24. Financial risk

The Group is subject to risks related to changes in interest rates, exchange rates, fuel prices, counterparty credit and liquidity within the framework of its business operations.

Interest rate risk

The Group is subject to risks arising from interest rate movements in connection with its bank debt, aircraft financing and cash investments. Interest rate swaps and interest rate collars are used to manage these risks and are usually designated as cash flow hedges of the interest rate.

Currency risk

The Group has activities in a large number of countries and is therefore subject to the risk of exchange rate fluctuations. Currency risks arise in connection with the sourcing of services from destinations outside the source market. In addition, US dollar exposure arises on the procurement of fuel and operating supplies for aircraft, as well as investments in aircraft.

The Group requires subsidiaries to identify and appropriately hedge all trading exposures in line with established policies.

The Group uses currency forwards, currency swaps and plain vanilla currency options to manage currency risks and these are usually designated as cash flow hedges of forecast future transactions.

Fuel price risk

Exposure to fuel price risk arises due to flying costs for the Group's aircraft. Fuel price contracts are entered into to manage the risk of adverse changes in the price of fuel. The Group's policy is to hedge up to 80% of the fuel requirement for the flight schedule concerned, with all fuel exposures hedged between 6 and 18 months prior to consumption. Hedging is implemented with a combination of fixed price contracts (swaps) and net purchased options, either in crude oil, gas oil or kerosene.

The market risks that the Group is subject to have been identified as interest rate risk, exchange rate risk and fuel price risk. The impact of reasonably possible changes in these risk variables on the Group, based on the period end holdings of financial instruments have been calculated and are set out in the tables below. In each case it has been assumed that all other variables remain constant. As explained in note 23, fuel price risk is hedged through the use of a combination of derivative instruments. For the purpose of illustrating sensitivity, the price of the underlying commodity in each instrument has been assumed to change by 20%.

	2009		2008	
Interest rate risk	**Impact on profit before tax £m**	**Impact on equity £m**	Impact on profit before tax £m	Impact on equity £m
1% (2008: 1%) increase in interest rates	**(2.2)**	**–**	0.7	–
0.25% (2008: 1%) decrease in interest rates	**0.5**	**–**	(0.7)	–

	2009		2008	
Exchange rate risk	**Impact on profit before tax £m**	**Impact on equity £m**	Impact on profit before tax £m	Impact on equity £m
5% strengthening of euro	**8.8**	**30.5**	(1.4)	37.2
5% weakening of euro	**(10.7)**	**(30.2)**	(2.6)	(28.8)
5% strengthening of US dollar	**10.0**	**63.6**	(7.4)	75.2
5% weakening of US dollar	**(9.2)**	**(57.3)**	2.3	(67.7)

	2009		2008	
Fuel price risk	**Impact on profit before tax £m**	**Impact on equity £m**	Impact on profit before tax £m	Impact on equity £m
20% increase in fuel price	**3.6**	**62.4**	–	150.0
20% decrease in fuel price	**(3.5)**	**(63.0)**	–	(138.1)

Liquidity risk

The liquidity position of the Group is significantly influenced by the booking and payment pattern of customers. As a result, liquidity is at its lowest in the winter months and at its highest in the summer months. The Group manages the seasonal nature of its liquidity by making use of its bank revolving credit facility.

Short-term liquidity is primarily invested in bank deposits and, to a lesser extent, in securities having at least an investment grade rating.

Financial liabilities are analysed below based on the time between the period end and their contractual maturity. The amounts shown are estimates of the undiscounted future cash flows and will differ from both carrying value and fair value.

