

CHIEF EXECUTIVE'S OPERATIONAL REVIEW

In the year ended 30 June 2005, Redrow delivered a 14% increase in profit before tax to £141.1m (2004: £124.1m) and a 13% increase in earnings per share to 62.1p (2004: 54.8p), whilst continuing its unique track record amongst major homebuilders of increasing legal completions in every year since 1990 as legal completions reached 4,372 (2004: 4,284).

These results were achieved against a backdrop of a changing trading environment as the housing market began to adjust from the very strong conditions of the last few years towards a more normal market. This change in market conditions resulted from successive increases in interest rates and increasing concerns expressed by the Governor of the Bank of England regarding the level of consumer debt. As a result, the consumer exercised greater caution, reflected in reduced levels of activity in the housing market which began to take effect in the middle of 2004 and has continued through 2005.

Strategy

Redrow had recognised that the strength displayed in the housing market in the period up to the middle of 2004 was not sustainable and it was inevitable that there would be a period of adjustment as the market returned to more normal levels of activity. The Group was positioned to meet the short term challenges of this adjustment and adopted a strategy that would provide the capability to deliver shareholder value in more normal markets.

The first element in the strategy was focused upon sales. By establishing a strong forward sales position and increasing the number of sales outlets to provide some protection against a period of relative weakness in demand, we achieved an increase in forward sales from an historic norm of approximately 15 weeks to 28 weeks at June 2004. In addition, having delivered an uplift in the number of sales outlets during 2004, we further increased our outlets in the financial year to June 2005 and reached 112 as we entered the new financial year.

The strength of our forward sales position and the increased number of outlets have been fundamental to delivering growth in profit before tax not only for the year to June 2005 but in particular during the second half of the year when the Group increased its profit before tax by 7% to £72.0m (2004: £67.4m) despite the more challenging markets.

As anticipated, the market slowed during the financial year, and we adjusted our sales strategy accordingly. With the support of the Group's strong forward sales position established in previous years, during the last twelve months we focused on the maximisation of sales values and the protection of margins in the face of the softer sales environment. As a consequence of this deliberate differing approach, sales were 9% below the extraordinary level of the previous year. At June 2005, the Group was well placed with forward sales of 2,129 (2004: 2,344), comfortably in excess of our historic norm. This provides some continued protection over the next 12 months, as we anticipate the market will continue to operate below normal levels of activity. In addition, we expect to increase our outlets by 10% over the period up to Spring 2006 to further support our sales performance.

The second element in our strategy has been to position Redrow to have the capability to deliver enhanced volume growth. Over the last few years, we have focused upon the fundamental drivers of land, product and people. These aspects will become increasingly

important as house price inflation relates more closely to growth in earnings and margins return to more sustainable levels. In these circumstances, delivery of value for shareholders will depend more upon the ability to drive volume for top line growth and the management of the cost base to support margins. The strength of the Redrow land bank, the effectiveness of the product range and the contribution and commitment of the Redrow team underpins our ability to achieve these objectives.

Land

The success of a developer is dependent on the quality of its land bank. Redrow continues to take a long term approach to land acquisition as this approach provides the capability to deliver sustainable margins in normal markets and the platform for volume growth.

The current land bank provides for our short term needs. Whilst the Government has indicated a desire to improve the supply of land for new homes, it is still important within the current land bank to hold land owned with planning, representing approximately three years supply. This provides some insulation from the delays experienced from the planning system that currently do not appear to be reducing.

During the financial year, Redrow increased land owned with planning by over 5% to 15,800 plots (2004: 15,000 plots). The quality of the land bank with planning is reflected in the year end plot cost of £29,300 (2004: £27,300). This represents approximately 17% of the current estimated average selling price of the land bank and maintains it as one of the most cost effective land banks in the industry. In addition, it also provides the strength to allow the Group some flexibility within the land market. During the financial year, we exercised some caution in terms of new commitments to land acquisition and this is reflected in the reduction of land controlled under contract to 1,500 plots (2004: 2,400 plots). However, the Redrow land bank as at June 2005 had the capability to provide 100% of projected needs from land owned with planning for the new financial year and 85% of the projected requirements for 2006/07 from the current land bank. Our land bank provides both visibility in terms of growth of outlets for 2005/06 and also the potential for further outlet growth in the medium term.

Forward land plays a key part in our long term approach to land acquisition, providing land at enhanced margins and reducing the need to buy land in the current market. The quality of Redrow's forward land bank is demonstrated by its contribution to the current land bank and its ability to continue to make that contribution into the future. In 2004/05, 13 forward land sites were transferred into the current land bank contributing some 2,200 plots representing 43% of land purchased. This includes Peacock Farm, Bracknell which will provide a significant core development for Redrow Homes (Southern) during the next 10 years. Over the last 3 years, forward land has contributed one third of the land acquired.

In the future, the forward land bank has the potential to continue this contribution. It comprises 22,100 plots (2004: 22,500) of which over one third either has planning or is allocated for residential development in local plans. The forward land bank has a broad geographic spread with 67 different locations across the three Regions. The terms of these options generally allow land to be purchased at a discount to open market value. There are some 750 plots on 4 sites where the land already has a planning consent with a further 7,500 plots on 16 sites allocated in local plans. Finally there are a further 47 locations amounting to 13,850 plots that have a realistic prospect of securing a residential planning consent.

