Achieving business benefits

Pete Redfern
Group Chief Executive

Following the successful completion of the largest ever merger in the UK homebuilding industry, we are making excellent progress with our integration plans.

At the time of the merger, we outlined a series of business benefits that would be delivered as a result of the transaction and I would like to take this opportunity to update you on the advances that we are making in each of these areas.

Improving margin growth in the UK

The UK Housing businesses of both Taylor Woodrow and George Wimpey were operating in the bottom quartile of the listed peer group in terms of margin performance prior to the merger. However, the reasons for this underperformance were fundamentally different. Whilst Taylor Woodrow had a very strong long term landbank, it had higher than average build costs and was not converting all of the value through the build and sales processes. In contrast, George Wimpey's cost efficiency was amongst the best in the sector, but its landbank mainly comprised of more expensive, short term land.

The merger has given us a well balanced land portfolio, a position that neither legacy business would have been able to achieve in such a short period of time as a standalone entity. This brings with it the ability to benefit from the lower land costs associated with strategic land, whilst mitigating the risk of planning delay through the use of short term land to fill in any 'gaps' in the land pipeline.

By bringing these two businesses together we have had the opportunity to blend the best practices of each operation to create the foundations for a more competitive organisation moving forward. For example, we have performed a review of similar housetypes from the Bryant Homes and George Wimpey product ranges to identify improvements to quality and reductions in cost that can be rolled out across future developments.

We have also been able to optimise our business structure, with the result that overheads going forward will represent a smaller percentage of overall sales than was the case for either legacy business.

Both legacy businesses were operating with higher sales rates per outlet than the industry average prior to the merger. We have taken the decision to prioritise margin over volume and have therefore reduced sales rates since the merger. In the more subdued market conditions that we have experienced in the UK this has meant that we have not had to chase sales and therefore that we can be more selective with regard to the incentives that are offered to secure a sale.

I am delighted by the progress that has been made by the UK Housing business over the last six months. More detail is provided on pages 22 to 27, but the evidence of our success can be seen in the increase in the pro forma operating margin** from 12.8% in 2006 to 15.2% in 2007.

** The basis of preparation of pro forma financial information is set out on page 104.

Economies of scale in the UK

Bringing together two businesses brings with it opportunities to benefit from the increased size of the combined operations. For our UK Housing business, these opportunities lie in three main areas: procurement and supply chain; overhead efficiency; and land management.

Whilst both legacy businesses had already put in place a number of initiatives to ensure the efficiency of their purchasing and supply chain processes, the increased scale of the combined business provides further opportunities for improvement. For example, following the merger, we have undertaken an exercise to compare the prices paid for materials by each of the legacy businesses. As a result, we have been able to ensure that we take advantage of the best deals for future completions.

However, our size enables us to go beyond this approach. We are currently working with our major suppliers to establish how we can take costs out of the process of supplying our raw materials to the benefit of both ourselves and our suppliers. Examples might include sharing more detailed forecast information with our suppliers to enable them to anticipate key periods of demand for their products and analysing the location of our sites to minimise transport costs.

We have structured our UK Housing business in such a way as to optimise overhead costs. The UK Housing head office, based in High Wycombe, is a lean team providing support and specialist guidance to our 34 regional businesses. Each of these regional businesses is staffed in accordance with the expected number of completions. The optimal size of a region is around 650 completions and, once a region approaches this scale, we will create a new 'satellite' operation to facilitate ongoing growth. To maintain overhead efficiency, these satellites will receive support from their originating region until such time as the level of completions merits an increase in the size of the team.

Our increased scale also enables us to adapt our approach to land buying in the UK. The strength of our balance sheet and the skills of our land and planning teams will enable us to participate in projects that our legacy businesses might not have been able to consider. We are also able to invest proportionately more money into strategic land, which brings with it the potential for higher profits on sites that are successfully promoted through the planning process.

A stronger business in North America

Market conditions remain exceptionally challenging in North America, but the merger brings benefits which leave us better placed than the legacy businesses would have been on their own.

There was an excellent geographical fit between the two legacy businesses in the US. Both Taylor Woodrow and Morrison Homes had operations in Arizona, California, Florida and Texas. Combining these operations has enabled us to increase our scale in these key States, bringing with it overhead efficiencies, increased buying power, greater market presence and marketing efficiencies.

The combination of the two businesses has brought us a broader product offering, appealing to a wider range of consumer preferences. Whilst the legacy Morrison Homes business was focused on the mid-market, the Taylor Woodrow business also had experience of building luxury homes. We go forward with a product range catering to buyers from entry level apartments to luxury country club homes. We also have a land development business which sells lots to other homebuilders, as well as supplying our own operations.

