19 February 2013

DRAX GROUP PLC (Symbol: DRX)

PRELIMINARY RESULTS FOR THE YEAR ENDED 31 DECEMBER 2012

Biomass transformation well underway

Year ended 31 December	2012	2011
Key financial performance measures		
EBITDA (£ million) [(1)]	298	334
Underlying earnings (£ million) [(2)]	193	202
Underlying earnings per share (pence) [(2)]	51.9	55.5
Total dividends (pence per share) [(3)]	25.3	27.8
Statutory accounting measures		
Profit before tax (£ million)	190	338
Reported earnings per share (pence) [(4)]	44.1	127.3

Financial and Operational Highlights

- 2012 profits in line with expectations - continued strength in operations
- 27.1TWh - record output
- Financing to support growth plans secured
- Strong balance sheet - £311 million net cash at 31 December 2012

Biomass Highlights

Biomass transformation well underway:

- First unit will be converted to biomass in April 2013; second unit planned for 2014
- On-site biomass storage and handling construction on track
- Good progress securing fuel and logistics for first two unit conversions

Dorothy Thompson, Chief Executive of Drax, said:

"Last year was pivotal for Drax. After ten years developing significant knowledge and experience in all aspects of using sustainable biomass in place of coal at our power station, we now have the mandate, means and expertise to transform the business into a predominantly biomass-fuelled generator.

"With Government support and our financing secured, both in the second half of 2012, we are on track to convert our first generating unit fully to biomass in April of this year, with the second to follow in 2014.

"We will be investing significant capital over these two years, as we transform the business. EBITDA in this period will be impacted adversely by the increasing costs of carbon. However, as we move beyond this investment phase and replace substantial quantities of coal with sustainable biomass, we are confident that we will deliver attractive returns for our shareholders, who have provided us with strong support.

"This transformation will also provide reliable, cost effective renewable power for consumers and secure a significant number of jobs both at Drax and throughout our supply chain."

2012 Review

Financial

- EBITDA in line with expectations at £298 million
  - Year on year reduction reflects higher operating costs, with a double planned outage and costs incurred to accelerate biomass plans
- 2012 effective tax rate of 14% (2011: 21%, before exceptional tax credit)
  - Reflects reductions in corporation tax rate and one-time adjustment to prior year taxes
- Underlying earnings per share decreased 6% to 52 pence
  - Reported earnings per share of 44 pence. 2011 reported earnings per share of 127 pence include exceptional tax credit of £198 million
- Capital investment plans on track
  - 2012 total capital investment: £224 million, including £180 million for biomass transformation
  - 2013 capital investment guidance: c.£250 million to £300 million, including c.£50 million for plant efficiency and other projects (non-biomass transformation)
  - Total capital costs for biomass transformation remain in the range £650 million to £700 million, incorporating:
    - Delivery, storage and distribution infrastructure for biomass fuel, plus necessary plant modifications, for a three unit conversion
    - Two US based pellet plants (delivering 900,000t pa) and one US port export facility
    - Potential investment to support compliance with the Industrial Emissions Directive
- Final dividend of 10.9 pence per share, or £44 million (2011: 11.8 pence per share, or £43 million), in line with our policy to distribute 50% of underlying earnings
- Financing secured for growth plans
  - Strong balance sheet, with net cash of £311 million at 31 December 2012
  - Effective sub-investment grade business model fully implemented
- One-time costs (gross margin) for first unit conversion of £20 million, to be incurred in 2013
- Strong potential for attractive returns from biomass transformation

Operational

Year ended 31 December	**2012**	**2011**
Key operational performance measures		
Total recordable injury rate [(5)]	0.17	0.10
Forced outage rate (%)	4.8	5.8
Availability (%)	86	88
Electrical output (net sales) (TWh)	27.1	26.4

- Maintaining world class standards of safety and operations
- Good availability and plant despatch economics - record output in 2012
  - Load factor 82%, compared with average of 50% and 31% for other coal and gas plants[(6)]

Biomass research and development

- Demonstrated technical capability to convert Drax units fully to biomass
- Developed technical solutions to deliver reliable and flexible generation with attractive rates of efficiency and output
  - Output and efficiency c.10% lower and c.1.5% lower than coal respectively
  - Early availability c.80% - in time expect similar to coal
- Work on-going: use of additives, corrosion tests and optimisation of NOx performance

Notes:

(1) EBITDA is profit before interest, tax, depreciation, amortisation, and unrealised gains/losses on derivative contracts.

(2) 2012 underlying earnings and underlying earnings per share exclude unrealised losses on derivative contracts of £36 million (2011: unrealised gains of £90 million) and the associated tax. 2011 underlying earnings and underlying earnings per share exclude the exceptional tax credit of £198 million.

(3) Based on 50% of underlying earnings. 2012 comprises the interim dividend of 14.4 pence per share (equivalent to £53 million) and final proposed dividend of 10.9 pence per share (equivalent to £44 million).

(4) 2011 reported earnings include the exceptional tax credit of £198 million.

(5) Calculated as (lost time injuries + worse than first aid injuries) / hours worked x 100,000.

(6) Drax estimate of average load factor for January to December 2012 based on settlement data.

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Forward Looking Statements

This announcement may contain certain statements, statistics and projections that are or may be forward-looking. The accuracy and completeness of all such statements, including, without limitation, statements regarding the future financial position, strategy, projected costs, plans and objectives for the management of future operations of Drax Group plc ("Drax") and its subsidiaries (the "Group") are not warranted or guaranteed. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that may occur in the future. Although Drax believes that the expectations reflected in such statements are reasonable, no assurance can be given that such expectations will prove to be correct. There are a number of factors, many of which are beyond the control of the Group, which could cause actual results and developments to differ materially from those expressed or implied by such forward-looking statements. These factors include, but are not limited to, factors such as: future revenues being lower than expected; increasing competitive pressures in the industry; and/or general economic conditions or conditions affecting the relevant industry, both domestically and internationally, being less favourable than expected. We do not intend to publicly update or revise these projections or other forward-looking statements to reflect events or circumstances after the date hereof, and we do not assume any responsibility for doing so.

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Management Presentation and Conference Call

Management will host a presentation for analysts and investors at 9:00am (UK Time) today, Tuesday 19 February 2013, at **UBS, 1 Finsbury Avenue, London EC2M 2PP**.

Would anyone wishing to attend please confirm by either e-mailing jscott@brunswickgroup.com or calling Jenny Scott at Brunswick Group on +44 (0) 20 7404 5959.

The meeting can also be accessed remotely via a conference call or alternatively via a live webcast, as detailed below. After the meeting, a video webcast and recordings of the call will be made available and access details for these recordings are also set out below.

A copy of the presentation will be made available from 7:00am (UK time) on Tuesday 19 February 2013 for download at:
www.draxgroup.plc.uk>>investors>>results and reports>>IR presentations>>2013
or use the link http://www.draxgroup.plc.uk/investor/results_and_reports/presentations

Event Title	Drax Group plc: Preliminary Results
Event Date	Tuesday 19 February 2013
Event Time	9:00am (UK time)
UK Call In Number	0808 237 0033
International Call In Number	+44 (0)203 426 2886
US Call In Number	+1 866 928 6048
Webcast Live Event Link	http://cache.cantos.com/webcast/static/ec2/4000/5275/9523/10700/Lobby/default.htm

Instant Replay	
UK Call In Number	0808 237 0026
International Call In Number	+44 (0)203 426 2807
US Call In Number	+1 866 535 8030
Passcode	636305#
Start Date	Tuesday 19 February 2013
Delete Date	Tuesday 19 March 2013
Video Webcast	
Start Date	Tuesday 19 February 2013
Delete Date	Tuesday 18 February 2014
Archive Link	http://cache.cantos.com/webcast/static/ec2/4000/5275/9523/10700/Lobby/default.htm

For further information please contact:

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Chairman's introduction

We have long believed that generating electricity from sustainable biomass has great potential and that it should have an important role as a low carbon, cost-effective and reliable renewable technology in the future energy mix of the UK. We are determined that Drax should be a leading provider of this attractive renewable power for the UK.

In 2012, we built on the work of previous years to deliver solid foundations for the Group's future as a major renewable generator. We made significant progress with very encouraging results in our biomass research and development and we secured committed financing for our strategic capital investment from our shareholders and lenders. This was possible because the UK Government delivered certainty through decisions on the new regulatory framework for electricity generation from biomass. We have now moved firmly into execution of our plans to transform the business into a predominantly biomass-fuelled generator.

Although much effort in the year was focused on our biomass strategy and future, we did not neglect our other key priorities and I am pleased to say that once again I can report a year of strong operational and trading performance across the business. Our earnings (EDITDA[(1)]) of £298 million for 2012 were lower than in 2011 (£334 million). However, this includes a year on year increase in gross margin, with a record level of generation at the power station, offset at EBITDA level by higher operating costs due to the two planned outages and costs incurred in accelerating our plans to convert our first generating unit to biomass in April 2013.

In accordance with our dividend policy, the Board proposes a final dividend in respect of 2012 of 10.9 pence per share, equivalent to £44 million. This would give total dividends for the year of £97 million (2011: £102 million).

Haven Power Limited ("Haven Power"), our electricity retail company serving business customers, again made good progress and delivered sizeable growth in its sales in 2012 compared to the previous year. We have been pleased with the way the business has developed and with it the value that the Group is now deriving from its success. Over time Haven Power will play an increasingly important role as a credit efficient, direct sales channel for our power.

Another strong year of generation performance saw record levels of generation output for the power station and a double planned outage accomplished in good time. At all times our focus on high safety standards was maintained and despite the significant number of man-hours worked due to the outages and project activity our safety performance remained industry-leading.

This is the fifth year running that I have made reference to the £100 million turbine upgrade project, and I make no apology for reporting on the completion of the largest steam turbine modernisation project in UK history. Drax Power Station is now benefiting from an overall improvement in its efficiency of 5% and a consequent reduction in emissions of carbon dioxide amounting to 1 million tonnes each year. A testament to the diligence, expertise and teamwork of our engineers, this achievement is a clear demonstration of our competence in project execution.

On governance-related matters, I am pleased to welcome a new member to our Board. Melanie Gee joined the Board on 1 January 2013 as a non-executive director, bringing with her many years' experience in corporate finance. Her expertise will be a valuable addition and will strengthen further the proficiency of the Board.

I am, however, sorry to announce that Tim Barker will be stepping down from the Board at the conclusion of the Annual General Meeting in April. Tim is bowing out after nine years of service, joining us at a formative time for the Company and assisting us through the Listing process. My sincere thanks go to Tim for his time, commitment and considerable contribution to the Group. The Board has appointed David Lindsell to take over from Tim as Senior Independent Director, and Tony Thorne as Chairman of the Remuneration Committee, each with effect from Tim's retirement from the Board.

We have always recognised that our people are a key resource to the business, but I believe the milestone achievements of last year underline that sentiment. The many and varied disciplines that make up our business continued to demonstrate true commitment to delivering on our key priorities and preparing the ground for our future. My sincere thanks go to all Group staff for their devotion and hard work.

