbury Square
London
EC4Y 8BB
1 June 2006

Consolidated income statement

for the year ended 31 December 2005

	Note	Before separately disclosable items 2005 £m	Separately disclosable items (note 4) 2005 £m	Total 2005 £m	Before separately disclosable items 2004 £m	Separately disclosable items (note 4) 2004 £m	Total 2004 £m
Group revenue	2(a)	2,340.1	–	2,340.1	2,265.9	–	2,265.9
Cost of sales	3	(2,014.4)	–	(2,014.4)	(1,908.4)	(122.9)	(2,031.3)
Gross profit		325.7	–	325.7	357.5	(122.9)	234.6
Other operating income	3	12.8	4.1	16.9	19.5	13.5	33.0
Administrative costs	3	(192.5)	(18.7)	(211.2)	(216.9)	(217.3)	(434.2)
		146.0	(14.6)	131.4	160.1	(326.7)	(166.6)
Share of results of joint ventures and associates		40.9	(0.9)	40.0	30.5	–	30.5
Group operating profit/(loss)		186.9	(15.5)	171.4	190.6	(326.7)	(136.1)
Profit on sale and termination of businesses		–	–	–	–	32.4	32.4
Profit/(loss) before financing costs	2(b)	186.9	(15.5)	171.4	190.6	(294.3)	(103.7)
Financial income	5	7.9	–	7.9	11.4	–	11.4
Financial expenses	5	(66.6)	(12.1)	(78.7)	(94.9)	–	(94.9)
Net financing costs	5	(58.7)	(12.1)	(70.8)	(83.5)	–	(83.5)
Profit/(loss) before taxation		128.2	(27.6)	100.6	107.1	(294.3)	(187.2)
Taxation	6(a)	(23.6)	(0.4)	(24.0)	(18.9)	(1.9)	(20.8)
Profit/(loss) on continuing operations after taxation		104.6	(28.0)	76.6	88.2	(296.2)	(208.0)
Profit from discontinued operations and profit on sale of discontinued operations, net of tax	2(b)	33.6	179.9	213.5	53.0	3.5	56.5
Profit/(loss) for the financial year		138.2	151.9	290.1	141.2	(292.7)	(151.5)
Attributable to:							
Equity stockholders of the parent				279.8			(161.6)
Minority interests in subsidiaries				10.3			10.1
				290.1			(151.5)
Earnings per £1 nominal of deferred stock:							
Basic EPS	9			37.4p			(22.6)p
Diluted EPS	9			37.0p			(22.6)p
Basic EPS from continuing operations				8.5p			(30.3)p
Diluted EPS from continuing operations				8.4p			(30.3)p
Basic EPS from discontinued operations				28.9p			7.7p
Diluted EPS from discontinued operations				28.6p			7.7p

For underlying measures of EPS see note 9.

Consolidated statement of recognised income and expense

for the year ended 31 December 2005

	Note	2005 £m	2004 £m
Foreign exchange translation differences		94.4	(54.7)
Net gain/(loss) on hedge of net investments in foreign subsidiaries		(18.6)	–
Recycled exchange on disposals		0.1	–
Effective portion of net changes in fair value of cash flow hedges		(1.0)	–
Cash flow hedges transferred to income statement		17.5	–
Fair value movements on available-for-sale financial assets		0.6	–
Net actuarial losses		(167.3)	(48.6)
Income and expense recognised directly in equity		(74.3)	(103.3)
Profit/(loss) for the financial year		290.1	(151.5)
Total recognised income and expense for the financial year	25	215.8	(254.8)
Effect of change in accounting policy			
Effect of adoption of IAS 32 and 39 on 1 January 2005 (with 2004 not restated) on:			
Retained earnings		(4.2)	–
Cash flow hedge reserve		(23.0)	–
	36	(27.2)	–
Total recognised income and expense is attributable to:			
Equity stockholders of the parent	25	205.7	(263.4)
Minority interests in subsidiaries	25	10.1	8.6
		215.8	(254.8)

Of the income and expense recognised directly in equity for the financial year, £26.7m net gain has arisen in joint ventures and associates (2004 £44.7m net loss), of which £40.3m gain (2004 £38.7m loss) is in respect of foreign exchange translation differences, £4.9m loss (2004 £nil) is in respect of the effective portion of net changes in the fair value of cash flow hedges and £8.7m loss (2004 £6.0m loss) relates to net actuarial gains and losses, net of a £0.1m credit (2004 £nil) in respect of deferred tax.

Tax of £3.3m (2004 £9.6m credit) has been charged directly to equity in the consolidated statement of recognised income and expense. This consists of an income tax charge of £1.4m (2004 £3.5m credit) arising on foreign exchange translation differences and a deferred tax charge of £1.9m (2004 £6.1m credit) made up of a charge of £2.0m (2004 £6.1m credit) arising on actuarial gains and losses less a credit of £0.1m (2004 £nil) arising on the effective portion of net changes in the fair value of cash flow hedges. In addition, the effect of adoption of IAS 32 and 39 on 1 January 2005 gave rise to a £0.6m credit in respect of deferred tax.

Net actuarial gains and losses includes a £122.6m charge being the Group's share of the Merchant Navy Officers' Pension Fund deficit at 30 September 2005, when the Group commenced accounting for the fund as a defined benefit pension scheme, as set out in note 28 on pages 77 and 78 and also includes a charge of £17.5m being the Group's share of the exit payments made by P&O Nedlloyd into the P&O UK Pension scheme on forming its own UK scheme, as set out in note 28 on page 78.

Consolidated balance sheet

at 31 December 2005

	Note	2005 £m	2004 £m
Non-current assets			
Intangible assets	10	85.5	92.7
Prepaid leases	11	153.5	145.0
Property, plant and equipment	12	1,160.8	1,233.7
Investments in joint ventures and associates	13	386.6	501.4
Other investments	19	14.4	11.2
Deferred tax assets	14	6.5	16.7
Trade and other receivables	18	9.2	7.2
		1,816.5	2,007.9
Current assets			
Properties held for development and sale	16	149.8	508.5
Inventories	17	36.6	43.2
Other investments	19	34.6	5.2
Trade and other receivables	18	475.4	410.2
Tax recoverable	15	–	0.8
Cash and cash equivalents	20	99.5	50.2
Non-current assets held for sale	8	1.1	–
		797.0	1,018.1
Current liabilities			
Bank overdrafts	20	(17.3)	(20.8)
Interest bearing loans and borrowings	21	(30.6)	(79.7)
Trade and other payables	22	(424.4)	(383.2)
Income tax liabilities	15	(89.1)	(105.7)
Employee benefits	28	(23.0)	(24.2)
Provisions	23	(51.2)	(94.1)
		(635.6)	(707.7)
Net current assets		161.4	310.4
Non-current liabilities			
Interest bearing loans and borrowings	21	(656.2)	(1,131.3)
Trade and other payables	22	(35.1)	(56.2)
Deferred tax liabilities	14	(64.8)	(83.3)
Employee benefits	28	(282.8)	(268.9)
Provisions	23	(67.8)	(40.9)
		(1,106.7)	(1,580.6)
Net assets		871.2	737.7
Equity			
Issued capital	24	822.2	813.5
Share premium	25	792.2	782.9
Reserves	25	172.6	111.6
Retained earnings	25	(969.8)	(1,017.1)
Total equity attributable to equity holders of the parent		817.2	690.9
Minority interests in subsidiaries	25	54.0	46.8
Total equity		871.2	737.7

The accounts were approved by a duly authorised committee of the Board of directors and signed on its behalf on 1 June 2006 by:

Robert Woods

Michael Gradon

Consolidated statement of cash flows

for the year ended 31 December 2005

	Note	2005 £m	2004 £m
Profit/(loss) for the year		290.1	(151.5)
Share of results of joint ventures and associates		(62.5)	(78.3)
(Profit)/loss on sale of property, plant and equipment		(3.9)	11.2
Profit on sale and termination of businesses		(178.3)	(43.1)
Amounts written off investments		-	1.1
Net financing costs		75.0	88.9
Interest received		3.9	10.0
Share-based payments		5.4	4.5
Taxation expense		28.1	22.3
Depreciation, amortisation and impairment charges		109.9	322.3
Decrease in properties held for development and sale		352.0	267.2
Decrease inventories		3.3	8.2
Increase in trade and other receivables		(87.1)	(14.3)
Increase in trade and other payables		31.2	36.3
(Decrease)/increase in provisions		(39.5)	50.2
Decrease in liabilities for pensions and employee benefits		(111.5)	(35.9)
Taxation paid		(57.0)	(37.3)
Dividends received from joint ventures and associates		49.7	22.1
Net cash inflow from operating activities		408.8	483.9
Purchase of property, plant and equipment		(186.6)	(154.1)
Purchase of investments		(0.4)	(2.2)
Sale of property, plant and equipment		48.6	102.9
Sale of investments		0.1	0.1
Interest received		-	16.4
Purchase of subsidiaries and businesses	31(a)	-	1.6
Advances to and purchase of joint ventures and associates		(40.7)	(63.3)
Sale of subsidiaries and termination of businesses	31(b)	128.0	186.5
Repayments by and sale of joint ventures and associates		398.1	155.9
Net cash inflow from investing activities		347.1	243.8
Issue of stock		18.2	12.6
Purchase of own stock		(5.8)	(14.2)
Loan drawdowns		1,289.2	838.6
Loan repayments		(1,848.5)	(1,329.6)
Finance lease capital payments		(10.2)	(30.7)
Interest paid		(73.4)	(114.6)
Finance lease interest paid		(2.1)	(2.4)
Dividends paid to minority interests		(2.9)	(4.6)
Dividends paid		(70.0)	(91.6)
Net cash outflow from financing activities		(705.5)	(736.5)
Net increase/(decrease) in cash and cash equivalents		50.4	(8.8)
Cash and cash equivalents at 1 January	20	29.4	36.5
Effect of exchange rate fluctuations on cash held		2.4	1.7
Cash and cash equivalents at 31 December	20	82.2	29.4

Notes to the consolidated financial statements

1 Significant accounting policies

The Peninsular and Oriental Steam Navigation Company is a company domiciled in the United Kingdom. The consolidated financial statements of the Company for the year ended 31 December 2005 comprise the Company and its subsidiaries (together referred to as the "Group") and the Group's interests in associates and jointly controlled entities.

The consolidated financial statements were authorised for issuance by the directors on 1 June 2006.

Transition to International Financial Reporting Standards ("IFRS")

The consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU and its interpretations adopted by the International Accounting Standards Board ("IASB"). These are the Group's first consolidated financial statements under IFRS and IFRS 1 'First-time Adoption of International Financial Reporting Standards' has been applied.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Group is provided in note 36.

The Company has elected to prepare its financial statements in accordance with UK GAAP. These are presented on pages 97 to 114.

Basis of preparation

These financial statements are presented in sterling, the Group's functional currency, rounded to the nearest 0.1 million. They are prepared on the historical cost basis except for derivative financial instruments and available-for-sale assets, which are stated at fair value, and non-current assets held for sale which are stated at the lower of previous carrying amount and fair value less costs to sell.

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of IFRS that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 35.

The following accounting policies, unless otherwise stated, have been applied consistently to all periods presented in these consolidated financial statements in dealing with items which are considered material in relation to these consolidated financial statements and in preparing an opening IFRS balance sheet at 1 January 2004 for the purposes of transition to IFRS.

They have been applied consistently by Group entities.

Transitional arrangements

The rules for first time adoption of IFRS are set out in IFRS 1. In general a company is required to determine its IFRS accounting policies and apply these retrospectively to determine the opening IFRS compliant balance sheet. The standard permits a number of exceptions to this general principle to assist companies as they transition to IFRS.

When preparing the Group's IFRS balance sheet at 1 January 2004, the date of transition, the following optional exemptions, provided by IFRS 1, from full retrospective application of IFRS accounting policies have been adopted:

- IFRS 3 'Business Combinations' – the provisions of IFRS 3 have been applied prospectively from 1 January 2004, and the classification and accounting treatment of business combinations that occurred prior to this date have not been reconsidered in the preparation of the Group's opening IFRS balance sheet at 1 January 2004;
- IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' – the provisions of IAS 32 and IAS 39 have not been applied to the financial statements for the year ended 31 December 2004, which form the comparative period to the Group's first IFRS compliant financial statements and which, for these purposes, have been prepared on the basis of previous UK GAAP accounting policies. The Group has applied the exemption available under IFRS 1 that allows comparatives not to be restated for IAS 32 and IAS 39. The effect of adopting IAS 32 and IAS 39 is explained in note 36;
- Until 31 December 2004 the Group adopted hedge accounting for interest rate transactions and foreign exchange transactions in accordance with UK GAAP. With effect from 1 January 2005, subject to specific criteria, derivative financial instruments, financial assets and financial liabilities may be designated as forming hedge relationships as a result of which fair value changes are offset in the income statement or recognised directly in the statement of recognised income and expense depending on the nature of the hedge relationship;
- Where items of property, plant and equipment have previously been revalued, the revalued amount at 1 January 2004 has been deemed to be the cost at that date;
- Cumulative translation differences arising on consolidation of subsidiaries – IAS 21 'The Effects of Changes in Foreign Exchange Rates' requires such differences to be held in a separate reserve, rather than included in the profit and loss reserve under UK GAAP. This reserve has been deemed to be nil on 1 January 2004; and
- IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations' has been applied prospectively from 1 January 2005 (see page 48).

1 Significant accounting policies (continued)

Basis of consolidation

Intragroup balances and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains from transactions with joint ventures and associates are eliminated to the extent of the Group's interest in the entity. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Subsidiaries

The Group financial statements include the results of the Company and its subsidiary undertakings together with the Group's share of the results of its joint ventures and associates. A subsidiary is an entity controlled by the Company. Control is regarded as the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are presently exercisable or convertible are taken into account. The financial statements of subsidiaries are consolidated from the date that control commences until the date that control ceases.

Associates

An associate is an undertaking in which the Group has significant influence, but not control, over the financial and operating policies. The Group's share of the total recognised gains and losses of associates is included on an equity accounted basis in the consolidated income statement or statement of recognised income and expense (as appropriate) and its interest in their net assets is included within investments in the consolidated balance sheet from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations in respect of the associate.

Joint ventures

A joint venture is an undertaking in which the Group has joint control, established by a contractual arrangement with one or more other parties. The Group equity accounts for its joint ventures and therefore its share of the profits less losses of joint ventures are included in the consolidated income statement or statement of recognised income and expense (as appropriate) and its interest in their net assets is included in investments in the consolidated balance sheet.

Foreign currency

Foreign currency transactions

Transactions in foreign currencies are recorded at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into sterling at the rate of exchange ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary asset and liabilities that are measured in terms of historical cost in a foreign currency are translated using the rate of exchange ruling at the date of the transaction.

Financial statements of foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to sterling at the rates of exchange ruling at the balance sheet date. The revenues and expenses of foreign operations are translated into sterling at rates approximating to the rates of exchange ruling at the dates of the transactions. Foreign exchange differences arising on retranslation are recognised directly in a separate component of equity.

Net investment in foreign operations

Exchange differences arising from the translation of the net investment in foreign operations, and of related hedges, are taken to the translation reserve in accordance with the hedging policy described below.

Financial instruments

IAS 32 and IAS 39 address the accounting for, and reporting of, financial instruments. IAS 39 sets out detailed accounting requirements in relation to financial assets and liabilities. As outlined above under transitional arrangements, this has been applied by the Group for the first time for the year ended 31 December 2005. Under the exemption available in IFRS 1 the comparatives have not been restated for IAS 32 and IAS 39 and continue to reflect previously applied UK GAAP. The respective accounting policies are described below.

The Group uses derivative financial instruments, including interest rate swaps, foreign exchange contracts and options to hedge its exposure to foreign exchange and interest rate risks arising from operating, financing and investing activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for speculative purposes.

Derivative financial instruments are recognised initially at cost. Subsequent to initial recognition, derivative financial instruments are stated at fair value. Where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see accounting policy for hedging), otherwise the gain or loss on remeasurement to fair value is recognised immediately in profit or loss.

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties. The fair value of forward exchange contracts is their quoted market price at the balance sheet date.

1 Significant accounting policies (continued)

Hedging

Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. When the forecasted transaction subsequently results in the recognition of a non-financial asset or non-financial liability, or the forecast transaction for a non-financial asset or non-financial liability becomes a firm commitment for which fair value hedge accounting is applied, the associated cumulative gain or loss is removed from equity and included in the initial cost or other carrying amount of the non-financial asset or non-financial liability. If a hedge of a forecasted transaction subsequently results in the recognition of a financial asset or a financial liability, the associated gains and losses that were recognised directly in equity are reclassified into profit or loss in the same period or periods during which the asset acquired or liability assumed affects profit or loss (i.e. when interest income or expense is recognised). For cash flow hedges other than those covered by the preceding two policy statements, the associated cumulative gain or loss is removed from equity and recognised in the income statement in the same period or periods during which the hedged forecast transaction affects profit or loss. Any gain or loss arising on an ineffective part of a hedge transaction is recognised in the income statement immediately.

When a hedging instrument expires or is sold, terminated or exercised, or the entity revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in equity is recognised immediately in the income statement.

Hedge of net investment in foreign operations

Where a foreign currency liability hedges a net investment in a foreign operation, the portion of foreign exchange differences arising on translation of the liability that is determined to be an effective hedge is recognised directly in equity. The ineffective portion is recognised immediately in profit or loss. Where exchange differences have been deferred in equity, they are recycled to the income statement upon disposal of the respective foreign operation.

As noted above, the comparatives have not been restated for IAS 32 and IAS 39. Accordingly the Group has continued to apply its previous UK GAAP accounting policy, in its comparative figures. Under this accounting policy amounts payable or receivable in respect of interest rate swaps are recognised within the interest expense over the period of the contracts. Non interest bearing amounts due after one year are discounted at a rate approximating to current interest rates. Gains and losses on instruments used for hedging are not recognised until the exposure that is being hedged is itself recognised.

Financial guarantees

The Group has not adopted amendments to IAS 39 and IFRS 4 in relation to financial guarantee contracts which will apply for periods commencing on or after 1 January 2006.

Where the Group enters into financial guarantee contracts to guarantee the indebtedness of joint ventures or associates, the Group considers these to be insurance arrangements, and accounts for them as such. In this respect, the Group treats the guarantee contract as a contingent liability until such time as it becomes probable that the Group will be required to make a payment under the guarantee.

The Group does not expect the amendments to have any impact on the financial statements for the period commencing 1 January 2006.

Investments

Investments in debt and equity securities

Where the Group has the positive intent and ability to hold debt instruments to maturity, they are stated at amortised cost less impairment losses.

Other investments in debt and equity securities held by the Group are classified as being available-for-sale and are stated at fair value, with any resultant gain or loss being recognised directly in equity, except for impairment losses and, in the case of monetary items such as debt securities, foreign exchange gains and losses. When these investments are derecognised, the cumulative gain or loss previously recognised in equity is recognised in profit or loss. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss.

The fair value of financial instruments classified as available-for-sale is their quoted bid-price at the balance sheet date. Available-for-sale investments are recognised/derecognised by the Group on the date it commits to purchase/sell the investments. Securities held-to-maturity are recognised/derecognised on the day they are transferred to/by the Group.

The Group does not hold investments in debt or equity securities for trading purposes.

The comparative information for other investments are presented in accordance with UK GAAP and are stated at historical cost net of provisions for impairment.

Intangible assets

Goodwill arising on consolidation

Purchased goodwill represents amounts arising on acquisition of subsidiaries, associates and joint ventures. Goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

1 Significant accounting policies (continued)

In respect of acquisitions prior to 1 January 2004, goodwill is included on the basis of its deemed cost which represents the carrying amount (net of accumulated amortisation) as recorded previously under UK GAAP.

Goodwill is stated at cost or deemed cost less any accumulated impairment losses. Goodwill is allocated to cash generating units and is not amortised but is tested annually for impairments (see accounting policy for impairment). In respect of associates and joint ventures the carrying amount of goodwill is included as part of the carrying amount of the investment in the associate or joint venture.

Negative goodwill arising on acquisition is recognised directly in the income statement.

The Group's policy prior to 1998 was to eliminate goodwill arising upon acquisitions against reserves. Under IFRS 1 and IFRS 3, such goodwill remains eliminated against reserves.

Property, plant and equipment

Owned assets

Items of property, plant and equipment are stated at cost or deemed cost less accumulated depreciation (see below) and impairment losses (see accounting policy for impairment). The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads. Interest incurred in respect of costs relating to assets under construction is capitalised into the cost of the asset concerned.

Certain items of property, plant and equipment that had been revalued to fair value on or prior to 1 January 2004, the date of transition to IFRS, are measured on the basis of deemed costs, being the revalued amount at the date of that revaluation.

Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for as separate items of property, plant and equipment.

Leased assets

Leases under which the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases. An asset acquired by way of a finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation (see below) and impairment losses (see accounting policy for impairment). The capital element of future lease payments is treated as a liability. The interest element is charged to the income statement over the period of the finance lease in proportion to the balance of capital repayments.

All other leases are classified as operating leases with the lease rentals payable being charged to the income statement on a systematic basis over the term of the lease.

Subsequent expenditure

Expenditure incurred to replace a component of an item of property, plant and equipment that is accounted for separately, including major inspection and overhaul expenditure, is capitalised. Other subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property, plant and equipment. All other expenditure is recognised in the income statement as an expense as incurred.

Depreciation

Depreciation is calculated to write down the cost of property, plant and equipment to their estimated residual value on a straight line basis over the expected useful life of the asset concerned. Generally for ships this is between 10 and 35 years, for freehold property 50 years and for other fixed assets (reported within plant and machinery, fixtures and fittings) various periods of up to 40 years, the most significant of which are cold storage facilities (up to 40 years), port equipment, such as cranes and straddle carriers (up to 25 years), Ports IT systems (up to 10 years) and other port equipment, such as forklifts, tractors and trailers (5 to 10 years). Leased assets are depreciated over the remainder of the lease period. No depreciation is provided on freehold land.

Assets constructed by the Group are depreciated from the date on which they come into use.

Prepaid leases

Advance payments at the inception of operating leases are recognised as prepayments in respect of that lease and recognised in profit or loss over the lease term on a systematic basis.

Properties held for development and sale

Properties held for development and sale are included in current assets at the lower of cost and net realisable value, with any resultant gain or loss recognised in the income statement. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. Interest and other outgoings less income receivable are charged to the income statement during development, except in respect of properties where the development period is extensive, when such amounts are included in cost.

Inventories

Inventories and work in progress are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The cost of inventories within Ferries is based on the First-in-First-out principle, whilst within Ports inventories are accounted for on a weighted average basis.

1 Significant accounting policies (continued)

Trade and other receivables

Trade and other receivables are stated at their cost less impairment losses (see accounting policy for impairment).

Cash and cash equivalents

Cash and cash equivalents comprises cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Trade and other payables

Trade and other payables are stated at cost.

Impairment

The carrying amounts of the Group's assets, other than properties held for development and sale (see accounting policy for properties held for development and sale), inventories (see accounting policy for inventories) and deferred tax assets (see accounting policy for taxation), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. For goodwill the recoverable amount is estimated at each balance sheet date as well as when there are indications that the carrying value may not be recoverable. An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash generating units, and then to reduce the carrying amount of the other assets in the unit on a pro rata basis. A cash generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash flows from other assets or groups of assets.

On transition to IFRS all goodwill was tested for impairment as at 1 January 2004, the date of transition, even though no indication of impairment existed.

Calculation of recoverable amount

The recoverable amount of assets other than receivables, is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash generating unit to which the asset belongs.

Reversals of impairment

An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Interest bearing loans and borrowings

Interest bearing loans and borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest bearing loans and borrowings are stated at amortised costs with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

Share capital

Preference and concessionary stock

Preference and concessionary stock are classified as equity as they are non-redeemable and the directors retain discretion over dividend payments. Dividends are recognised as distributions within equity and are recognised as a liability in the period in which they are declared.

Repurchase of share capital

When share capital recognised as equity is purchased by the Company, the amount of the consideration paid, including directly attributable costs, is recognised as a change in equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity.

Employee benefits

Pensions

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is discounted to determine the present value, and the fair value of any plan assets is deducted. The calculation is performed by a qualified actuary using the projected unit credit method. The discount rate is the yield at the balance sheet date on AA credit rated bonds or local equivalent that have maturity dates approximating to the terms of the Group's obligations.

1 Significant accounting policies (continued)

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the income statement on a straight line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in the income statement.

Actuarial gains and losses that arise in calculating the Group's obligation in respect of a plan are recognised in the period in which they arise directly in the statement of recognised income and expenses.

The operating and financing costs of defined benefit pension plans are recognised separately in the income statement; current service costs are spread systematically over the expected average remaining service lives of employees and financing costs are recognised in the periods within which they arise.

Contributions, including lump sum payments, in respect of defined contribution pension schemes and multi employer defined benefit schemes where it is not possible to identify the Group's share of the scheme, are charged to the income statement as they fall due.

Share-based payments

The Group operated five employee share plans: the Executive Stock Option Plan ("P&O Option Plan"), the P&O 2004 UK Sharesave Plan ("2004 Plan"), the Deferred Bonus and Co-investment Matching Plan ("Matching Plan"), the P&O Performance Share Plan ("Performance Share Plan") and the P&O 2005 Matching Share Plan ("2005 Matching Share Plan"). The fair values of grants under the P&O Option Plan and 2004 Plan were calculated using binomial valuation models. The fair values of awards under the Matching Plan, Performance Share Plan and 2005 Matching Share Plan are calculated by discounting the share price at the date of award in respect of the relevant performance conditions. The fair value is measured at grant date and, in accordance with IFRS 2 'Share-based Payment', the resulting cost is charged to the income statement over the period during which the employees become unconditionally entitled to the options or shares. The amount recognised as an expense is adjusted to reflect changes in expected and actual levels of options vesting.

Long term service benefits

The Group's net obligation in respect of long term service benefits, other than pension plans, is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using the projected unit credit method and is discounted to its present value and the fair value of any related assets is deducted. The discount rate is the yield at the balance sheet date on AA credit rated bonds (or local equivalent) that have maturity dates approximating to the terms of the Group's obligations.

Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation, and where the amount of the associated costs can be reliably estimated. If the effect is material, provisions are calculated by discounting the expected future cash flows at a rate that reflects current market assessments of the time value of money, and where appropriate the risks specific to the liability.

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for.

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

Revenue

Revenue comprises amounts derived from the provision of goods and services to third parties (excluding VAT and similar sales taxes) and includes rent receivable from properties. Revenue from the provision of goods includes sales of properties held for development and sale, recognised when contracts become unconditional. Revenue from the provision of services is recognised on the delivery of those services, which for Ports is once the relevant throughput has taken place, for Ferries is on provision of carriage and for Container Shipping is on completion of the shipping or transport operation. For Cold Logistics storage revenue is recognised over the period during which storage is provided and for its handling and transport operations on completion of the service.

Net financing costs

Net financing costs comprise interest payable on borrowings calculated using the effective interest rate method, the interest expense element of finance lease payments, interest receivable on funds invested, foreign exchange gains and losses reflected in the income statement, dividend income, the unwinding of discounts on provisions and gains and losses on interest hedging instruments that are recognised in the income statement.

The interest expense component of finance lease payments is recognised in the income statement using the effective interest rate method.

Taxation

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

1 Significant accounting policies (continued)

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that the Group can control the timing of reversal of the differences and that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

Discontinued operations

A discontinued operation is a clearly distinguishable component of the Group's business that is abandoned or terminated pursuant to a single plan, and which represents a separate major line of business or geographical area of operations.

Non-current assets held for sale

Immediately before classification as held for sale, the measurement of the assets (and all assets and liabilities in a disposal group) is brought up-to-date in accordance with applicable IFRS. Then, on initial classification as held for sale, non-current assets and disposal groups are recognised at the lower of carrying amount and fair value less costs to sell.