	Amount due				
At 30 September 2009	**in less than 3 months £m**	**between 3 and 12 months £m**	**between 1 and 5 years £m**	**in more than 5 years £m**	**Total £m**
Trade and other payables	**1,628.5**	**100.7**	**7.7**	**2.2**	**1,739.1**
Borrowings	**423.9**	**200.3**	**324.1**	**18.0**	**966.3**
Obligations under finance leases	**65.6**	**181.1**	**37.1**	**23.7**	**307.5**
Derivative financial instruments – payable	**1,015.4**	**1,552.0**	**69.6**	**–**	**2,637.0**
– receivable	**(964.1)**	**(1,397.6)**	**(62.3)**	**–**	**(2,424.0)**
	2,169.3	**636.5**	**376.2**	**43.9**	**3,225.9**

Notes to the financial statements continued

24. Financial risk continued

At 30 September 2008	Amount due in less than 3 months £m	Amount due between 3 and 12 months £m	Amount due between 1 and 5 years £m	Amount due in more than 5 years £m	Total £m
Trade and other payables	1,641.4	80.8	8.8	–	1,731.0
Borrowings	50.4	345.6	441.8	18.1	855.9
Obligations under finance leases	69.7	128.0	229.1	22.6	449.4
Derivative financial instruments – payable	366.1	442.9	176.3	–	985.3
– receivable	(222.2)	(386.9)	(137.0)	–	(746.1)
	1,905.4	610.4	719.0	40.7	3,275.5

Estimated undiscounted future cash flows are disclosed above in respect of derivatives with a negative fair value at the period end. These cash flows include amounts in respect of fuel derivatives which are based on the period end fair values. Estimated cash flows relating to fuel option derivatives have all been reported in the 'amount due in less than three months' category. Trade and other payables includes non-financial liabilities of £186.8m (2008: £161.6m) which have not been analysed above.

Counterparty credit risk

The Group is exposed to credit risk in relation to deposits, derivatives with a positive fair value and trade and other receivables. The maximum exposure in respect of each of these items at the balance sheet date is their carrying value. The Group assesses its counterparty exposure in relation to the investment of surplus cash, fuel contracts, foreign exchange and interest rate hedging contracts and undrawn credit facilities. The Group uses published credit ratings, credit default swap prices and share price performance in the previous 30 day period to assess counterparty strength and therefore to define the credit limit for each counterparty. The Group's approach to credit risk in respect of trade and other receivables is explained in Note 18.

25. Insurance

Management of insurance risk

Incidental to its main business, the Group, through its subsidiary White Horse Insurance Ireland Limited, issues contracts that transfer significant insurance risk and that are classified as insurance contracts. As a general guideline, the Group defines as significant insurance risk the possibility of having to compensate the policyholder if a specified uncertain future event adversely affects the policyholder.

Business written includes standard commercial risks for the Group and travel insurance for both Group and non-Group customers.

The principal nature of travel insurance risks is one of short term, low value and high volume. Underwriting performance is monitored on an ongoing basis and pricing reviewed annually for each individual contract. Exposure is capped by specific limits within the insurance policy and by using reinsurance contracts for any claims in excess of these retention limits. Commercial policies with the Group are subject to policy excesses and single event and aggregate limits.

Insurance risk is spread across several European countries where the Group operates including the UK, Ireland and Continental Europe.

When estimating the cost of claims outstanding at the period end, the principal assumption underlying the estimates is the Group's past development pattern. This includes assumptions in respect of historic claims costs, average claims handling expenses and market developments. The Group also uses an independent actuary to review its liabilities to ensure that the carrying values are adequate. Any changes to these variables are not expected to have a material effect on the Group financial statements.

The Group operates a reinsurance policy approved by the White Horse Insurance Ireland Ltd board which ensures that reinsurers have a financial stability rating of B+ (A M Best) or above. The Group has assessed these credit ratings as being satisfactory in diminishing the Group's exposure to the credit risk of its insurance receivables.

Income and expenses arising directly from insurance contracts

	2009 £m	2008 £m
Revenue		
Net earned premium income	**7.9**	7.8
Deposit Interest	**0.5**	2.5
Other Income	**0.4**	–
	8.8	10.3
Expenses		
Claims incurred	**11.4**	14.4
Other operating expenses	**2.3**	2.0
	13.7	16.4