Note:
(1) EBITDA is defined as profit before interest, tax, depreciation, amortisation and unrealised gains and losses on derivative contracts.

Chief Executive's statement

Introduction

I am very pleased to say that 2012 was a good and extremely important year for the Group. Good in the sense that the business performed well delivering profits in line with expectations underpinned by continued strength in operations, and important in that we now have the clear mandate, means and expertise to transform Drax into a predominantly biomass-fuelled generator.

Through the year we made excellent progress with our biomass research and development work. We demonstrated that we could operate a single generating unit on a fully converted basis for a sustained period and we delivered very encouraging results from our engineering optimisation work. As a result we gained full confidence in our ability to deliver reliable and flexible renewable power through converted units at attractive rates of efficiency and output.

The much needed regulatory clarity and certainty was delivered in the Government's conclusions on the future support levels for biomass electricity and proposals for sustainability criteria, which saw clear recognition of the true benefits of biomass and its potential to play a strategically important role in the UK's future energy mix.

The final piece of the jigsaw, securing the means to finance our biomass strategy, was achieved through raising a mixture of equity and debt. Equity of £190 million was raised through a share placing, and we secured new debt of £200 million through term loan facilities with M&G UK Companies Financing Fund and the UK Green Investment Bank, at £100 million each. In addition, our working capital/letter of credit facility was increased to £400 million and the maturity extended to April 2016.

All in all, 2012 was a positive and pivotal year marking real progress in our journey to transform the business, whilst maintaining our focus on excellence in operations, and disciplined capital project execution across our generation and retail businesses.

Strategy

Our vision for Drax is to be a bold, customer oriented power generation and retail business, driven by biomass innovation. We have two key strategic initiatives to enable us to achieve our vision, namely, our project to convert Drax Power Station into a predominantly biomass-fuelled generating asset and our programme for the expansion of our retail business, Haven Power Limited ("Haven Power") through growing our sales to businesses.

Commodity markets

The gas market continued to be the dominant factor in driving power prices. The impact of the incident at one of Japan's nuclear power stations continued to be felt through the country's increased demand for liquefied natural gas ("LNG") and consequent increasing Asian LNG prices. As a result the UK saw reduced LNG imports and gas prices remained strong. Accordingly, some gas-fired plant capacity was withdrawn from the market and in some cases considered for closure.

International coal prices were weak as a result of excess supply. Exports from the US to Europe, in particular, increased significantly. A combination of low prices and high stocks put pressure on the UK's domestic coal producers.

Carbon prices remained at their lowest point for three years driven by over-supply of carbon emissions allowances in Phase II of the EU Emissions Trading System ("EU ETS"). As of 1 January 2013, we entered into Phase III of the EU ETS, which introduced 100% auctioning of allowances to the power sector – a departure from receiving allowances in the previous Phases.

With Phase II surplus bankable in Phase III a range of interventions is being considered by the European Commission to rectify the over-supply, but these are by no means certain to proceed.

Dark green spreads, the difference between the price of power and the cost of coal and carbon, have been relatively good for coal-fired generators.

The introduction to the UK of the carbon price support mechanism from April 2013 is likely to erode the competitive position in the market of our coal-fired generation business, but at the same time it strengthens the case for biomass generation.

During 2012, bark spreads for co-firing, the difference between power price and renewable support and the cost of biomass, remained weak with most traded biomass commanding lower margins than coal. Consequently, the amount of commercial biomass burnt during the year was much lower than previous years. Substantially all of the biomass burnt during the period was at a loss, but in support of critical research and development work.

The Government's new support levels for biomass electricity through conversion and co-firing come into effect in April 2013. We expect co-firing at low levels to remain uneconomic, but generation through converted units will become economic and yield attractive rates of return on the required capital investment.

Retail performance

During 2012 our retail business, Haven Power, delivered substantial growth in a highly competitive market with retail sales over 60% higher than in 2011. Sales growth remains a key priority for the business, targeting the industrial and commercial ("I&C"), and small and medium enterprise ("SME") markets. Due to our continued drive for growth across these markets we expect Haven Power to make a modest loss up to 2015.

An excellent standard of customer service is central to our proposition for this business, and we were pleased to see recognition of that through being ranked No. 1 for customer satisfaction in the SME market in the 2012 Datamonitor Survey.

Selling our output through Haven Power continues to provide us with a credit-efficient route to market for our power sales compared to the wholesale electricity market, as well as a route to market for the Renewables Obligation Certificates and Levy Exemption Certificates associated with our renewable power generation.

Generation performance

We continued to deliver industry-leading performance in 2012 amid higher than ever output levels, and significant project and construction activity.

As in previous years, our load factor was high compared to other thermal capacity on the system and we recorded our highest ever generation out-turn level. With high availability and reliability throughout 2012 we were able to continue to deliver additional value to the business through providing flexible generation output and balancing services to the System Operator, National Grid, in support of system stability and security.

Two planned unit outages were undertaken during 2012, and both were completed in good time. With two outages and considerable biomass project work activity, the number of engineering man-hours worked throughout the year was significant. Yet against this backdrop our safety statistics continued to be industry-leading, reflecting the emphasis we place on safety.

For the year, our forced outage rate, which measures any reduction in plant availability excluding planned outages, was close to our long-term target of 5%, which has been set through extensive benchmarking with UK and international coal-fired plants to determine the optimum balance between performance and cost.

We continued to work on increasing our burn of fuels which have a higher margin or lower carbon footprint over the standard bituminous coal which we burn. These advantaged fuels – petcoke, pond fines and commercial or economic biomass – accounted for 7% of the total fuel burnt during the year.

Assessment of the technical solutions available to us for compliance with the more stringent emissions standards of the Industrial Emissions Directive from 2016 is well advanced. The key factors in determining the optimal solution for compliance are plant flexibility and fuel mix. Hence, the level of biomass burn is an important consideration. The legislative arrangements in place afford us some flexibility in the timing and the extent of the required modifications which fits well with our biomass conversion programme.

Biomass transformation

During the year we completed our engineering designs of the plant modifications and new facilities required for unit conversion. We made good progress on the time critical construction of the receipt, storage and delivery systems for biomass, including the erection of the first two biomass storage domes. Building on the early work undertaken in 2012 and making use of the existing biomass co-firing infrastructure we believe it will be technically feasible to convert single units in 2013, 2014 and 2015. However, the actual timing is dependent on biomass fuel sourcing.

We have made good progress towards securing sufficient biomass to run two converted units and we plan to convert the first unit in April 2013 and the second unit in 2014. We are now in advanced negotiations for a large proportion of the biomass necessary to fuel the third unit. Established North American suppliers, Enviva, Green Circle, Pinnacle and Plum Creek are amongst those with whom we have entered into term contracts for the supply of wood pellets and sustainable forest fibre.

Elsewhere in the supply chain, at the end of 2012 the final investment decision was taken to develop two US-based pellet plants, one in each of the states of Mississippi and Louisiana, with a combined capacity of 900,000 tonnes a year, and to invest in a port facility in Louisiana with an export capacity of 3 million tonnes a year. We are now finalising the construction arrangements for these facilities.

In addition, terms have been agreed with UK port operators to provide us with biomass import facilities. This will involve the development of new facilities and the expansion of existing ones. Finally, the fabrication of bespoke rail wagons to transport biomass from the ports to the power station is underway.

Biomass sustainability

All our biomass is procured against our own robust sustainability criteria, which include greenhouse gas emission reduction requirements, and habitats and biodiversity protection, as well as socio-economic considerations in the source areas. A programme of independent audits ensures all our suppliers comply with our sustainability criteria.

We firmly believe that robust, mandatory sustainability criteria are vital to maintain and enhance public acceptance, and ensure that sustainable practices are implemented. Assessment of the full life cycle carbon footprint of biomass, that is, from field or forest-to-furnace, is now well developed, especially in the UK where a mandatory life cycle standard is scheduled to come into effect later this year.

With a number of years' experience of calculating the life cycle carbon footprint of all the biomass we procure, we are confident that our sustainable biomass fuel sources will meet the UK's new mandatory standard which will ensure we continue to earn regulatory support.

Our calculations show that the range of sustainable biomass materials we have burnt over the last few years has a far lower carbon footprint than that of fossil fuel-fired generating plant. In 2012, the average greenhouse gas saving, over the full life cycle, resulting from burning sustainable biomass in place of coal was above 80%.

Further carbon abatement

In addition to the carbon dioxide ("CO_2") savings through burning sustainable biomass in place of coal, we have also progressed other carbon abatement activities.

The low pressure and high pressure turbine modules of all six generating units have now been replaced and are operating as expected. This means we are operating at an overall coal-based efficiency for the power station of around 40%, and through this upgrade alone we are reducing our CO_2 emissions by 1 million tonnes a year.

We have also taken the decision to upgrade the intermediate pressure turbines of the three generating units that will be converted to biomass. The first will be undertaken during 2014. This will deliver further efficiency improvement benefits. Siemens will again be responsible for the manufacture and assembly of the turbines from its facility in Mülheim with installation support from Siemens in Newcastle.

Together Drax, Alstom UK and BOC (a member of The Linde Group) have formed a consortium in support of the White Rose Carbon Capture and Storage ("CCS") Project, a proposed 426MW oxyfuel CCS demonstration project based at the Drax Power Station site. At the beginning of July 2012 the consortium, in conjunction with National Grid Carbon Limited, submitted a bidder proposal for funds through the UK CCS Commercialisation Programme, which was launched in April 2012.

At the end of October 2012, the White Rose CCS Project was one of four shortlisted for the next phase of the UK competition. The consortium is fully engaged in the process, but the project will be dependent on successful outcomes from external funding processes and Electricity Market Reform mechanisms to incentivise low carbon technologies.

Legislative framework

In November 2012, the Energy Bill was introduced to Parliament marking the start of its passage through both the House of Commons and the House of Lords. At the heart of the Bill is Electricity Market Reform, which will see, amongst other things, the introduction of Contracts for Difference ("CfD") providing long-term contracts and a stable revenue stream enabling investment in low carbon generating technologies, and a capacity market to mitigate future risks to the security of electricity supplies.

CfD will replace the Renewables Obligation in 2017 for new renewable generation facilities, but not those already in operation. We are exploring the CfD mechanism for biomass and have participated in a call for evidence, launched by National Grid as part of its potential role as delivery body, to support the development of strike prices under the mechanism.

We have also had preliminary discussions with the Department of Energy & Climate Change on the possibility of securing long-term contracts to enable early investment in advance of the CfD mechanism coming into force.

Looking ahead

We enter 2013 with a strong hedge from forward power sales, but with no national carbon emissions allocation under Phase III of the EU ETS and, from April, increased carbon costs under the UK carbon support mechanism. Both of these changes are recognised in current stock market forecasts.

We intend to continue our hard work to deliver leading operating and cost performance and to retain our focus on building options to burn advantaged fuels.

With a commitment to deliver value to our shareholders, we are now in full execution mode to transform Drax into a predominantly biomass-fuelled generator. In doing so we are confident that we will not only secure an attractive future for the business and our shareholders, but also deliver a significant amount of cost-effective renewable power for the consumer and make a meaningful contribution to the UK's 2020 climate change targets.