Impairment losses on initial classification as held for sale are included in profit or loss, even when there is a revaluation. The same applies to gains and losses on subsequent remeasurement.

Separately disclosable items

Separately disclosable items are outside the normal course of business and include write-down or disposal of property, plant and equipment; restructuring costs and reversals of any provisions for restructuring costs; disposals of investments and profit/loss on disposal of discontinued operations.

2 Segment reporting

The segment information is presented in the consolidated financial statements in respect of the Group's business and geographical segments. The primary format, business segments, reflects the Group's management and internal reporting structure.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Segment capital expenditure is the total cost incurred during the period to acquire segment assets that are expected to be used for more than one period.

Business segments

The Group is comprised of the following main business segments:

- **Ports** The operation and development of terminals and related logistical operations worldwide.
- **Ferries** The operation of freight and passenger ferries within Europe and related road haulage.
- **Property** A development property portfolio in the US, the UK and Continental Europe.

The Container Shipping and Cold Logistics business segments were sold during June 2005 and December 2005, respectively (see note 8).

Geographical segments

The Ports segment is managed on a global basis, but operates in four principal geographical areas: Europe, Americas, Australasia and Asia. The Property segment operates in Europe and Americas. Ferries operates in Europe only.

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets are based on the geographical location of the assets.

(a) Segmental analysis of revenue

By division:	Group	Joint ventures	Total	Group	Joint ventures	Total
	2005	2005	2005	2004	2004	2004
	£m	£m	£m	£m	£m	£m
Continuing operations						
Ports	913.9	235.3	1,149.2	844.4	174.9	1,019.3
Ferries	895.4	–	895.4	984.0	–	984.0
Property	530.8	3.9	534.7	437.5	6.1	443.6
Revenue from continuing operations	2,340.1	239.2	2,579.3	2,265.9	181.0	2,446.9
Discontinued operations						
Cold Logistics	222.8	–	222.8	205.6	–	205.6
Container Shipping	–	–	–	–	478.9	478.9
Revenue for the financial year	2,562.9	239.2	2,802.1	2,471.5	659.9	3,131.4
By geographical area of origin:	Group	Joint ventures	Total	Group	Joint ventures	Total
	2005	2005	2005	2004	2004	2004
	£m	£m	£m	£m	£m	£m
Continuing operations						
Europe	1,492.0	65.1	1,557.1	1,329.6	60.3	1,389.9
Americas	362.2	106.8	469.0	489.6	73.6	563.2
Australasia	308.5	38.1	346.6	293.7	18.0	311.7
Asia	177.4	29.2	206.6	153.0	29.1	182.1
Revenue from continuing operations	2,340.1	239.2	2,579.3	2,265.9	181.0	2,446.9
Discontinued operations						
Europe	–	–	–	–	142.3	142.3
Americas	134.0	–	134.0	126.8	84.8	211.6
Australasia	88.8	–	88.8	78.8	31.8	110.6
Asia	–	–	–	–	220.0	220.0
Revenue for the financial year	2,562.9	239.2	2,802.1	2,471.5	659.9	3,131.4

2 Segment reporting (continued)

(b) Segmental analysis of operating profit/(loss) and discontinued operations

	Joint ventures and associates			Joint ventures and associates		
	Group 2005 £m	and associates 2005 £m	Total 2005 £m	Group 2004 £m	and associates 2004 £m	Total 2004 £m
By division:						
Continuing operations						
Before separately disclosable items						
Ports	120.7	56.0	176.7	113.8	42.3	156.1
Ferries	14.7	–	14.7	(5.9)	–	(5.9)
Property	10.6	2.1	12.7	52.2	1.8	54.0
	146.0	58.1	204.1	160.1	44.1	204.2
Separately disclosable items						
Ports	(0.4)	–	(0.4)	7.9	–	7.9
Ferries	1.6	–	1.6	(280.6)	–	(280.6)
Property	0.2	(0.9)	(0.7)	(54.0)	–	(54.0)
Unallocated	(16.0)	–	(16.0)	–	–	–
	(14.6)	(0.9)	(15.5)	(326.7)	–	(326.7)
Total						
Ports	120.3	56.0	176.3	121.7	42.3	164.0
Ferries	16.3	–	16.3	(286.5)	–	(286.5)
Property	10.8	1.2	12.0	(1.8)	1.8	–
Unallocated	(16.0)	–	(16.0)	–	–	–
	131.4	57.2	188.6	(166.6)	44.1	(122.5)
Less:						
Joint ventures and associates net financing costs	–	(5.0)	(5.0)	–	(4.9)	(4.9)
Joint ventures and associates taxation	–	(11.1)	(11.1)	–	(8.4)	(8.4)
Joint ventures and associates minority interest	–	(1.1)	(1.1)	–	(0.3)	(0.3)
Operating profit/(loss)	131.4	40.0	171.4	(166.6)	30.5	(136.1)
Discontinued operations						
Before separately disclosable items						
Container Shipping	(2.1)	29.0	26.9	(3.9)	63.7	59.8
Cold Logistics	21.0	–	21.0	18.4	–	18.4
	18.9	29.0	47.9	14.5	63.7	78.2
Separately disclosable items						
Container Shipping	–	–	–	(0.4)	0.3	(0.1)
Cold Logistics	2.1	–	2.1	(9.2)	–	(9.2)
	2.1	–	2.1	(9.6)	0.3	(9.3)
Total						
Container Shipping	(2.1)	29.0	26.9	(4.3)	64.0	59.7
Cold Logistics	23.1	–	23.1	9.2	–	9.2
	21.0	29.0	50.0	4.9	64.0	68.9
Less:						
Net financing costs	(4.2)	(4.8)	(9.0)	(5.4)	(12.3)	(17.7)
Taxation	(3.6)	(1.7)	(5.3)	(1.5)	(3.4)	(4.9)
Minority interest	–	–	–	–	(0.5)	(0.5)
Net profit from discontinued operations	13.2	22.5	35.7	(2.0)	47.8	45.8
Profit on sale of Container Shipping interests			188.0			9.6
Loss on sale of Cold Logistics			(15.0)			–
Profit on sale of other discontinued businesses			4.8			1.1
Profit from discontinued operations and profit on sale of discontinued operations, net of tax			213.5			56.5

2 Segment reporting (continued)

(c) Geographical analysis of operating profit/(loss) before joint venture and associate net financing costs, taxation and minority interests

	Group 2005 £m	Joint ventures 2005 £m	Associates 2005 £m	Total 2005 £m	Group 2004 £m	Joint ventures 2004 £m	Associates 2004 £m	Total 2004 £m
By geographical area of origin:								
Continuing operations								
Europe	20.5	5.1	(0.8)	24.8	(327.1)	2.7	2.5	(321.9)
Americas	23.0	8.0	–	31.0	69.3	0.3	–	69.6
Australasia	33.8	3.3	1.1	38.2	43.4	3.7	0.1	47.2
Asia	54.1	7.2	33.3	94.6	47.8	7.7	27.1	82.6
	131.4	23.6	33.6	188.6	(166.6)	14.4	29.7	(122.5)
Discontinued operations								
Europe	(2.1)	–	29.0	26.9	(2.0)	3.7	14.5	16.2
Americas	12.1	–	–	12.1	10.9	2.1	9.0	22.0
Australasia	11.0	–	–	11.0	(1.5)	0.8	3.3	2.6
Asia	–	–	–	–	(2.5)	5.4	25.2	28.1
	152.4	23.6	62.6	238.6	(161.7)	26.4	81.7	(53.6)

(d) Segmental analysis of total assets

	Segment assets 2005 £m	Investment in joint ventures and associates 2005 £m	Taxation assets 2005 £m	Total assets 2005 £m	Segment assets 2004 £m	Investment in joint ventures and associates 2004 £m	Taxation assets 2004 £m	Total assets 2004 £m
By division:								
Continuing operations								
Ports	1,364.3	289.9	6.5	1,660.7	1,109.9	235.6	8.0	1,353.5
Ferries	552.9	2.1	–	555.0	566.3	0.9	2.3	569.5
Property	303.2	94.6	–	397.8	598.5	89.5	4.9	692.9
	2,220.4	386.6	6.5	2,613.5	2,274.7	326.0	15.2	2,615.9
Discontinued operations								
Container Shipping	–	–	–	–	3.5	175.2	1.7	180.4
Cold Logistics	–	–	–	–	228.9	0.2	0.6	229.7
Total assets	2,220.4	386.6	6.5	2,613.5	2,507.1	501.4	17.5	3,026.0

	Segment assets 2005 £m	Investment in joint ventures and associates 2005 £m	Taxation assets 2005 £m	Total assets 2005 £m	Segment assets 2004 £m	Investment in joint ventures and associates 2004 £m	Taxation assets 2004 £m	Total assets 2004 £m
By geographical area of origin:								
Continuing operations								
Europe	958.3	99.1	1.9	1,059.3	1,191.1	90.7	4.8	1,286.6
Americas	412.8	65.4	1.5	479.7	214.6	53.3	9.8	277.7
Australasia	290.9	17.6	1.8	310.3	422.4	7.9	(0.3)	430.0
Asia	558.4	204.5	1.3	764.2	446.6	174.1	0.9	621.6
	2,220.4	386.6	6.5	2,613.5	2,274.7	326.0	15.2	2,615.9
Discontinued operations								
Europe	–	–	–	–	0.8	43.3	0.4	44.5
Americas	–	–	–	–	152.8	30.6	0.7	184.1
Australasia	–	–	–	–	77.0	11.2	0.3	88.5
Asia	–	–	–	–	1.8	90.3	0.9	93.0
Total assets	2,220.4	386.6	6.5	2,613.5	2,507.1	501.4	17.5	3,026.0

2 Segment reporting (continued)

(e) Segmental analysis of total liabilities

By division:	Segment liabilities	Taxation liabilities	Total liabilities	Segment liabilities	Taxation liabilities	Total liabilities
	2005	2005	2005	2004	2004	2004
	£m	£m	£m	£m	£m	£m
Continuing operations						
Ports	768.4	100.5	868.9	683.1	90.0	773.1
Ferries	577.0	15.7	592.7	736.9	12.1	749.0
Property	243.0	37.7	280.7	478.7	66.0	544.7
	1,588.4	153.9	1,742.3	1,898.7	168.1	2,066.8
Discontinued operations						
Container Shipping	–	–	–	75.6	11.1	86.7
Cold Logistics	–	–	–	125.0	9.8	134.8
Total liabilities	1,588.4	153.9	1,742.3	2,099.3	189.0	2,288.3

(f) Segmental analysis of additions to intangible assets, prepaid leases and property, plant and equipment

By division:	2005	2004
	£m	£m
Continuing operations		
Ports	164.0	130.7
Ferries	15.3	19.1
Property	1.9	9.5
	181.2	159.3
Discontinued operations		
Cold Logistics	7.7	6.3
Total additions	188.9	165.6

By geographical area of origin:

	2005	2004
	£m5	£m
Continuing operations		
Europe	54.1	79.5
Americas	47.0	14.3
Australasia	27.8	18.7
Asia	52.3	46.8
	181.2	159.3
Discontinued operations		
Americas	4.5	4.7
Australasia	3.2	1.6
Total additions	188.9	165.6

(g) Segmental analysis of depreciation and other significant non-cash expenses

By division:	Depreciation and amortisation	Impairments	Total	Depreciation and amortisation	Impairments	Total
	2005	2005	2005	2004	2004	2004
	£m	£m	£m	£m	£m	£m
Continuing operations						
Ports	92.3	–	92.3	78.7	6.6	85.3
Ferries	30.2	–	30.2	45.8	188.4	234.2
Property	1.6	–	1.6	5.6	–	5.6
	124.1	–	124.1	130.1	195.0	325.1
Discontinued operations						
Container Shipping	20.2	–	20.2	40.5	–	40.5
Cold Logistics	9.1	–	9.1	10.3	10.1	20.4
	153.4	–	153.4	180.9	205.1	386.0

Included in the above is a depreciation and amortisation charge of £43.5m (2004 £63.7m) in relation to the Group's share of its joint venture and associates.

2 Segment reporting (continued)

(h) Segmental analysis of net operating assets

By division:	Group share of joint ventures and associates			Total	Group share of joint ventures and associates			Total
	Net operating assets	Loans	Other net non-operating assets/ (liabilities)		Net operating assets	Loans	Other net non-operating assets/ (liabilities)	
	2005	2005	2005	2005	2004	2004	2004	2004
	£m	£m	£m	£m	£m	£m	£m	£m
Continuing operations								
Ports	1,457.6	(90.6)	(24.4)	1,342.6	1,223.8	(59.7)	(7.9)	1,156.2
Ferries	321.8	-	-	321.8	279.6	-	-	279.6
Property	217.7	(13.5)	19.1	223.3	539.4	(26.2)	19.7	532.9
	1,997.1	(104.1)	(5.3)	1,887.7	2,042.8	(85.9)	11.8	1,968.7
Discontinued operations								
Container Shipping	-	-	-	-	259.5	(25.4)	(62.9)	171.2
Cold Logistics	-	-	-	-	198.1	-	-	198.1
	1,997.1	(104.1)	(5.3)	1,887.7	2,500.4	(111.3)	(51.1)	2,338.0

By geographical area of origin:	Net operating assets	Net operating assets
	2005	2004
	£m	£m
Continuing operations		
Europe	702.0	895.6
Americas	361.2	334.2
Australasia	252.4	241.7
Asia	681.5	571.3
	1,997.1	2,042.8
Discontinued operations		
Europe	-	73.3
Americas	-	174.9
Australasia	-	85.1
Asia	-	124.3
	1,997.1	2,500.4

Net operating assets are reconciled to net assets as follows:

	2005	2004
	£m	£m
Net operating assets	1,997.1	2,500.4
Group share of joint venture and associate loans	(104.1)	(111.3)
Group share of joint venture and associate other net non-operating liabilities	(5.3)	(51.1)
	1,887.7	2,338.0
Net derivative financial instruments	(21.3)	-
Net borrowings	(604.6)	(1,181.6)
Amounts relating to previous corporate disposals	48.4	35.7
Other investments	11.7	10.2
Net employee benefit liabilities	(303.3)	(293.1)
Net corporation and deferred taxation	(147.4)	(171.5)
Net assets	871.2	737.7

2 Segment reporting (continued)

(i) Ports operating profit and net operating assets

	Operating profit				Net operating assets	
	Before separately disclosable	Separately disclosable	Total	Total	2005	2004
	items 2005 £m	items 2005 £m	2005 £m	2004 £m	£m	£m
Asia	95.6	(1.6)	94.0	81.4	679.7	563.1
Americas	24.5	2.3	26.8	19.3	252.9	193.4
Australasia	31.4	–	31.4	39.4	226.2	212.3
Europe	17.8	(1.1)	16.7	16.9	273.7	225.8
	169.3	(0.4)	168.9	157.0	1,432.5	1,194.6
Maritime Services	7.4	–	7.4	7.0	25.1	29.2
	176.7	(0.4)	176.3	164.0	1,457.6	1,223.8

Ports net operating assets include assets under construction of £27.7m (2004 £39.2m).

3 Net operating costs

	Before separately disclosable	Separately disclosable	Total	Before separately disclosable	Separately disclosable	Total
	items 2005 £m	items 2005 £m	2005 £m	items 2004 £m	items 2004 £m	2004 £m
Continuing operations						
Cost of sales	(2,014.4)	–	(2,014.4)	(1,908.4)	(122.9)	(2,031.3)
Other operating income	12.8	4.1	16.9	19.5	13.5	33.0
Administrative costs	(192.5)	(18.7)	(211.2)	(216.9)	(217.3)	(434.2)
	(2,194.1)	(14.6)	(2,208.7)	(2,105.8)	(326.7)	(2,432.5)
Discontinued operations						
Cost of sales	(191.9)	–	(191.9)	(178.9)	0.8	(178.1)
Administrative costs	(12.0)	–	(12.0)	(12.2)	(10.4)	(22.6)
	(2,398.0)	(14.6)	(2,412.6)	(2,296.9)	(336.3)	(2,633.2)
Net operating costs include:					2005	2004
					£m	£m
Depreciation and amortisation of prepaid leases and property, plant and equipment					(109.9)	(117.2)
Impairment charge					–	(205.1)
Audit fee					(2.3)	(2.3)
Rental of land and buildings					(107.8)	(100.2)
Hire of ships					(49.3)	(60.3)
Hire of plant and machinery					(34.4)	(35.5)

Other operating income includes insurance claim proceeds of £5.9m in respect of business interruption and fixed assets damaged due to hurricane Katrina.

The administrative costs within continuing operations includes an impairment charge of £nil (2004 £205.6m).

3 Net operating costs (continued)

Fees paid to the Company's principal auditor (KPMG)	UK	Overseas	Total	Percentage	UK	Overseas	Total	Percentage
	2005	2005	2005	of total fees	2004	2004	2004	of total fees
	£m	£m	£m	%	£m	£m	£m	%
Audit services								
Statutory audit	1.8	0.4	2.2	37.9	1.2	1.0	2.2	42.3
Audit-related regulatory reporting	0.5	0.1	0.6	10.4	0.2	–	0.2	3.9
Total audit services	2.3	0.5	2.8	48.3	1.4	1.0	2.4	46.2
Further assurance services	0.2	1.5	1.7	29.3	1.1	0.1	1.2	23.0
Tax services								
Compliance services	–	0.3	0.3	5.2	–	0.4	0.4	7.7
Advisory services	0.2	0.6	0.8	13.8	0.4	0.5	0.9	17.3
Other services	0.1	0.1	0.2	3.4	0.2	0.1	0.3	5.8
Total of non-audit services	0.5	2.5	3.0	51.7	1.7	1.1	2.8	53.8
Total of audit and non-audit services	2.8	3.0	5.8	100.0	3.1	2.1	5.2	100.0

Fees for further assurance services in 2005 principally relate to due diligence work in respect of the disposal of the Cold Logistics business.

In addition to the above £0.1m (2004 £0.1m) was paid to secondary auditors in respect of audit fees bringing the statutory audit fee for the Group to £2.3m (2004 £2.3m). The Group's share of fees paid to KPMG by joint ventures and associates was £nil (2004 £1.1m), of which £nil (2004 £0.6m) was in respect of audit work and £nil (2004 £0.5m) was in respect of non-audit work.

4 Separately disclosable items

Separately disclosable items consist of:

	Operating	Net financing	Profit on sale of discontinued operations		Total	Total
	profit	costs	Taxation	net of tax	2005	2004
	2005	2005	2005	2005	£m	£m
	£m	£m	£m	£m		
Profit/(loss) on sale of property, plant and equipment	0.9	–	–	2.1	3.0	(11.8)
Profit on sale of Container Shipping interests	–	–	–	188.0	188.0	9.6
Loss on sale of Cold Logistics	–	–	–	(15.0)	(15.0)	–
Profit on sale of other discontinued businesses	–	–	–	4.8	4.8	1.1
Loss on ineffective hedges	–	(12.1)	–	–	(12.1)	–
Corporate relocation and reorganisation	(15.4)	–	0.4	–	(15.0)	–
Takeover costs	(3.3)	–	–	–	(3.3)	–
Other income	2.3	–	(0.8)	–	1.5	11.6
Profit on sale of businesses	–	–	–	–	–	30.9
Property and other impairments	–	–	–	–	–	(60.7)
Ferries reorganisation and impairment	–	–	–	–	–	(273.4)
	(15.5)	(12.1)	(0.4)	179.9	151.9	(292.7)

The loss on ineffective hedges arose due to the reduction in net borrowings following the sale of the Group's interest in Royal P&O Nedlloyd.

The other income in 2005 relates to a gain arising from the recovery of insured losses on fixed assets damaged by hurricane Katrina in the US Ports. In 2004 the balance relates to other income received in the year by the Australian operation of the Ports division.

5 Net financing costs

	2005 £m	2004 £m
Financial income		
Interest income and similar items	4.1	6.8
Exchange gains	3.8	–
Gain on refinancing	–	4.6
	7.9	11.4
Financial expenses		
Interest payable and similar items	(60.1)	(92.6)
Debt redemption and other costs	(0.2)	(2.1)
Ineffective portion of cash flow hedges recycled through the income statement	(12.1)	–
Exchange losses	(2.1)	–
Interest capitalised	2.8	5.3
Unwinding of discounts on provisions	(5.4)	(2.7)
Other net financing costs in respect of pension plans	(1.6)	(1.5)
Breakage of swap contracts	–	(1.3)
	(78.7)	(94.9)
Net financing costs	(70.8)	(83.5)

Interest capitalised in the year comprises £1.0m (2004 £1.4m) in respect of property, plant and equipment and £1.8m (2004 £3.9m) in respect of properties held for development and sale. At the year end the aggregate interest capitalised was £2.4m (2004 £2.0m) on property, plant and equipment and £2.1m (2004 £8.1m) on properties held for development and sale.

The net financing costs is before an interest charge of £4.2m (2004 £5.4m) in respect of discontinued operations.

6 Taxation

(a) Analysis of taxation on profit/(loss) on ordinary activities

	2005 £m	2005 £m	2004 £m	2004 £m
UK corporation tax				
Current tax on income for the period		(29.1)		(18.6)
Adjustment in respect of prior periods		4.4		5.3
		(24.7)		(13.3)
Double taxation relief		28.2		17.1
		3.5		3.8
Overseas tax				
Current tax on income for the period	(45.1)		(66.7)	
Adjustment in respect of prior periods	14.3		37.3	
		(30.8)		(29.4)
Total current tax		(27.3)		(25.6)
Deferred tax				
Origination/reversal of temporary differences	1.3		9.8	
Adjustment in respect of prior years	2.0		(5.0)	
		3.3		4.8
Tax on profit/(loss) on ordinary activities		(24.0)		(20.8)

The tax on profit/(loss) on ordinary activities is after a taxation charge of £0.4m (2004 £1.9m) in respect of separately disclosable items.

6 Taxation (continued)**(b) Factors affecting the taxation charge for the current period**

The total taxation charge is lower (2004 higher) than the profit/(loss) on ordinary activities multiplied by the standard rate of corporation tax in the UK, 30 per cent (2004 30 per cent). The differences are explained below:

	2005 %	2005 £m	2004 %	2004 £m
Profit/(loss) on ordinary activities before taxation		100.6		(187.2)
Profit/(loss) on ordinary activities before taxation multiplied by standard rate of corporation tax in the UK of 30 per cent (2004 30 per cent)	30.0	(30.2)	30.0	56.2
Effects of:				
Profits and losses on sale of fixed assets and businesses not subject to taxation	9.2	(9.3)	5.4	10.1
Expenses not deductible and other permanent adjustments	3.1	(3.1)	(0.8)	(1.5)
Unutilised tax losses arising in the year	11.6	(11.7)	(4.2)	(7.9)
Impairments	–	–	(43.4)	(81.2)
Write off of investments	–	–	(3.4)	(6.4)
Tonnage tax in UK Group	(2.2)	2.2	(5.3)	(9.9)
Effect of tax rates in foreign jurisdictions	4.8	(4.8)	(7.5)	(14.0)
Effect of joint ventures and associates	(12.2)	12.3	(2.0)	(3.8)
Adjustments in respect of prior periods	(20.5)	20.6	20.1	37.6
Taxation charge for the year	23.8	(24.0)	(11.1)	(20.8)

The profit before tax of £100.6m (2004 £187.2m loss) includes the Group's share of profits of joint ventures and associates within continuing operations of £40.0m (2004 £30.5m) which is net of a tax charge of £11.1m (2004 £8.4m). In addition, the profit on discontinued items of £213.5m (2004 £56.5m) is net of a tax charge of £5.8m (2004 £4.9m).

The Group's principal shipping businesses operate under the UK tonnage tax regime under which the current year tax charge arising is calculated by reference to the net tonnage of the ships operated by the business rather than the tax adjusted profit or loss of the business.

The Group's overseas tax rates are typically a mixture of rates higher and lower than 30 per cent. They include the effect of overseas tax benefits available to some infrastructure projects.

The prior year credit of £20.6m (2004 £37.6m) arises from the finalisation and agreement of tax computations for years up to and including the year ended 31 December 2004 for companies in the UK and overseas.

7 Dividends on share capital

Dividends paid are as follows:	2005 £m	2004 £m
Deferred stock	(66.2)	(87.8)
Preferred stock	(0.1)	(0.1)
5.5% concessionary stock	(3.7)	(3.7)
	(70.0)	(91.6)

After the balance sheet date a dividend of 6.0p per £1 nominal of deferred stock was proposed by the directors in respect of 2005 (2004 6.0p). This dividend has not been provided.

8 Discontinued operations and non-current assets held for sale

Discontinued operations

In June 2005 the Group sold its 25 per cent holding in Royal P&O Nedlloyd N.V. ("RPONL"), which represented the entire Container Shipping division (a separate business segment see note 2).

The holding was sold for £381.0m cash before costs, resulting in a pre and post tax gain of £188.0m.

RPONL was an associated company and the only cash flow in the six months ended 30 June 2005 was a dividend receipt of £6.9m.

The effect of the disposal was a decrease in net assets of the Group of £191.2m, before taking account of the cash consideration received of £381.0m.

In December 2005, the Group sold its Cold Logistics business (a separate business segment see note 2). The division was sold for £173.2m before costs and working capital adjustments, resulting in a pre tax loss of £14.5m and a tax charge of £0.5m. The proceeds comprised £140.2m in cash and £33.0m in the form of convertible debentures.

During the year ended 31 December 2005, the Group's Cold Logistics business earned revenue of £222.8m (2004 £205.6m), less net expenses of £199.7m (2004 £196.4m) and finance charges of £4.2m (2004 £5.4m), generating a pre-tax profit of £18.9m (2004 £3.8m) and related income tax charge of £3.6m (2004 £1.5m). It contributed £22.8m (2004 £26.8m) to the Group's net operating cash flow, generated £7.5m (2004 £0.6m) cash inflow from investing activities, and utilised £6.5m (2004 £4.5m) in respect of financing activities.

Non-current assets held for sale

As part of normal asset management, it has been decided that a warehouse in Portsmouth within the Ferries division will be sold. A sale is expected in 2006 and accordingly the warehouse has been presented as a non-current asset held for sale of £1.1m. There has been no impairment recognised relating to this asset.

9 Earnings per £1 nominal of deferred stock

The calculations of the basic earnings per £1 nominal of deferred stock of 37.4p (2004 (22.6)p) are based on the earnings for the financial year attributable to deferred stockholders of £276.0m (2004 £165.4m loss) and the weighted average number of £1 nominal of deferred stock of 745.1m (2004 731.9m).

	2005 £m	2004 £m
Profit for the year attributable to equity stock holders of the parent	279.8	(161.6)
Less profit attributable to preferred and concessionary stock holders	(3.8)	(3.8)
Basic and diluted earnings attributable to deferred stock holders	276.0	(165.4)

The diluted earnings per £1 nominal of deferred stock 37.0p (2004 (22.6)p) has been calculated by reference to an adjusted average number of £1 nominal of deferred stock as follows:

	2005 £m	2004 £m
Weighted average per basic calculation	737.9	731.9
Adjustment to reflect dilutive deferred stock under option	7.2	–
	745.1	731.9

The diluted loss per £1 nominal of deferred stock in 2004 was the same as the basic loss per £1 nominal of deferred stock as the issue of additional stock arising on exercise of options would reduce the loss per £1 nominal of deferred stock and therefore these are not dilutive under IAS 33.

Earnings per share from continuing and discontinued operations can be calculated based upon the information presented in the income statement.