We are also better placed to take advantage of future market recovery in the US as a result of the merger.

The increased strength of our business, both in North America and at a Group level, leaves us well positioned to take advantage of land acquisition opportunities as the market starts to recover. However, it remains too early to make significant land purchases in the US.

Material annual synergies

At the time of the announcement of the merger, we indicated that we expected to deliver an exit rate of at least £70 million of pre-tax synergies by the end of 2008. We anticipated one-off costs associated with the merger of around £60 million to be incurred primarily during 2007.

We subsequently increased our synergy estimates at the Interim Results in July. This was a result of the additional work that we were able to do as the merger progressed. We have actions in place to deliver these increased exit rate targets of £70 million by the end of 2008 and £100 million in aggregate by the end of 2009, with further progress expected. The one-off costs associated with the merger were in line with the expected £60 million and have been recognised in the 2007 accounts.

These synergies are in excess of the previously announced cost savings of £25 million in George Wimpey's UK business and combined savings in excess of US$20 million in the legacy businesses in North America. I am very pleased to be able to confirm that both of these targets were also achieved during 2007.

People

We were able to take advantage of the fact that the transaction was an agreed merger to make significant progress on integration planning before the deal completed. When we announced the merger we were also able to announce the proposed structure of the combined Board.

We set up integration teams, comprising employees from both legacy businesses, which were tasked with putting together detailed plans that could be put into effect as soon as the merger completed. These teams worked together exceptionally well, enabling us to hit the ground running on 3 July 2007.

Since the merger, I have spent a lot of my time visiting the different parts of our combined business and I have been very impressed by the positive attitude of the people that I have met and by their determination to make the merger work.

Corporate responsibility

Corporate responsibility is an integral part of corporate governance and one of the hallmarks of a well managed company. We are committed to being a responsible company and to playing our part in building increasingly sustainable homes and communities.

We also believe that corporate responsibility makes sound commercial sense. It helps us to:

- Demonstrate high standards of governance to stakeholders whose opinions and actions can have an impact on our business
- Meet our customers' current and future needs and wants
- Attract and retain high calibre employees
- Save money, reduce business risk and protect our reputation by managing our business effectively, rather than engaging in expensive or damaging remedial action
- Win competitive tenders that are increasingly based on sustainability criteria
- Respond to the growing sustainability requirements of governments in the regions in which we operate
- Identify opportunities for business development and innovation
- Anticipate and comply promptly with new legislation

Since the merger of George Wimpey and Taylor Woodrow in July 2007, we have focused on learning from the experience and expertise within each of our legacy businesses with a view to integrating best practice for the future.

During 2007, we focused on analysing our legacy companies' approach in all business areas, engaging with internal and external stakeholders to identify best practice and deciding on how best to move forward. We are now updating our policies, procedures and systems and, once this process is complete, we will focus on implementing and embedding these new approaches.

Sustainability performance

George Wimpey and Taylor Woodrow had a strong track record in terms of corporate responsibility performance. The Next Generation 2007 sustainability benchmark placed both companies in the top three of the UK's 20 largest housebuilders. Taylor Woodrow and George Wimpey scored 73% and 72% respectively in the benchmark, in comparison with an average sector score of 39%. We were two of just three companies to score over 70% in this WWF, Insight Investment and Housing Corporation benchmark. We are also included in the FTSE4Good and Dow Jones Sustainability Group indices.

Our involvement in developments such as the Design for Manufacture site at Oxley Woods and the Millennium Communities in Greenwich, Telford and Manchester are a further testament to our sustainability performance.

Outlook

The Group is well placed following the merger to benefit from a strengthened landbank, operational efficiencies, ongoing cost savings programmes and a strong financial position. We have continued to identify additional areas for further savings and efficiencies.

In the UK, although sales and cancellation rates have improved in the early part of 2008, they remain weaker than seasonal norms. Our order book at the end of February 2008 is £1.3 billion with a greater than historical weighting towards affordable homes. We anticipate that the current subdued conditions will continue, with interest rates and mortgage availability being key determinants of customer confidence. Our focus is on preserving value through maintaining a steady, but reduced, sales rate and controlling land and work in progress spend tightly. We anticipate that these actions will result in significant cash generation, particularly in the second half of 2008.

In North America, we do not expect market conditions in the US to improve significantly during 2008. In the short term, our strategy remains to focus on managing out existing sites and reducing the cost base. We are well placed to take advantage of land acquisition opportunities as they arise in the future.

Pete Redfern
Group Chief Executive