Commodity markets

The trends in commodity prices witnessed in 2011 and 2012 are described further in the following paragraphs.

Gas

After a significant step up in prices following the Fukushima disaster in 2011, continued restrictions on nuclear generation kept upward pressure on the global liquefied natural gas ("LNG") market during 2012. The resulting rise in Asian LNG prices limited the attractiveness of the UK spot market, leading to falling imports of LNG.

UK spot gas prices remained strong throughout 2012. With the ongoing decline in production from the UK Continental Shelf, UK gas prices continue to be pulled upwards towards oil indexed European prices (and international LNG prices) to attract imports.

European and UK gas prices remain at a premium to US prices, where advances in technology are leading to a large supply of low priced shale gas, adding to already significant reserves which may enable the US to become self-sufficient. However, shale gas developments outside the US are in their infancy and will, therefore, have little impact in the short to medium term. Furthermore, demand for gas is rising rapidly so that even with the possibility of increased shale gas production, global markets may well remain strong.

Power

Power prices continue to be driven by the gas market. With a peak in the first half of 2011 following the Japanese earthquake, prices fell back on mild weather towards the end of the year but recovered early in 2012 and remained relatively stable throughout the second half of the year.

Coal

Asian demand, particularly from China, pushed global steam coal market prices to a peak in mid-2011. Since that point, coal prices have steadily fallen. The low US gas prices described above have forced a dramatic increase in US coal exports. Combined with a rise in Colombian and Australian shipments to Europe, this has resulted in a weak global short-term market characterised by low international prices and high stocks in Europe. Although Asian demand has continued to grow, it has been insufficient to absorb the excess supply.

These market dynamics, as well as increasing operating costs, have increased the pressure on UK domestic coal producers.

Carbon

Carbon prices also rose in the immediate aftermath of the Japanese earthquake, but then dropped sharply in the second half of 2011 amid fears for the Eurozone economies.

This trend continued throughout 2012, with prices falling to record lows around the end of the year. With any Phase II surplus bankable into Phase III, pricing has been driven by political and macroeconomic factors. The increasing renewable generation build rate and the slow pace of economic recovery have led to a large over supply of carbon allowances in Phase III. The EU is considering a range of options to remedy this over-supply, but these are by no means certain to proceed.

Dark green spread

The combination of stable power prices and lower coal and carbon prices drove an improvement in dark green spreads during 2012.

Biomass

Types of biomass

Biomass used in energy production comes in many different forms, but the important characteristics shared by the wide range of biomass fuels are that they are renewable and can be sustainable.

The three most common types of biomass used to generate electricity are forestry products and residues, agricultural residues, and energy crops. Recovered materials offer another, very useful, source.

Forestry products and residues
Sustainably produced woody biomass can be produced from managed forests and forestry residues, such as thinnings, tree tops, branches and bark. The economics of forest management usually mean that energy is well down the list of potential uses for wood. Timber, the most valuable part of a tree, is generally used for furniture and building materials, while smaller diameter wood can be used for fence posts or by the paper and wood panel industries. This leaves the lower value thinnings and branches for energy production as they often have no other commercial use. In some geographic regions, decline of industries such as construction and paper and pulp means that energy producers may be able to afford fibre previously supplied to these, currently declining, markets. This is welcomed by the forest owners who need to harvest mature trees and thereby maintain investment in sustainable forest management.

Agricultural residues
The by-products of food production, such as straw, oat husks, peanut husks, grape flour, cocoa shells, olive cake and many more, can all be used as biomass for energy production. Importantly, because they are by-products of food production they do not reduce the amount of land available for farming, and they are readily available. Residues from non-food crops, such as cork fines, can also be used. By placing a value on what may be an unwanted by-product of farming, the use of biomass to produce energy provides a new income stream for farmers.

Energy crops
These are crops that are planted specifically for the purpose of producing energy. Energy crops include short rotation coppice willow and miscanthus, commonly known as elephant grass. Since the start of the UK's Energy Crop Scheme in 2000, thousands of hectares of miscanthus and other short rotation coppice crops have been planted in the UK alone.

Recovered materials
Recovered wood is an example of a material that could be used as a biomass fuel. The construction and demolition sectors are very large producers of recoverable wood.

Availability of biomass
Biomass is a diverse, readily available and plentiful fuel source. According to the International Energy Agency, biomass is the fourth largest energy resource in the world after oil, coal and gas. It estimates that by 2050, sustainable sources of biomass could be enough to supply the world with 10%-20% of its primary energy requirements.

The EU has indicated that the use of biomass will double over the next few years, and be responsible for around a half of the total effort in reaching the EU's 20% renewable energy target by 2020. In the UK, the Government's 2012 update to the Renewable Energy Roadmap reports on analysis which indicates that by 2020 as much as 11% of the UK's total primary energy demand (across heat, transport and electricity) could come from bioenergy.

Biomass procurement
Our biomass is procured against our industry-leading sustainability policy which is independently audited. We are in our sixth year of monitoring the carbon footprint of all the biomass we burn.

Operational and financial performance

Introduction

Our 2012 profit reflects continued strength in our operations. We also delivered another year of industry-leading safety statistics, against a backdrop of significant project activity at the Drax site, including a planned double outage and commencement of construction on our new biomass storage and handling facilities.

EBITDA was £298 million for the year ended 31 December 2012 compared to £334 million in 2011 and underlying basic earnings per share were 52 pence compared to 56 pence last year.

A year on year increase in gross margin reflects a record level of generation at the power station. This was offset at EBITDA level by higher operating costs of the planned double outage and costs we incurred, following the Government's confirmation of regulatory support for biomass, as we accelerated our plans to put ourselves in the best possible position to convert a first unit to biomass in April 2013.

Our retail business, Haven Power Limited ("Haven Power") continued to deliver good growth during 2012. Sales increased from 3.3TWh in 2011 to 5.1TWh in 2012, largely as a result of the planned growth of the industrial and commercial customer base.

Towards the end of the year we secured the financing required to support our biomass transformation plans, with the successful completion of a share placing, agreement of new term loan facilities, and the refinancing of our working capital and letter of credit facilities. With net cash of £311 million at the year end, we have in place a strong financial platform from which to realise our ambitions.

At the upcoming Annual General Meeting, the Board will recommend a final dividend for 2012 of 10.9 pence per share, taking total dividends for the year to £97 million.

This review includes further explanation and commentary in relation to our principal performance indicators and the results for the year.

Results of business

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Total revenue	**1,779.8**	1,835.9
Fuel costs in respect of generation[1]	**(929.2)**	(1,020.8)
Cost of power purchases[2]	**(141.7)**	(172.3)
Grid charges[3]	**(167.8)**	(117.6)
Other retail costs[4]	**(30.2)**	(24.4)
Total cost of sales	**(1,268.9)**	(1,335.1)
Gross profit	**510.9**	500.8
Other operating and administrative expenses excluding depreciation, amortisation and unrealised (losses)/gains on derivative contracts[5]	**(212.5)**	(167.2)
EBITDA[6]	**298.4**	333.6
Depreciation and amortisation	**(58.5)**	(57.2)
Unrealised (losses)/gains on derivative contracts	**(36.1)**	89.8
Operating profit	**203.8**	366.2
Net finance costs	**(13.6)**	(28.1)
Profit before tax	**190.2**	338.1
Tax (charge)/credit		
— Before exceptional items and impact of corporation tax rate change	**(41.5)**	(87.5)
— Impact of change in rate of corporation tax on deferred tax	**15.1**	16.1
— Exceptional items	**—**	197.9
Tax (charge)/credit	**(26.4)**	126.5
Profit for the year attributable to equity shareholders	**163.8**	464.6

Earnings per share	**pence per share**	pence per share
— Statutory basic	**44**	127
— Statutory diluted	**44**	126
— Underlying basic[7]	**52**	56
— Underlying diluted[7]	**51**	55

All results relate to continuing operations.

Notes:

(1) Fuel costs in respect of generation consists predominantly of coal, sustainable biomass and carbon dioxide ("CO_2") emissions allowances, together with pond fines, petcoke and oil.
(2) Cost of power purchases represents power purchased in the market.
(3) Grid charges include transmission network use of system charges ("TNUoS"), balancing services use of system charges ("BSUoS") and distribution use of system charges ("DUoS").
(4) Other retail costs include broker fees, ROCs, LECs, metering and Feed-in-Tariff levelisation.
(5) Other operating and administrative expenses excluding depreciation, amortisation and unrealised gains and losses on derivative contracts include salaries, maintenance costs and other administrative expenses.
(6) EBITDA is defined as profit before interest, tax, depreciation, amortisation and unrealised gains and losses on derivative contracts.
(7) Calculated using underlying earnings, being profit attributable to equity shareholders adjusted to exclude the after tax impact of unrealised gains and losses on derivative contracts and exceptional items.

Segmental information

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Revenue		
Power sales	**1,527.4**	1,641.0
ROC and LEC sales	**62.6**	69.2
Ancillary services income	**14.5**	17.4
Other income	**25.5**	7.6
Total generation revenue	**1,630.0**	1,735.2
Retail revenue	**451.4**	275.5
Intercompany sales	**(301.6)**	(174.8)
Total Group revenue	**1,779.8**	1,835.9
Cost of sales		
Fuel costs in respect of generation	**(929.2)**	(1,020.8)
Generation cost of power purchases	**(138.4)**	(172.0)
Generation grid charges	**(66.3)**	(58.0)
Total generation cost of sales	**(1,133.9)**	(1,250.8)
Retail cost of power purchases	**(278.9)**	(170.9)
Retail grid charges	**(101.5)**	(59.5)
Other retail costs	**(56.2)**	(28.7)
Total retail cost of sales	**(436.6)**	(259.1)
Intercompany purchases	**301.6**	174.8
Total Group cost of sales	**(1,268.9)**	(1,335.1)
Gross profit		
Generation gross profit	**496.1**	484.4
Retail gross profit	**14.8**	16.4
Total Group gross profit	**510.9**	500.8
Operating and administrative expenses		
Generation operating and administrative expenses	**(193.1)**	(148.3)
Retail operating and administrative expenses	**(19.4)**	(18.9)
Total Group operating and administrative expenses	**(212.5)**	(167.2)
EBITDA		
Generation EBITDA	**303.0**	336.1
Retail EBITDA	**(4.6)**	(2.5)
Total Group EBITDA	**298.4**	333.6

Generation results

Revenue

Total generation revenue for the year ended 31 December 2012 was £1,630 million compared to £1,735 million in 2011. Total generation revenue in 2012 includes power sales of £1,527 million (2011: £1,641 million), ROC and LEC sales of £63 million (2011: £69 million), ancillary services income of £15 million (2011: £17 million) and other income of £26 million (2011: £8 million).

Net power sold increased to 27.1TWh in 2012, compared to 26.4TWh in 2011, but at a lower average achieved electricity price of £51.3 per MWh compared to £55.6 per MWh in 2011, resulting in the overall reduction in revenue from power sales in the year.

Our average achieved price of electricity reflects the contracted position at the start of the year, as well as power prices during the period. 2011 benefited from earlier forward sales captured at enhanced prices, as well as higher power prices in the year, with prices peaking in the first half following the Japanese earthquake (see Commodity markets).