9 Earnings per £1 nominal of deferred stock (continued)

Reconciliation of underlying earnings:

	2005 £m	2004 £m
Profit/(loss) for the financial year	290.1	(151.5)
Less:		
Dividends to preference stockholders	(3.8)	(3.8)
Profit attributable to minority interests	(10.3)	(10.1)
Profit/(loss) for the financial year attributable to deferred stockholders (Basic and diluted earnings/(loss))	276.0	(165.4)
Adjusted for separately disclosable items net of tax:		
Relocation, reorganisation and impairment	15.0	334.1
Loss on ineffective hedges	12.1	–
Profit on sale of discontinued operations	(177.8)	(10.7)
(Loss)/profit on sale of property, plant and equipment	(3.0)	11.8
Takeover costs	3.3	–
Other income	(1.5)	(11.6)
Profit on sale and termination of businesses	–	(30.9)
Underlying earnings	124.1	127.3
Less: Profit from discontinued operations	(33.6)	(53.0)
Underlying earnings from continuing operations	90.5	74.3
Underlying EPS	16.8p	17.4p
Underlying EPS from continuing operations	12.3p	10.2p

Underlying earnings are calculated by adjusting underlying profit after tax (page 116) for profit attributable to minority interests and preference stockholders.

As set out under “Transitional arrangements” in note 36, the Group has applied IAS 32 and IAS 39 from 1 January 2005. The Group has applied the exemption available in IFRS 1 that allows comparatives not to be restated for IAS 32 and IAS 39, accordingly the comparative amounts reported for the year ended 31 December 2004 are in accordance with UK GAAP.

The effect on the income statement of applying these two standards in the year ended 31 December 2005 is not material and, accordingly, there is no impact on earnings per £1 nominal of deferred stock as reported above.

10 Intangible assets

	Goodwill £m
Cost at 1 January 2004	217.0
Exchange movements	(4.8)
Disposals	(2.3)
Cost at 31 December 2004	209.9
Exchange movements	7.4
Disposals	(15.4)
Cost at 31 December 2005	201.9
Impairment losses at 1 January 2004	(0.9)
Exchange movements	–
Impairments	(116.3)
Impairment losses at 31 December 2004	(117.2)
Exchange movements	–
Impairments	–
Disposals	0.8
Impairment losses at 31 December 2005	(116.4)
At 31 December 2005	85.5
At 31 December 2004	92.7

10 Intangible assets (continued)**Impairment tests for cash-generating units containing goodwill**

The following units have significant carrying amounts of goodwill:

	2005 £m	2004 £m
Ports	85.5	79.0
Cold Logistics	–	13.7
	85.5	92.7

Goodwill principally arises in respect of ports in North America, Belgium and Australia. The directors have determined each port to be an Income Generating Unit (IGU), as each represents the smallest identifiable group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. Goodwill arising on acquisition at these ports is included within representative IGUs. The recoverable amount of each of the IGUs is based on value in use calculations.

The value in use for each IGU was calculated with reference to the net present value of the future cash inflows projected to be derived from its assets, using cash flows based on approved five year plans. These plans are consistent with expectations of growth in local economies. The plans include assumptions regarding cash flows based upon management's expectations of the performance of each port over the period. The discount rate applied to these projections was based on the estimated weighted average cost of capital for the port location, adjusted for the related underlying tax. The weighted average of the effective pre-tax discount rates used was 6.3 per cent.

The impairment in 2004 was principally the result of a review performed on an IGU by IGU basis following the Fundamental Business Review of the Ferries division. These reviews have been reperformed in 2005. This exercise did not indicate a requirement to adjust the impairments made in 2004.

There is no impairment charge for the Group during the year.

11 Prepaid leases

	£m
Cost at 1 January 2004	158.1
Exchange movements	(3.6)
Cost at 31 December 2004	154.5
Exchange movements	15.3
Cost at 31 December 2005	169.8
Amortisation at 1 January 2004	(6.4)
Exchange movements	0.5
Amortisation charge for the year	(3.6)
Amortisation at 31 December 2004	(9.5)
Exchange movements	(1.4)
Amortisation charge for the year	(5.4)
Amortisation at 31 December 2005	(16.3)
At 31 December 2005	153.5
At 31 December 2004	145.0

12 Property, plant and equipment

	Property		Ships		Plant and machinery, fixtures and fittings		Total £m
	Freehold £m	Leasehold £m	Owned £m	Leased £m	Owned £m	Leased £m	
Cost at 1 January 2004	174.5	358.6	540.0	140.5	1,030.0	24.5	2,268.1
Exchange movements	(6.7)	(8.7)	(0.4)	(0.8)	(36.8)	(0.7)	(54.1)
On acquisition of subsidiaries and businesses	–	–	–	–	0.6	–	0.6
Additions	11.5	48.2	7.7	1.9	86.5	9.8	165.6
Purchase of leased assets	–	–	32.1	(32.1)	8.5	(8.5)	–
Reclassification between categories	(2.5)	0.7	–	–	2.5	(0.7)	–
Disposals	(12.0)	(14.2)	(178.7)	(34.0)	(70.6)	(0.8)	(310.3)
On disposal of subsidiaries	(98.9)	(37.1)	(3.8)	–	(39.6)	–	(179.4)
Cost at 31 December 2004	65.9	347.5	396.9	75.5	981.1	23.6	1,890.5
Exchange movements	3.6	23.9	2.6	0.7	51.0	1.0	82.8
Additions	8.1	53.5	4.5	1.0	121.0	0.8	188.9
Purchase of leased assets	–	–	26.8	(26.8)	0.3	(0.3)	–
Reclassification between categories	0.4	0.3	–	–	(0.4)	(0.3)	–
Transfer to properties held for development and sale	–	(0.4)	–	–	–	–	(0.4)
Transfer to assets classified as held for sale	(1.5)	–	–	–	–	–	(1.5)
Disposals	(6.5)	(15.5)	(32.8)	(4.3)	(60.4)	(2.6)	(122.1)
On disposal of subsidiaries	(34.0)	–	–	–	(206.3)	(4.8)	(245.1)
Cost at 31 December 2005	36.0	409.3	398.0	46.1	886.3	17.4	1,793.1
	Property		Ships		Plant and machinery, fixtures and fittings		Total £m
	Freehold £m	Leasehold £m	Owned £m	Leased £m	Owned £m	Leased £m	
Depreciation and amortisation at 1 January 2004	(6.0)	(68.6)	(175.9)	(29.5)	(419.0)	(13.5)	(712.5)
Exchange movements	0.4	2.6	0.1	0.4	9.0	0.1	12.6
Depreciation and amortisation charge for the year	(2.7)	(14.3)	(28.6)	(4.2)	(62.2)	(1.6)	(113.6)
Impairments	–	(12.2)	(40.8)	(7.4)	(28.4)	–	(88.8)
Purchase of leased assets	–	–	(4.6)	4.6	(7.9)	7.9	–
Reclassification between categories	–	(0.7)	–	–	–	0.7	–
Disposals	0.1	5.6	155.8	7.2	46.5	0.8	216.0
On disposal of subsidiaries	5.9	3.3	1.1	–	19.2	–	29.5
Depreciation and amortisation at 31 December 2004	(2.3)	(84.3)	(92.9)	(28.9)	(442.8)	(5.6)	(656.8)
Exchange movements	(0.2)	(2.3)	(1.5)	(0.4)	(17.7)	(0.8)	(22.9)
Depreciation and amortisation charge for the year	(0.2)	(13.3)	(21.2)	(2.2)	(65.8)	(1.8)	(104.5)
Purchase of leased assets	–	–	(15.3)	15.3	–	–	–
Transfer to assets classified as held for sale	0.4	–	–	–	–	–	0.4
Disposals	–	2.9	23.2	4.3	46.8	2.4	79.6
On disposal of subsidiaries	–	–	–	–	70.5	1.4	71.9
Depreciation and amortisation at 31 December 2005	(2.3)	(97.0)	(107.7)	(11.9)	(409.0)	(4.4)	(632.3)
At 31 December 2005	33.7	312.3	290.3	34.2	477.3	13.0	1,160.8
At 31 December 2004	63.6	263.2	304.0	46.6	538.3	18.0	1,233.7

- (a) Plant and machinery, fixtures and fittings in the above table includes assets under construction totalling £27.7m (2004 £39.2m).
- (b) In 2004 the Group recognised impairments totalling £88.8m of which £73.6m arose in Ferries following the Fundamental Business Review. The impairment reviews were updated in 2005 and no further impairments were required.

13 Investments in joint ventures and associates

	Investment in joint ventures £m	Investment in associates £m	Joint venture and associate loans £m	Total £m
Cost at 1 January 2004	454.1	104.6	54.5	613.2
Exchange movements	(23.9)	(14.8)	(1.6)	(40.3)
Additions	11.6	13.3	25.6	50.5
Transfers between categories	(138.1)	138.1	–	–
Transfer from other investments	–	0.9	–	0.9
Transfer on acquisitions as subsidiaries	(0.6)	–	(31.9)	(32.5)
On acquisition of subsidiaries	0.6	–	(1.0)	(0.4)
Share of retained profits/(losses) for the year before impairment	0.1	57.0	–	57.1
Group share of actuarial gains/(losses)	4.0	(10.0)	–	(6.0)
Disposals/repayments	(140.6)	(1.1)	(4.0)	(145.7)
Transfer on sell down to associates	–	–	4.6	4.6
Cost at 31 December 2004	167.2	288.0	46.2	501.4
Effect of adoption of IAS 32 and IAS 39 on 1 January 2005	–	3.1	–	3.1
At 1 January 2005	167.2	291.1	46.2	504.5
Exchange movements	11.6	28.7	4.1	44.4
Additions	1.1	13.7	20.3	35.1
Transfers from other investments	–	0.7	–	0.7
Share of retained profits/(losses) for the year before impairment	(1.7)	18.9	–	17.2
Group share of actuarial gains/(losses)	–	(8.7)	–	(8.7)
Group share of fair value movements	1.5	(6.4)	–	(4.9)
Disposals/repayments	(6.0)	(193.0)	(2.7)	(201.7)
Cost at 31 December 2005	173.7	145.0	67.9	386.6
Provisions at 1 January 2004	–	–	(1.5)	(1.5)
Transfer on acquisitions as subsidiaries	–	–	1.5	1.5
Provisions at 31 December 2004 and 31 December 2005	–	–	–	–
At 31 December 2005	173.7	145.0	67.9	386.6
At 31 December 2004	167.2	288.0	46.2	501.4

- (a) The Group's loans to joint ventures and associates totalled £49.4m (2004 £43.4m) and £18.5m (2004 £2.8m) respectively.
- (b) The Group's investment in joint ventures at 31 December 2005 totalled £223.1m (2004 £210.6m). This is made up of non-current assets of £281.1m (2004 £225.7m), current assets of £131.4m (2004 £124.8m), current liabilities of £142.9m (2004 £54.2m) and non-current liabilities of £46.5m (2004 £85.7m). Non-current assets include goodwill arising on the Group's acquisition of joint ventures of £7.8m (2004 £7.9m).
- (c) The Group's investment in associates at 31 December 2005 totalled £163.5m (2004 £290.8m). This is made up of non-current assets of £254.2m (2004 £465.8m), current assets of £49.1m (2004 £207.4m), current liabilities of £124.9m (2004 £373.7m) non-current liabilities of £14.9m (2004 £8.7m). The Group's share of revenue from associates was £565.2m (2004 £741.0m). Non-current assets include goodwill arising on the Group's acquisition of associates of £0.7m (2004 £nil).
- (d) The Group's share of the pre-tax profit of joint ventures and associates was £19.8m (2004 £18.3m) and £56.6m (2004 £72.6m) respectively.
- (e) On 29 June 2005 the Group sold its 25 per cent interest in Royal P&O Nedlloyd N.V. Total proceeds of £381.0m (€56.25 per share) before costs were received on 30 June 2005 and resulted in a gain of £188.0m.
- (f) During the year the Group's trading with joint ventures and associates included £47.3m (2004 £57.2m) received from P&O Nedlloyd. The Group's operating profit also includes £5.4m (2004 £4.6m) in respect of management and guarantee fees from joint ventures and associates during the year, in addition to the Group's share of joint ventures' and associates' results.

13 Investments in joint ventures and associates (continued)

(g) The principal joint ventures and associates are shown on page 115. Joint ventures and associates are stated at the Group's share of underlying net assets plus any goodwill on acquisition. The issued share capital of the principal joint ventures and associates at 31 December 2005 was as follows:

	Number in issue	Nominal value of each class of share capital and issued debt	Percentage held
Joint ventures			
PT Terminal Petikemas Surabaya	255,768,115	IR 1 ordinary shares	49
Port Newark Container Terminal LLC	–	Limited partnership	50
Portsynergy SAS	1,700,000	€10 ordinary shares	50
Associates			
Antwerp Gateway N.V.	6,200	€10 ordinary shares	42.5
Laem Chabang International Terminal Co Ltd	75,000,000	Bht 10 ordinary shares	34.5
Manutention General Mediterranee SA ("Marseille")	1,213,315	€0.5 ordinary shares	20.4
Manutention Terminal Nord Developpement SA ("Le Havre")	90,000	€15.24 ordinary shares	36.7
Qingdao Qianwan Container Terminal	–	Equity partnership	29
Shekou Container Terminals Ltd	–	Equity partnership	22
South Asia Gateway Terminals Pte Ltd	378,848,590	Rs10 ordinary shares	16.2
Tilbury Container Services Ltd	51	£1 'P' shares	100
	50	£1 'T' shares	–
	49	£1 'A' shares	–

14 Deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2005 £m	2004 £m	2005 £m	2004 £m	2005 £m	2004 £m
Property, plant and equipment	(0.1)	(2.9)	87.6	86.7	87.5	83.8
Intangible assets	(0.4)	(0.5)	0.5	0.5	0.1	–
Investment in joint ventures	–	–	7.3	6.9	7.3	6.9
Other investments	–	–	0.5	0.9	0.5	0.9
Inventories	(0.1)	(0.1)	–	–	(0.1)	(0.1)
Employee benefits	(14.4)	(16.0)	0.6	2.1	(13.8)	(13.9)
Provisions	(13.8)	(8.2)	–	–	(13.8)	(8.2)
Tax value of loss carry-forwards recognised	(6.9)	(6.2)	–	–	(6.9)	(6.2)
Other	(7.8)	(5.7)	5.3	9.1	(2.5)	3.4
Tax (assets)/liabilities	(43.5)	(39.6)	101.8	106.2	58.3	66.6
Tax set off	37.0	22.9	(37.0)	(22.9)	–	–
Net tax (assets)/liabilities	(6.5)	(16.7)	64.8	83.3	58.3	66.6

At 31 December 2005, a deferred tax liability of £103.7m (2004 £92.3m) relating to investment in subsidiaries has not been recognised because the Company controls whether the liability will be incurred and it is satisfied that it will not be incurred in the foreseeable future. £32.3m of this liability (2004 £25.0m) may be covered by losses for which no asset is recognised (see below).

The UK tonnage tax regime includes provision whereby a proportion of capital allowances previously claimed by the Group may be subject to tax in the event of a significant number of ships owned at the time the Group entered tonnage tax being sold and not replaced. This contingent liability diminishes to nil over the period to 31 December 2008. At 31 December 2005, the Group's contingent liability in respect of this provision would be £5.4m (2004 £7.4m) on the assumption that all ships and related assets are sold at book value and not replaced.

Unrecognised deferred tax assets

	2005 £m	2004 £m
Deductible temporary differences	33.3	35.0
Tax losses	64.6	46.5
	97.9	81.5

Deferred tax is not recognised on losses where it is not probable that future taxable profits will be available against which the losses can be utilised or where agreement of the losses and/or the ability to offset the losses against future taxable profits is uncertain.

14 Deferred tax assets and liabilities (continued)**Movement in temporary differences during the year**

	Balance 1 January 2004 £m	Exchange movement £m	Recognised in income £m	Recognised in equity £m	Balance 31 December 2004 £m
Property, plant and equipment	84.4	(2.8)	2.2	–	83.8
Intangible assets	(0.1)	–	0.1	–	–
Investment in joint ventures	5.2	–	1.7	–	6.9
Other investments	0.9	–	–	–	0.9
Inventories	–	–	(0.1)	–	(0.1)
Employee benefits	(9.6)	–	1.8	(6.1)	(13.9)
Provisions	3.2	(0.2)	(11.2)	–	(8.2)
Tax value of loss carry-forwards utilised	(4.2)	0.4	(2.4)	–	(6.2)
Other items	3.2	0.2	–	–	3.4
	83.0	(2.4)	(7.9)	(6.1)	66.6

	Balance 31 December 2004 £m	Adoption of IAS 39 £m	Balance 1 January 2005 £m	Exchange movement £m	Recognised in income £m	Recognised in equity £m	Balance 31 December 2005 £m
Property, plant and equipment	83.8	–	83.8	3.7	–	–	87.5
Intangible assets	–	–	–	–	0.1	–	0.1
Investment in joint ventures	6.9	–	6.9	–	0.4	–	7.3
Other investments	0.9	–	0.9	–	(0.4)	–	0.5
Inventories	(0.1)	–	(0.1)	–	–	–	(0.1)
Employee benefits	(13.9)	–	(13.9)	(0.1)	(1.8)	2.0	(13.8)
Provisions	(8.2)	–	(8.2)	(0.3)	(5.3)	–	(13.8)
Tax value of loss carry-forwards utilised	(6.2)	–	(6.2)	(0.6)	(0.1)	–	(6.9)
Other items	3.4	(0.6)	2.8	0.1	(5.3)	(0.1)	(2.5)
	66.6	(0.6)	66.0	2.8	(12.4)	1.9	58.3

15 Tax recoverable and income tax liabilities

Current income tax liabilities of £89.1m (2004 £105.7m) represents amounts of corporate tax payable in respect of current and prior periods.

The current tax recoverable of £nil (2004 £0.8m) represents amounts of corporate tax recoverable.

16 Properties held for development and sale

	USA £m	UK £m	Other £m	Total £m
At 1 January 2004	288.8	164.2	297.2	750.2
Exchange movements	(12.7)	–	(4.3)	(17.0)
On acquisition of subsidiaries and businesses	–	43.7	–	43.7
Additions	13.4	82.5	0.3	96.2
Disposals	(160.7)	(73.3)	(70.7)	(304.7)
Write down	–	(4.6)	(55.3)	(59.9)
At 31 December 2004	128.8	212.5	167.2	508.5
Exchange movements	10.9	–	(5.5)	5.4
Transfer from property, plant and equipment	–	0.4	–	0.4
Additions	6.5	69.1	–	75.6
Disposals	(79.2)	(215.2)	(142.0)	(436.4)
Write down	–	(0.6)	(3.1)	(3.7)
At 31 December 2005	67.0	66.2	16.6	149.8

Costs in respect of the separate London Gateway Port and Business Park proposals total £38.1m (2004 £29.1m). These costs included above are shown within the net operating assets (note 2(h)) respectively of the Ports and Property divisions. The projects received "minded to grant" approvals from respective Secretaries of State in July 2005 specifying certain issues which needed to be resolved before planning consents would be granted. Progress has been made on these issues and final decisions on planning consents are expected in the first half of 2006.

17 Inventories

	2005 £m	2004 £m
Raw materials and consumables	16.4	16.0
Work in progress	6.5	8.1
Goods for resale	13.7	19.1
	36.6	43.2

18 Trade and other receivables

	2005		2004	
	Current £m	Non current £m	Current £m	Non current £m
Trade receivables	224.8	1.5	253.3	1.4
Amounts owed by associates	–	–	0.9	–
Other receivables	170.2	–	88.2	3.5
Prepayments and accrued income	77.8	2.5	67.8	2.3
Employee benefits assets (note 28)	–	2.5	–	–
Fair value of derivative financial instruments	2.6	2.7	–	–
	475.4	9.2	410.2	7.2
	484.6		417.4	

Other receivables include £55.2m (2004 £35.7m) relating to previous corporate disposals, net of provisions, of which £nil (2004 £3.4m) falls due in more than 1 year. Included within amounts receivable relating to previous corporate disposals is an amount outstanding of £42.6m (2004 £32.2m) net of relevant provisions arising following the sale of Bovis Group plc in 1999. Further information on this is set out on page 79.

The current expectation is that all current trade and other receivables will be received prior to 31 December 2006.

19 Other investments

Current	2005 £m	2004 £m
Available-for-sale financial assets	34.6	–
Unlisted investments	–	5.2
	34.6	5.2

The available-for-sale financial assets in the above table represent Versacold Income Fund 7% Extendible Convertible Unsecured Subordinated Debentures acquired by the Group on disposal of P&O Cold Logistics on 19 December 2005. Under the terms of this transaction, the Group has committed to retain ownership of these debentures for at least four months from that date.

Non-current	2005 £m	2004 £m
Debt securities held-to-maturity	11.2	–
Available-for-sale financial assets	3.2	–
Unlisted investments	–	11.2
	14.4	11.2

20 Cash and cash equivalents

	2005 £m	2004 £m
Bank balances	67.4	40.6
Call deposits	32.1	9.6
Cash and cash equivalents in the balance sheet	99.5	50.2
Bank overdrafts	(17.3)	(20.8)
Cash and cash equivalents in the statement of cash flows	82.2	29.4

21 Interest bearing loans and borrowings

	2005 £m	2004 £m
US dollar bonds and notes 2007 – 2027 (unsecured)	13.5	12.0
Term loans: secured	34.9	284.6
unsecured	590.3	850.8
Finance leases	43.4	58.9
Mortgage debenture stocks	1.4	1.4
Unsecured loan stock	3.3	3.3
	686.8	1,211.0

All the above loans are non-convertible.

Secured loans and other secured creditors are secured on ships, properties and other assets of the Group.

Group loans are denominated in the following currencies:

	Sterling £m	US dollars £m	Canadian dollars £m	Australian dollars £m	Euro £m	Indian rupees £m	Other £m	Total £m
At 31 December 2005	163.8	90.1	85.3	66.0	13.4	176.6	91.6	686.8
At 31 December 2004	398.3	275.4	43.9	128.5	156.7	126.1	82.1	1,211.0

An analysis of the maturity and interest rates of Group fixed rate loans is as follows:

The fixed rate bands below include the effect of interest rate swaps with net principal value totalling £242.3m (2004 £496.3m).

Interest rate	Repayable					2005 Total £m	2004 Total £m
	Within one year £m	Between one and two years £m	Between two and five years £m	Between five and ten years £m	Over ten years £m		
6% or less	28.8	36.2	67.8	74.3	2.3	209.4	433.9
Over 6% to 8%	4.8	20.8	127.2	5.3	7.9	166.0	345.6
Over 8%	8.2	12.2	29.5	1.1	2.5	53.5	57.8
At 31 December 2005	41.8	69.2	224.5	80.7	12.7	428.9	
At 31 December 2004	43.5	68.1	597.2	110.4	18.1		837.3

An analysis of the maturity of total Group loans is as follows:

At 31 December 2005	30.6	40.1	539.0	41.2	35.9	686.8
At 31 December 2004	79.7	323.0	713.7	51.4	43.2	1,211.0

The maturity profile of the Group's financial liabilities at 31 December 2005 was as follows:

	2005 £m	2004 £m
In one year or less, or on demand	47.9	100.5
In more than one year, but not more than two years	40.1	323.0
In more than two years, but not more than five years	565.6	719.8
In more than five years	77.1	94.6
	730.7	1,237.9

The undrawn committed facilities available at 31 December 2005 in respect of which all conditions precedent had been met at that date were as follows:

	2005 £m	2004 £m
Expiring in one year or less	4.4	164.0
Expiring in more than one year, but not more than two years	4.9	306.0
Expiring in more than two years	677.0	190.6
	686.3	660.6

As a result of the change of control following the DP World takeover on 8 March 2006 (see note 34) facilities totalling £1,084.6m may be cancelled at the bank's option. DP World has arranged sufficient acquisition finance to allow any amounts drawn under these facilities to be repaid as they fall due.

21 Interest bearing loans and borrowings (continued)**Finance lease liabilities**

Finance lease liabilities are payable as follows:

	Minimum lease	Interest	Principal	Minimum lease	Interest	Principal
	payments			payments		
	2005	2005	2005	2004	2004	2004
	£m	£m	£m	£m	£m	£m
Less than one year	5.8	2.3	3.5	16.5	3.2	13.3
Between one and five years	19.8	6.6	13.2	23.1	7.9	15.2
More than five years	37.4	10.7	26.7	42.1	11.7	30.4
	63.0	19.6	43.4	81.7	22.8	58.9

22 Trade and other payables

	2005		2004	
	Current	Non-current	Current	Non-current
	£m	£m	£m	£m
Payments received on account	6.9	–	8.8	–
Trade payables	126.1	0.2	128.0	–
Amounts owed to joint ventures and associates	65.1	8.3	20.0	50.1
Social security and other taxation	13.6	–	17.8	–
Other payables: secured	–	–	0.3	–
unsecured	61.1	0.3	67.7	0.2
Accruals and deferred income	142.2	9.1	140.6	5.9
Fair value of derivative financial instruments	9.4	17.2	–	–
	424.4	35.1	383.2	56.2
	459.5		439.4	

The current expectation is that all current trade and other payables will be paid prior to 31 December 2006.

23 Provisions

	Employee	Reorganisation	Other	Total
	compensation	and	provisions	
	£m	restructuring	£m	£m
At 1 January 2005	33.0	73.5	28.5	135.0
Exchange movements	4.4	–	(0.7)	3.7
Transfers from profit and loss account	10.8	9.7	48.1	68.6
Transfers to profit and loss account	–	(6.9)	(0.1)	(7.0)
Change in actuarial assumptions	2.9	–	–	2.9
On disposal of subsidiaries	–	–	(0.8)	(0.8)
Applied during the year	(5.8)	(50.4)	(27.2)	(83.4)
At 31 December 2005	45.3	25.9	47.8	119.0
Disclosed as:				
Current	7.2	23.2	20.8	51.2
Non-current	38.1	2.7	27.0	67.8
	45.3	25.9	47.8	119.0

The reorganisation and restructuring provision includes an amount of £4.5m (2004 £nil) for onerous leases as a result of the Group's relocation to its new offices in December 2005.

Other provisions include £21.4m (2004 £nil) in respect of rental guarantees for properties in Germany and the UK, £3.4m (2004 £4.3m) for onerous leases over several properties in the UK and £6.4m (2004 £4.1m) relating to the repayment of state aid following an EC ruling. Transfers from the profit and loss account for the year include a charge of £2.5m (2004 £2.7m) for the unwinding of discounts on provisions.

The directors expect the current provision balance to be utilised prior to 31 December 2006.

24 Issued capital

The authorised share capital is £956.5m (2004 £956.5m) being the allotted capital together with £134.3m (2004 £143.0m) of unclassified stock. The nominal value of each class of stock unit is £1.

The allotted, called up and fully paid share capital is as follows:

	2005 £m	2004 £m
Deferred stock	752.3	743.6
Preferred stock	3.3	3.3
5.5% concessionary stock	66.6	66.6
	822.2	813.5

Rights at 31 December 2005

The rights attached to preferred and concessionary stock at 31 December 2005 are summarised below:

Holders of preferred stock, which ranked before all other stock, received a discretionary fixed cumulative dividend of 5 per cent per annum (net of tax credit). On a liquidation they were entitled to receive, subject to the rights of preferential creditors, a return of capital together with all unpaid dividend arrears and accruals and a premium based upon the average price of the stock in the six months preceding the liquidation. Holders were entitled to one vote for each unit of stock held, both on a show of hands and on a poll.

Holders of the 5.5 per cent concessionary stock, which ranked after the preferred stock, received a discretionary fixed non-cumulative dividend of 5.5 per cent per annum (net of tax credit). Should the directors terminate the concessionary fare scheme, this dividend would be replaced by an annual fixed cumulative dividend equal to or exceeding 5.5 per cent (net of tax credit) so that the market price of the stock at the date of termination is at least 100p per £1 nominal of stock. In such circumstances the stock would be redeemed with a 20p premium within six months of the date of termination. On a liquidation they were entitled to receive, subject to the rights of preferential creditors, all unpaid dividends and the amount paid up on their stock. Holders were entitled to one vote on a show of hands and on a poll to one vote for every £4 nominal of stock held.