Product

Whilst land provides the key to sustainable margins and the ability to deliver volume growth, our product provides the catalyst to convert that land into profit and cash. The Redrow product portfolio enables us to optimise the margins and return on capital employed inherent in our land bank as it provides a range of product designed to appeal to a broad customer base and the tools to deliver improved control of the cost base.

Redrow has rationalised the product portfolio into three distinct offerings, each appealing to different homebuyers. The Signature Range represents our core product. This is complemented by In the City, Redrow's major apartment schemes, and Debut, the Group's new affordable product. During the year, the first Debut units were legally completed on our development at Rugby

Signature is now the Group's core housing range, combining the former Contemporary, Sapphire and Emerald specifications. These had an average selling price in the last financial year of £166,200 (2004: £155,400) maintaining the average sales price broadly in line with that of new homes in the UK. This range can be adapted in terms of internal specification and external elevations to make it appropriate to the target market and local environment. The range includes 'tool kit' types such as flats over garages, corner turn and bridge units that allow enhanced street scenes and optimisation of coverage. There is also a selection of apartment floor plates that are designed to be efficient in terms of construction and can be configured in blocks to suit each site. The increased use of these house types will provide both improved certainty of cost and delivery of build.

Redrow continues to undertake In the City schemes whilst carefully managing its commitment to this sector of the market. During the year, the Group legally completed 667 In the City units (2004: 460) at an average selling price of £207,400 (2004: £148,700). Legal completions were secured at Altolusso in Cardiff, Jupiter in Birmingham and at Neptune Marina in Ipswich as well as at our higher value development at Odyssey in London Docklands, the impact of which is reflected in the average selling price during the year. The Group is currently progressing Vie in Manchester, Celestia in Cardiff Bay and The Boardwalk at Sovereign Harbour as well as the next phase of Jupiter in Birmingham. Because of the timing of construction, In the City developments are likely to represent a lower proportion of completions in 2006 than in 2005 and will be weighted towards the second half. We continue to procure the construction of these schemes through our central project management team that has developed a skill base to optimise design and specification to deliver building efficiency and control of cost.

Debut by Redrow

It is widely recognised that there is a fundamental inequality between the demand and supply of homes in the market. The Barker Report clearly highlighted the under provision of new homes and the Government has shown an increasing focus on delivering affordable homes for people to buy. Redrow introduced the Debut range to address this key sector of demand in the market largely ignored by the new homes industry. It delivers on aspects of Government policy relating to affordability, use of Modern Methods of Construction and improved sustainability.

Debut homes range from 275 sq. ft. to 700 sq. ft. and on the first development at Rugby, sold for an initial cash consideration ranging from £49,995 up to £109,995. Debut will create communities with a sense of place and neighbourly spirit and delivers quality homes which are contemporary in design to suit the target market. Quality of construction and the environment is a key component within the Debut concept and the use of Modern Methods of Construction, in particular lightweight steel frames produced by Framing Solutions, improves both efficiency and quality. To deliver more sustainable communities, Debut schemes target Eco-Excellent ratings under the BRE classification and the first scheme at Rugby is one of the few developments in the UK to have achieved this demanding target. Debut is targeted at customers who wish to buy and live in their own home and the legal framework prevents purchase by investors. Redrow intends to operate the management of the developments into the future to ensure that the initial quality is maintained.

Importantly, Debut delivers margins broadly in line with the Signature range, thereby delivering appropriate returns for Shareholders. Increased coverage and speed of build mitigate the increased cost associated with the quality of build and the enhanced sustainability. However, Debut will benefit the Group's return on capital employed as it enables us to bring forward the development of some of our land bank as well as securing a faster rate of sales and build to return cash for re-investment more quickly.

The Debut concept commenced development in the middle of 2004 and within 12 months has delivered its first legal completions. It demonstrates Redrow's ability to be imaginative and innovative and to adapt its business to the market. We now have planning permission for nearly 300 Debut units and have submitted planning applications for a further 400 units on five sites. We have been particularly encouraged by the response of the Local Authorities in respect of our first three Debut schemes, each of which secured planning consent unanimously and within the Government's thirteen week target. This new product offers a significant opportunity for incremental volume growth for Redrow and we have set our objective of delivering 2,000 Debut homes per annum within five years.

Homes Operations

Overall, the Homes operations increased legal completions by 2% to 4,372 (2004: 4,284). The average selling price was £172,400 as compared with £154,700 last year. This increase of 11% primarily reflected the product mix with an increased proportion of In the City legal completions, particularly on the higher value Odyssey scheme in London Docklands. Turnover increased by 14% to £753.8m (2004: £662.7m). Operating margins for the year were broadly maintained at 19.6% as compared with 19.8% last year. As we have previously indicated, we anticipate an easing in margins in the current year as the inflationary element within our land bank continues to unwind.