Margins available to coal-fired generators improved in 2012, largely as a result of lower international coal and carbon prices. Our high availability and superior efficiency in comparison to other coal-fired generators has allowed us to take advantage of the good margins available, driving the increase in net power sold.

Revenue from the sale of ROCs and LECs is a function of both the movement of ROC and LEC assets in the balance sheet, and the volume of biomass burnt in the period. ROC and LEC assets held in the balance sheet fell from £32 million at the end of 2011 to £19 million at 31 December 2012. This was offset by lower levels of biomass burn in 2012 (see Fuel costs). As a result ROC and LEC sales were £63 million in 2012 compared to £69 million in 2011 (including sales to Haven Power).

We changed our accounting policy for ROCs in 2012 so that they now match the value generated to the period in which biomass is burnt rather than the period in which ROCs are sold. However, with support for biomass at only 0.5ROC/MWh until April 2013, the change in policy had negligible impact on our financial results in this annual report and accounts.

Ancillary services income decreased slightly from £17 million to £15 million. This revenue arises from the services we provide to National Grid to balance system supply and demand. As a flexible generator, Drax continues to play a significant role in supporting the balancing of the system.

Other income of £26 million in 2012 includes £9 million for the sale of by-products (2011: £8 million) and £17 million for fuel sales. During 2012 certain coal inventories (at port) were sold to a third party for stock management purposes.

Fuel costs (coal, sustainable biomass and other fuels)

Fuel costs were £929 million in 2012, compared to £1,021 million in 2011.

We burnt approximately 9.6 million tonnes of coal in the year ended 31 December 2012, compared to approximately 9.1 million tonnes in 2011 reflecting higher generation and lower biomass burn. This coal was purchased from a variety of domestic and international sources under either fixed or variable priced contracts with different maturities. Coal represented around 90% of total fuel burnt (by heat content) in 2012 and 87% in 2011.

We also burnt 0.1 million tonnes of petcoke and 0.6 million tonnes of pond fines in both years. Our petcoke burn volume is driven by its pricing relative to coal. Pond fines is a coal mining residue, which trades at a significant discount to coal, and requires specific blending and handling techniques to burn in large volumes.

In 2012, we burnt 0.7 million tonnes of biomass (2011: 1.3 million tonnes) representing 5% of total fuel burnt by heat content (2011: 9%). The majority of the biomass we burnt in 2012 related to our research and development (“R&D”) trial work. Very little commercial biomass was burnt during the year, as the margins remain weak at current support levels.

The average cost of fuel per MWh (excluding CO_2 emissions allowances) was £30.6 for the year ended 31 December 2012 (net of £17 million fuel sales described above), compared to £33.3 in 2011. The decrease in average fuel prices was driven by the falling price of international coal (see Commodity markets) and the fuel mix, with much lower biomass burn in 2012.

Fuel costs (CO_2 emissions allowances)

For Phase II of the EU ETS (2008–2012), Drax had an allocation of 9.5 million tonnes of CO_2 emissions allowances per annum under the UK NAP. We purchase CO_2 emissions allowances under fixed price contracts with different maturity dates from a variety of domestic and international sources.

Our CO_2 emissions allowances requirement for the year ended 31 December 2012, in excess of those allocated under the UK NAP, was approximately 13.1 million tonnes compared to approximately 11.6 million tonnes in 2011. This was a result of higher generation and the change in fuel mix described above.

Our average price of carbon is a function of the timing of purchases under fixed price contracts in the forward and near-term markets. The average price expensed for purchased CO_2 emissions allowances during the year ended 31 December 2012 was £6.3 per tonne compared to £12.0 per tonne in 2011. This reflects the significant fall in carbon prices since mid-2011 (see Commodity markets).

Cost of power purchases

We purchase power in the market when the cost of power in the market is below our marginal cost of production in respect of power previously contracted for generation and delivery by us, and to cover any shortfall in generation. For the year ended 31 December 2012, the cost of purchased power for the generation business was £138 million, compared to £172 million incurred in 2011, reflecting lower average power prices in 2012 (see Commodity markets).

Grid charges

Grid charges for generation for the year ended 31 December 2012 were £66 million, compared to £58 million in 2011. The increase resulted from higher generation and an increase in the rate charged by National Grid to reflect the impact of increased intermittent generation on system balancing costs.

Higher net power sold and improved dark green spreads resulted in generation gross profit for the year ended 31 December 2012 of £496 million compared to £484 million in 2011.

Operating and administrative expenses

Generation other operating and administrative expenses before depreciation and amortisation were £193 million for the year ended 31 December 2012, compared to £148 million in 2011, an increase of £45 million.

Most of this increase (£38 million) was captured in our operating cost guidance set out at the beginning of 2012. This included £20 million as a direct result of the planned double outage in 2012 (single outage in 2011), together with a structural uplift in business rates charges. Investment in growth, including the completion of our biomass R&D work, added a further £10 million, and cost inflation of £8 million (5%) following three successive years holding underlying costs level.

Following the Government's confirmation of the regulatory support for biomass in the second half of the year, we accelerated our plans to put ourselves in the best possible position to convert the first unit to biomass in April 2013. We incurred additional preventative maintenance, system and other costs of around £7 million in 2012 to execute these plans.

We remain focused on achieving strong operational cost performance and we will continue to carefully control our cost base.

As a result of the double planned outage and the acceleration of our biomass transformation plans, generation EBITDA for the year ended 31 December 2012 was £303 million compared to £336 million in 2011.

Retail results

Revenue

Retail sales volumes increased from 3.3TWh in the year ended 31 December 2011 to 5.1TWh in 2012. This reflects planned growth in Haven Power's industrial and commercial customer base and increased sales to the small and medium size enterprise market.

As a result, retail revenue was £451 million for the year ended 31 December 2012, compared to £276 million in 2011.

This is in line with our strategy to target a 10-15TWh business at Haven Power, with retail sales being a credit-efficient alternative to selling power in the wholesale market. Whilst the markets in which Haven Power operates remain highly competitive, we have been successful in securing growth through good customer service, and our bad debt experience remains low.

Cost of power purchases

Retail cost of power purchases were £279 million for the year ended 31 December 2012 compared to £171 million in 2011. Haven Power purchases power for delivery to its retail customers. The vast majority of these purchases are from Drax Power Limited and are eliminated on a group basis. The increase in Haven Power's cost of power purchases is a result of the significant increase in sales volumes.

Grid charges

Haven Power incurred £102 million of grid charges during the year ended 31 December 2012 and £60 million during the year ended 31 December 2011. Charges have increased as a result of higher sales volumes together with substantial increases in the rates charged by the network operators and National Grid.

Other retail costs

Other retail costs which include broker fees, ROCs, LECs, Feed-in-Tariff levelisation and metering were £56 million in the year ended 31 December 2012, compared to £29 million in 2011. In addition to the effect of higher volumes, costs have increased in 2012 due to large increases in the Renewables Obligation and the Feed-in-Tariff levelisation costs resulting from the continued high uptake of solar photovoltaic subsidies.

Retail gross profit for the year ended 31 December 2012 was £15 million compared to £16 million in 2011.

Operating and administrative expenses

Retail operating and administrative expenses excluding depreciation and amortisation were £19 million for the year ended 31 December 2012, consistent with 2011. Higher staff costs to support the continued growth in the business have been offset by a reduction in other operating and administrative expenses.

Retail EBITDA for the year ended 31 December 2012 was a loss of £5 million compared to a loss of £3 million in 2011.

Central costs

Depreciation and amortisation

Depreciation and amortisation was £59 million for the year ended 31 December 2012 and £57 million for the year ended 31 December 2011.

Unrealised gains and losses on derivative contracts

The Group recognises unrealised gains and losses on forward contracts which meet the definition of derivatives under IFRSs. Where possible, we take the own use exemption for derivative contracts entered into and held for our own purchase, sale or usage requirements, including forward domestic coal and biomass contracts.

As such, the movement in the net unrealised gains and losses recognised in the balance sheet relates to the mark-to-market of our forward contracts for power yet to be delivered, as well as the mark-to-market on other commodities and foreign exchange contracts. The following table shows the movements in unrealised gains and losses and where they are recorded in our financial statements.

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Net unrealised gains/(losses) in the balance sheet at 1 January	**30.7**	(61.0)
Unrealised (losses)/gains recognised in the income statement	**(36.1)**	89.8
Fair value (losses)/gains recognised in the hedge reserve (a component of equity)	**(105.7)**	2.6
Premium on options	**0.8**	(0.7)
Net unrealised (losses)/gains in the balance sheet at 31 December	**(110.3)**	30.7

Mark-to-market movements on most of our derivative contracts, considered to be effective hedges, have been recognised through the hedge reserve, a component of shareholders' equity in the balance sheet. Movements in unrealised gains and losses recognised in the hedge reserve are mainly the result of unwinding mark-to-market positions relating to power delivered during a reporting period, and the recording of mark-to-market positions on power yet to be delivered at the end of that period.

The average price of power that had been contracted but had yet to be delivered at 31 December 2011 was higher than market prices, driving an unrealised gain. Offsetting this was an unrealised loss on coal and carbon contracts resulting in a net unrealised gain in the balance sheet of £31 million at 31 December 2011.

The fair value losses of £106 million recognised in the hedge reserve in 2012 reflect the unwinding of the 2011 year end position as the power was delivered. Relatively stable power prices through most of 2012, resulted in the average contracted power price ending the year at a similar level to market prices.

The unrealised losses recognised in the income statement of £36 million for the year ended 31 December 2012 and unrealised gains of £90 million in 2011 arise from mark-to-market movements on our derivative contracts which do not qualify for hedge accounting; largely financial coal and foreign exchange.

As we look to secure an increasing number of international contracts for the supply of biomass to support our strategy for renewable generation, we have entered into forward foreign exchange contracts to limit our exposure to fluctuations in exchange rates. A weakening US dollar at the end of 2012 resulted in unrealised losses recognised through the income statement and in the balance sheet at 31 December 2012 in respect of these contracts.

This combination of factors resulted in the recognition of an unrealised loss of £110 million in the balance sheet at 31 December 2012.

In considering mark-to-market movements, it is important to recognise that profitability is driven by our strategy to deliver market level dark green or bark spreads, not by the absolute price of any single commodity at any given date.

After allowing for the unrealised gains and losses on derivative contracts, depreciation and amortisation, operating profit for the year ended 31 December 2012 was £204 million compared to £366 million in 2011.

Interest

Net finance costs for the year ended 31 December 2012 were £14 million compared with £28 million in 2011.

Finance costs for 2011 include interest and other charges associated with the balance of a term loan of £135 million which was repaid in full in July 2011, resulting in lower costs for 2012. However, finance costs for 2012 did include £6 million in respect of the refinancing completed in December.

Tax

The tax charge before exceptional items was £26 million (an effective rate of 14%), compared to £71 million in 2011 (an effective rate of 21%). 2012 includes the impact of a revision to previous years' capital allowances claims now agreed with HMRC, resulting in a tax credit of £8 million recognised in the period.