Changes since 31 December 2005

The following changes took place in consequence of the approval of schemes of arrangement under section 425 Companies Act 1985 between P&O and the holders of the deferred stock (the 'Deferred Scheme') and the concessionary stock (the 'Concessionary Scheme').

Following approval by stockholders of the Deferred Scheme on 13 February 2006 and the Court's sanction on 2 March 2006, on 7 March 2006 £1,000 nominal of special deferred stock (new deferred stock which temporarily had additional rights attached in connection with the implementation of the Schemes) was allotted and issued to Thunder FZE ("Thunder") and its nominee Ports, Customs and Free Zone Corporation ("DP World"). On 8 March 2006 the existing deferred stock (other than that in respect of which stockholders had elected to receive loan notes) was cancelled and deferred stockholders received 520p per £1 nominal of deferred stock. An amount of new deferred stock equal to the amount of deferred stock cancelled on 8 March 2006 has been allotted and issued to Thunder and its nominee DP World, in proportion to their respective holdings of special deferred stock.

On 13 February 2006, stockholders approved the cancellation of the preferred stock conditional upon the implementation of the Deferred Scheme. On 8 March 2006, the principal amount of £3,344,000 was cancelled and a total amount of £3,416,836 (representing the principal and an accrued dividend of 2.17808p per unit of preferred stock) was paid to the preferred stockholders on 16 March 2006.

On 13 February 2006 stockholders approved, and on 2 March 2006 the Court sanctioned, the Concessionary Scheme, under which on 16 March 2006 concessionary stockholders received £1.20 for each unit of concessionary stock held or, at their option, £1.00 plus a unit of entitlement to discounted fares on certain P&O ferry routes (a 'Concessionary Unit') conferring the same concessionary travel benefits as the concessionary stock. On 8 March 2006 the concessionary stock was cancelled and an equal amount of new deferred stock was allotted and issued to Thunder and its nominee DP World.

The movements in deferred stock in the year were as follows:

	Deferred stock £
At 1 January 2005	743,557,989
Exercise of options granted under stock option schemes	8,740,848
At 31 December 2005	752,298,837

The movements during the year in rights of subscription for, or rights of conversion into, deferred stock were as follows:

	At 1 January 2005 £	Granted £	Lapsed £	Exercised £	At 31 December 2005 £
Executive stock option schemes	35,247,101	-	(1,439,302)	(8,172,938)	25,634,861
1994 Save As You Earn Stock Option Scheme/ 2004 Sharesave Plan	8,062,296	1,128,770	(930,168)	(567,910)	7,692,988
	43,309,397	1,128,770	(2,369,470)	(8,740,848)	33,327,849

24 Issued capital (continued)

The executive stock options were generally exercisable not later than 15 April 2014 at prices between 166p and 266p per £1 nominal of deferred stock.

The Save As You Earn Stock Options and the Sharesave Plan options were exercisable not later than 17 April 2009 at prices between 128p and 270p per £1 nominal of deferred stock.

Following the takeover of the Group by DP World on 8 March 2006, all of the above options became exercisable from that date. Any options remaining unexercised will lapse on 7 September 2006.

25 Capital and reserves

	Share capital £m	Share premium account £m	Translation reserve £m	Hedging reserve £m	Other reserves £m	Retained earnings £m	Total £m	Minority interest £m	Total equity £m
At 1 January 2004	807.6	778.3	–	–	163.7	(706.6)	1,043.0	40.7	1,083.7
Total recognised income and expense	–	–	(52.1)	–	–	(211.3)	(263.4)	8.6	(254.8)
Exercise of options granted under stock option schemes	5.9	6.7	–	–	–	–	12.6	–	12.6
Debt redemption costs	–	(1.6)	–	–	–	1.6	–	–	–
Amortisation of debt issue costs	–	(0.5)	–	–	–	0.5	–	–	–
Purchases of own stock	–	–	–	–	–	(14.2)	(14.2)	–	(14.2)
Share-based payments	–	–	–	–	–	4.5	4.5	–	4.5
Dividends to stockholders	–	–	–	–	–	(91.6)	(91.6)	–	(91.6)
Changes in composition and dividends	–	–	–	–	–	–	–	(2.5)	(2.5)
At 31 December 2004	813.5	782.9	(52.1)	–	163.7	(1,017.1)	690.9	46.8	737.7
Effect of adoption of IAS 32 and 39 on 1 January 2005	–	–	–	(23.0)	–	(4.2)	(27.2)	–	(27.2)
At 1 January 2005	813.5	782.9	(52.1)	(23.0)	163.7	(1,021.3)	663.7	46.8	710.5
Total recognised income and expense	–	–	69.2	14.8	–	121.7	205.7	10.1	215.8
Exercise of options granted under stock option schemes	8.7	9.5	–	–	–	–	18.2	–	18.2
Amortisation of debt issue costs	–	(0.2)	–	–	–	0.2	–	–	–
Purchases of own stock	–	–	–	–	–	(5.8)	(5.8)	–	(5.8)
Share-based payments	–	–	–	–	–	5.4	5.4	–	5.4
Dividends to stockholders	–	–	–	–	–	(70.0)	(70.0)	–	(70.0)
Changes in composition and dividends	–	–	–	–	–	–	–	(2.9)	(2.9)
At 31 December 2005	822.2	792.2	17.1	(8.2)	163.7	(969.8)	817.2	54.0	871.2

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations that are not integral to the operations of the Company, as well as from the effective portion of translation of liabilities that hedge the Company's net investment in a foreign subsidiary.

Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

Retained earnings

The P&O Group Employee Benefit Trust (the "Trust") is used in connection with the Group's Deferred Bonus and Co-investment Matching Plan (the "Matching Plan"), the P&O Performance Share Plan (the "Performance Share Plan") and the P&O 2005 Matching Share Plan (the "2005 Matching Share Plan"), the terms of which are set out in the directors' remuneration report on pages 28 to 35. The Trust may also be used in connection with the Group's other share based plans, including the Executive Stock Option Plan. The Trustee of the Trust purchases the Company's stock in the open market, as required, on the basis of regular reviews of the anticipated liabilities of the Group, with financing provided by the Company. All expenses of the Trust are settled directly by the Company and charged in the financial statements as incurred.

As at 31 December 2005 the Trust held £12,096,283 nominal of deferred stock of the Company (2004 £11,435,110 nominal) representing 1.6 per cent (2004 1.5 per cent) of the Company's deferred stock. During the year the Trust acquired £1,900,000 nominal of deferred stock of the Company (2004 £4,934,437 nominal), representing 0.3 per cent (2004 0.7 per cent) of the Company's deferred stock, and £1,238,827 nominal of deferred stock of the Company (2004 £144,518 nominal), representing 0.2 per cent (2004 nil per cent) of the Company's deferred stock, was distributed by the Trust to participants in the Matching Plan under the terms of that plan.

Retained earnings is stated after the deduction of £30.8m (2004 £28.4m) in respect of £12,096,283 nominal of deferred stock of the Company (2004 £11,435,110 nominal) held by the Trust, of which £516,069 nominal (2004 £402,032 nominal) has been conditionally awarded to participants in the Matching Plan. Further stock awards over £4,287,491 nominal (2004 £2,132,996 nominal) have been granted to participants under the Matching Plan, the Performance Share Plan and the 2005 Matching Share Plan, which will be met by the Trust to the extent that the performance conditions are met. The market value of the deferred stock held by the Trust as at 31 December 2005 was £56.4m.

Retained earnings is also stated after a credit of £11.0m (2004 £6.6m) relating to charges made to the income statement in respect of equity settled share-based payments, including the fair values of awards and grants under the Matching Plan, the Performance Share Plan and the 2005 Matching Share Plan, which will be met by the Trust, and the fair value of options granted under the Executive Stock Option Plan and the P&O 2004 UK Sharesave Plan.

Exchange movements in the Group retained earnings include a loss of £49.4m (2004 £45.0m gain) in respect of foreign currency net borrowings.

26 Directors' emoluments

The aggregate emoluments of the directors of the Company were:

	2005 £000	2004 £000
Fees	508	149
Salaries and benefits	2,092	2,264
Performance related bonuses	1,252	1,078
Short term employment benefits	3,852	3,491
Pensions costs	512	439
Equity settled share-based payments	859	531
	5,223	4,461

Amounts totalling £217,000 (2004 £188,000) in respect of 2004 performance related bonuses were settled in 2005 by way of equity settled share-based payments under the Deferred Bonus and Co-Investment Matching Plan.

Pension costs represent the estimated cost to the Group of providing pensions benefits in respect of current year service measured in accordance with IAS 19 'Employee Benefits'.

Further details on directors' emoluments, long term incentives, pension entitlements and deferred stock under option held by the directors are shown in the directors' remuneration report on pages 28 to 35.

27 Employees

The average number of people employed by the Group was:

	2005	2004
UK full time	2,620	2,899
UK part time	155	204
Overseas full time	11,119	12,018
Overseas part time	2,768	2,883
Sea staff	2,803	4,034
	19,465	22,038

The aggregate payroll costs, excluding directors' emoluments, were:

	2005 £m	2004 £m
Wages and salaries	425.6	449.7
Social security costs	10.4	14.5
Pensions costs	39.4	27.9
	475.4	492.1

Amounts totalling £3.9m (2004 3.4m) in respect of equity settled share-based payments were charged to the income statement.

Amounts totalling £0.4m (2004 £0.4m) in respect of 2004 performance related bonuses were settled in 2005 by way of equity settled share-based payments under the Deferred Bonus and Co-Investment Matching Plan.

Certain comparatives have been adjusted to make them consistent with current year classifications.

Equity settled share-based payments

The Group operated five employee share plans: the Executive Stock Option Plan ("P&O Option Plan"), the P&O 2004 UK Sharesave Plan ("2004 Plan"), the Deferred Bonus and Co-investment Matching Plan ('Matching Plan'), the P&O Performance Share Plan ("Performance Share Plan") and the P&O 2005 Matching Share Plan ("2005 Matching Share Plan"). Upon the takeover of the Group by DP World in March 2006, awards under these plans vested according to the provisions of the relevant plan rules.

The following analysis includes only those awards and grants made under the above share plans since 7 November 2002 in accordance with the transitional arrangements of IFRS 2 'Share-based Payment', so is not a complete analysis of all awards or grants which were outstanding during the year.

The Performance Share Plan

Under the Performance Share Plan, executive directors and a limited number of other senior employees who had significant influence over the Group's ability to meet its strategic objectives were eligible to receive annual awards, in the form of deferred stock, worth up to 120 per cent of salary. In order to provide flexibility, the scheme rules allowed annual awards of up to a maximum of 200 per cent of salary.

27 Employees (continued)

Awards would vest after three years subject to the Company's TSR ("Total Shareholder Return") performance against the constituents of the FTSE 350 (excluding investment trusts) at the date of award, 25 per cent of the award would vest if the Company was ranked at the median. The full award would vest if the Company was ranked at, or above, the upper quartile. Between these two points, the award would vest on a straight line basis. No portion of the award would vest if the Company was ranked below the median, and any unvested award at the end of the three year period would automatically lapse.

Awards would only vest subject to the remuneration committee determining that the TSR performance was a genuine reflection of the Company's underlying financial performance over the three year period.

Awards could be satisfied by the use of stock purchased in the market or newly issued stock and to the extent that new issue stock was used this was subject to the normal dilution limits (i.e. options/awards over stock in the Company did not exceed 5 per cent of the Company's issued deferred stock in any rolling 10 year period in respect of executive schemes, or 10 per cent in any 10 year period in respect of all schemes).

The 2005 Matching Share Plan

Executive directors were able to invest their own cash resources up to a limit of 50 per cent of their maximum bonus opportunity into stock in the Company ("Invested Stock"). Participants who made such investment received a performance based matching award equal in value to the Invested Stock (valuing the Invested Stock on a pre-tax basis). Awards were designed to vest after three years, subject in normal circumstances to the participant continuing to hold the Invested Stock for the three year period and would vest based on the same TSR performance conditions as under the Performance Share Plan.

The Matching Plan

The Matching Plan provided participants with the opportunity to receive matching awards of deferred stock depending upon the performance of the Company over a two year retention period following the year in which an original bonus-related award was earned.

One third of any annual bonus awarded to directors and other executives who were participants in the Matching Plan was in the form of a Stock Award which was automatically invested in the Matching Plan. Participants were also invited to commit their own resources to the Matching Plan, by investing in further deferred stock in the Company (described as Invested Stock) subject to an overall limit on the amount invested in the Matching Plan in any one year of up to 75 per cent of base salary. Subject to the discretion of the Matching Plan Trustee, Matching Plan participants receive Matching Awards. Matching Awards entitled the participants to acquire a maximum amount of deferred stock which, at the date of grant, had a value equal to the aggregate value of the executive's Stock Award and Invested Stock (valuing Invested Stock on a gross of tax basis).

The amount of deferred stock over which a Matching Award might be exercised was dependent on the Company's TSR over the retention period compared to that of the other companies in the FTSE 350 index. If the Company achieved median performance a participant was entitled to exercise 25 per cent of his Matching Award and if the Company achieves upper quartile performance, a participant was entitled to exercise 100 per cent of his Matching Award. For performance between median and upper quartile, entitlement was calculated on a straight line basis.

Matching Awards were only exercisable if a secondary validating performance condition was also met. This required earnings per share ("EPS") growth (after appropriate adjustments to ensure consistency throughout the period) over the retention period to exceed the growth in the UK Index of Retail Prices by an average of at least 3 per cent per annum.

The P&O Option Plan

Options under this plan were generally exercisable three years after the date of grant subject to the achievement of performance conditions and remained exercisable until the tenth anniversary of grant. Performance conditions were generally based on the achievement of EPS growth (after appropriate adjustments to ensure consistency throughout the period) of an average of at least 3 per cent per annum in excess of the growth in the UK Retail Prices Index over a period of at least three years from grant.

No awards have been made under this plan since 2003, other than in exceptional circumstances.

The 2004 Plan

All employees were able to participate, subject to service conditions and limits, in the 2004 Plan. The 2004 Plan operated within specific tax legislation (including a requirement to finance the exercise of the option using the proceeds of a monthly savings contract) and exercise of the option was not subject to satisfaction of a performance target since this was an all-employee share scheme.

27 Employees (continued)

(a) Stock Award Plans

	Performance Share Plan		2005 Matching Share Plan		Matching Plan	
	Deferred stock '000	WAFV* pence	Deferred stock '000	WAFV* pence	Deferred stock '000	WAFV* pence
Stock awards (March 2005)	–	–	–	–	249	302
Matching awards (March 2005)	–	–	–	–	619	113
Share Plan awards (May 2005)	2,211	114	179	114	–	–
Dividend Replacement (June/November 2005)	16	178	1	178	6	349
Share Plan awards (August 2005)	196	134	–	–	–	–

* WAFV = Weighted average fair value

The fair values of grants under the Stock Award Plans are calculated by discounting the share price at the date of the award in respect of the relevant performance conditions.

(b) Stock Option Plans

	P&O Option Plan		2004 Plan	
	Options '000	WAEP pence	Options '000	WAEP pence
As at 31 December 2003				
Options outstanding	9,844	247	7,041	128
Movements during 2004				
Options granted	17	220	1,487	205
Options exercised	(110)	249	(146)	128
Options lapsed	(810)	249	(666)	131
Weighted average fair value of options granted during the year		55		89
As at 31 December 2004				
Options outstanding	8,941	247	7,716	143
Movements during 2005				
Options granted	–	–	1,129	270
Options exercised	(1,269)	249	(553)	130
Options lapsed	(184)	249	(884)	140
Dividend Stock				
Weighted average fair value of options granted during the year		–		102
As at 31 December 2005				
Options outstanding	7,488	246	7,408	163
Range of exercise prices		179p-249p		128p-270p
Weighted average remaining contractual life		2,819 days		446 days
Options exercisable	1,713	249	622	152

* WAEP = Weighted average exercise price

Stock options were exercised on a regular basis throughout the year.

27 Employees (continued)

The fair values of grants under the Stock Option Plans are calculated using binomial valuation models. The following table gives the assumptions applied to the options granted during the year. Expectations of early exercise are incorporated into the model.

	2005	2004
Average actual share price (pence)	334	243
Weighted average exercise price of options granted in the period (pence)		
P&O Option Plan	–	220
2004 Plan	270	205
Weighted average fair value of options granted in the period (pence)		
P&O Option Plan	–	55
2004 Plan	102	89
Expected volatility (%)	33.5	37.5
Dividend yield (%)	4.0	4.0
Risk-free interest rate (%)	5.0	5.0
Expected lives (years)		
P&O Option Plan	–	3.5
2004 Plan	3.5	3.5

The expected volatility is based on the historic volatility (calculated based on the weighted average life of the options) adjusted for any expected changes to future volatility due to publicly available information.

28 Employee benefits

Reconciliation of assets and liabilities recognised in the balance sheet

	2005	2004
	Total	Total
	£m	£m
Non-current		
Defined benefit pension schemes net liabilities	(275.7)	(262.8)
Liabilities from defined contribution pension schemes	(1.8)	–
Liability in respect of long service leave	(1.0)	(2.9)
Liability for other non-current deferred compensation	(1.8)	(3.2)
Current		
Liability for current deferred compensation	(23.0)	(24.2)
Net liabilities	(303.3)	(293.1)
Reflected in balance sheet as follows:		
Employee benefits assets: non-current (note 18)	2.5	–
Employee benefits liabilities: non-current	(282.8)	(268.9)
Employee benefits liabilities: current	(23.0)	(24.2)
	(303.3)	(293.1)

The defined benefit pension schemes net liabilities of £275.7m is in respect of the total Group schemes shown below. The £3.3m (2004 £42.6m) net liability in respect of the Group's share of joint ventures and associates is included within investments in joint ventures and associates in the consolidated balance sheet.

An expense of £5.3m (2004 £4.2m) has been recognised in administrative costs (£4.7m) (2004 £3.7m) and cost of sales (£0.6m) (2004 £0.5m) in the income statement in respect of employee benefits excluding pensions.

28 Employee benefits (continued)

Pensions

The Group participates in a number of pension schemes throughout the world. The principal scheme is located in the UK (the "P&O UK Scheme"). The P&O UK Scheme is a funded defined benefit scheme and was closed to routine new members on 1 January 2002. The assets of the scheme are managed on behalf of the trustee by independent fund managers.

The Group also operates a number of smaller defined benefit and defined contribution schemes. In addition, the Group participates in various industry schemes, the most significant of which is the Merchant Navy Officers' Pension Fund (the "MNOPF Scheme"). These generally have assets held in separate trustee administered funds.

Expenses recognised in income statement

	Defined Benefit Pension schemes			Total Group schemes £m	Share of joint ventures & associates schemes £m	2005 Total £m
	P&O UK Scheme £m	MNOPF Scheme £m	Other schemes £m			
Employer's current service cost	8.0	0.7	7.0	15.7	1.2	16.9
Employer's past service cost	0.7	–	–	0.7	–	0.7
Loss due to settlements/curtailments	0.7	–	–	0.7	–	0.7
	9.4	0.7	7.0	17.1	1.2	18.3
Expected return on scheme assets	(58.1)	(5.1)	(7.2)	(70.4)	(3.6)	(74.0)
Interest cost	59.9	5.3	6.7	71.9	3.9	75.8
	1.8	0.2	(0.5)	1.5	0.3	1.8
Total defined benefit expenses	11.2	0.9	6.5	18.6	1.5	20.1
Total defined contribution expenses				22.9	2.0	24.9
Total pension expenses	11.2	0.9	6.5	41.5	3.5	45.0

The expenses for defined benefit and defined contribution schemes are classified as follows in the consolidated income statement:

	Defined Benefit Pension schemes			Defined Contribution Pension schemes £m	Total Group schemes £m	Share of joint ventures & associates schemes £m	2005 Total £m
	P&O UK Scheme £m	MNOPF Scheme £m	Other schemes £m				
Cost of sales	1.8	0.7	4.0	20.1	26.6	–	26.6
Administrative costs	7.6	–	3.0	2.8	13.4	–	13.4
Share of results of joint ventures and associates	–	–	–	–	–	3.5	3.5
	9.4	0.7	7.0	22.9	40.0	3.5	43.5
Net financing costs	1.8	0.2	(0.5)	–	1.5	–	1.5
	11.2	0.9	6.5	22.9	41.5	3.5	45.0

	Defined Benefit Pension schemes			Total Group schemes £m	Share of joint ventures & associates schemes £m	2004 Total £m
	P&O UK Scheme £m	MNOPF Scheme £m	Other schemes £m			
Employer's current service cost	9.6	n/a	6.1	15.7	2.0	17.7
Employer's past service cost	0.4	n/a	–	0.4	0.1	0.5
Gain due to settlements/curtailments	(4.2)	n/a	(0.3)	(4.5)	–	(4.5)
	5.8	n/a	5.8	11.6	2.1	13.7
Expected return on scheme assets	(47.2)	n/a	(6.6)	(53.8)	(10.0)	(63.8)
Interest cost	48.3	n/a	7.0	55.3	10.3	65.6
	1.1	n/a	0.4	1.5	0.3	1.8
Total defined benefit expenses	6.9	n/a	6.2	13.1	2.4	15.5
Total defined contribution expenses				16.8	1.6	18.4
Total pension expenses	6.9	n/a	6.2	29.9	4.0	33.9

28 Employee benefits (continued)

The expenses for defined benefit and defined contribution schemes are classified as follows in the consolidated income statement:

	Defined Benefit Pension schemes			Defined Contribution Pension schemes £m	Total Group schemes £m	Share of joint ventures & associates schemes £m	2004 Total £m
	P&O UK Scheme £m	MNOFF Scheme £m	Other schemes £m				
Cost of sales	0.9	n/a	3.3	12.9	17.1	–	17.1
Administrative costs	4.9	n/a	2.5	3.9	11.3	–	11.3
Share of results of joint ventures and associates	–	–	–	–	–	4.0	4.0
	5.8	n/a	5.8	16.8	28.4	4.0	32.4
Net financing costs	1.1	n/a	0.4	–	1.5	–	1.5
	6.9	n/a	6.2	16.8	29.9	4.0	33.9

Total amount of actuarial losses recognised in the statement of recognised income and expense

	2005 £m	2004 £m
Total actuarial losses recognised in the statement of recognised income and expense in the year	147.9	54.7

The cumulative amount of actuarial losses recognised in the statement of recognised income and expense is a loss of £202.6m (2004 £54.7m).

Actuarial valuations and assumptions

The latest valuations of the defined benefit schemes have been updated to 31 December 2005 by qualified independent actuaries. The principal assumptions are included in the table below.

The assumptions used by the actuaries are the best estimates chosen from a range of possible actuarial assumptions, which, due to the timescale covered, may not necessarily be borne out in practice.

	P&O UK Scheme		MNOFF Scheme		Other schemes		Share of joint ventures & associates schemes	
	2005	2004	2005	2004	2005	2004	2005	2004
Discount rates	4.75%	5.30%	4.75%	n/a	5.00%	5.40%	4.85%	5.30%
Expected rates of salary increases	4.20%	4.20%	4.20%	n/a	3.60%	3.70%	3.75%	4.15%
Pension increases:								
– deferment	2.70%	2.70%	2.70%	n/a				
– payment	2.50%	2.50%	2.50%	n/a	2.25%	1.60%	2.70%	2.60%
Inflation	2.70%	2.70%	2.70%	n/a	2.65%	2.25%	2.70%	2.70%
Expected rates of return on scheme assets	5.80%	6.20%	6.60%	n/a	6.45%	6.60%	6.50%	6.25%

The assumptions for pensioner longevity under both the P&O UK Scheme and the MNOFF Scheme are based on analyses of pensioner death trends under the respective schemes for many years. In each case the assumptions follow those used for the most recent funding valuation, and include allowances for future reductions in death rates for all members. For the P&O UK Scheme the PA92U2004 tables are used (with a +1 year age rating applied for females), together with a reduction of 0.1 per cent in the discount rate to allow for further longevity improvements. For the MNOFF Scheme the PA80C2003 tables are used (with a +1 year age rating applied for both males and females) together with a reduction of 0.25 per cent in the discount rate. These assumptions will be reviewed following the next funding valuation, due no later than 30 September 2007 for the P&O UK Scheme and 31 March 2006 for the MNOFF Scheme.

The expected long-term rates of return for each of the main asset classes are subjective judgements based on market indicators, economic background, historical analysis of returns and industry forecasts. They take into account the schemes' strategic asset allocations across the sectors of the main asset classes.

28 Employee benefits (continued)

	P&O UK Scheme		MNOFF Scheme		Other schemes		Total Group schemes fair value £m	Share of joint ventures & associates schemes fair value £m	Total fair value £m
	Expected long term rate of return % p.a.	Fair value £m	Expected long term rate of return % p.a.	Fair value £m	Expected long term rate of return % p.a.	Fair value £m			
2004									
Equities	8.00	346.8	n/a	n/a	8.10	62.7	409.5	58.4	467.9
Bonds	4.70	393.5	n/a	n/a	4.70	39.6	433.1	64.0	497.1
Other	3.70	26.0	n/a	n/a	5.20	8.0	34.0	4.3	38.3
	6.20	766.3	n/a	n/a	6.60	110.3	876.6	126.7	1,003.3
2005									
Equities	7.70	517.7	7.70	192.3	7.95	72.3	782.3	4.9	787.2
Bonds	4.40	711.8	4.50	80.8	4.20	45.0	837.6	3.1	840.7
Other	3.70	13.4	5.45	35.1	5.40	8.7	57.2	0.2	57.4
	5.80	1,242.9	6.60	308.2	6.45	126.0	1,677.1	8.2	1,685.3

Reconciliation of the opening and closing balances of the fair value of scheme assets and the present value of the defined benefit obligation

	P&O UK Scheme £m	MNOFF Scheme £m	Other schemes £m	Total Group schemes £m	Share of joint ventures & associates schemes £m	2005 Total £m	2004 Total £m
Present value of obligation at 1 January	(1,008.2)	–	(131.1)	(1,139.3)	(169.4)	(1,308.7)	(1,338.6)
Employer's interest cost	(59.9)	(5.3)	(6.7)	(71.9)	(3.9)	(75.8)	(65.6)
Employer's current service cost	(8.0)	(0.7)	(7.0)	(15.7)	(1.2)	(16.9)	(17.7)
Past service costs — vested benefits	(0.7)	–	–	(0.7)	–	(0.7)	(0.5)
Contributions by scheme participants	(2.0)	(0.2)	(1.6)	(3.8)	(0.3)	(4.1)	(4.3)
Foreign currency exchange	–	–	(2.6)	(2.6)	–	(2.6)	1.9
Benefits paid	57.2	3.8	13.1	74.1	3.1	77.2	56.8
Sale of businesses	–	–	2.6	2.6	112.9	115.5	143.1
Curtailments	–	–	–	–	–	–	0.3
Settlements	(0.7)	–	–	(0.7)	–	(0.7)	9.4
Provision reclassified as defined benefit scheme	–	–	(1.0)	(1.0)	–	(1.0)	–
Amounts recognised in the statement of recognised income and expense							
New schemes entered into during the year	–	(416.9)	(0.6)	(417.5)	–	(417.5)	–
Amounts arising from P&O Nedlloyd transfer/sale	(214.7)	–	–	(214.7)	53.7	(161.0)	–
Actuarial loss on obligation	(123.3)	(18.7)	(19.6)	(161.6)	(6.4)	(168.0)	(93.5)
Present value of obligation at 31 December	(1,360.3)	(438.0)	(154.5)	(1,952.8)	(11.5)	(1,964.3)	(1,308.7)
Fair value of scheme assets at 1 January	766.3	–	110.3	876.6	126.7	1,003.3	1,027.3
Expected return on scheme assets	58.1	5.1	7.2	70.4	3.6	74.0	63.8
Contributions by employer	147.1	5.9	10.9	163.9	10.2	174.1	44.6
Contributions by scheme participants	2.0	0.2	1.6	3.8	0.3	4.1	4.2
Foreign currency exchange	–	–	2.0	2.0	–	2.0	(1.1)
Benefits paid	(57.2)	(3.8)	(13.1)	(74.1)	(3.1)	(77.2)	(56.8)
Sale of businesses	–	–	(2.7)	(2.7)	(90.9)	(93.6)	(112.3)
Settlements	–	–	–	–	–	–	(5.2)
Amounts recognised in the statement of recognised income and expense							
New schemes entered into during the year	–	294.3	0.5	294.8	–	294.8	–
Amounts arising from P&O Nedlloyd transfer/sale	231.7	–	–	231.7	(40.3)	191.4	–
Actuarial gain on assets	94.9	6.5	9.3	110.7	1.7	112.4	38.8
Fair value of scheme assets at 31 December	1,242.9	308.2	126.0	1,677.1	8.2	1,685.3	1,003.3
Defined benefit schemes net liabilities	(117.4)	(129.8)	(28.5)	(275.7)	(3.3)	(279.0)	(305.4)
Actual return on scheme assets	153.0	11.6	16.5	181.1	5.3	186.4	102.6

28 Employee benefits (continued)

It is anticipated that the company will make the following contributions to the pension schemes in 2006:

	P&O UK Scheme £m	MNOPF Scheme £m	Other schemes £m	Total Group schemes £m	Share of joint ventures & associates schemes £m	Total £m
Pension scheme contributions	39.7	6.8	6.0	52.5	0.4	52.9

	P&O UK Scheme £m	MNOPF Scheme £m	Other schemes £m	Total Group schemes £m	Share of joint ventures & associates schemes £m	Total £m
2004						
Present value of the defined benefit obligations	(1,008.2)	n/a	(131.1)	(1,139.3)	(169.4)	(1,308.7)
Fair value of scheme assets	766.3	n/a	110.3	876.6	126.7	1,003.3
Surplus or deficit in the scheme	(241.9)	n/a	(20.8)	(262.7)	(42.7)	(305.4)
Experience gains/(losses) on scheme assets	29.9	n/a	3.9	33.8	5.0	38.8
Experience gains/(losses) on scheme liabilities	(75.3)	n/a	(7.3)	(82.6)	(10.9)	(93.5)

	P&O UK Scheme £m	MNOPF Scheme £m	Other schemes £m	Total Group schemes £m	Share of joint ventures & associates schemes £m	Total £m
2005						
Present value of the defined benefit obligations	(1,360.3)	(438.0)	(154.5)	(1,952.8)	(11.5)	(1,964.3)
Fair value of scheme assets	1,242.9	308.2	126.0	1,677.1	8.2	1,685.3
Surplus or deficit in the scheme	(117.4)	(129.8)	(28.5)	(275.7)	(3.3)	(279.0)
Experience gains/(losses) on scheme assets	94.9	6.5	9.3	110.7	1.7	112.4
Experience gains/(losses) on scheme liabilities	(123.3)	(18.7)	(19.6)	(161.6)	(6.4)	(168.0)

P&O UK Scheme

Formal actuarial valuations of the P&O UK Scheme are normally carried out triennially by qualified independent actuaries, the latest regular valuation report for the scheme being at 1 April 2003, using the projected unit method. As a result of the decision by P&O Nedlloyd to form its own UK scheme and the request to transfer its share of the assets and liabilities of the P&O UK Scheme into that new scheme, an additional valuation was carried out as at 30 September 2004 using the projected unit method.