The tax charge includes the impact of a 2% reduction in corporation tax rate for both years on current and deferred taxes, resulting in a £15 million tax credit in 2012 (2011: £16 million). The effective tax rate before exceptional items and the impact of changes in the corporation tax rate was 22% in 2012 (2011: 26%).

The exceptional tax credit of £198 million in the year ended 31 December 2011 reflects the agreement reached with HMRC over the Eurobond tax position and a number of other legacy issues.

As a result of the above factors, profit attributable to equity shareholders for the year ended 31 December 2012 was £164 million compared to £465 million in 2011, and basic and diluted earnings per share were 44 pence compared to 127 pence and 126 pence, respectively, in 2011.

Underlying profit attributable to equity shareholders (that is profit excluding the after tax impact of unrealised gains and losses on derivative contracts and exceptional items) was £193 million for the year ended 31 December 2012, compared to £202 million in 2011. Underlying basic and diluted earnings per share were 52 pence and 51 pence respectively in 2012, compared to 56 pence and 55 pence, respectively, in 2011.

Other key factors affecting the business

Outages and plant utilisation levels

	Year ended 31 December 2012	Year ended 31 December 2011
Electrical output (net sales) (TWh)	**27.1**	26.4
Load factor (%)	**81.6**	79.7
Availability (%)	**86.0**	88.4
Winter forced outage rate (%)	**3.7**	3.9
Forced outage rate (%)	**4.8**	5.8
Planned outage rate (%)	**9.6**	6.2
Total outage rate[(1)] (%)	**14.0**	11.6

Notes:
(1) The forced outage rate is expressed as a percentage of planned capacity available (that is, it includes a reduction for planned losses). The planned outage rate is expressed as a percentage of registered capacity. Accordingly, the aggregation of the forced outage rate and planned outage rate will not equate to the total outage rate.

Production performance was once again very strong in 2012. Plant availability of 86.0% for the year ended 31 December 2012, compared to 88.4% in 2011, demonstrates our leadership position in the coal-fired generation sector, with the impact of a double planned outage only marginally lowering availability.

The forced outage and Winter forced outage rates for the year ended 31 December 2012 were 4.8% and 3.7% respectively, compared to 5.8% and 3.9% in 2011. Forced outage rates remain consistent with our long-term target of circa 5%.

The planned outage rate achieved for the year ended 31 December 2012 was 9.6%, compared to 6.2% in 2011, with two major planned outages completed in 2012, compared to one major outage in 2011. Our maintenance regime includes a major planned outage for each of our six units once every four years. Consequently, there is an irregular pattern to planned outages and associated expenditure, since in two of the four years two units will each undergo a major planned outage. Two units will undergo a major planned outage in 2013.

As a result of this performance, and the plant despatch dynamics described in Generation results above, our load factor for the year ended 31 December 2012 was 81.6% compared to 79.7% in 2011. This is equivalent to 95% utilisation when available, and reflects an increase in electrical output (net power sales) to 27.1TWh in 2012 compared with 26.4TWh in 2011.

Health and safety

Our lost time injury rate and total recordable injury rate were 0.06 and 0.17 respectively for the year ended 31 December 2012 compared to 0.08 and 0.10 respectively in 2011. Our safety record continues to be industry-leading and was delivered alongside a significant amount of project activity and a double outage in 2012. Our commitment to deliver a positive health and safety culture will continue.

Liquidity and capital resources

Net cash was £311 million as at 31 December 2012, compared to £225 million at 31 December 2011. Cash and short-term deposits were £402 million as at 31 December 2012, compared to £233 million at 31 December 2011. An analysis of cash flows for both years is set out in the following table.

Analysis of cash flows

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
EBITDA	**298.4**	333.6
Decrease in ROC assets	**13.4**	1.0
Increase in carbon assets	**(39.0)**	–
Increase in working capital	**(9.3)**	(51.2)
Other	**(0.3)**	(1.5)
Cash generated from operations	**263.2**	281.9
Income taxes paid	**(50.6)**	(67.7)
Other (losses)/gains	**(0.8)**	0.7
Net interest paid	**(8.7)**	(16.4)
Net cash from operating activities	**203.1**	198.5
Cash flows from investing activities		
Purchases of property, plant and equipment	**(206.0)**	(43.8)
Short-term investments	**–**	65.0
Net cash (used in)/from investing activities	**(206.0)**	21.2
Cash flows from financing activities		
Equity dividends paid	**(95.7)**	(123.7)
Proceeds from issue of share capital	**187.7**	–
Repayment of borrowings	**(10.5)**	(135.4)
New borrowings	**100.0**	10.0
Other financing costs paid	**(9.7)**	(3.8)
Net cash from/(used in) financing activities	**171.8**	(252.9)
Net increase/(decrease) in cash and cash equivalents	**168.9**	(33.2)
Cash at 1 January	**202.8**	236.0
Cash at 31 December	**371.7**	202.8
Short-term investments at 31 December	**30.0**	30.0
Borrowings at 31 December	**(90.7)**	(7.6)
Net cash at 31 December	**311.0**	225.2

Cash generated from operations was £263 million in the year ended 31 December 2012, compared to £282 million in 2011.

This includes the fall of £35 million in EBITDA, partially offset by a decrease in ROC and LEC assets in 2012 of £13 million compared to £1 million in 2011 (as described in Generation results).

Also included in cash generated from operations for 2012 is an outflow of £39 million for carbon allowances purchased in advance for future periods (2011: £nil).

The working capital outflow of £9 million in 2012 is driven by an increase of £30 million in the value of biomass stocks, offset by a reduction of £11 million in the value of coal stocks. Biomass and coal stock levels both increased at 31 December 2012 by 0.2 million tonnes (to 0.4 million tonnes and 1.6 million tonnes respectively) compared to the previous year end. However, as described in Commodity markets, coal prices have fallen significantly over the last 18 months.

The working capital outflow in 2011 of £51 million largely reflects an increase in the value of coal stocks (£24 million), and a lower carbon creditor (£21 million), both driven by commodity market price movements during 2011.

Income taxes paid were £51 million in the year ended 31 December 2012, compared to £68 million in 2011. 2012 payments include settlement of the 2011 liability, as well as payments on account for 2012.

Net cash flows from investing activities include payments in respect of capital expenditure of £206 million for the year ended 31 December 2012 and £44 million in 2011 (see Capital expenditure). 2011 also includes a reduction in short-term investments of £65 million comprising short-term deposits with a maturity of more than three months at inception.

Net cash from financing activities was £172 million in the year ended 31 December 2012, compared to net cash used in financing activities of £253 million in 2011. The 2012 amount includes equity dividends paid of £96 million, net proceeds on the issue of share capital of £188 million and new borrowings drawn down in the year of £100 million. The 2011 amount includes equity dividends paid of £124 million and term loan repayments of £135 million (see Capital resources and refinancing).

The increase in cash and cash equivalents was therefore £169 million in the year ended 31 December 2012, compared to a decrease of £33 million in 2011. The Group's policy is to invest available cash in short-term bank, building society or other low risk deposits.

Capital resources and refinancing

On 25 October 2012, we announced the placing of approximately 36.5 million new ordinary shares. The placing raised £188 million net of expenses and was undertaken, alongside the other financing activities described below, to secure the funding for our biomass transformation.

In July 2012 we announced agreement of a new £100 million amortising term loan facility with Prudential M&G UK Companies Financing Fund, subsequently fully drawn down just before year end. In December 2012 we secured up to a further £100 million amortising term loan facility, with the UK Green Investment Bank. Both loans have six to eight year maturities.

Also in December 2012 we completed the refinancing of our £310 million revolving credit facility, due to mature in April 2014, repaying in the process the £10 million term loan previously drawn. This facility was replaced with a £400 million working capital and letter of credit facility which matures in April 2016. The margin on this new facility is 225 basis points above LIBOR.

Finally, as part of this refinancing, we have also successfully executed a new commodity trading facility. This is an innovative new structure, we believe the first of its kind in Europe, which allows us to transact prescribed volumes of commodity trades at attractive pricing without the requirement to post collateral. It works by offering trading counterparties uncapped access to the security package available to our senior lenders. Interest in this new facility has been strong, and we already have a number of counterparties signed-up.

Standard and Poor's have assigned a credit rating of BB+ to our new debt facilities. Over the past three years we have taken a number of steps to restructure our business and trading arrangements to enable us to operate successfully as either an investment grade or sub investment grade entity. These steps include the growth of Haven Power, execution of bilateral agreements with trading counterparties to cap collateral exposure, a shorter tenor to our trading strategy, implementation of the new commodity trading facility and increasing the quantum of our working capital/letter of credit facility.

Going concern

The Group's business activities, together with the factors likely to affect future developments, performance and position including principal risks and uncertainties are set out in the Chief Executive's statement, this Operational and financial performance and below. Our cash flows and borrowing facilities are described above.

We have significant headroom in our new banking facilities, and a recent history of cash generation, strong covenant compliance, and good visibility in near-term forecasts, due to our progressive hedging strategy. Our Business Plan, taking account of our capital investment plans and reasonably possible changes in trading performance, shows that we should be able to operate within the level of our current banking facilities.

Accordingly, the directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future, and continue to adopt the going concern basis of accounting when preparing these financial statements.

Seasonality of borrowing

Our business is seasonal with higher electricity prices and despatch in the Winter period and lower despatch in the Summer months, when prices are lower and plant availability is affected by planned outages.

Accordingly, cash flow during the Summer months is materially reduced due to the combined effect of lower prices and output, while maintenance expenditures are increased during this period due to major planned outages. The Group's £400 million working capital and letter of credit facility assists in managing the cash low points in the cycle where required (see Capital resources and refinancing).

Creditor payment policy and practice

Terms of payment are agreed with suppliers when negotiating each transaction and the Group's policy is to abide by those terms and pay creditors when sums owing fall due for payment, provided that the suppliers also comply with all relevant terms and conditions. Drax Group plc, the parent company of the Group, has no trade creditors. In respect of Group activities, the amounts due to trade creditors at 31 December 2012 represented approximately 23 days of average daily purchases through the year (2011: 22 days). The figure is based upon the ratio of amounts owed to trade creditors against the amounts the Group was invoiced by suppliers during the financial year.

Capital expenditure and biomass transformation

Fixed asset additions were £224 million in the year ended 31 December 2012, compared to £45 million in 2011.

2012 includes £180 million (2011: £5 million) of expenditure for our biomass transformation, being construction in progress for fuel delivery, storage and distribution systems.

2012 also includes the final instalment of our turbine upgrade project, which was completed on time and to budget. Since 2007, we have invested around £100 million to upgrade the high pressure and low pressure turbine modules on all six generating units to improve efficiency. The technology is performing to guarantee with all units achieving an overall baseload efficiency (that is, the ratio of energy out to energy in when operating at full capacity) approaching 40% at full load. This represents a 5% improvement on original baseload efficiency of 38% and annual savings of 1 million tonnes of CO_2 emissions allowances and approximately half a million tonnes of coal.

Looking forward, we expect total biomass transformation capital investment to be in the region of £650–£700 million (including the expenditure already incurred in 2012). This investment will allow us to progressively convert three generating units to biomass.