At this date, allowing for the P&O Nedlloyd transfer and related transactions, the market value of the P&O UK Scheme's assets were £987m and the value of accrued benefits to members allowing for future increases in earnings was £1,176m giving a deficit of £189m and a funding ratio of 83.9 per cent.

Excluding the deficit reduction payments, the average contribution rates for the P&O UK Scheme were 22.8 per cent for the year to 31 December 2005 and 23.7 per cent from 1 January 2006.

The principal long term assumptions in the P&O UK Scheme's 2004 valuation are:

	Nominal % per annum
Price inflation	3.00
Investment return on pre retirement portfolio	6.50
Investment return on post retirement portfolio	5.50
Earnings escalation	4.50
LEL escalation	3.00
Increases in accrued pensions on excess over Guaranteed Minimum Pensions	2.75

As a result of this valuation and the subsequent take over of the Group by DP World, the Group made a further deficit contribution to the scheme of £25m in March 2006 and has committed to further regular monthly deficit payments totalling £75m over the next five years. These monthly payments are supported by a bank guarantee.

Merchant Navy Officers' Pension Fund

The MNOPF Scheme is a defined benefit multi-employer scheme in which officers employed by companies within the Group have participated and continue to participate.

The scheme is divided into two sections, the Old Section and the New Section, both of which are closed to new members and the latest valuation was carried out at 31 March 2003.

The Old Section has been closed to benefit accrual since 1978. The scheme's independent actuary advised that at 31 March 2003 the market value of the scheme's assets for the Old Section was £1,316m, representing approximately 115 per cent of the value of the benefits accrued to members. The assets of the Old Section were substantially invested in bonds.

28 Employee benefits (continued)

As at 31 March 2003, the date of the most recent formal actuarial valuation, the New Section had assets with a market value of £1,168m, representing approximately 86 per cent of the benefits accrued to members. The valuation assumptions were as follows:

	Nominal % per annum
Discount rate	7.80
Rate of national average earnings increase	4.00
Rate of pension increases (where increases apply)	2.50

At the date of the valuation, approximately 59 per cent of the New Section's assets were invested in equities, 28 per cent in bonds and 13 per cent in property and cash.

Following a court decision in 2005, the trustee has advised the Group that its share of the net deficit of the New Section is 18.319 per cent and has issued a schedule of regular deficit payments from Group companies totalling £5.5m per annum commencing on 30 September 2005 and payable annually on 31 March thereafter until 31 March 2014. Therefore, the Group has accounted for the MNOPF New Section as a defined benefit scheme from 30 September 2005. Prior to that date, the Group accounted for the New Section as a defined contribution scheme as it was unable to determine its share of the scheme. The proportion of the deficit attributable to the Group will change following the next actuarial valuation, to be prepared as at 31 March 2006, as not all employers have made their deficit payments, with shortfalls to be reallocated to other employers, and part of the deficit payments being made by Carnival plc are attributable to the Group under the terms of the demerger agreement relating to the demerger of P&O Princess Cruises in 2000.

Merchant Navy Ratings' Pension Fund

The Merchant Navy Ratings' Pension Fund (the "MNRPF Scheme") is an industry wide multi-employer defined benefit pension scheme in which sea staff employed by companies within the Group have participated. The scheme has a significant funding deficit and has been closed to further benefit accrual.

As at 31 March 2005, the date of the most recent full triennial actuarial valuation carried out by an independent actuary, the scheme had assets with a market value of £590m, representing 86 per cent of the benefits accrued to members allowing for future increases. Approximately 68 per cent of the scheme's assets were invested in bonds, 25 per cent in equities and 7 per cent in property and cash. The valuation assumptions were as follows:

	Nominal % per annum
Investment return on pre retirement portfolio	6.50
Investment return on post retirement portfolio	5.00
Rate of national average earnings increase	4.20
Rate of pension increases (where increases apply)	2.70

Following this valuation the Group is yet to receive any adjustments to the previous schedule of payments. The Group is making current contributions in respect of subsidiaries that are current employers in the scheme and voluntary payments in respect of subsidiaries that have settled the relevant statutory debt obligations and are no longer current employers within the scheme. Current contributions and voluntary payments by the Group to the scheme in 2005 totalled £5.8m, which included amounts previously provided for. These payments are included within total defined contribution expense for the Group.

P&O has appointed an independent actuary to estimate the deficit of the MNRPF Scheme at 31 December 2005 using the same assumptions as applied for the IAS 19 valuation of the P&O UK Scheme as set out above. Based on the share of current contributions to the scheme by P&O Group companies, the Group's share of the estimated deficit could be between £8m and £10m.

The Group cannot identify its share of the underlying assets and liabilities of the MNRPF Scheme on a consistent and reasonable basis and is therefore accounting for contributions and payments to the MNRPF Scheme under IAS 19 as if it were a defined contribution scheme.

Other schemes

Other defined benefit schemes include schemes in Australia, Ireland, Canada, Indonesia, South Africa, Pakistan, North America and the Philippines.

Other industry schemes are mainly overseas multi-employer schemes, in which the Group is unable to identify its share of the underlying assets and liabilities on a consistent and reasonable basis. The Group is therefore accounting for contributions to these schemes as if they were defined contribution schemes for IAS 19 purposes.

P&O Nedlloyd

During 2005, P&O Nedlloyd formed its own UK pension scheme and 25 per cent of the assets and liabilities of the P&O UK Scheme were transferred in to the P&O Nedlloyd scheme. P&O Nedlloyd in addition made an exit payment into the remaining P&O UK Scheme of £70m. The Group's share of this scheme was included within share of joint ventures and associates until the investment in P&O Nedlloyd was disposed of on 29 June 2005.

29 Commitments

Capital	2005	2004
Contracted	£m	£m
Ships	76.9	2.7
Land and buildings	7.5	13.6
Other	40.2	45.6
	124.6	61.9

Of the above capital commitments it is expected that the Group will pay £124.6m in 2006. The Group's share of capital commitments within its joint ventures is £19.4m (2004 £26.1m) and associates is £8.0m (2004 £23.6m).

Revenue

Leases as lessee

The commitment of the Group in respect of non-cancellable operating leases is as follows:

Lease expiring:	Property		Other	
	2005 £m	2004 £m	2005 £m	2004 £m
Within one year	67.3	70.5	77.1	79.2
Between one and five years	287.5	271.7	120.8	155.0
Over five years	1,188.0	1,168.4	106.3	107.7
	1,542.8	1,510.6	304.2	341.9

Leases as lessor

The Group leases out its properties held for development and sale and a vessel surplus to ongoing operations. The future minimum lease receipts under non-cancellable leases are as follows:

Lease expiring:	Property		Other	
	2005 £m	2004 £m	2005 £m	2004 £m
Within one year	0.6	1.1	2.7	–
Between one and five years	4.1	4.7	1.3	–
Over five years	–	–	–	–
	4.7	5.8	4.0	–

30 Contingent liabilities

	2005	2004
	£m	£m
Loan and lease guarantees on behalf of joint ventures and associates		
Ports	75.0	37.6
Property	7.1	3.6
	82.1	41.2
Other contingent liabilities	30.6	103.8
	112.7	145.0

Other contingent liabilities in the Group include £14.0m (2004 £78.7m) relating to guarantees of the financial liability for a vessel leased to Associated Bulk Carriers Limited, a previous associate of the Group. This lease expires in 2008. Associated Bulk Carriers Limited was sold to Eurotower Holdings SA in December 2003 and as part of the transaction, P&O received a counter indemnity for this liability from First Omega Shipping Inc, the owner of Eurotower Holdings SA.

Included within amounts receivable relating to previous corporate disposals is an amount outstanding of £42.6m (2004 £32.2m) net of relevant provisions arising following the sale of Bovis Group plc in 1999. Pursuant to the sale terms P&O is obliged to provide loan funding and partial indemnification for one of Bovis' projects, the construction of which is now completed and is the subject of litigation. Most of this litigation has been the subject of a settlement agreement as a result of which the bulk of such amounts receivable are expected to be repaid over the next twelve months.

A contingent liability exists in a joint venture of the Group relating to a value added tax assessment resulting from a tax audit for the year 2003. The joint venture company believes that there is no liability. Accordingly it has objected to the assessment and is currently awaiting rulings from the tax authority. The Group's share of the contingent liability relating to the 2003 assessment is £2.2m. If the assessment for 2003 is upheld, there may be liabilities relating to other years but these cannot be reliably estimated until tax rulings following the objection have been published.

31 Notes to the statement of cash flows

	Fair value balance sheets 2005 £m	Fair value balance sheets 2004 £m
(a) Purchase of subsidiaries and businesses		
Net assets acquired:		
Property, plant and equipment	–	0.6
Investments in joint ventures and associates	–	0.6
Properties held for development and sale	–	43.7
Other net current assets	–	3.1
Loans	–	(17.0)
Cash and overdrafts	–	2.3
Minority interests	–	(0.1)
	–	33.2
Goodwill	–	–
	–	33.2
Satisfied by:		
Cash	–	0.7
Investments already owned	–	32.5
	–	33.2

The cash outflow of £nil (2004 inflow £1.6m) on the purchase of subsidiaries and businesses comprises the cash consideration of £nil (2004 £0.7m), less net cash of £nil (2004 £2.3m) of the subsidiaries at the dates of acquisition. The investments already owned of £nil (2004 £32.5m) represent the reserves of and loans to joint ventures and associates now consolidated as subsidiaries. There were no fair value adjustments in respect of the above acquired subsidiaries and businesses.

	Cold Logistics 2005 £m	Disposal balance sheets 2005 £m	Disposal balance sheets 2004 £m
(b) Sale of subsidiaries and termination of businesses			
Net assets sold:			
Intangible assets	14.6	14.6	2.3
Property, plant and equipment	173.2	173.2	149.9
Other net current assets/(liabilities)	7.7	7.7	(3.1)
Loans	(6.7)	(6.7)	(6.1)
Cash and overdrafts	6.6	6.6	4.8
Income and deferred taxation	–	–	(2.7)
Employee benefits	(6.5)	(6.5)	(4.2)
Provisions	(0.8)	(0.8)	–
Minority interests	–	–	2.0
Less: investment in joint ventures and associates retained	–	–	(4.6)
	188.1	188.1	138.3
(Loss)/profit on sale and termination of businesses		(9.5)	32.7
		178.6	171.0
Satisfied by:			
Net cash consideration		134.6	191.3
Other investments		33.0	–
Deferred consideration		18.2	(20.0)
Accrued costs		(7.2)	(0.3)
		178.6	171.0

The cash inflow of £128.0m (2004 £186.5m) on the sale of subsidiaries and termination of businesses comprises cash received of £134.6m (2004 £191.3m) less net cash of £6.6m (2004 £4.8m) of the subsidiaries at the dates of disposal.

32 Financial instruments

The transitional arrangements for the reporting of financial instruments for both the year ended 31 December 2005 and the comparative information are explained in note 1 and note 36. The main impact on the Group's financial statements on the introduction of IAS 39 is the inclusion of the fair value position of derivative financial instruments on the balance sheet.

The Group's policies and procedures in relation to the role and management of financial instruments and financial risk are set out below. These have not been impacted by the introduction of IFRS.

Financial risk

The financial instruments held by the Group to finance its operations include cash, overdrafts, loans, and a limited amount of interest bearing and non-interest bearing investments. Derivative financial instruments are used to manage the interest rate, currency and fuel price risks arising from its operations and its sources of finance. The derivatives employed for this purpose are principally interest rate swaps, cross currency swaps, forward foreign currency contracts and fuel price swaps.

The Group has in place established treasury policies. The purpose of these is to ensure that adequate cost effective funding is available to the Group at all times and that exposure to financial risk is minimised.

The main financial risks to which the Group is exposed are foreign currency risk, interest rate risk and liquidity risk as summarised below. No transactions of a speculative nature are undertaken. The Board receives regular reports which monitor these risks in accordance with agreed policies. None of these policies have been altered during the year.

Liquidity risk

The Group has cash balances and undrawn committed facilities to provide liquidity as required. At 31 December 2005 committed undrawn facilities totalled £686.3m (2004 £660.6m). Most of this borrowing capacity is available under a syndicated loan which is repayable in June 2010. The syndicated loan agreement contains representations, warranties, undertakings (including financial condition covenants and undertakings requiring the provision of guarantees from various subsidiary companies) in favour of the lenders which are typical for this type of credit agreement and customary events of default upon occurrence of which the lenders may terminate and demand repayment of the facility. The agreement also includes the requirement to effect a mandatory prepayment upon a change of control of The Peninsular and Oriental Steam Navigation Company.

The DP World takeover has affected liquidity and the effect is shown in the loan note on page 66.

Foreign currency risk

The Group has extensive overseas and international business operations and operates in a number of foreign currencies which gives rise to transactional and translational foreign exchange risk. The most important foreign currency to the Group is the US dollar, followed by the Australian dollar and the Indian rupee. In general, the Group's profits and stockholders' funds benefit if these currencies are strong against sterling. The year end rate for the US dollar was \$1.717=£1 (2004 \$1.92=£1), for the Australian dollar it was \$2.340=£1 (2004 \$2.449=£1) and for the Indian rupee it was INR77.271=£1 (2004 INR83.458=£1).

Translational currency risk

The proportion of the Group's net operating assets denominated in foreign currencies is 73 per cent with the result that the Group's sterling consolidated balance sheet, and in particular stockholders' funds, can be significantly affected by currency movements when it is retranslated at each period end rate. The Group mitigates the effect of such movements by borrowing in the same currencies as those in which the assets are denominated and using cross currency swaps. In addition the majority of the Group's operating profit in 2005 was generated by businesses with functional currencies other than sterling. The results of these businesses are translated into sterling at average exchange rates for the purposes of consolidation. The impact of currency movements on operating profit is mitigated partially by interest costs being incurred in foreign currencies.

Exchange arising on foreign currency investments are taken directly to equity. Most foreign currency loans are accounted for as hedges and the exchange arising from retranslating these loans at each balance sheet date is taken to equity to the extent that this hedge is deemed to be effective. Where cross currency swaps are used to hedge overseas equity investments the movement in the fair value of the instrument is also taken to equity.

Transactional currency risk

A portion of the Group's businesses generate part of their revenue and incur some costs outside their main functional currency. Due to the diverse number of locations in which the Group operates there is some natural hedging that occurs within the Group. When it is considered that currency volatility could have a material impact on the results of an operation, hedging, generally up to 12 months using forward contracts, is undertaken to reduce the short term effect of currency movements.

When the Group's businesses enter into capital expenditure or lease commitments in currencies other than their main functional currency, these commitments are hedged in most instances using forward contracts and currency swaps in order to fix the cost when converted to the functional currency. The main exposure of the Group's foreign currency commitments of this nature is in respect of ferry operating lease commitments. Forward contracts match the expected cash flows of capital and lease commitments.

The Group classifies its forward exchange contracts hedging forecasted transactions as cash flow hedges and in accordance with IAS 39 states them at fair value. The fair value of forward exchange contracts at 1 January 2005 was adjusted against the opening balance of the hedging reserve at that date. The fair values of hedges of forecasted transactions at 31 December 2005 are shown in the fair value table below.

As well as the direct effect on cash flows, exchange rates also affect the Group's businesses because of their overall economic influence. In particular, exchange rates affect international trade flows which impact on the activities of the Group.

32 Financial instruments (continued)

Interest rate risk

A small proportion of the Group's underlying borrowings are at fixed rates of interest. In addition, the Group uses interest rate swaps and other instruments to fix the interest cost on its floating rate borrowings in order to limit the impact of increases in interest rates. In the medium term, the Group's policy is to maintain between 50 per cent and 75 per cent of borrowings at a fixed rate of interest. In the short term, the level of fixed rate borrowings may move out of the 50 per cent to 75 per cent range, in which case a plan is put in place to move back within this range. Interest rate swaps have been taken out for periods of between 2 and 13 years with an average life of 3.7 years at 31 December 2005 (2004 £837.3m), either directly or indirectly through swap arrangements. This represents 71 per cent (2004 71 per cent) of net borrowings, with 66 per cent (2004 62 per cent) at rates fixed for more than one year.

The Group classifies interest rate swaps as cash flow hedges and states them at fair value. The fair value of swaps at 1 January 2005 was adjusted against the opening balance of the hedging reserve at that date. The net fair values of swaps at 31 December 2005 are shown in the fair value table below.

Fuel price risk

During 2005 P&O Ferries used fuel price swaps to fix a proportion of its fuel requirement for 2006 in accordance with its fuel hedging policy. These swaps are classified as cash flow hedges and stated at fair value. The fair value of the swaps at the 31 December 2005 was £nil (2004 £nil). There were no fuel swaps outstanding in Group companies at the end of 2004.

Credit risk

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet.

Effective interest rates and repricing analysis

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their effective interest rates at 31 December 2005 and the periods in which they reprice.

	Note	Effective interest rate %	Total £m	Within one year £m	1 to 2 years £m	2 to 5 years £m	More than 5 years £m
Cash and cash equivalents*	20		99.5	99.5	–	–	–
Bank overdrafts*	20		(17.3)	(17.3)	–	–	–
Available-for-sale financial assets	19	7.00	34.6	–	–	34.6	–
Debt securities held-to-maturity	19	4.41	11.2	11.2	–	–	–
Bank loans, bonds and finance leases							
GBP fixed rate bonds and loans	21	6.29	(4.7)	–	–	–	(4.7)
GBP floating rate loans and finance leases	21	5.04	(159.1)	(159.1)	–	–	–
Effect of GBP swaps		1.25	–	80.0	–	(30.0)	(50.0)
US\$ fixed rate loans and bonds	21	7.95	(16.4)	(0.8)	(9.7)	(1.3)	(4.6)
US\$ floating rate loans	21	4.66	(97.0)	(97.0)	–	–	–
Effect of US\$ swaps		0.83	23.3	67.0	–	(20.4)	(23.3)
C\$ floating rate loans	21	3.63	(85.3)	(85.3)	–	–	–
A\$ floating rate loans	21	5.97	(66.0)	(66.0)	–	–	–
Effect of A\$ swaps		(0.09)	–	21.3	–	(21.3)	–
Euro fixed rate loans	21	4.52	(6.6)	(1.0)	(1.0)	(2.7)	(1.9)
Euro floating rate loans	21	2.78	(6.8)	(6.8)	–	–	–
Indian rupee fixed rate loans	21	7.18	(145.6)	(12.0)	(15.7)	(112.6)	(5.3)
Indian rupee floating rate loans	21	4.12	(7.7)	(7.7)	–	–	–
Effect of INR swaps		–	(23.3)	–	–	(23.3)	–
Other currency fixed rate loans	21	6.75-13.00	(59.7)	(0.4)	(42.8)	(12.9)	(3.6)
Other currency floating rate loans	21	4.70-14.80	(31.9)	(31.9)	–	–	–
£ loans from joint ventures and associates		4.50	(8.7)	(8.7)	–	–	–
US\$ loans from joint ventures and associates		5.38	(47.2)	(47.2)	–	–	–
US\$ loans to joint ventures and associates		4.88	14.9	14.9	–	–	–
Euro loans to joint ventures and associates		4.84	15.4	15.4	–	–	–
			(584.4)	(231.9)	(69.2)	(189.9)	(93.4)

* Due to the variety of different currencies and number of bank accounts in which the Group holds its cash and cash equivalents or has overdrafts, calculating an effective interest rate for the different balances would not give a meaningful result. Generally cash is only held where required to provide working capital liquidity to the relevant operation rather than to provide an investment return or provide long term facilities. Where overdrafts are used they are generally at a rate of 1 per cent or less above the relevant base rate.

32 Financial instruments (continued)

The table below presents the carrying amounts under IFRS and the fair values of the Group's financial assets and liabilities at 31 December 2005. Comparative information is presented on the UK GAAP basis applicable at that date rather than in accordance with IAS 32 and IAS 39 as described in note 1.

A comparison by category of book value and fair value of the Group's financial assets and liabilities is as follows:

	2005		2004	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Primary financial instruments held or issued to finance the Group's operations:				
Trade and other receivables	396.5	396.5	346.4	346.4
Trade and other payables	(187.7)	(187.7)	(196.2)	(196.2)
Loans	(686.8)	(687.8)	(1,211.0)	(1,211.8)
Cash and cash equivalents	99.5	99.5	50.2	50.2
Bank overdrafts	(17.3)	(17.3)	(20.8)	(20.8)
Available-for-sale financial assets	37.8	37.8	–	–
Debt securities held to maturity	11.2	11.2	–	–
Unlisted investments	–	–	16.4	16.4
Loans from associates	(73.4)	(73.4)	(70.1)	(70.1)
Loans to associates	67.9	67.9	47.1	47.1
Derivative financial instruments held to manage the interest rate and currency profile:				
Interest rate swaps:				
Assets	1.6	1.6	–	1.4
Liabilities	(22.3)	(22.3)	–	(27.2)
Currency swaps:				
Assets	0.4	0.4	–	–
Liabilities	–	–	–	(0.7)
Derivative financial instruments held or issued to hedge the currency exposure on expected future transactions:				
Forward foreign currency contracts:				
Assets	3.2	3.2	–	5.6
Liabilities	(2.4)	(2.4)	–	(8.1)
Other derivatives:				
Assets	0.1	0.1	–	–
Liabilities	(1.9)	(1.9)	–	(1.9)
	(373.6)	(374.6)	(1,038.0)	(1,069.7)

The following valuation methods have been used under both IAS 39, for the year ended 31 December 2005, and FRS 13, for the comparative information.

The fair value of trade and other receivables and trade and other payables approximates to book value due to the short term maturity of these instruments.

The fair value of non-convertible bonds and dollar notes included in loans above is based on the quoted market price of comparable debt. Other loans include term loans and finance leases. These are largely at variable interest rates and therefore the book value normally equates to the fair value.

The fair value of debt securities held to maturity and available-for-sale financial assets are based on the quoted market value of similar assets.

The fair value of other investments is based on the year end quoted price for listed investments and the estimated recoverable amount for unlisted investments.

The fair value of cash and bank overdrafts approximates to the book value due to the short term maturity of the instruments.

The fair value of derivative financial instruments is discounted to the net present value using prevailing market rates and foreign currency rates at the balance sheet date.

32 Financial instruments (continued)

The following comparative information has been presented under UK GAAP in accordance with the Group's transition to IFRS. See note 1 for further details.

Under UK GAAP gains and losses on instruments used for hedging are not recognised until the exposure that is being hedged is itself recognised. Unrecognised gains and losses on forward foreign currency contracts, fuel price swaps, cross currency swaps and interest rate swaps are as follows:

	Gains £m	(Losses) £m	Net gains/ (losses) £m
At 31 December 2003	10.8	(45.1)	(34.3)
Gains/(losses) arising before 1 January 2004 that were recognised during the year ended 31 December 2004	(2.2)	18.0	15.8
Gains/(losses) arising before 1 January 2004 that were not recognised during the year ended 31 December 2004	8.6	(27.1)	(18.5)
Gains/(losses) arising in the year to 31 December 2004 that were not recognised during the year ended 31 December 2004	(1.6)	(8.9)	(10.5)
At 31 December 2004	7.0	(36.0)	(29.0)
Of which:			
Gains/(losses) expected to be recognised in less than one year	2.0	(12.5)	(10.5)
Gains/(losses) expected to be recognised after more than one year	5.0	(23.5)	(18.5)
	7.0	(36.0)	(29.0)

The interest rate profile of the financial liabilities of the Group after taking into account the effect of interest rate swaps is set out in the tables below:

31 December 2004	Total £m	Variable rate financial liabilities £m	Fixed rate financial liabilities £m	Financial liabilities on which no interest is paid £m	Weighted average interest rate for fixed rate financial liabilities %	Average time over which interest rate is fixed months
Currency:						
Sterling	397.8	204.8	192.8	0.2	6.30	52
Sterling: irredeemable	4.7	–	4.7	–	6.29	n/a
US dollars	286.1	66.1	218.4	1.6	5.71	33
Australian dollars	130.1	52.6	77.4	0.1	5.65	28
Euro	159.1	151.1	8.0	–	3.38	3
Indian rupees	128.3	2.5	125.8	–	7.58	43
Other	125.9	67.0	58.9	–	7.63	44
Total	1,232.0	544.1	686.0	1.9	6.27	40

The Group borrows in a range of currencies at both fixed and variable rates of interest.

The variable rate financial liabilities comprise bank borrowings and overdrafts bearing interest at rates fixed in advance for periods ranging from one to six months by reference to the applicable reference rate, primarily LIBOR for sterling, US dollar and euro borrowings, and the BBSY rate for Australian dollar borrowings.