Approximately half of the total capital cost is investment in substantial equipment installations and modifications at the Drax Power Station site which commenced in 2012 as described above. The remainder is investment in upstream supply chain infrastructure, mainly pelleting facilities in the US, and any necessary work to ensure the plant is compliant with the Industrial Emissions Directive.

Our US pellet operations will be based on the Gulf Coast and will comprise of two pellet plants with combined capacity of 900,000 tonnes of pellet production per annum and a port facility with export capacity of up to 3 million tonnes per annum.

We expect to incur capital expenditure for the biomass transformation of around £200–£250 million in 2013. By the end of 2014 we anticipate the Drax site development will be substantially complete and our US based pellet operations to be very well advanced.

With the phased introduction of new plant and equipment, supported by the use of our existing biomass co-firing systems, we expect to convert our first unit in April 2013 and our second unit in 2014. Timing of the second and third unit conversion will depend on our progress with fuel sourcing.

The Chief Executive's statement provides more information in relation to our biomass transformation plans.

Contingent liability

We were obliged under the Community Energy Saving Programme ("CESP") to deliver energy saving measures to domestic consumers during the period 1 October 2009 to 31 December 2012. We entered into an agreement with a third party, pursuant to which the third party was obliged to deliver our CESP obligation for a total cost of £17 million. The third party has failed to comply fully with its obligation under the agreement, leaving a significant shortfall against our CESP obligation. We will be considering legal proceedings for breach of contract against this third party. We have entered into further agreements with additional third parties in order to rectify this shortfall so far as practicable.

At this stage it is not possible to predict whether any enforcement action may be imposed. No additional provisions have been recognised in respect of this matter as we are not able to reliably measure what the financial impact, if any, might be.

Future developments

Positions under contract for 2013, 2014 and 2015

We continue to follow our stated trading strategy of making steady forward power sales with corresponding purchases of CO_2 emissions allowances and fuel purchases. Our aim is to deliver market level dark green spreads across all traded market periods and, as part of this strategy, we retain power to be sold into the prompt (within season) power markets.

As at 11 February 2013, the positions under contract for 2013, 2014 and 2015 were as follows:

	2013	2014	2015
Power sales (TWh) comprising:	22.1	11.2	2.9
– Fixed price power sales (TWh) at an average achieved price (per MWh)	19.7 at £51.9	8.6 at £53.6	1.0 at £56.5
– Fixed margin and structured power sales (TWh)	2.4	2.6	1.9
CO_2 emissions allowances hedged, including UK NAP allocation, market purchases, structured contracts, and benefit of biomass co-firing (TWh equivalent)	20.9	10.5	2.7
Solid fuel at fixed price/hedged, including structured contracts (TWh equivalent)	23.0	17.6	9.5

Fixed price power sales include approximately 0.2TWh supplied in the period 1 January 2013 to 11 February 2013 under the five year 300MW baseload contract, which commenced on 1 October 2010, with Centrica.

Fixed margin power sales include approximately 2.4TWh in 2013, 2.6TWh in 2014 and 1.9TWh in 2015 in connection with the above contract.

Under this contract the Group will supply power on terms which include Centrica paying for coal, based on international coal prices, and delivering matching CO_2 emissions allowances amounting in aggregate to approximately 2.4 million tonnes in both 2013 and 2014, and approximately 1.8 million tonnes in 2015.

The contract provides the Group with a series of fixed dark green spreads agreed in October 2009.

Distributions

Distribution policy

The Board has previously committed to a pay-out ratio of 50% of underlying earnings (being profit attributable to equity shareholders adjusted to exclude the after tax impact of unrealised gains and losses on derivative contracts, and exceptional items) in each year. Underlying earnings for the year ended 31 December 2012 were £193 million.

Dividends paid

On 20 February 2012, the Board resolved, subject to approval by shareholders at the Annual General Meeting ("AGM") on 18 April 2012, to pay a final dividend for the year ended 31 December 2011 of 11.8 pence per share (£43 million). The final dividend was paid on 11 May 2012.

On 30 July 2012, the Board resolved to pay an interim dividend for the six months ended 30 June 2012 of 14.4 pence per share (£53 million), representing 50% of underlying earnings for the period. The interim dividend was paid on 12 October 2012.

Dividends proposed

At the forthcoming AGM the Board will recommend to shareholders that a resolution is passed to approve payment of a final dividend for the year ended 31 December 2012 of 10.9 pence per share (£44 million), payable on or before 17 May 2013. Shares will be marked ex-dividend on 24 April 2013.

Principal risks and uncertainties

The effective management of risks within the Group underpins the delivery of our key priorities.

The Group has a comprehensive structure of governance controls in place to manage risks. Policies have been established in key areas of the business such as trading, treasury, production and health and safety to ensure that these risks are managed in a controlled manner and in accordance with the policies set by the Board.

Commodity market price risk

Context
We experienced volatility in the commodity markets in which we traded during 2012

Risk

- We are exposed to the effect of fluctuations in commodity prices, particularly the price of electricity and gas, the price of coal and sustainable biomass (and other fuels), and the price of CO_2 emissions allowances.

Potential impact

- Volatility in financial results.

Associated objective and key priorities

- Maximise the value of the Drax business.

Examples of mitigating activities

- Well understood progressive hedging strategy, forward power sales with corresponding purchases of fuel and CO_2 emissions allowances when profitable to do so.

Counterparty risk

Context
The recent recession and uncertain economic growth potentially impact on counterparty risk

Risk

- We rely on third party suppliers for the delivery of fuel and other goods and services. We purchase a significant quantity of our fuel under contracts with a number of large UK and international suppliers, so are exposed to the risk of non-performance by these suppliers.
- We enter into fixed price and fixed margin contracts for the sale of electricity to a number of counterparties, so are exposed to the risk of failure of one or more of these counterparties.

Potential impact

- Additional costs associated with securing fuel and other goods and services from other suppliers.
- Failure to secure fuel from other suppliers resulting in limitation of operations.
- Adverse effect on cash flow and earnings arising from the failure of one or more of the counterparties to whom we sell power.

Associated objective and key priorities

- Maximise the value of the Drax business.

Examples of mitigating activities

- Diversified fuel supply in terms of source and counterparties.
- Good portion of purchases at market indexed prices (no mark-to-market exposure).
- Diversified logistics routes.
- Target to optimise holding of fuel stocks.
- Close monitoring and reporting of concentration risk in suppliers.
- Full suite of power counterparties with strong credit ratings.

- Close monitoring and reporting of concentration risk in power counterparties.
- Trading contracts generally include provisions that force counterparties to post collateral where their credit rating drops, subject to certain restrictions.

Power and renewables market liquidity risk

Context

Liquidity in the markets is dependent on there being a sufficient number of counterparties willing to trade actively

Risk

- The market structure and consolidation of the existing generation and supply businesses in the UK could result in a reduction in the number of active participants in the market with whom we are able to trade power and other commodities, including ROCs.

Potential impact

- Inability to hedge short to medium term exposure to electricity prices through wholesale market trading.
- Increased exposure to short-term market volatility.
- Inability to sell all of our output.
- Lower revenues and increased costs to achieve trading objectives.
- Adverse effect on financial results and cash flows.

Associated objective and key priorities

- Grow our retail business.
- Maximise the value of the Drax business.
- Maximise profitability from our coal generation capacity.
- Deliver our biomass strategy.

Examples of mitigating activities

- Grow direct sales through Haven Power, our electricity supply business.
- Initiatives to be active and responsive make Drax an attractive business partner.
- Oppose structural changes that impact our market access, such as clearing and margining.
- Work with other independent generators (via Independent Generators Group) to achieve positive market and regulatory changes to improve liquidity.

Biomass market risk

Context

Sustainable biomass is well placed to provide the UK with low cost and flexible renewable power, and contribute to meeting carbon reduction targets

Risk

- We could fail to secure sustainable biomass supplies and/or logistics arrangements which meet our hurdle return rates and operational requirements.
- Most of the sustainable biomass that we can procure is priced in foreign currency which increases our exposure to fluctuations against sterling and poses a risk to profitability.

Potential impact

- Inability to progress the biomass growth strategy.
- Adverse effect on financial results and cash flows.

Associated objective and key priorities

- Deliver our biomass strategy.

Examples of mitigating activities

- Contract with suppliers where a robust operational plant and logistics infrastructure is already in place; work with new suppliers to help develop such infrastructure.
- Hedge currency exposures or secure contracts in sterling to the extent that it is appropriate.

Plant operating risk

Context

Equipment failure and the impact on personnel and operations.

Risk

- Plant failure may be caused by the underperformance or outright failure of plant, transmission assets or other equipment and components including the IT systems used to operate the plant or conduct trading activities. The duration of the resultant forced outages is influenced by the lead time to manufacture and procure replacement components and to carry out repairs.
- As we progress our plans to convert to a predominantly biomass-fuelled generator, we are exposed to a broader range, and increased level of technical risk.

Potential impact

- Personnel injury.
- Lower revenues.
- Increased costs and contractual penalties.
- Adverse effect on financial results and cash flows.

Associated objective and key priorities

- Maintain operational excellence.
- Deliver excellent people leadership across our operations.

Examples of mitigating activities

- Comprehensive risk-based plant investment and maintenance programme.
- Maintaining a trained and competent workforce.
- Strong health and safety culture.
- Target to optimise holding of spare components for use in the event of plant failure particularly long lead time items.
- Business continuity plan for IT systems.
- Significant amounts of research and development work have been undertaken in terms of handling and burning biomass.

Regulatory and political risk

Context

The Government’s market reform agenda is driven predominantly by the need to move to a sustainable, low carbon energy sector which delivers affordable supplies to customers whilst maintaining security of supply over the longer term. Laws and regulations are many and complex, are frequently changing, and becoming ever more stringent, particularly in relation to environmental matters

Risk

- Changes to the current regulatory regime surrounding renewables, Carbon Price Support and other legislation could adversely affect our biomass strategy.
- The EU, UK and local environmental and health and safety laws and regulations cover many aspects of our operations including limits on emissions to air and water, noise, soil/groundwater contamination, waste, and health and safety standards.

Potential impact

- Less funding available for plant retrofit/investment costs to meet increasingly stringent environmental requirements.
- Lower load factors/generation levels.
- Adverse effect on financial results and cash flows.

Associated objective and key priorities

- Deliver our biomass strategy.
- Maintain operational excellence.

Examples of mitigating activities

- Briefing, representation and engagement at EU and UK level.
- Development of abatement and alternative generation options.
- Regular third party assurance over system effectiveness.
- Strong safety culture and related training.

Note: Ratings risk is no longer listed in the principal risks and uncertainties, following the development and implementation of a sub-investment grade business model, as set out in Operational and financial performance.

Responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the management report, which is incorporated into the Directors' report, includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Consolidated income statement

	Notes	Years ended 31 December 2012 £m	2011 £m
Revenue		**1,779.8**	1,835.9
Fuel costs in respect of generation		**(929.2)**	(1,020.8)
Cost of power purchases		**(141.7)**	(172.3)
Grid charges		**(167.8)**	(117.6)
Other retail costs		**(30.2)**	(24.4)
Total cost of sales		**(1,268.9)**	(1,335.1)
Gross profit		**510.9**	500.8
Other operating and administrative expenses		**(271.0)**	(224.4)
Unrealised (losses)/gains on derivative contracts		**(36.1)**	89.8
Operating profit		**203.8**	366.2
Interest payable and similar charges		**(15.3)**	(30.3)
Interest receivable		**1.7**	2.2
Profit before tax		**190.2**	338.1
Tax:			
— Before exceptional items	4	**(26.4)**	(71.4)
— Exceptional items	4	**–**	197.9
		(26.4)	126.5
Profit for the year attributable to equity holders		**163.8**	464.6

Earnings per share		**pence**	pence
— Basic	6	**44**	127
— Diluted	6	**44**	126

All results relate to continuing operations.

Underlying earnings and underlying earnings per share are set out in note 6.

Consolidated statement of comprehensive income

	Notes	Years ended 31 December 2012 £m	2011 £m
Profit for the year		**163.8**	464.6
Actuarial losses on defined benefit pension scheme		**(9.0)**	(3.7)
Deferred tax on actuarial losses on defined benefit pension scheme	4	**2.1**	0.9
Fair value (losses)/gains on cash flow hedges		**(105.7)**	2.6
Deferred tax on cash flow hedges before corporation tax rate change	4	**26.0**	(0.7)
Impact of corporation tax rate change on deferred tax on cash flow hedges	4	**–**	1.9
Other comprehensive (expense)/income		**(86.6)**	1.0
Total comprehensive income for the year attributable to equity holders		**77.2**	465.6

Consolidated balance sheet

	Notes	As at 31 December 2012 £m	2011 £m
Assets			
Non-current assets			
Goodwill and other intangible assets		**49.7**	10.7
Property, plant and equipment		**1,360.6**	1,195.7
Derivative financial instruments		**7.7**	11.0
		1,418.0	1,217.4
Current assets			
Inventories		**157.6**	137.6
ROC and LEC assets		**18.7**	32.1
Trade and other receivables		**224.8**	269.3
Derivative financial instruments		**37.6**	120.6
Short-term investments		**30.0**	30.0
Cash and cash equivalents		**371.7**	202.8
		840 .4	792.4
Liabilities			
Current liabilities			
Trade and other payables		**275.9**	292.8
Current tax liabilities		**14.6**	33.8
Borrowings	7	**0.3**	7.1
Derivative financial instruments		**100.4**	95.6
		391.2	429.3
Net current assets		**449.2**	363.1
Non-current liabilities			
Borrowings	7	**90.4**	0.5
Derivative financial instruments		**55.2**	5.3
Provisions		**31.5**	30.5
Deferred tax liabilities		**170.7**	203.8
Retirement benefit obligations		**42.1**	37.0
		389.9	277.1
Net assets		**1,477.3**	1,303.4
Shareholders' equity			
Issued equity	8	**46.4**	42.1
Capital redemption reserve		**1.5**	1.5
Share premium		**420.7**	420.7
Merger reserve		**710.8**	710.8
Hedge reserve		**(16.4)**	63.3
Retained profits		**314.3**	65.0
Total shareholders' equity		**1,477.3**	1,303.4

Consolidated statement of changes in equity

	Issued equity £m	Capital redemption reserve £m	Share premium £m	Merger reserve £m	Hedge reserve £m	Retained profits/ (accumulated losses) £m	Total £m
At 1 January 2011	42.1	1.5	420.7	710.8	59.5	(276.6)	958.0
Profit for the year	–	–	–	–	–	464.6	464.6
Other comprehensive income/(expense)	–	–	–	–	3.8	(2.8)	1.0
Total comprehensive income for the year	–	–	–	–	3.8	461.8	465.6
Equity dividends paid (note 5)	–	–	–	–	–	(123.7)	(123.7)
Movement in equity associated with share-based payments	–	–	–	–	–	3.5	3.5
At 1 January 2012	42.1	1.5	420.7	710.8	63.3	65.0	1,303.4
Profit for the year	–	–	–	–	–	163.8	163.8
Other comprehensive expense	–	–	–	–	(79.7)	(6.9)	(86.6)
Total comprehensive (expense)/income for the year	–	–	–	–	(79.7)	156.9	77.2
Equity dividends paid (note 5)	–	–	–	–	–	(95.7)	(95.7)
Issue of share capital (note 8)	4.3	–	–	–	–	183.4	187.7
Movement in equity associated with share-based payments	–	–	–	–	–	4.7	4.7
At 31 December 2012	**46.4**	**1.5**	**420.7**	**710.8**	**(16.4)**	**314.3**	**1,477.3**

Consolidated cash flow statement

	Notes	Years ended 31 December 2012 £m	2011 £m
Cash generated from operations	9	**263.2**	281.9
Income taxes paid		**(50.6)**	(67.7)
Other (losses)/gains		**(0.8)**	0.7
Interest paid		**(10.6)**	(18.9)
Interest received		**1.9**	2.5
Net cash from operating activities		**203.1**	198.5
Cash flows from investing activities			
Purchases of property, plant and equipment		**(206.0)**	(43.8)
Short-term investments/income		**–**	65.0
Net cash (used in)/generated from investing activities		**(206.0)**	21.2
Cash flows from financing activities			
Equity dividends paid	5	**(95.7)**	(123.7)
Proceeds from issue of share capital	8	**187.7**	–
Repayment of borrowings		**(10.5)**	(135.4)
New borrowings	7	**100.0**	10.0
Other financing costs paid		**(9.7)**	(3.8)
Net cash generated from/(used in) financing activities		**171.8**	(252.9)
Net increase /(decrease) in cash and cash equivalents		**168.9**	(33.2)
Cash and cash equivalents at 1 January		**202.8**	236.0
Cash and cash equivalents at 31 December		**371.7**	202.8

Notes to the consolidated financial statements

1. General information

The consolidated financial information for Drax Group plc (the "Company") and its subsidiaries (together "the Group") set out in this preliminary announcement has been derived from the audited consolidated financial statements of the Group for the year ended 31 December 2012 (the "financial statements").

This preliminary announcement does not constitute the full financial statements prepared in accordance with International Financial Reporting Standards ("IFRSs"). The financial statements were approved by the Board of directors on 18 February 2013. Statutory accounts for 2011 have been delivered to the Registrar of Companies and those for 2012 will be delivered in due course.

The report of the auditors on the financial statements was unqualified, did not draw attention to any matters by way of emphasis without qualifying their report, and did not contain a statement under Section 498 (2) or (3) of the Companies Act 2006 or equivalent preceding legislation.

2. Basis of preparation

The financial statements have been prepared in accordance with IFRSs adopted by the European Union and therefore the consolidated financial statements comply with Article 4 of the EU IAS Regulations.

The financial statements have been prepared on a going concern basis, and on the historical cost basis, except for certain financial assets and liabilities that have been measured at fair value.

3. Summary of significant accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set in the 2012 Annual report and accounts. These policies have been consistently applied to both years presented.

4. Taxation

The income tax expense reflects the estimated effective tax rate on profit before tax for the Group for the year ended 31 December 2012 and the movement in the deferred tax balance in the year, so far as it relates to items recognised in the income statement.

Exceptional items

The 2011 comparative figures include an exceptional tax credit of £197.9 million, following agreement reached with HMRC on 5 April 2011, resulting in the resolution of the Eurobond tax position and certain other smaller legacy tax matters. The 2011 income statement therefore includes a current tax credit of £149.5 million and a deferred tax credit of £48.4 million.

Changes in the rate of corporation tax

Following the announcement of the 2012 Budget, the Finance Act 2012 (the “Act”) was enacted by Parliament in July 2012. The Act confirmed reductions in the rate of corporation tax from 26% to 24% from April 2012, and from 24% to 23% from April 2013, both of which were enacted during the year. In addition, in the 2012 Budget, the Government proposed further reductions in the rate of corporation tax from 23% to 22% from 1 April 2014, and in the 2012 Autumn Statement announced an acceleration of this decrease in corporation tax to 21% from 1 April 2014. These proposals had not been substantively enacted at the balance sheet date.

	Years ended 31 December	
	2012 £m	2011 £m
Tax charge/(credit) comprises:		
Current tax before exceptional items	**31.4**	61.3
Deferred tax before exceptional items:		
— Before impact of corporation tax rate change	**10.1**	26.2
— Impact of corporation tax rate change	**(15.1)**	(16.1)
Tax charge before exceptional items	**26.4**	71.4
Exceptional items:		
— Current tax	**–**	(149.5)
— Deferred tax	**–**	(48.4)
Exceptional items	**–**	(197.9)
Total tax charge/(credit)	**26.4**	(126.5)

	Years ended 31 December	
	2012 £m	2011 £m
Tax on items (credited)/charged to other comprehensive income:		
Deferred tax on actuarial losses on defined benefit pension scheme	**(2.1)**	(0.9)
Deferred tax on cash flow hedges	**(26.0)**	0.7
Impact of corporation tax rate change on deferred tax on cash flow hedges	**-**	(1.9)
	(28.1)	(2.1)

The tax differs from the standard rate of corporation tax in the UK of 24.5% (2011: 26.5%). The differences are explained below:

	Years ended 31 December	
	2012 £m	2010 £m
Profit before tax	**190.2**	338.1
Profit before tax multiplied by the rate of corporation tax in the UK of 24.5% (2011: 26.5%)	**46.6**	89.6
Effects of:		
Adjustments in respect of prior periods	**(7.6)**	(3.8)
Expenses not deductible for tax purposes	**1.3**	1.3
Other	**1.2**	0.4
Change to corporation tax rate	**(15.1)**	(16.1)
Total tax charge before exceptional items	**26.4**	71.4
Exceptional items	**–**	(197.9)
Total tax charge/(credit)	**26.4**	(126.5)

5. Dividends

	Years ended 31 December	
	2012 £m	2011 £m
Amounts recognised as distributions to equity holders in the year (based on the number of shares in issue at the record date):		
Interim dividend for the year ended 31 December 2012 of 14.4 pence per share paid on 12 October 2012 (2011: 16.0 pence per share paid on 14 October 2011)	**52.6**	58.4
Final dividend for the year ended 31 December 2011 of 11.8 pence per share paid on 11 May 2012 (2011: 17.9 pence per share paid on 13 May 2011)	**43.1**	65.3
	95.7	123.7

At the forthcoming Annual General Meeting the Board will recommend to shareholders that a resolution is passed to approve payment of a final dividend for the year ended 31 December 2012 of 10.9 pence per share (equivalent to approximately £44 million) payable on or before 17 May 2013. The final dividend has not been included as a liability as at 31 December 2012.

6. Earnings per share

Basic earnings per share is calculated by dividing the earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year. In calculating diluted earnings per share the weighted average number of ordinary shares outstanding during the year is adjusted, when relevant, to take account of outstanding share options in relation to the Group's Approved Savings-Related Share Option Plan ("SAYE Plan") and contingently issuable shares under the Group's Executive Share Incentive Plan ("ESIP") and Bonus Matching Plan ("BMP"). The underlying earnings per share has been calculated after excluding the after tax impact of marking-to-market derivative contracts which are not hedged, and exceptional items.