Financial liabilities on which no interest is paid do not have fixed periods to maturity.

32 Financial instruments (continued)

The interest rate profile of the financial assets of the Group is set out in the tables below:

	Total £m	Variable rate financial assets £m	Fixed rate financial assets £m	Financial assets on which no interest is received £m	Weighted average interest rate for fixed rate financial assets %	Average time over which interest rate is fixed months
31 December 2004						
Currency:						
Sterling	14.9	14.1	–	0.8	n/a	n/a
US dollars	17.8	16.7	–	1.1	n/a	n/a
Australian dollars	3.5	2.5	–	1.0	n/a	n/a
Euro	6.1	4.1	–	2.0	n/a	n/a
Other	29.2	29.0	–	0.2	n/a	n/a
Total	71.5	66.4	–	5.1	n/a	n/a

The majority of variable rate financial assets comprise bank accounts bearing interest at the applicable LIBOR rate for sterling deposits or the applicable local equivalent rate. Fixed rate financial assets include deferred consideration relating to the sale of fixed assets and businesses, and other interest bearing and non-interest bearing investments.

The financial assets on which no interest is received do not have fixed periods to maturity.

The following table shows the Group's currency exposures, being exposures that give rise to the net currency gains and losses recognised in the income statement. Such exposures comprise the monetary assets and liabilities of the Group that are not denominated in the functional currency of the operating unit concerned, excluding certain non-sterling borrowings treated as hedges of net investments in overseas operations.

The amounts shown take into account the effect of any forward contracts entered into to manage currency exposures.

31 December 2004	Net foreign currency monetary assets/(liabilities)					Total £m
	Sterling £m	US dollars £m	Australian dollars £m	Euro £m	Other £m	
Functional currency of Group operation:						
Sterling	–	–	–	(19.2)	–	(19.2)
Australian dollar	–	(0.3)	–	0.2	1.4	1.3
Other	–	(0.4)	–	–	–	(0.4)
	–	(0.7)	–	(19.0)	1.4	(18.3)

33 Related parties

Identity of related parties

The Group has a related party relationship with its associates, joint ventures (see note 13) and with its directors.

Transactions with key management personnel

It is considered that, given the operational and organisational structure of the Group, the key management personnel as defined under IAS 24 'Related Party Disclosures' consists of the executive directors of the Company. Details of the executive directors' remuneration and any relevant transactions are given in the directors' remuneration report on pages 28 to 35.

Other related party transactions

Transactions with joint ventures and associates have been disclosed in note 13.

Ultimate parent company

The Company's immediate controlling party is Thunder FZE, a wholly owned subsidiary of Ports, Customs and Free Zone Corporation, Dubai. No other group financial statements include the results of the Group.

34 Post balance sheet events

On 1 February 2006, the Group announced it had sold its entire property portfolio in Denver to Shea Homes Limited Partnership. The portfolio had a book value of approximately US\$120m (£67m) and as a result of the sale, the Group has largely exited its property interests in the US.

The Tariff Authority for Major Ports in India ("TAMP") has after review passed an order dated 7 March 2006 amending the royalty allowed at Nhava Sheva International Container Terminal ("NSICT") resulting in a reduction in the scale of rates of NSICT by 12 per cent. The said order amends TAMP's order dated 22 July 2005. NSICT is seeking to challenge this new order.

Takeover by DP World

On 29 November 2005, the P&O Board recommended the cash acquisition of P&O by Thunder FZE (a wholly owned subsidiary of Ports, Customs and Free Zone Corporation, Dubai ("DP World")) by way of schemes of arrangement. Following the announcement of an offer by PSA Venture (UK) Limited (a wholly owned subsidiary of PSA International Pte Ltd ("PSA") of Singapore) (also recommended by the Board) on the morning of 26 January 2006, the Board recommended revised proposals from Thunder FZE on the evening of 26 January 2006. These proposals were approved by the stockholders at meetings held on 13 February 2006, and following approval of the schemes by the High Court the schemes became effective on 8 March 2006 and P&O became a wholly owned subsidiary of DP World as at that date.

34 Post balance sheet events (continued)

Following the acquisition of the Company by DP World, it has been announced that the Group's US ports business, P&O Ports North America, will be sold. A sale process has commenced.

As a result of DP World acquiring control of the Company, the Port Authority of New York and New Jersey has commenced legal proceedings that could, if pursued and if successful, result in the termination of the lease of a terminal by Port Newark Container Terminal LLC, a partnership in which the Group has a 50 per cent interest. It is anticipated that this litigation will be resolved by the sale of P&O Ports North America, without the lease being terminated.

The Group is engaged in ongoing litigation with its joint venture partners in its port businesses in Miami. The Group is confident of its contractual position and does not anticipate any significant adverse financial or operational impact from this litigation.

In addition to this litigation the Group is in dispute with shareholders and other stakeholders over matters arising from the takeover in respect of its port businesses in Mundra (India), Colombo (Sri Lanka) and Laem Chabang (Thailand). The Group is confident of its contractual position and does not anticipate any significant adverse financial impact from these disputes.

As a result of the change of control following the DP World takeover certain borrowing and loan facilities may be cancelled at the bank's option (see note 21). DP World has arranged sufficient finance to allow any amounts drawn under these facilities to be repaid as they fall due.

35 Accounting estimates and judgements

Management discussed with the Audit Committee the development, selection and disclosure of the Group's critical accounting policies and estimates and the application of these policies and estimates.

Key sources of estimation uncertainty

Note 10 contains information about the assumptions and their risk factors relating to goodwill impairment.

Pension assumptions

For each pension scheme the Group has decided on the expected long term rate of return for each of the main asset classes based on market indicators, economic background, historical analysis of returns and industry forecasts. If these were to reduce, then the Group's share of the increased deficit would be charged to reserves and recognised in the balance sheet in 2006. A more detailed analysis of these assumptions is provided in note 28.

36 Explanation of transition to IFRS

As stated in note 1, these are the Group's first consolidated financial statements prepared in accordance with IFRS.

The accounting policies referred to in note 1 have been applied in preparing the financial statements for the year ended 31 December 2005, the comparative information presented in these financial statements for the year ended 31 December 2004 and the preparation of an opening IFRS balance sheet at 1 January 2004 (the Group's date of transition).

In preparing its opening IFRS balance sheet, the Group has adjusted amounts reported previously in financial statements prepared in accordance with UK GAAP.

An explanation of how the transition from UK GAAP to IFRS has affected the Group's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany the tables. This information differs to that published in a press release on 15 June 2005 due to balance sheet reclassifications relating to provisions and employee benefits, income statement reclassifications to reflect discontinued operations for businesses sold and an adjustment to the income statement and balance sheets (both 1 January 2004 and 31 December 2004) to reflect a revision to the accounting treatment of certain leases.

The major accounting changes which were required by the adoption of IFRS are:

- Pensions, where defined benefit pension scheme surpluses and deficits are now recognised on the balance sheet
- The consolidation of the entity which owned the Hanseatic Trade Center property development in Hamburg, which had been accounted for as an associate under UK GAAP
- The cessation of amortisation of goodwill
- The recording of share-based payments at fair value
- The provision of deferred tax on unremitted earnings of certain overseas subsidiaries, joint ventures and associates, revalued assets and rolled over gains
- Accounting for the partial sell down of the Group's holding in P&O Nedlloyd

Additionally there are significant presentational changes in the income statement and cash flow statement, particularly in respect of equity accounted joint ventures and associates.

The Group has applied the exemption available under IFRS 1 'First-time Adoption of International Financial Reporting Standards' that allows for comparatives not to be restated for IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement' and for IFRS 5 'Non-current assets held for sale and discontinued operations' to be applied prospectively from 1 January 2005. The summarised accounting policies in respect of these items, as applied from 1 January 2005, are outlined in Section B below.

IFRS restatement of the consolidated income statement

31 December 2004

	Adjustments			Restated in accordance with IFRS £m	Reclassification due to sale of businesses £m	Balance as per income statement £m	
	As previously reported (UK GAAP) £m	Reformatting changes £m	IFRS Adjustments £m				
Group turnover	2,397.5	–	74.0	2,471.5	(205.6)	2,265.9	Group revenues
Cost of sales	(2,078.4)	(11.2)	(119.8)	(2,209.4)	178.1	(2,031.3)	Cost of sales
Gross profit	319.1	(11.2)	(45.8)	262.1	(27.5)	234.6	Gross profit
Other operating income	27.2	–	5.8	33.0	–	33.0	Other operating income
Administrative costs	(460.3)	(1.1)	4.6	(456.8)	22.6	(434.2)	Administrative costs
Group operating loss	(114.0)	(12.3)	(35.4)	(161.7)	(4.9)	(166.6)	
Share of operating results of joint ventures and associates	79.6	(33.9)	32.6	78.3	(47.8)	30.5	Share of results of joint ventures and associates
Total operating loss: Group and share of joint ventures and associates	(34.4)	(46.2)	(2.8)	(83.4)	(52.7)	(136.1)	Group operating loss
Loss on sale of fixed assets	(10.9)	10.9	–	–	–	–	
Loss on sale and termination of businesses	(33.2)	(3.1)	79.4	43.1	(10.7)	32.4	Profit on sale and termination of businesses
Loss on sale and termination of discontinued businesses	(3.1)	3.1	–	–	–	–	
Amounts written off investments	(30.3)	1.1	29.2	–	–	–	
Loss on ordinary activities before interest and taxation	(111.9)	(34.2)	105.8	(40.3)	(63.4)	(103.7)	Loss before financing costs
Interest payable and similar items	(93.5)	5.2	(12.0)	(100.3)	5.4	(94.9)	Financial expenses
Interest receivable and similar items	16.6	(5.2)	–	11.4	–	11.4	Financial income
Interest payable joint ventures and associates	(21.2)	21.2	–	–	–	–	
Loss on ordinary activities before taxation	(210.0)	(13.0)	93.8	(129.2)	(58.0)	(187.2)	Loss before taxation
Taxation	(25.4)	12.2	(9.1)	(22.3)	1.5	(20.8)	Taxation
Loss on ordinary activities after taxation	(235.4)	(0.8)	84.7	(151.5)	(56.5)	(208.0)	Loss on continuing operations
	–	–	–	–	56.5	56.5	Profit from discontinued operations and profit on sale of discontinued operations, net of tax
Equity minority interests	(235.4)	(0.8)	84.7	(151.5)	–	(151.5)	Loss for the financial year
	(14.9)						
Loss attributable to stockholders	(250.3)						
	(250.3)	–	88.7	(161.6)	–	(161.6)	Attributable to:
	14.9	(0.8)	(4.0)	10.1	–	10.1	Equity stockholders of the parent
	(235.4)	(0.8)	84.7	(151.5)	–	(151.5)	Minority interests in subsidiaries

IFRS restatement of the consolidated balance sheet

1 January 2004

	Adjustments			Restated in accordance with IFRS £m	
	As previously reported (UK GAAP) £m	Reformatting changes £m	IFRS adjustments £m		
Fixed assets					Non current assets
Intangible assets: Goodwill	237.3	–	(21.2)	216.1	Intangible assets
	–	–	151.7	151.7	Prepaid leases
Tangible assets: Land and buildings	585.3	1,092.7	(122.4)	1,555.6	Property, plant and equipment
Tangible assets: Ships and other fixed assets	1,092.7	(1,092.7)	–	–	
Investments: Joint ventures and associates	749.0	–	(135.8)	613.2	Investments in joint ventures and associates
Investments: Other	12.6	–	–	12.6	Other investments
	–	1.3	4.2	5.5	Deferred tax assets
	–	40.1	–	40.1	Trade and other receivables
	2,676.9	41.4	(123.5)	2,594.8	
Current assets					Current assets
Property held for development and sale	478.6	–	271.6	750.2	Properties held for development and sale
Stock	60.1	–	–	60.1	Inventories
Debtors: amounts falling due within one year	427.2	–	(2.3)	424.9	Trade and other receivables
Debtors: amounts falling due after one year	40.1	(40.1)	–	–	
Cash at bank and in hand	64.0	–	1.4	65.4	Cash and cash equivalents
	1,070.0	(40.1)	270.7	1,300.6	
Creditors: amounts falling due within one year					Current liabilities
	–	(28.9)	–	(28.9)	Bank overdrafts
Loans	(100.8)	–	–	(100.8)	Interest bearing loans and borrowings
Other creditors	(627.7)	148.7	70.9	(408.1)	Trade and other payables
	–	(119.8)	1.0	(118.8)	Income tax liabilities
	–	–	(22.0)	(22.0)	Employee benefits
	–	(48.3)	–	(48.3)	Provisions
	(728.5)	(48.3)	49.9	(726.9)	
Net current assets	341.5	(88.4)	320.6	573.7	Net current assets
Creditors: amounts falling due in more than one year					Non current liabilities
Loans	(1,437.0)	–	(221.5)	(1,658.5)	Interest bearing loans and borrowings
Other creditors	(55.7)	–	(3.2)	(58.9)	Trade and other payables
	–	(71.5)	(17.0)	(88.5)	Deferred tax liabilities
	–	(27.6)	(216.2)	(243.8)	Employee benefits
Provisions for liabilities and charges	(180.2)	146.1	(1.0)	(35.1)	Provisions
	(1,672.9)	47.0	(458.9)	(2,084.8)	
Net assets	1,345.5	–	(261.8)	1,083.7	Net assets

IFRS restatement of the consolidated balance sheet

31 December 2004

	Adjustments			Restated in accordance with IFRS £m	
	As previously reported (UK GAAP) £m	Reformatting changes £m	IFRS adjustments £m		
Fixed assets					Non current assets
Intangible assets: Goodwill	105.2	–	(12.5)	92.7	Intangible assets
	–	–	145.0	145.0	Prepaid leases
Tangible assets: Land and buildings	447.6	903.1	(117.0)	1,233.7	Property, plant and equipment
Tangible assets: Ships and other fixed assets	903.1	(903.1)	–	–	
Investments: Joint ventures and associates	558.4	–	(57.0)	501.4	Investments in joint ventures and associates
Investments: Other	11.2	–	–	11.2	Other investments
	–	4.8	11.9	16.7	Deferred tax assets
	–	7.2	–	7.2	Trade and other receivables
	2,025.5	12.0	(29.6)	2,007.9	
Current assets					Current assets
Property held for development and sale	361.7	–	146.8	508.5	Properties held for development and sale
Stock	43.2	–	–	43.2	Inventories
	–	5.2	–	5.2	Other investments
Debtors: amounts falling due within one year	419.9	(6.0)	(3.7)	410.2	Trade and other receivables
Debtors: amounts falling due after one year	7.2	(7.2)	–	–	
	–	0.8	–	0.8	Tax recoverable
Cash at bank and in hand	50.8	–	(0.6)	50.2	Cash and cash equivalents
	882.8	(7.2)	142.5	1,018.1	
Creditors: amounts falling due within one year					Current liabilities
	–	(20.8)	–	(20.8)	Bank overdrafts
Loans	(79.7)	–	–	(79.7)	Interest bearing loans and borrowings
Other creditors	(551.9)	126.1	42.6	(383.2)	Trade and other payables
	–	(104.1)	(1.6)	(105.7)	Income tax liabilities
	–	–	(24.2)	(24.2)	Employee benefits
	–	(94.1)	–	(94.1)	Provisions
	(631.6)	(92.9)	16.8	(707.7)	
Net current assets	251.2	(100.1)	159.3	310.4	Net current assets
Creditors: amounts falling due in more than one year					Non current liabilities
Loans	(979.9)	–	(151.4)	(1,131.3)	Interest bearing loans and borrowings
Other creditors	(55.1)	3.1	(4.2)	(56.2)	Trade and other payables
	–	(65.0)	(18.3)	(83.3)	Deferred tax liabilities
	–	(30.3)	(238.6)	(268.9)	Employee benefits
Provisions for liabilities and charges	(220.3)	180.3	(0.9)	(40.9)	Provisions
	(1,255.3)	88.1	(413.4)	(1,580.6)	
Net assets	1,021.4	–	(283.7)	737.7	Net assets

(a) Overall impact of changes

The tables below summarise the major impacts of IFRS on the Group and further details of these adjustments are given in Section B below.

Income statement

Reconciliation of the loss before tax for the year ended 31 December 2004:

	Before separately disclosable items £m	Separately disclosable items £m	Total £m
Profit/(loss) before tax – UK GAAP	170.2	(380.2)	(210.0)
Pensions and post retirement benefits (IAS 19)	7.8	40.8	48.6
Scope of consolidation (IAS 27)	(9.0)	8.9	(0.1)
Goodwill (IFRS 3)	15.2	37.6	52.8
Share-based payments (IFRS 2)	(1.9)	–	(1.9)
Other items	(6.0)	–	(6.0)
Profit/(loss) before tax – IFRS (UK GAAP format)	176.3	(292.9)	(116.6)
Reformat joint venture and associate tax	(11.8)	–	(11.8)
Reformat joint venture and associate minorities	(0.8)	–	(0.8)
Profit/(loss) before tax – IFRS (IFRS format)	163.7	(292.9)	(129.2)
Effect of IFRS 5 (Cold Logistics and Container Shipping)	(56.6)	(1.4)	(58.0)
Loss before tax – IFRS	107.1	(294.3)	(187.2)

The IFRS adjustments result in related tax adjustments. In addition, IAS 12 results in further adjustments to the tax charge and tax provisions (see Section B 'Taxation').

The IFRS treatment of the P&O Nedlloyd transaction is the major adjustment affecting separately disclosable items (see Section B 'Partial sell down of holding in P&O Nedlloyd').

The majority of the impact of IAS 27 on 2004 pre-tax profit relates to a specific property transaction. £6.4m of the £15.2m adjustment to goodwill amortisation in 2004 relates to Ferries. All goodwill in Ferries as at 31 December 2004 was written off.

Net assets

Reconciliation of net assets as at 31 December 2004:

	Net assets excluding net debt £m	Net debt £m	Net assets £m
Net assets – UK GAAP	2,051.0	(1,029.6)	1,021.4
Pensions and post retirement benefits (IAS 19)	(296.0)	–	(296.0)
Scope of consolidation (IAS 27)	142.7	(145.9)	(3.2)
Goodwill (IFRS 3)	11.4	–	11.4
Dividend recognition (IAS 10)	46.0	–	46.0
Taxation (IAS 12)	(20.7)	–	(20.7)
Other items	(15.1)	(6.1)	(21.2)
Net assets – IFRS	1,919.3	(1,181.6)	737.7

Cash flow

IFRS accounting adjustments have no impact on the Group's actual cash flow. However, the reclassification of certain balance sheet items slightly changes the reported cash equivalent balance and, as can be seen from the net asset statement above, the change to the scope of consolidation increases the Group's borrowings (see Section B 'Scope of consolidation').

(b) Changes in accounting policies

The significant changes in the Group's accounting policies required by IFRS are set out below.

Presentation of financial statements

The Group's financial statements have been presented in accordance with IAS 1 'Presentation of Financial Statements'.

The major impact on the income statement is in the presentation of the Group's share of the results of associates and equity accounted joint ventures as a single line item. Under UK GAAP, the Group's share of operating results, interest, taxation and minorities were reported separately within the relevant sub totals of the Group's profit and loss statement. Thus under IFRS the Group's share of the taxation and minority interests of joint ventures and associates is included in profit before taxation. This does not affect the profit attributable to stockholders.

The format of the balance sheet has been changed to reflect the items required by IAS 1 to be disclosed on the face of the balance sheet and a number of other reclassifications.

These presentational changes are set out on pages 87 to 89 which reconciles the UK GAAP format to the IFRS format before the IFRS accounting policy adjustments described in the remainder of this section.

Transitional arrangements

IFRS 1 sets out the rules for first time adoption of IFRS. In general, these require a company to determine its IFRS accounting policies and then apply those retrospectively to determine its opening or 'transition balance sheet'. There are, however, certain exemptions to this general transitional requirement which the Group has adopted as follows:

- The Group has elected not to restate business combinations that took place before the transition date
- In some cases the latest valuations of property at the transition date have been used as deemed cost and property will no longer be revalued
- The Group has taken advantage of the exemption available under IFRS to 'zero' the foreign currency translation reserve at transition date
- The Group has applied the exemption available under IFRS 1 that allows for comparatives not to be restated for IAS 32 and IAS 39
- IFRS 5 has been applied prospectively from 1 January 2005

Pensions and other post retirement benefits

IAS 19 'Employee Benefits' requires defined benefit pension fund surpluses and deficits to be recognised on the balance sheet and separate recognition of the operating and financing costs of the schemes within the income statement. There are a number of options for the recognition of any actuarial gains and losses which arise and the Group has adopted the policy to recognise any variations in full in the statement of recognised income and expense.

These accounting treatments have no impact on the cash funding of the schemes.

The impact of IAS 19 can be summarised as follows:

	Year ended 31 December 2004 £m	
Income statement		
Operating loss		13.5
Share of result of joint ventures and associates		1.2
Net financing costs		(1.5)
Loss on sale of businesses		35.4
Adjustment to loss before taxation		48.6
Related taxation adjustment		(2.2)
Adjustment to loss after taxation		46.4
Adjustment to loss before taxation analysed as		
Before separately disclosable items		7.8
Separately disclosable items		40.8
		48.6
	At 1 January 2004 £m	At 31 December 2004 £m
Net assets		
Write back SSAP 24 balances	6.1	(10.6)
Include pension holiday prepayment	–	5.3
Include IAS 19 pension liability:		
Main P&O pension scheme	(218.7)	(242.0)
Share of P&O Nedlloyd pension schemes*	(69.5)	(39.4)
Other pension schemes and benefits	(22.1)	(23.0)
	(304.2)	(309.7)
Related taxation adjustment	9.7	13.7
Adjustment to net assets	(294.5)	(296.0)

* Included within investments in joint ventures and associates

For 2004 under IFRS, the Group continued to account for the two merchant navy industry-wide schemes (the MNOPF and the MNRPF) on a cash basis as if they were defined contribution schemes. However, following the court decision in 2005, in respect of the MNOPF the Group has sufficient information to account for its share of the scheme as a defined benefit scheme under IAS 19 and recognise its share of the deficit on the balance sheet for 2005. Page 78 outlines in detail the effect of the court case on the Group in 2005.

The deficit on the main P&O scheme is higher than that disclosed under UK GAAP (FRS 17) due to the adoption of bid values for the scheme assets and the capitalisation of the present value of the future scheme administration costs associated with past benefit accruals.

Scope of consolidation

IAS 27 'Consolidated and Separate Financial Statements' requires that the 'power to control' is considered in determining whether an entity should be consolidated, which is a broader definition than under UK GAAP. The Group reviewed the facts and circumstances of all of its investments at the transition date and concluded that there was one entity, the Hanseatic Trade Center ('HTC'), which was accounted for as a 47.5 per cent associate under UK GAAP where the existence of certain options over the interests of the other partners need to be taken into account under IFRS. Hence the entity has been consolidated as a subsidiary under IFRS. For the Company financial statements which are still being prepared under UK GAAP HTC is treated as an associate.

The impact of the change can be summarised as follows:

	Year ended 31 December 2004 £m
Income statement	
Operating loss	(52.2)
Share of loss of joint ventures and associates pre-tax	32.8
Amounts written off investments	29.2
Net financing costs	(9.9)
Adjustment to loss before taxation	(0.1)
Share of joint ventures and associates tax	0.4
Adjustment to IFRS loss before taxation	0.3
Related taxation adjustment	(0.8)
Adjustment to loss after taxation	(0.5)
Adjustment to loss before taxation analysed as	
Before separately disclosable items	(9.0)
Separately disclosable items	8.9
	(0.1)

	At 1 January 2004 £m	At 31 December 2004 £m
Net assets		
Movement in joint ventures and associates	(54.1)	1.1
Increase in property held for development and sale	271.6	146.8
Decrease in net current assets	(1.7)	(4.3)
Increase in borrowings	(217.2)	(145.2)
	(1.4)	(1.6)
Related taxation adjustment	(1.0)	(1.6)
Adjustment to net assets	(2.4)	(3.2)

The HTC property was sold during 2005. Under IFRS, the cash proceeds of approximately €200m (£140m) were recognised in the Group's cash flow statement.

Goodwill and business combinations

IFRS 3 'Business Combinations' prohibits the amortisation of goodwill. It requires goodwill to be carried at cost with an annual impairment test performed. Under IFRS goodwill previously written off to reserves is not 'clawed back' when the relevant business is sold, as it was under UK GAAP.

The Group has elected to adopt the exemption available under IFRS 1 and has applied IFRS 3 prospectively from the transition date. This results in the value of any goodwill being frozen at the transition date and any amortisation previously charged in the year ended 31 December 2004 being reversed as part of the IFRS restatement.

The impact of these changes can be summarised as follows:

	Year ended 31 December 2004 £m	
Income statement		
Reversal of goodwill amortisation in subsidiaries		12.9
Movements in negative goodwill		(0.4)
Reversal of goodwill amortisation in joint ventures and associates		2.1
Reversal of goodwill clawback on sale of businesses		44.6
Additional impairment of goodwill		(6.4)
Adjustment to loss before taxation		52.8
Related taxation adjustment		–
Adjustment to loss after taxation		52.8
Adjustment to loss before taxation analysed as		
Before separately disclosable items		15.2
Separately disclosable items		37.6
		52.8
	At 1 January 2004 £m	At 31 December 2004 £m
Net assets		
Reversal of goodwill amortisation	–	12.9
Additional impairment of goodwill	(0.9)	(7.1)
Adjustments to goodwill within joint ventures and associates	0.2	1.8
Write back negative goodwill	4.5	3.8
	3.8	11.4
Related taxation adjustment	–	–
Adjustment to net assets	3.8	11.4

Dividend recognition

Under IAS 10 'Events After the Balance Sheet Date' dividends are not recognised until they are declared. As a result the accrued final dividend on deferred stock has been reversed. This adjustment has increased net assets by £67.7m at 1 January 2004 and £46.0m at 31 December 2004.

Share-based payments

The approach to share-based payments is different to that previously applied under UK GAAP. IFRS 2 'Share-based Payment' requires that a fair value charge is made to the income statement for all share-based payments granted to employees since 7 November 2002.

The impact of this treatment is a charge to the income statement of £1.9m in 2004. There is no material tax impact and no impact on net assets.

Taxation

The taxation impact of each of the IFRS adjustments has been included within the details of the relevant adjustment above.

In addition there are a number of specific requirements under IAS 12 'Income Tax' whereby it is necessary to reflect the deferred taxation impact of certain temporary differences which was not required under UK GAAP:

- Provision for deferred tax on unremitted earnings of certain overseas subsidiaries, joint ventures and associates
- Provision for deferred tax on revalued assets and rolled over gains

These changes result in an additional tax charge in 2004 of £6.2m, and net additional tax provisions within net assets of £20.7m as at 1 January 2004 and £20.7m as at 31 December 2004.

Other items

Included within other items are adjustments to both the income statement and balance sheets to reflect changes in accounting for lease incentives and a number of balance sheet reclassifications, the most significant of which relates to the reclassification of £145m to prepaid leases from other asset categories as at 31 December 2004.

Partial sell down of holding in P&O Nedlloyd

The accounting for the partial sale of P&O Nedlloyd ('PONL') in 2004 is complex, and results in a profit on disposal under IFRS as opposed to the previously reported loss on disposal under UK GAAP. The principal reasons for this change are:

- The inclusion of PONL's share of pension deficits in its balance sheet at the transaction date, reducing the net assets disposed
- The fact that it is not permitted under IFRS to 'clawback' goodwill previously written off to reserves

The impact of the change can be summarised as follows:

	UK GAAP £m	IFRS £m
Cash consideration	139.2	139.2
25% share of the net assets of Royal P&O Nedlloyd after the transaction	180.9	150.2
	320.1	289.4
50% share of the net assets of PONL prior to the transaction	(341.2)	(279.8)
	(21.1)	9.6
Goodwill clawback	(44.3)	–
Net (loss)/profit on disposal	(65.4)	9.6

Financial instruments

IAS 32 covers the disclosure and presentation of financial instruments, while IAS 39 deals with the recognition and measurement of financial instruments including hedging arrangements.