Reconciliations of the earnings and weighted average number of shares used in the calculation are set out below:

	Years ended 31 December	
	2012 £m	2011 £m
Earnings:		
Earnings attributable to equity holders of the Company for the purposes of basic and diluted earnings	**163.8**	464.6
After tax impact of unrealised gains and losses on derivative contracts	**29.0**	(64.3)
Exceptional items (note 4)	**–**	(197.9)
Underlying earnings attributable to equity holders of the Company	**192.8**	202.4

	Years ended 31 December	
	2012	2011
Number of shares:		
Weighted average number of ordinary shares for the purposes of basic earnings per share (millions)	**371.7**	364.9
Effect of dilutive potential ordinary shares under share plans	**3.5**	2.6
Weighted average number of ordinary shares for the purposes of diluted earnings per share (millions)	**375.2**	367.5
Earnings per share – basic (pence)	**44**	127
Earnings per share – diluted (pence)	**44**	126
Underlying earnings per share – basic (pence)	**52**	56
Underlying earnings per share – diluted (pence)	**51**	55

7. Borrowings

	As at 31 December	
	2012 £m	2011 £m
Current:		
Revolving credit facility	**–**	6.8
Finance lease liabilities	**0.3**	0.3
	0.3	7.1

	As at 31 December	
	2012 £m	2011 £m
Non-current:		
Term loans	**90.3**	–
Finance lease liabilities	**0.1**	0.5
	90.4	0.5

Refinancing

As set out in Operational and financial performance, on 20 December 2012 we completed the refinancing of our revolving credit facilities which were due to mature in April 2014. This facility was replaced with a larger £400 million revolving credit facility which matures in April 2016 and can be used for both letters of credit and working capital purposes. The margin over LIBOR on our new facility is 2.25%. In addition to the revolving credit facility, we executed two new committed term loans of £100 million each with the Prudential M&G UK Companies Financing Fund and the UK Green Investment Bank. The loans have an identical repayment profile, amortising from the date 6 years after signing with the final repayment 8 years after signing. At the same time as concluding the financing agreements above, we also executed a commodities trading line, which allows trading counterparties to benefit from the security package offered to senior lenders instead of Drax posting collateral for certain volumes of trades. The Prudential M&G UK Companies Financing Fund loan of £100 million was fully drawn at the year end.

Analysis of borrowings

Borrowings at 31 December 2012 and 31 December 2011 consisted principally of amounts drawn down against bank loans and the revolving credit facility respectively.

	As at 31 December 2012		
	Borrowings before deferred finance costs £m	Deferred finance costs £m	Net borrowings £m
Term loans	**100.0**	**(9.7)**	**90.3**
Finance lease liabilities	**0.4**	**–**	**0.4**
Total borrowings	**100.4**	**(9.7)**	**90.7**
Less current portion	**(0.3)**	**–**	**(0.3)**
Non-current borrowings	**100.1**	**(9.7)**	**90.4**

	As at 31 December 2011		
	Borrowings before deferred finance costs £m	Deferred finance costs £m	Net borrowings £m
Term loans	10.0	(3.2)	6.8
Finance lease liabilities	0.8	–	0.8
Total borrowings	10.8	(3.2)	7.6
Less current portion	(10.3)	3.2	(7.1)
Non-current borrowings	0.5	–	0.5

8. Issued equity

	As at 31 December	
	2012 £m	2011 £m
Authorised:		
865,238,823 ordinary shares of $11\frac{16}{29}$ pence each	**100.0**	100.0
Issued and fully paid:		
2011 — 364,862,718 ordinary shares of $11\frac{16}{29}$ pence each	**–**	42.1
2012 — 401,587,564 ordinary shares of $11\frac{16}{29}$ pence each	**46.4**	–
	46.4	42.1

The movement in allotted and fully paid share capital of the Company during each year was as follows:

	Years ended 31 December	
	2012 (number)	2011 (number)
At 1 January	**364,862,718**	364,859,988
Issued under employee share schemes	**250,219**	2,730
Issue of share capital	**36,474,627**	–
At 31 December	**401,587,564**	364,862,718

The Company has only one class of shares, which are ordinary shares of $11\frac{16}{29}$ pence each, carrying no right to fixed income. No shareholders have waived their rights to dividends.

Issued under employee share schemes

On 30 April 2012, a total of 246,017 shares were issued in satisfaction of shares vesting in accordance with the rules of the Group's Bonus Matching Plan granted in 2009. Additionally, on 10 February, 14 September and 24 December 2012 a total of 1,776 shares, 873 shares and 1,553 shares, respectively, were issued on early exercise of options under the Group's Savings-Related Share Option Plan by three separate individuals whose employment with the Group had terminated due to retirement (28 September 2011: 274 shares, one individual). No shares were issued in satisfaction of the Bonus Matching Plan for employees whose employment terminated due to retirement during 2012 (1 April 2011: 2,456 shares, one individual).

Share Placing

As part of the funding for the capital investment required for biomass transformation, on 29 October 2012 the Group placed 36,474,627 shares, representing 9.9% of the existing issued ordinary share capital at that time. The placing raised gross proceeds of £189.7 million. Associated transaction costs of £2.0 million have been deducted directly from equity.

The placing shares have been credited as fully paid and rank equally in all respects with the existing ordinary shares of $11\frac{16}{29}$ pence each in the capital of the Company, including the right to receive all dividends and other distributions declared, made or paid in respect of such shares after the date of issue of the placing shares.

The share placing was achieved through a “cash box” placing arrangement, which is legally structured such that the merger relief criteria within the Companies Act 2006 apply. Accordingly, the funds raised in excess of the nominal value of the shares issued have been treated as distributable within retained reserves rather than credited to the share premium account. As a consequence, of the £187.7 million net proceeds raised, share capital increased by £4.3 million with the balance of £183.4 million increasing retained profits in the year ended 31 December 2012.

9. Cash generated from operations

	Years ended 31 December	
	2012 £m	2011 £m
Profit for the year	**163.8**	464.6
Adjustments for:		
Interest payable and similar charges	**15.3**	30.3
Interest receivable	**(1.7)**	(2.2)
Tax charge/(credit)	**26.4**	(126.5)
Depreciation and amortisation	**58.5**	57.2
Unrealised losses/(gains) on derivative contracts	**36.1**	(89.8)
Defined benefit pension scheme current service cost	**5.7**	5.4
Non-cash charge for share-based payments	**4.7**	3.5
Operating cash flows before movement in working capital	**308.8**	342.5
Changes in working capital		
Increase in inventories	**(19.9)**	(21.0)
Decrease/(increase) in receivables	**44.5**	(36.6)
(Decrease)/increase in payables	**(33.9)**	6.4
Total increase in working capital	**(9.3)**	(51.2)
Increase in carbon assets	**(39.0)**	–
Decrease in ROC assets	**13.4**	1.0
Defined benefit pension scheme contributions	**(10.7)**	(10.4)
Cash generated from operations	**263.2**	281.9

Glossary

Ancillary services
Services provided to National Grid used for balancing supply and demand or maintaining secure electricity supplies within acceptable limits. They are described in Connection Condition 8 of the Grid Code.

Availability
Average percentage of time the units were available for generation.

Average achieved price
Power revenues divided by volume of net sales (includes imbalance charges).

Average capture price
Revenue derived from bilateral contracts divided by volume of net merchant sales.

Balancing Mechanism
The sub-set of the market through which the System Operator can call upon additional generation/consumption or reduce generation/consumption, through market participants' bids and offers, in order to balance the system minute by minute.

Baseload
Running 24 hours per day, seven days per week remaining permanently synchronised to the system.

Bilateral contracts
Contracts with counterparties and power exchange trades.

Company
Drax Group plc.

Dark green spread
The difference between the price available in the market for sales of electricity and the marginal cost of production (being the cost of coal and other fuels including CO_2 emissions allowances).

EBITDA
Profit before interest, tax, depreciation and amortisation, gains/(losses) on disposal of property, plant and equipment and unrealised gains/(losses) on derivative contracts.

EU ETS
The EU Emissions Trading System is a mechanism introduced across the EU to reduce emissions of CO_2; the scheme is capable of being extended to cover all greenhouse gas emissions.

Forced outage
Any reduction in plant availability excluding planned outages.

Feed-in Tariff with Contracts for Difference (FiT CfD)
A long-term contract set at a fixed level where variable payments are made to ensure the generator receives an agreed tariff (assuming they sell their electricity at the market price). The Feed-in Tariff payment would be made in addition to the generator's revenues from selling electricity in the market. The FiT CfD can be a two-way mechanism that has the potential to see generators return money to consumers if electricity prices are higher than the agreed tariff.

Forced outage rate
The capacity which is not available due to forced outages or restrictions expressed as a percentage of the maximum theoretical capacity, less planned outage capacity.

Frequency response service
Services purchased by National Grid to maintain system frequency.

Grid charges
Includes transmission network use of system charges ("TNUoS"), balancing services use of system charges ("BSUoS") and distribution use of system charges ("DUoS").

Group
Drax Group plc and its subsidiaries.

IFRSs
International Financial Reporting Standards.

LECs
Levy Exemption Certificates. Evidence of Climate Change Levy exempt electricity supplies generated from qualifying renewable sources.

Load factor
Net sent out generation as a percentage of maximum sales.

Lost time injury rate
The frequency rate is calculated on the following basis: lost time injuries/hours worked times 100,000. Lost time injuries are defined as occurrences where the injured party is absent from work for more than 24 hours.

Net Balancing Mechanism
Net volumes attributable to accepted bids and offers in the Balancing Mechanism.

Net cash/(debt)
Comprises cash and cash equivalents, short-term investments less overdrafts and borrowings net of deferred finance costs.

Net merchant sales
Net volumes attributable to bilateral contracts and power exchange trades.

Net sales
The aggregate of net merchant sales and net Balancing Mechanism.

Occupational health and safety assessment series (OHSAS)
The OHSAS specification gives requirements for an occupational health and safety management system to enable an organisation to control occupational health and safety risks and improve its performance.

Planned outage
A period during which scheduled maintenance is executed according to the plan set at the outset of the year.

Planned outage rate
The capacity not available due to planned outages expressed as a percentage of the maximum theoretical capacity.

Pond fines
Coal dust and waste coal from the cleaning and screening process which can be used for coal-fired power generation.

Power exchange trades
Power sales or purchases transacted on the APX UK power trading platform.

Power revenues
The aggregate of bilateral contracts and Balancing Mechanism income/expense.

ROCs
Renewables Obligation Certificates.

Summer
The calendar months April to September.

Technical availability
Total availability after planned and forced outages.

Total recordable injury rate (TRIR)
The frequency rate is calculated on the following basis: (lost time injuries + worst than first aid)/hours worked x 100,000.

UK NAP
UK National Allocation Plan.

Underlying earnings per share
Calculated as profit attributable to equity holders, adjusted to exclude the after tax impact of unrealised gains and losses on derivative contracts, and exceptional items, divided by the weighted average number of ordinary shares outstanding during the period.

Winter
The calendar months October to March.