The Group has applied the exemption available under IFRS 1 that allows for comparatives not to be restated for IAS 32 and IAS 39.

All derivative financial instruments are accounted for at fair market value whilst other financial instruments are accounted for either at amortised cost or at fair value depending on their classification. Subject to specific criteria, derivative financial instruments, financial assets and financial liabilities may be designated as forming hedge relationships as a result of which fair value changes are offset in the income statement or recognised directly in the statement of recognised income and expense depending on the nature of the hedge relationship.

From 1 January 2005 hedge accounting has been adopted for the Group's interest rate swaps, currency swaps and forward foreign currency contracts, thereby reducing potential volatility in the income statement.

The impact of the transition to IFRS in respect of financial instruments as at 1 January 2005 is summarised below:

	£m	£m
Net assets at 31 December 2004		737.7
Adjustments to net assets:		
Fair value of foreign exchange derivatives	(4.4)	
Related taxation effect (see note 14)	0.6	
		(3.8)
Fair value of interest rate derivatives		(26.5)
Fair value of derivative financial instruments within joint ventures and associates		3.1
Adjusted net assets at 1 January 2005		710.5

The above adjustments to net assets at 1 January 2005 total £27.2m of which, as set out in the consolidated statement of recognised income and expense on page 39, £23.0m is in respect of effective cash flow hedges, and is taken to the hedging reserve, and the balance of £4.2m is an adjustment to retained earnings (see note 25).

As noted above, the Group has not restated comparative amounts for IAS 32 and IAS 39. Had the Group balance sheet as at 31 December 2004 been restated in this regard, trade and other payables would have increased by £37.9m (of which £13.1m is current and £24.8m non-current), trade and other receivables would have increased by £7.0m (of which £2.5m is current and £4.5m non-current), investments in joint ventures and associates would have increased by £3.1m and deferred tax liabilities would have decreased by £0.6m.

The effect on the income statement of applying these two standards in the comparatives is not material.

In accordance with FRS 13 of UK GAAP, the Group disclosed the fair value of derivative financial instruments in its 2004 accounts. This forms an appropriate basis for guidance as to the impact of IAS 39 on the Group's balance sheet at 1 January 2005.

Non-current assets held for sale and discontinued operations

Immediately before classification as held for sale, the measurement of the assets (and all assets and liabilities in a disposal group) is brought up to date in accordance with applicable IFRS. On initial classification as held for sale, non-current assets and disposal groups are recognised at the lower of carrying amount and fair value less costs to sell. Impairment losses on initial classification as held for sale are included in profit or loss, including where there has been a revaluation. The same applies to gains and losses on subsequent remeasurement.

A discontinued operation is a component of the Group's business that represents a separate major line of business or geographical area of operations or is a subsidiary acquired exclusively with a view to resale. Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier.

The implementation of IFRS 5 has no impact on previously reported net assets, although has led to the reclassification of certain items within the comparative income statements.

Company balance sheet

at 31 December 2005

	Note	2005 £m	Restated 2004 £m
Fixed assets			
Tangible assets:			
Ships and other fixed assets	E	23.8	20.7
Investments:			
Subsidiaries	F	2,698.8	3,292.2
Participating interests in joint ventures	G	46.4	46.4
Participating interests in associates	G	104.5	206.9
Other investments	G	0.1	0.1
		2,873.6	3,566.3
Current assets			
Properties held for development and sale	H	29.2	27.1
Debtors:			
Amounts falling due within one year	I	53.9	42.9
Amounts falling due after more than one year	I	–	3.4
		53.9	46.3
Cash at bank and in hand		68.6	50.9
		151.7	124.3
Creditors: amounts falling due within one year			
Loans	J	–	(20.0)
Other creditors	K	(82.9)	(107.0)
		(82.9)	(127.0)
Net current assets/(liabilities)		68.8	(2.7)
Total assets less current liabilities		2,942.4	3,563.6
Creditors: amounts falling due in more than one year			
Loans	J	(241.2)	(538.8)
Other creditors	K	(754.0)	(1,138.2)
		(995.2)	(1,677.0)
Provisions for liabilities and charges	L	(111.4)	(94.5)
Net assets		1,835.8	1,792.1
Capital and reserves			
Called up share capital	M	822.2	813.5
Share premium account	N	792.2	782.9
Profit and loss account	N	221.4	195.7
Stockholders' funds		1,835.8	1,792.1

The accounts were approved by a duly authorised committee of the Board of directors and signed on its behalf on 1 June 2006 by:

Robert Woods
Michael Gradon

Notes to the Company accounts

A Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the accounts of the Company except as noted below.

Basis of preparation of accounts

The accounts have been prepared on the historical cost basis and in accordance with the Companies Act 1985.

The accounts have been prepared in accordance with applicable United Kingdom accounting standards, and on a consistent basis except as noted below.

Under section 230(4) of the Companies Act 1985 the Company is exempt from the requirement to present its own profit and loss account.

Under Financial Reporting Standard 1 (Revised 1996), the Company is exempt from the requirement to prepare a cash flow statement as the Group cash flow statement is published on page 41.

Accounting policies for new standards

The Company has adopted the following accounting standards from 1 January 2005.

The Accounting Standards Board ("ASB") first issued FRS 17 'Retirement benefits' in November 2000, and the Company has applied the transitional arrangements under FRS 17, relating to disclosures, since the year ended 31 December 2001. FRS 17 has been fully adopted by the Company for the first time in the year ended 31 December 2005. Under full application, the Company's net obligation in respect of defined benefit pension plans has been reflected as a liability on its balance sheet. Actuarial gains and losses that arise in calculating the Company's obligations in respect of such plans are recognised directly in reserves. The operating and financial costs of such plans are recognised separately in the profit and loss account.

The ASB issued FRS 20 'Share-based Payment' in April 2004. The Company operated five employee share plans: the Executive Stock Option Plan ("P&O Option Plan"), the P&O 2004 UK Sharesave Plan ("2004 Plan"), the Deferred Bonus and Co-investment Matching Plan ("Matching Plan"), the P&O Performance Share Plan ("Performance Share Plan") and the P&O 2005 Matching Share Plan ("2005 Matching Share Plan"). The fair values of grants under the P&O Option Plan and 2004 Plan were calculated using binomial valuation models. The fair values of awards under the Matching Plan, Performance Share Plan and 2005 Matching Share Plan are calculated by discounting the share price at the date of award in respect of the relevant performance conditions. The fair value is measured at grant date and, in accordance with FRS 20, the resulting cost is charged to the profit and loss account over the period during which the employees become unconditionally entitled to the options or shares. The amount recognised as an expense is adjusted to reflect changes in expected and actual levels of options vesting.

The ASB issued FRS 21 'Events after the balance sheet date' in May 2004. This standard replaced Statement of Standard Accounting Practice 17 'Accounting for post balance sheet events' and the main effect of this change is to prohibit the recording of a provision for a proposed dividend where the dividend is declared after the balance sheet date. FRS 21 is applicable for accounting periods beginning on or after 1 January 2005. Therefore final dividends are now only recognised in the profit and loss account when stockholders have approved such amount and interim dividends are only recognised when paid.

During the year the Company also adopted FRS 23 'The Effects of Changes in Foreign Exchange Rates', FRS 25 'Financial Instruments: Disclosure and Presentation', FRS 26 'Financial Instruments: Measurement' and FRS 28 'Corresponding Amounts'. The adoption of these standards has not had a material impact on the Company's balance sheet.

The impact of first time adoption of these standards is set out in note N to the Company accounts.

Ships and other fixed assets

These assets are stated at cost less accumulated depreciation.

Assets acquired under finance leases are stated at cost less accumulated depreciation, the future capital payments being included in loans.

Depreciation is calculated to write off the cost of these assets to estimated residual value, on a straight line basis over the expected useful life of the asset concerned. Generally for ships this is between 10 and 35 years, and for other fixed assets (reported within plant and machinery, fixtures and fittings) various periods of up to 40 years.

Provision for any impairment in value of ships and other fixed assets is made in the profit and loss account.

Assets constructed by the Company are depreciated from the date on which they come into use. Interest incurred in respect of assets under construction is capitalised into the cost of the asset concerned.

Properties held for development and sale

Properties held for development and sale are included in current assets at the lower of cost and net realisable value.

Turnover

Turnover comprises amounts derived from the provision of goods and services to third parties (excluding VAT and similar sales taxes). Turnover from the provision of services is recognised on the delivery of those services.

Leases

Ships, plant and machinery and land and buildings financed by leasing agreements giving rights approximating to ownership are capitalised as tangible fixed assets at cost less accumulated depreciation. The capital element of future lease payments is treated as a liability. The interest element is charged to the profit and loss account over the period of the finance lease in proportion to the balance of capital repayments outstanding.

All other leases are classified as operating leases with the lease rentals payable being charged to the profit and loss account on a straight line basis.

A Accounting policies (continued)

Employee benefits

Pensions

The Company's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods. That benefit is discounted to determine the present value, and the fair value of any plan assets is deducted. The calculation is performed by a qualified actuary using the projected unit credit method. The discount rate is the yield at the balance sheet date on AA credit rated bonds or local equivalent that have maturity dates approximating to the terms of the Group's obligations.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the profit and loss account on a straight line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in the profit and loss account.

Actuarial gains and losses that arise in calculating the Company's obligation in respect of a plan are recognised in the period in which they arise directly in reserves.

The operating and financing costs of defined benefit pension plans are recognised separately in the profit and loss account; current service costs are spread systematically over the expected average remaining service lives of employees and financing costs are recognised in the periods within which they arise.

Contributions, including lump sum payments, in respect of defined contribution pension schemes and multi employer defined benefit schemes where it is not possible to identify the Company's share of the scheme, are charged to the profit and loss account as they fall due.

Deferred taxation

Deferred tax is recognised without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet dates except in respect of revalued fixed assets where there is no commitment to sell the asset, gains on sale of assets which are rolled over into replacement assets and the remittance of taxable subsidiary, associate or joint venture earnings where no commitment has been made to the remittance of those earnings.

Foreign currency

Foreign currency transactions

Transactions in foreign currencies are recorded at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into sterling at the rate of exchange ruling at that date. Foreign exchange differences arising on translation are recognised in the profit and loss account. Non-monetary asset and liabilities that are measured in terms of historical cost in a foreign currency are translated using the rate of exchange ruling at the date of the transaction.

Net investment in foreign operations

Exchange differences arising from the translation of the net investment in foreign operations, and of related hedges, are taken to the translation reserve in accordance with the hedging policy described below.

Financial instruments

FRS 25 and FRS 26 address the accounting for, and reporting of, financial instruments. FRS 26 sets out detailed accounting requirements in relation to financial assets and liabilities. As outlined above under 'Accounting policies for new standards', this has been applied by the Company for the first time for the year ended 31 December 2005. Under the exemption available the comparatives have not been restated for FRS 25 and FRS 26 and continue to reflect the disclosure requirements of FRS 13 'Derivatives and other Financial instruments: disclosures'.

A Accounting policies (continued)**Hedging****Hedge of foreign investments**

Where a foreign currency liability hedges a net investment in a foreign operation, the portion of foreign exchange differences arising on translation of the liability that is determined to be an effective hedge is recognised directly in equity. The ineffective portion is recognised immediately in profit or loss. Where exchange differences have been deferred in equity, they are recycled to the income statement upon disposal of the respective foreign investments.

As noted above, the comparatives have not been restated for FRS 25 and FRS 26. Accordingly the Company has continued to reflect FRS 13, in its comparative figures.

Financial guarantees

The Company has not adopted the amendment to FRS 26 in relation to financial guarantee contracts which will apply for periods commencing on or after 1 January 2006.

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its group, joint ventures or associates, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

The Company does not expect the amendment to have any impact on the financial statements for the period commencing 1 January 2006.

Investments**Investments in debt and equity securities**

Where the Company has the positive intent and ability to hold debt instruments to maturity, they are stated at amortised cost less impairment losses.

Other investments in debt and equity securities held by the Company are classified as being available-for-sale and are stated at fair value, with any resultant gain or loss being recognised directly in equity, except for impairment losses and, in the case of monetary items such as debt securities, foreign exchange gains and losses. When these investments are derecognised, the cumulative gain or loss previously recognised in equity is recognised in profit or loss. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss.

The fair value of financial instruments classified as available-for-sale is their quoted bid-price at the balance sheet date. Available-for-sale investments are recognised/derecognised by the Company on the date it commits to purchase/sell the investments. Securities held-to-maturity are recognised/derecognised on the day they are transferred to/by the Company.

The Company does not hold investments in debt or equity securities for trading purposes.

The comparative information for other investments are presented in accordance with FRS 13 and are stated at historical cost net of provisions for impairment.

B Audit Fees

The Company's audit fee paid to KPMG was £0.5m (2004 £0.5m).

C Dividends on share capital

Dividends paid are as follows:	2005 £m	Restated 2004 £m
Deferred stock	(66.2)	(87.8)
Preferred stock	(0.1)	(0.1)
5.5% concessionary stock	(3.7)	(3.7)
	(70.0)	(91.6)

After the balance sheet date a dividend of 6.0p per £1 nominal of deferred stock was proposed by the directors in respect of 2005 (2004 6.0p). This dividend has not been provided.

D Profit for the financial year attributable to stockholders

The profit for the financial year attributable to stockholders, being the profit on ordinary activities after taxation, was £188.6m (2004 £199.5m).

E Ships and other fixed assets

	Leased ships £m	Owned plant and machinery, fixtures and fittings £m	Total £m
Cost at 1 January 2005	30.7	6.7	37.4
Additions	–	5.3	5.3
Disposals	–	(2.7)	(2.7)
Cost at 31 December 2005	30.7	9.3	40.0
Depreciation at 1 January 2005	(11.9)	(4.8)	(16.7)
Depreciation charge for the year	(1.2)	(0.6)	(1.8)
Disposals	–	2.3	2.3
Depreciation at 31 December 2005	(13.1)	(3.1)	(16.2)
At 31 December 2005	17.6	6.2	23.8
At 31 December 2004	18.8	1.9	20.7

There is no interest capitalised.

F Investment in subsidiaries

	Shares at cost £m	Loans £m	Provisions against shares £m	Provisions against loans £m	Total £m
At 1 January 2005	2,013.1	1,614.6	(132.0)	(203.5)	3,292.2
Exchange movements	–	20.3	–	–	20.3
Additions/increases	–	208.0	(2.9)	(0.5)	204.6
Disposals/decreases	(99.0)	(781.2)	61.4	0.5	(818.3)
At 31 December 2005	1,914.1	1,061.7	(73.5)	(203.5)	2,698.8

The principal subsidiaries are shown on page 115.

G Joint ventures, associates and other investments

	Investment in joint ventures £m	Investment in associates £m	Joint venture and associate loans £m	Other investments £m	Total £m
Cost at 1 January 2005	53.5	206.9	10.4	0.1	270.9
Exchange movements	–	–	(0.2)	–	(0.2)
Additions	–	104.5	12.5	–	117.0
Transfer on acquisitions as subsidiaries	–	–	–	–	–
Disposals/repayments	–	(206.9)	–	–	(206.9)
Cost at 31 December 2005	53.5	104.5	22.7	0.1	180.8
Provisions at 1 January 2005	(7.1)	–	(10.4)	–	(17.5)
Transfers from profit and loss account	–	–	(12.3)	–	(12.3)
Provisions at 31 December 2005	(7.1)	–	(22.7)	–	(29.8)
At 31 December 2005	46.4	104.5	–	0.1	151.0
At 31 December 2004	46.4	206.9	–	0.1	253.4

- (i) During the year the Company's trading with joint ventures and associates included £47.3m (2004 £57.2m) received from P&O Nedlloyd. The Company's operating profit also includes £0.4m (2004 £1.9m) in respect of management and guarantee fees from joint ventures and associates during the year.
- (ii) On 29 June 2005 the Company sold its 25 per cent interest in Royal P&O Nedlloyd N.V. Total proceeds of £381.0m (€56.25 per share) were received on 30 June 2005 and resulted in a gain of £173.0m.
- (iii) The issued share capital of the principal joint ventures and associates at 31 December 2005 was as follows:

	Number in issue	Nominal value of each class of share capital and issued debt	Percentage held
Joint ventures			
Managed Offices Limited	4,800,100	Ordinary	50
Wyseproperty Limited	20,000,000	Ordinary A	–
	20,000,000	Ordinary B	100
Associates			
HTC Hanseatic Trade Center GmbH & Co Grundbesitz KG	2,000,000	Limited partnership	47.5
PTS Holdings Limited	4,692,406	Ordinary	46.9

H Properties held for development and sale

	Total £m
At 1 January 2005	27.1
Additions	2.1
At 31 December 2005	29.2

All properties held for development and sale are in the UK and are in respect of the separate London Gateway Port and Business Park proposals. The projects received "minded to grant" approvals from respective Secretaries of State in July 2005 specifying certain issues which needed to be resolved before planning consents would be granted. Progress has been made on these issues and final decisions on planning consents are expected in the first half of 2006.

I Debtors

	2005 Falling due		Restated 2004 Falling due	
	within 1 year £m	in more than 1 year £m	within 1 year £m	in more than 1 year £m
Trade debtors	1.0	–	1.3	–
Amounts owed by joint ventures and subsidiaries	7.1	–	–	–
Other debtors	45.1	–	41.6	3.4
Prepayments and accrued income	0.7	–	–	–
	53.9	–	42.9	3.4
		53.9		46.3

Other debtors include £42.6m (2004 £35.7m) relating to previous corporate disposals, net of provisions, arising from the sale of Bovis Group plc in 1999 of which £nil (2004 £3.4m) falls due in more than 1 year.

J Loans

	2005 £m	2004 £m
US dollar bonds and notes 2007 – 2027 (unsecured)	13.5	12.0
Term loans: unsecured	226.3	545.4
Mortgage debenture stocks	1.4	1.4
	241.2	558.8

All the above loans are non-convertible.

Loans are denominated in the following currencies:

	Sterling £m	US dollars £m	Australian dollars £m	Euro £m	Other £m	Total £m
At 31 December 2005	104.7	83.9	15.6	6.9	30.1	241.2
At 31 December 2004	233.4	230.5	55.4	3.6	35.9	558.8

An analysis of the maturity and interest rates of fixed rate loans is as follows:

Interest rate	Repayable					2005 Total £m	2004 Total £m
	Within one year £m	Between one and two years £m	Between two and five years £m	Between five and ten years £m	Over ten years £m		
6% or less	–	–	–	–	1.4	1.4	1.4
Over 6% to 8%	–	8.9	–	–	4.6	13.5	12.0
Over 8%	–	–	–	–	–	–	–
At 31 December 2005	–	8.9	–	–	6.0	14.9	
At 31 December 2004	–	–	7.9	–	5.5		13.4

An analysis of the maturity of total loans is as follows:

At 31 December 2005	–	8.9	226.3	–	6.0	241.2
At 31 December 2004	20.0	276.1	257.2	–	5.5	558.8

J Loans (continued)

The maturity profile of financial liabilities, other than short term creditors (such as trade creditors and accruals), at 31 December 2005 was as follows:

	2005 £m	2004 £m
In one year or less, or on demand	46.0	84.6
In more than one year, but not more than two years	8.9	276.1
In more than two years, but not more than five years	226.3	257.2
In more than five years	6.0	5.5
	287.2	623.4

The undrawn committed facilities available at 31 December 2005 in respect of which all conditions precedent had been met at that date were as follows:

	2005 £m	2004 £m
Expiring in one year or less	–	162.7
Expiring in more than one year, but not more than two years	–	221.7
Expiring in more than two years	616.1	99.6
	616.1	484.0

As a result of the change of control following the DP World takeover on 8 March 2006 (see note U) facilities totalling £890.9m may be cancelled at the bank's option. DP World has arranged sufficient acquisition finance to allow any amounts drawn under these facilities to be repaid as they fall due.

K Other creditors

	2005 Falling due		Restated 2004 Falling due	
	within 1 year £m	in more than 1 year £m	within 1 year £m	in more than 1 year £m
Unsecured bank overdrafts	46.0	–	64.8	–
Trade creditors	0.1	–	0.1	–
Amounts owed to joint ventures and associates	17.7	–	8.7	–
Amounts owed to subsidiaries	–	754.0	5.9	1,137.8
Social security and other taxation	1.3	–	3.7	–
Other unsecured creditors	2.4	–	9.5	0.4
Accruals and deferred income	15.4	–	14.3	–
	82.9	754.0	107.0	1,138.2
	836.9		1,245.2	

Amounts owed to subsidiaries have no fixed term of repayment.

L Provisions for liabilities and charges

	Employee benefits £m	Other provisions £m	Total £m
At 1 January 2005 (restated)	92.3	2.2	94.5
Transfers from profit and loss account	3.2	21.0	24.2
Transfers from/(to) statement of total recognised gains and losses	88.5	–	88.5
Exchange movements	–	0.3	0.3
Applied during the year	(87.7)	(8.4)	(96.1)
At 31 December 2005	96.3	15.1	111.4

	2005 £m	2004 £m
Deferred taxation comprises:		
Accelerated capital allowances	–	0.1
Other	–	(0.1)
	–	–

Provisions for employee benefits relate to defined benefit pension schemes as set out in note Q.

Other provisions include £12.5m (2004 £nil) in respect of rental guarantees for properties in Germany and £1.5m (2004 £nil) for onerous leases as a result of the Company's relocation to its new offices in December 2005. The directors expect £9.9m of the other provision balance to be utilised prior to 31 December 2006.

M Share capital

Details of the Company's share capital are set out in note 24 to the Group financial statements.

N Reserves

	Share premium account £m	Profit and loss account £m	Total £m
At 1 January 2005	782.9	244.8	1,027.7
Prior year adjustment	–	(49.1)	(49.1)
At 1 January 2005 (restated)	782.9	195.7	978.6
Exchange movements	–	(0.7)	(0.7)
Issues of stock	9.5	–	9.5
Amortisation of debt issue costs	(0.2)	0.2	–
Purchases of own stock	–	(5.8)	(5.8)
Share-based payments	–	1.9	1.9
Actuarial gains and losses	–	(88.5)	(88.5)
Retained profit for the financial year	–	118.6	118.6
At 31 December 2005	792.2	221.4	1,013.6

The P&O Group Employee Benefit Trust (the "Trust") is used in connection with the Group's Deferred Bonus and Co-investment Matching Plan (the "Matching Plan"), the P&O Performance Share Plan (the "Performance Share Plan") and the P&O 2005 Matching Share Plan (the "2005 Matching Share Plan"), the terms of which are set out in the directors' remuneration report on pages 28 to 35. The Trust may also be used in connection with the Group's other share based plans, including the Executive Stock Option Plan. The Trustee of the Trust purchases the Company's stock in the open market, as required, on the basis of regular reviews of the anticipated liabilities of the Group, with financing provided by the Company. All expenses of the Trust are settled directly by the Company and charged in the financial statements as incurred.

As at 31 December 2005 the Trust held £12,096,283 nominal of deferred stock of the Company (2004 £11,435,110 nominal) representing 1.6 per cent (2004 1.5 per cent) of the Company's deferred stock. During the year the Trust acquired £1,900,000 nominal of deferred stock of the Company (2004 £4,934,437 nominal), representing 0.3 per cent (2004 0.7 per cent) of the Company's deferred stock, and £1,238,827 nominal of deferred stock of the Company (2004 £144,518 nominal), representing 0.2 per cent (2004 nil per cent) of the Company's deferred stock, was distributed by the Trust to participants in the Matching Plan under the terms of that plan.

The profit and loss account reserve is stated after the deduction of £30.8m (2004 £28.4m) in respect of £12,096,283 nominal of deferred stock of the Company (2004 £11,435,110 nominal) held by the Trust, of which £516,069 nominal (2004 £402,032 nominal) has been conditionally awarded to participants in the Matching Plan. Further stock awards over £4,287,491 nominal (2004 £2,132,996 nominal) have been granted to participants under the Matching Plan, the Performance Share Plan and the 2005 Matching Share Plan, which will be met by the Trust to the extent that the performance conditions are met. The market value of the deferred stock held by the Trust as at 31 December 2005 was £56.4m.

The profit and loss account reserve is also stated after a credit of £3.3m (2004 £2.5m) relating to charges made to the profit and loss account in respect of equity settled share-based payments, including the fair values of awards and grants under the Matching Plan, Performance Share Plan and 2005 Matching Share Plan, which will be met by the Trust, and the fair value of options granted under the Executive Stock Option Plan and the P&O 2004 UK Sharesave Plan.

As described in note A the Company has adopted a number of new reporting standards for the first time in the year ended 31 December 2005. Stockholders' funds at the beginning of the year, as previously reported, were £1,841.2m (2004 £1,717.5m), before the prior year adjustments of £95.1m (2004 £80.0m), arising on full adoption of FRS 17 'Retirement benefits', less £46.0m (2004 £67.7m), arising due to the reversal of dividend accruals on adoption of FRS 21 'Events after the balance sheet date'.

Exchange movements in the profit and loss account reserve include a loss of £0.7m (2004 £4.8m) in respect of foreign currency net borrowings.

O Directors' emoluments

Details on directors' emoluments, long term incentives, pension entitlements and deferred stock under option held by the directors are shown in the directors' remuneration report on pages 28 to 35.

P Employees

The average number of people employed by the Company was:

	2005	2004
UK full time	106	124
UK part time	6	8
Overseas full time	2	2
Overseas part time	–	–
	114	134

The aggregate payroll costs, excluding directors' emoluments, were:

	2005 £m	2004 £m
Wages and salaries	10.9	11.8
Social security costs	1.3	1.4
Pensions costs	2.1	3.8
	14.3	17.0

Amounts totalling £0.5m (2004 £0.6m) in respect of equity settled share-based payments were charged to the income statement.

Amounts totalling £0.1m (2004 £0.1m) in respect of 2004 performance related bonuses were settled in 2005 by way of equity settled share-based payments under the Deferred Bonus and Co-Investment Matching Plan.

Equity settled share-based payments

The Company operated five employee share plans: the Executive Stock Option Plan ("P&O Option Plan"), the P&O 2004 UK Sharesave Plan ("2004 Plan"), the Deferred Bonus and Co-investment Matching Plan ("Matching Plan"), the P&O Performance Share Plan ("Performance Share Plan") and the P&O 2005 Matching Share Plan ("2005 Matching Share Plan"). Upon the takeover of the Company by DP World in March 2006, awards under these plans vested according to the provisions of the relevant plan rules.

A summary of the terms and conditions of these plans is included in note 27 to the Group financial statements.

The following analysis includes only those awards and grants made under the above share plans since 7 November 2002 in accordance with the transitional arrangements of FRS 20 'Share-based Payment', so is not a complete analysis of all awards or grants which were outstanding during the year.

(a) Stock Award Plans

	Performance Share Plan		2005 Matching Share Plan		Matching Plan	
	Deferred stock '000	WAFV* pence	Deferred stock '000	WAFV* pence	Deferred stock '000	WAFV* pence
Stock awards (March 2005)	–	–	–	–	123	302
Matching awards (March 2005)	–	–	–	–	410	113
Share Plan awards (May 2005)	784	114	179	114	–	–
Dividend Replacement (June/November 2005)	5	178	1	178	3	350

* WAFV = Weighted average fair value

The fair values of grants under the Stock Award Plans are calculated by discounting the share price at the date of the award in respect of the relevant performance conditions.

P Employees (continued)**(b) Stock Option Plans**

	P&O Option Plan		2004 Plan	
	Options '000	WAEP* pence	Options '000	WAEP* pence
As at 31 December 2003				
Options outstanding	2,751	245	234	128
Movements during 2004				
Options granted	–	–	34	205
Options exercised	–	–	–	–
Options lapsed	(21)	249	(1)	205
Weighted average fair value of options granted during the year		–		89
As at 31 December 2004				
Options outstanding	2,730	245	267	138
Movements during 2005				
Options granted	–	–	13	270
Options exercised	(349)	249	(1)	205
Options lapsed	(26)	249	(7)	205
Dividend Stock	–	–	–	–
Weighted average fair value of options granted during the year		–		102
As at 31 December 2005				
Options outstanding	2,355	244	272	142
Range of exercise prices		223p-249p		128p-270p
Weighted average remaining contractual life		2,808 days		338 days
Options exercisable	373	249	74	128

* WAEP = Weighted average exercise price

Stock options were exercised on a regular basis throughout the year.

The fair values of grants under the Stock Option Plans are calculated using binomial valuation models. The following table gives the assumptions applied to the options granted during the year. Expectations of early exercise are incorporated into the model.

	2005	2004
Average actual share price (pence)	334	243
Weighted average exercise price of options granted in the period (pence)		
P&O Option Plan	–	–
2004 Plan	270	205
Weighted average fair value of options granted in the period (pence)		
P&O Option Plan	–	–
2004 Plan	102	89
Expected volatility (%)	33.5	37.5
Dividend yield (%)	4.0	4.0
Risk-free interest rate (%)	5.0	5.0
Expected lives (years)		
P&O Option Plan	–	3.5
2004 Plan	3.5	3.5

The expected volatility is based on the historic volatility (calculated based on the weighted average life of the options) adjusted for any expected changes to future volatility due to publicly available information.

Q Pensions

The Company participates in two funded UK defined benefit pension schemes and a Group Personal Pension arrangement. The principal scheme, The P&O Pension Scheme (the "P&O UK Scheme"), was closed to routine new members on 1 January 2002. The assets of the scheme are managed on behalf of the trustee by independent fund managers.

The Company also participates in the Merchant Navy Officers' Pension Fund (the "MNOFP Scheme") industry wide scheme.

The latest valuation of the P&O UK Scheme and the MNOFP scheme have been updated to 31 December 2005 by qualified independent actuaries.

The principal assumptions are included in the table below.

The assumptions used by the actuaries are the best estimates chosen from a range of possible actuarial assumptions, which, due to the timescale covered, may not necessarily be borne out in practice.

	P&O UK Scheme			MNOFP Scheme		
	2005	2004	2003	2005	2004	2003
Discount rates	4.75%	5.30%	5.40%	4.75%	n/a	n/a
Expected rates of salary increases	4.20%	4.20%	4.20%	4.20%	n/a	n/a
Pension increases:						
– deferment	2.70%	2.70%	–	2.70%	n/a	n/a
– payment	2.50%	2.50%	2.50%	2.50%	n/a	n/a
Inflation	2.70%	2.70%	2.70%	2.70%	n/a	n/a
Expected rates of return on scheme assets	5.80%	6.20%	6.80%	6.60%	n/a	n/a

The market value of the schemes' assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the schemes' liabilities, which are derived from cash flow projections over long periods and thus inherently uncertain are set out below:

	P&O UK Scheme		MNOFP Scheme		Total market value £m
	Expected long term rate of return %	Market value £m	Expected long term rate of return %	Market value £m	
2005					
Equities	7.70	337.2	7.70	22.1	359.3
Bonds	4.40	463.7	4.50	9.3	473.0
Other	3.70	8.7	5.45	4.0	12.7
	5.80	809.6	6.60	35.4	845.0
Present value of scheme liabilities		(891.0)		(50.3)	(941.3)
Deficit		(81.4)		(14.9)	(96.3)
Related deferred tax asset		–		–	–
Net pension liability		(81.4)		(14.9)	(96.3)
2004					
Equities	8.00	132.4	n/a	n/a	132.4
Bonds	4.70	150.4	n/a	n/a	150.4
Other	3.70	10.0	n/a	n/a	10.0
	6.20	292.8	n/a	n/a	292.8
Present value of scheme liabilities		(385.1)		n/a	(385.1)
Deficit		(92.3)		n/a	(92.3)
Related deferred tax asset		–		n/a	–
Net pension liability		(92.3)		n/a	(92.3)
2003					
Equities	8.30	148.2	n/a	n/a	148.2
Bonds	5.00	116.4	n/a	n/a	116.4
Other	3.70	2.7	n/a	n/a	2.7
	6.80	267.3	n/a	n/a	267.3
Present value of scheme liabilities		(353.4)		n/a	(353.4)
Deficit		(86.1)		n/a	(86.1)
Related deferred tax asset		–		n/a	–
Net pension liability		(86.1)		n/a	(86.1)

Q Pensions (continued)

The pension costs for defined benefit schemes are as follows:

	P&O UK Scheme £m	MNOFF Scheme £m	Total £m
2005			
Operating profit			
Current service cost	(1.8)	–	(1.8)
Past service cost	(0.2)	–	(0.2)
Net gain on settlement and curtailments	(0.7)	–	(0.7)
Total charge to operating profit	(2.7)	–	(2.7)
Other finance income/(expense)			
Expected return on pension scheme assets	35.5	0.6	36.1
Interest on pension scheme liabilities	(36.0)	(0.6)	(36.6)
Net return	(0.5)	–	(0.5)
Statement of total recognised gains and losses			
Actual return less expected return on pension scheme assets	71.1	0.8	71.9
Experience gains and losses on pension scheme liabilities	(86.7)	(0.3)	(87.0)
Amounts arising from P&O Nedlloyd transfer/sale	(57.4)	–	(57.4)
Changes in assumptions underlying the present value of scheme liabilities	–	(1.9)	(1.9)
Reclassification of defined contribution scheme as defined benefit scheme	–	(14.1)	(14.1)
Actuarial loss recognised in statement of total recognised gains and losses	(73.0)	(15.5)	(88.5)
	P&O UK Scheme £m	MNOFF Scheme £m	Total £m
2004			
Operating profit			
Current service cost	(3.6)	n/a	(3.6)
Past service cost	(0.2)	n/a	(0.2)
Net gain on settlement and curtailments	4.2	n/a	4.2
Total charge to operating profit	0.4	n/a	0.4
Other finance income/(expense)			
Expected return on pension scheme assets	18.0	n/a	18.0
Interest on pension scheme liabilities	(18.4)	n/a	(18.4)
Net return	(0.4)	n/a	(0.4)
Statement of total recognised gains and losses			
Actual return less expected return on pension scheme assets	11.1	n/a	11.1
Experience gains and losses on pension scheme liabilities	0.3	n/a	0.3
Changes in assumptions underlying the present value of scheme liabilities	(27.7)	n/a	(27.7)
Actuarial loss recognised in statement of total recognised gains and losses	(16.3)	n/a	(16.3)

Q Pensions (continued)

As the P&O UK Scheme and MNOFF Scheme are both closed to routine new entrants, under the Projected Unit valuation method, the current service cost as a percentage of relevant defined benefit pensionable payroll will increase as the members of the scheme approach retirement.

	2005	2004	2003	2002
P&O UK Scheme				
Difference between the expected and actual return on scheme assets (£m)	71.1	11.1	18.8	(48.6)
As a percentage of scheme assets (%)	8.8	3.8	4.4	(20.3)
Experience gains and losses on pension scheme liabilities (£m)	(86.7)	0.3	0.5	–
As a percentage of the present value of scheme liabilities (%)	(9.7)	0.1	0.2	–
Total actuarial loss recognised in the consolidated statement of total recognised gains and losses (£m)	(73.0)	(16.3)	(15.1)	(35.3)
As a percentage of the present value of scheme liabilities (%)	(8.2)	(4.2)	(4.5)	11.7
MNOFF Scheme				
Difference between the expected and actual return of scheme assets (£m)	0.8	n/a	n/a	n/a
As a percentage of scheme assets (%)	2.3	n/a	n/a	n/a
Experience gains and losses on pension scheme liabilities (£m)	(0.3)	n/a	n/a	n/a
As a percentage of the present value of scheme liabilities (%)	(0.6)	n/a	n/a	n/a
Total actuarial loss recognised in the consolidated statement of total recognised gains and losses (£m)	15.5	n/a	n/a	n/a
As a percentage of the present value of scheme liabilities (%)	(30.8)	n/a	n/a	n/a

	P&O UK Scheme £m	MNOFF Scheme £m	Total £m
Movement in deficit during the two years ended 31 December 2005			
Deficit in schemes at 1 January 2004	(86.1)	n/a	(86.1)
Current service cost	(3.6)	n/a	(3.6)
Contributions paid	10.1	n/a	10.1
Past service cost	(0.2)	n/a	(0.2)
Net gain on settlements and curtailments	4.2	n/a	4.2
Other finance expense	(0.4)	n/a	(0.4)
Actuarial loss	(16.3)	n/a	(16.3)
Deficit in schemes at 31 December 2004	(92.3)	n/a	(92.3)
Current service cost	(1.8)	–	(1.8)
Contributions paid	87.1	0.6	87.7
Past service cost	(0.2)	–	(0.2)
Net gain on settlements and curtailments	(0.7)	–	(0.7)
Other finance expense	(0.5)	–	(0.5)
Reclassification as Defined Benefit Scheme	–	(14.1)	(14.1)
Actuarial loss	(73.0)	(1.4)	(74.4)
Deficit in schemes at 31 December 2005	(81.4)	(14.9)	(96.3)

P&O UK Scheme actuarial valuation for funding purposes

Formal actuarial valuations of the P&O UK Scheme are normally carried out triennially by qualified independent actuaries, the latest regular valuation report for the scheme being at 1 April 2003, using the projected unit method. As a result of the decision by P&O Nedlloyd to form its own UK scheme and the request to transfer its share of the assets and liabilities of the P&O UK Scheme into that new scheme, an additional valuation was carried out as at 30 September 2004 using the projected unit method.

At this date, allowing for the P&O Nedlloyd transfer and related transactions, the market value of the P&O UK Scheme's assets were £987m and the value of accrued benefits to members allowing for future increases in earnings was £1,176m giving a deficit of £189m and a funding ratio of 83.9 per cent.

Excluding the deficit reduction payments, the average contribution rates for the P&O UK Scheme were 22.8 per cent for the year to 31 December 2005 and 23.7 per cent from 1 January 2006.

Q Pensions (continued)

The principal long term assumptions in the UK Scheme's 2004 valuation are:

	Nominal % per annum
Price inflation	3.00
Investment return on pre-retirement portfolio	6.50
Investment return on post-retirement portfolio	5.50
Earnings escalation	4.50
LEL escalation	3.00
Increases in pensions in excess of Guaranteed Minimum Pensions	2.75

As a result of this valuation and the subsequent take over of the Company by DP World, the Company made a further deficit contribution to the scheme of £25m in March 2006 and has committed to further regular monthly deficit payments totalling £75m over the next five years. These monthly payments are supported by a bank guarantee.

Industry schemes

The MNOPF Scheme is a defined benefit multi-employer scheme, in which officers employed by the Company have participated.

The scheme is divided into two sections, the Old Section and the New Section, both of which are closed to new members and the latest valuation was carried out at 31 March 2003.

The Old Section has been closed to benefit accrual since 1978. The scheme's independent actuary advised that at 31 March 2003 the market value of the scheme's assets for the Old Section was £1,316m, representing approximately 115 per cent of the value of the benefits accrued to members. The assets of the Old Section were substantially invested in bonds.

As at 31 March 2003, the date of the most recent formal actuarial valuation, the New Section had assets with a market value of £1,168m, representing approximately 86 per cent of the benefits accrued to members. The valuation assumptions were as follows:

	Nominal % per annum
Discount rate	7.80
Rate of salary increases	4.00
Rate of pension increases (where increases apply)	2.50
Expected return on assets	7.80

At the date of the valuation, approximately 59 per cent of the New Section's assets were invested in equities, 28 per cent in bonds and 13 per cent in property and cash.

The trustee has advised the Company that its share of the net deficit of the New Section is 18.319 per cent and has issued a schedule of regular deficit payments from the Company totalling £5.5m per annum commencing on 30 September 2005 and payable annually on 30 March thereafter until 30 March 2014. Therefore, the Company has accounted for the MNOPF New Section as a defined benefit scheme from 30 September 2005. Prior to that date, the Company accounted for the New Section as a defined contribution scheme as it was unable to determine its share of the scheme. The proportion of the deficit attributable to the Company will change following the next actuarial valuation, to be prepared as at 31 March 2006, as not all employer's have made their deficit payments, with short falls to be reallocated to other employers, and part of the deficit payments being made by Carnival plc are attributable to the Company under the terms of the demerger agreement relating to the demerger of P&O Princess Cruises in 2000.

R Commitments

The Company has no capital commitments.

Revenue

The commitment during the following year in respect of non-cancellable operating leases is as follows:

	Property	
	2005 £m	2004 £m
Lease expiring:		
Within one year	–	0.8
Between one and five years	6.9	0.8
Over five years	17.4	–
	24.3	1.6

S Contingent liabilities

	2005 £m	2004 £m
Loan and lease guarantees on behalf of joint ventures and associates	7.1	3.6
Loan and lease guarantees on behalf of subsidiaries	521.4	471.6
Other contingent liabilities	14.0	78.7
	542.5	553.9

The other contingent liability of £14.0m (2004 £78.7m) relates to a guarantee of the financial liability for a vessel leased to Associated Bulk Carriers Limited, a previous associate of the Company. The lease expires in 2008. Associated Bulk Carriers Limited was sold to Eurotower Holdings SA in December 2003 and as part of the transaction, P&O received a counter indemnity for this liability from First Omega Shipping Inc, the owner of Eurotower Holdings SA.

Included within amounts receivable relating to previous corporate disposals is an amount outstanding of £42.6m (2004 £32.2m) net of relevant provisions arising following the sale of Bovis Group plc in 1999. Pursuant to the sale terms P&O is obliged to provide loan funding and partial indemnification for one of Bovis' projects, the construction of which is now completed and is the subject of litigation. Most of this litigation has been the subject of a settlement agreement as a result of which the bulk of such amounts receivable are expected to be repaid over the next twelve months.

T Financial instruments

FRS 25 and FRS 26 have not been applied for the year ended 31 December 2004, which forms the comparative period and which, for these purposes, have been presented under the previous accounting policy in accordance with FRS 13. The Company has applied the exemption available that allows comparatives not to be restated for FRS 25 and FRS 26. No material adjustments would be required to be made to the comparative information in order to make it comply with FRS 25 and FRS 26.

The Company's policies and procedures in relation to the role and management of financial instruments and financial risk are set out below. These have not been impacted by the application of FRS 25 and FRS 26.

Financial risk

The financial instruments held by the Company to finance its operations include cash, overdrafts, loans, and a limited amount of interest bearing and non-interest bearing investments. The Group manages these risks on a consolidated basis. For an understanding of the Group's management of these risks see note 32 to the Group financial statements.

Effective interest rates and repricing analysis

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and the periods in which they reprice.

	Effective interest rate	Total	Within one year	1 to 2 years	2 to 5 years	More than 5 years
Cash at bank and in hand	4.67%	68.6	68.6	-	-	-
Secured bank loans:						
GBP fixed rate debenture	3.50%	(1.4)	-	-	-	(1.4)
Unsecured bank loans:						
GBP floating rate loan	5.10%	(103.3)	(103.3)	-	-	-
US\$ fixed rate bonds	7.50%	(13.5)	-	(8.9)	-	(4.6)
US\$ floating rate loan	4.72%	(70.5)	(70.5)	-	-	-
AUS\$ floating rate loan	5.89%	(15.6)	(15.6)	-	-	-
Euro floating rate loan	2.78%	(6.9)	(6.9)	-	-	-
HK\$ floating rate loan	4.69%	(30.0)	(30.0)	-	-	-
Loans to subsidiaries						
GBP loans to subsidiaries	5.50%	30.6	30.6	-	-	-
Euro loans to subsidiaries	3.16%	10.7	10.7	-	-	-
Loans from subsidiaries						
GBP loans from subsidiaries	5.50%	(18.8)	(18.8)	-	-	-
USD loans from subsidiaries	4.85%	(86.4)	(86.4)	-	-	-
Loans from joint ventures and associates	4.50%	(8.7)	(8.7)	-	-	-
Bank overdrafts	5.15%	(46.0)	(46.0)	-	-	-
		(291.2)	(276.3)	(8.9)	-	(6.0)

T Financial instruments (continued)

A comparison by category of book value and fair value of the Company's financial assets and liabilities is as follows:

	2005		2004	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Primary financial instruments held or issued to finance the Company's operations:				
Third party loans payable	(241.2)	(242.2)	(558.8)	(559.6)
Subsidiary loans receivable	1,061.7	1,061.7	1,614.6	1,614.6
Subsidiary loans payable	(754.0)	(754.0)	(1,137.8)	(1,137.8)
Joint venture and associate loans payable	(17.7)	(17.7)	(8.7)	(8.7)
Other investments and deferred consideration receivable	0.1	0.1	0.1	0.1
Cash at bank and in hand	68.6	68.6	50.9	50.9
Bank overdrafts	(46.0)	(46.0)	(64.8)	(64.8)
	71.5	70.5	(104.5)	(105.3)

The fair value of non-convertible bonds and dollar notes included in loans above is based on the quoted market price of comparable debt. Other loans include term loans and finance leases. These are largely at variable interest rates and therefore the book value normally equates to the fair value.

The fair value of other investments is based on the year end quoted price for listed investments and the estimated recoverable amount for unlisted investments.

The fair value of cash and bank overdrafts approximates to the book value due to the short term maturity of the instruments.

The fair value of subsidiary loans payable and receivable are largely at variable rates and therefore the book value normally equates to the fair value.

The following comparative information has been presented in accordance with FRS 13. See the 'Financial Instruments' accounting policy note on page 99.

The interest rate profile of the financial liabilities is set out in the tables below:

	Total £m	Variable rate financial liabilities £m	Fixed rate financial liabilities £m	Financial liabilities on which no interest is paid £m	Weighted average interest rate for fixed rate financial liabilities %	Average time over which interest rate is fixed months
31 December 2004						
Currency:						
Sterling	290.2	290.2	–	–	n/a	n/a
Sterling: irredeemable	1.4	–	1.4	–	3.50	n/a
US dollars	234.9	222.9	12.0	–	7.50	29
Australian dollars	55.4	55.4	–	–	n/a	n/a
Euro	5.8	5.8	–	–	n/a	n/a
Other	35.9	35.9	–	–	n/a	n/a
Total	623.6	610.2	13.4	–	7.08	29

The Company borrows in a range of currencies at both fixed and variable rates of interest.

The variable rate financial liabilities comprise bank borrowings and overdrafts bearing interest at rates fixed in advance for periods ranging from one to six months by reference to the applicable reference rate, primarily LIBOR for sterling, US dollar and euro borrowings, and the BBSY rate for Australian dollar borrowings.

Financial liabilities on which no interest is paid do not have fixed periods to maturity.

T Financial instruments (continued)

The interest rate profile of the financial assets is set out in the tables below:

	Total	Variable rate financial assets	Fixed rate financial assets	Financial assets on which no interest is received	Weighted average interest rate for fixed rate financial assets	Average time over which interest rate is fixed months
	£m	£m	£m	£m	%	
31 December 2004						
Currency:						
Sterling	35.1	34.9	–	0.2	n/a	n/a
US dollars	–	–	–	–	n/a	n/a
Australian dollars	–	–	–	–	n/a	n/a
Euro	19.3	19.3	–	–	n/a	n/a
Other	–	–	–	–	n/a	n/a
Total	54.4	54.2	–	0.2	n/a	n/a

The majority of variable rate financial assets comprise bank accounts bearing interest at the applicable LIBOR rate for sterling deposits or the applicable local equivalent rate. Fixed rate financial assets include deferred consideration relating to the sale of fixed assets and businesses, and other interest bearing and non-interest bearing investments.

The financial assets on which no interest is received do not have fixed periods to maturity.

U Post balance sheet events**Takeover by DP World**

On 29 November 2005, the P&O Board recommended the cash acquisition of P&O by Thunder FZE (a wholly owned subsidiary of Ports, Customs and Free Zone Corporation, Dubai ("DP World")) by way of schemes of arrangement. Following the announcement of an offer by PSA Venture (UK) Limited (a wholly owned subsidiary of PSA International Pte Ltd ("PSA") of Singapore) (also recommended by the Board) on the morning of 26 January 2006, the Board recommended revised proposals from Thunder FZE on the evening of 26 January 2006. These proposals were approved by the stockholders at meetings held on 13 February 2006, and following approval of the schemes by the High Court the schemes became effective on 8 March 2006 and P&O became a wholly owned subsidiary of DP World as at that date.

As a result of the change of control following the DP World takeover certain borrowing and loan facilities may be cancelled at the bank's option (see note J). DP World has arranged sufficient finance to allow any amounts drawn under these facilities to be repaid as they fall due.

Principal subsidiaries, joint ventures and associates

at 31 December 2005

	Country of incorporation	Percentage of equity share capital owned	Business description
Ports			
Antwerp Gateway NV	Belgium	42.5%	Container terminal operations
Asian Terminals Inc	The Philippines	84.1%#	Container terminal and other port operations
Chennai Container Terminal Private Ltd	India	75%	Container terminal operations
Container Terminals Australia Ltd	Australia	90.4%	Container terminal operations
Laem Chabang International Terminal Co Ltd	Thailand	34.5%	Container terminal operations
Manutention General Mediterranee SA ("Marseille")	France	20.4%#	Container terminal operations
Manutention Terminal Nord Developpement SA ("Le Havre")	France	36.7%#	Container terminal operations
Mundra International Container Terminal Limited	India	100%	Container terminal operations
Nhava Sheva International Container Terminal Private Ltd	India	100%	Container terminal operations
P&O Australia Ports Pty Ltd	Australia	100%	Holding company
P&O Maritime Services Pty Ltd	Australia	100%	Offshore services, ships agency and chartering
P&O Polar Australia Pty Ltd	Australia	100%	Antarctic research and resupply services
P&O PNG Ltd	Papua New Guinea	100%	Port and maritime services
P&O Ports Antwerp NV	Belgium	100%	Container terminal and other port operations
P&O Ports Canada Inc	Canada	100%	Container terminals and stevedoring
P&O Ports Ltd	Australia	100%	Container terminals, stevedoring and international port management
P&O Ports North America Inc	USA	100%	Stevedoring and passenger terminal services
Port Newark Container Terminal LLC	USA	50%	Container terminal operations
Ports Insurance Company Inc	USA	100%	Workers Compensation Insurance
Portsynergy SAS	France	50%	Container terminal operations
PT Terminal Petikemas Surabaya	Indonesia	49%	Container terminal operations
Qasim International Container Terminal Pakistan Ltd	Pakistan	55%	Container terminal operations
Qingdao Qianwan Container Terminal	PR China	29%#	Container terminal operations
Shekou Container Terminals Ltd	PR China	22%#	Container terminal operations
Southampton Container Terminals Ltd	England	51%	Container terminal operations
South Asia Gateway Terminals Pte Ltd	Sri Lanka	16.2%	Container terminal operations
Terminales Rio de la Plata SA	Argentina	53.1%	Container terminal operations
Tilbury Container Services Ltd	England	34%	Container terminal operations
Ferries			
Larne Harbour Ltd	Northern Ireland	100%*	Harbour operator
P&O European Ferries (Irish Sea) Ltd	England	100%	Ferry services
P&O European Ferries (Portsmouth) Ltd	England	100%	Ferry services
P&O Ferries (Holdings) Ltd	England	100%	Holding company
P&O Ferries Ltd	England	100%	Ferry services
P&O Ferrymasters Ltd	Northern Ireland	100%	International unit loads
P&O North Sea Ferries BV	Netherlands	100%	Ferry services
P&O North Sea Ferries Ltd	England	100%	Ferry services
Property			
Boston Wharf Company	USA	100%	Property development
HTC Hanseatic Trade Center GmbH & Co Grundbesitz KG	Germany	47.5%†	Property development
P&O Developments Ltd	England	100%	Property development
P&O Properties Boston LLC	USA	100%	Property development
P&O Properties Inc	USA	100%	Holding company
P&O Properties Ltd	England	100%	Property management
P&O Property Holdings Ltd	England	100%*	Property investment
TCD North Inc	USA	100%	Property development

Reflects economic interest

* owned directly by the Company

† As noted on page 93 HTC Hanseatic Trade Center GmbH & Co Grundbesitz KG (HTC) is classified as a subsidiary by the Group on adoption of IFRS. As the Company has prepared its accounts under UK GAAP HTC is treated as an associate in its accounts.

Underlying performance measures (unaudited)

Underlying performance measures

The Group has reviewed how it measures underlying performance following the adoption of IFRS and considers that the appropriate measures of underlying performance should:

- exclude items which will generally be separately disclosable items under IAS 1
- add back the relevant amounts relating to joint ventures and associates results such that they are presented on the same basis as the comparable Group items
- exclude non-trading items such as amounts arising from the revaluation of financial instruments and investments

	Earnings before net financing costs and tax 2005 £m	Pre-tax profit 2005 £m	Profit after tax 2005 £m	Earnings before net financing costs and tax 2004 £m	Pre-tax profit 2004 £m	Profit after tax 2004 £m
Per income statement	171.4	100.6	290.1	(103.7)	(187.2)	(151.5)
Adjusted for:						
Separately disclosable operating loss	15.5	15.5	15.5	326.7	326.7	326.7
Profit on sale and termination of businesses	–	–	–	(32.4)	(32.4)	(32.4)
Separately disclosable financing costs	–	12.1	12.1	–	–	–
Separately disclosable taxation on continuing operations	–	–	0.4	–	–	1.9
Discontinued operations	33.6	33.6	(179.9)	53.0	53.0	(3.5)
	220.5	161.8	138.2	243.6	160.1	141.2
Add back:						
Discontinued operations net financing costs	4.2	–	–	5.4	–	–
Discontinued operations taxation	3.6	3.6	–	3.6	3.6	–
Joint ventures and associates net financing costs	9.8	–	–	17.2	–	–
Joint ventures and associates taxation	12.8	12.8	–	11.8	11.8	–
Joint ventures and associates minority interest	1.1	1.1	1.1	0.8	0.8	0.8
Underlying performance measure	252.0	179.3	139.3	282.4	176.3	142.0

Underlying profit before depreciation and amortisation

	Underlying profit 2005 £m	Depreciation and amortisation 2005 £m	Underlying profit before depreciation and amortisation 2005 £m	Underlying profit before depreciation and amortisation 2004 £m
Continuing operations				
Ports	176.7	92.3	269.0	234.8
Ferries	14.7	30.2	44.9	39.9
Property	12.7	1.6	14.3	59.6
	204.1	124.1	328.2	334.3
Discontinued operations				
Container Shipping	26.9	20.2	47.1	100.3
Cold Logistics	21.0	9.1	30.1	28.7
	252.0	153.4	405.4	463.3

In the above table, underlying profit before depreciation and amortisation is stated after adding back to total underlying profit the depreciation and amortisation of all Group subsidiaries, joint ventures and associates.

Net financing costs

	2005 £m	2004 £m
Net financing costs	(70.8)	(83.5)
Add:		
Net financing costs from discontinued operations	(4.2)	(5.4)
Joint ventures and associates net financing costs from continuing operations	(5.0)	(4.9)
Joint ventures and associates net financing costs from discontinued operations	(4.8)	(12.3)
	(84.8)	(106.1)
Adjusted for separately disclosable net financing costs	12.1	–
Underlying net financing costs	(72.7)	(106.1)

Taxation

	2005 £m	2004 £m
Taxation per income statement	(24.0)	(20.8)
Add:		
Tax on group profits from discontinued operations	(3.6)	(3.6)
Joint ventures and associates taxation from continuing operations	(11.1)	(8.4)
Joint ventures and associates taxation from discontinued operations	(1.7)	(3.4)
	(40.4)	(36.2)
Adjusted for taxation on separately disclosable items	0.4	1.9
Underlying taxation	(40.0)	(34.3)

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