During the last twelve months, we have seen greater pressure on material prices than in recent years, particularly where materials have a high energy or steel content. Our policy of central purchasing and historic partnering arrangements have contained overall increases to a minimum level, with some 90% of materials on the Signature Range being sourced through Group deals. Encouragingly, we have experienced an easing of pressures on labour costs with the changing housing market but inevitably there are 'hot spots' in terms of labour rates where there are high levels of construction activity.

The Northern Region is our most mature area of operation and legally completed 1,832 units (2004: 2,108) in the year to June 2005. Whilst there remain opportunities to increase volumes in this Region, our key areas for volume growth are in the Western and Southern Regions. In the Western Region significant growth has been delivered over the last few years and 1,290 homes (2004: 1,134) were legally completed during the financial year. Redrow Homes (West Country) will make its maiden contribution in the year to June 2006 as it launches its first sites in the second half of this calendar year to increase the capacity for volume growth in this Region. In the Southern Region we delivered 1,250 legal completions (2004: 1,042). We have geographically positioned our operations to be able to take advantage of the growth areas identified by Government and have in addition established Redrow Homes (East Midlands) in Newark to provide a further opportunity for growth. It will launch its first sites in the second half of this calendar year and will also make its first contribution to volumes in the year to June 2006.

We have developed our organisational structure to provide us with the capacity to grow our business organically. We have the potential to drive top line growth and deliver 7,000 legal completions per annum in the medium term from our Signature and In the City products plus the opportunity for additional incremental growth from Debut, without significant further investment in our fixed cost base.

Mixed Use and Regeneration

The mixed use capability within the Group continues to assist in unlocking residential development opportunities. We have continued to progress our mixed use scheme at Buckshaw Village, Chorley where, in addition to the legal completion of 102 residential units during the financial year and securing our second Debut development for 71 units, we made significant progress with Matrix Park, the commercial scheme. During the year, we have disposed of two industrial units totalling 45,500 sq. ft., developed and sold four office units comprising 15,000 sq. ft. and completed the pre-sold investment of the 100,000 sq. ft. facility for Vernon Carus Limited. We have now commenced a further phase of offices on the development. In addition, at Western Approach, Bristol we completed the disposal of the 51,000 sq. ft. warehouse unit as well as the remaining land holdings on the distribution park.

As regards the future, amongst other opportunities, we continue to progress the major mixed use scheme at Bishopton near Glasgow through a development agreement with BAE SYSTEMS plc that has the potential to provide 1,500 residential plots and 100 acres of commercial development. During the last year, the Scottish Executive approved in principle a new motorway access to facilitate the development representing a major milestone in the progress towards securing a planning consent.

In addition, as part of the Group's long term strategy to land acquisition and to provide further opportunities for growth in London and the South East, Redrow Regeneration was established during the first half of the financial year to focus on large scale regeneration opportunities in this area. It has entered into a 50:50 joint venture for the redevelopment of Watford Junction railway station. This is a major transport hub and the scheme has the potential to deliver 2,200 residential units and 150,000 sq. ft. of commercial property as well as significant infrastructure and community benefits.

The strong trading performance from our mixed use developments means that even after taking into account the significant pre-development and option costs on the Watford

Regeneration joint venture, the mixed use and regeneration activities have generated £4.5m of operating profits (2004: £2.7m). The related turnover of £26.6m (2004: £7.2m) benefited the Group's year end cash position. Looking forward to the new financial year, we would expect that further pre-development expenditure within Redrow Regeneration is likely to offset profits from the mixed use elements of our developments.

Framing Solutions

Framing Solutions, our joint venture company that supplies lightweight steel frames to the housebuilding industry, performed in line with our expectations during the last financial year. In terms of financial results, its performance is not significant in a Group context and we expect to see a marginally reduced loss in the new financial year. There is an increasing focus on Modern Methods of Construction that were a feature of the Barker Report and which are an important element in current Government thinking. Lightweight steel frame construction plays an increasingly important role within Redrow, providing a system that offers benefits as regards build speed and quality. This system is now an integral part of the Group's new Debut product and in our success in reaching the final stages of the ODPM and English Partnership Design for Manufacture competition.

Employees and Skills

Redrow remains committed to developing the skills of its employees. During 2004/05 the in-house training@redrow team delivered some 40 different courses and approximately 4,000 equivalent days of training to our employees including formal induction for all new employees. All new Directors promoted from within and recruited externally attend an induction course. We continue to invest in the future by taking on young people as apprentices in a variety of trades and by continuing to develop the skills of our graduate trainees, more of whom have now reached manager level. In 2005 we are introducing a new Assistant Site Manager Development Programme aimed at those with the potential to progress their careers.

The Barker Report challenged the sector as a whole to develop skills within our industry. As part of the Major Home Builder Group, we are taking part in the skills initiative with CITB-ConstructionSkills to pilot an alternative apprenticeship aimed at providing a new route for young people to learn a trade, to develop a new qualification for our site managers and to aim for all persons working on our sites to have CSCS cards by December 2007, leading to a qualified workforce by December 2010.

We also remain committed to providing safe environments on our sites and Redrow is playing an active role in developing the Home Builders Federation Health & Safety Charter. All our operating companies once again received British Safety Council awards and a Silver Award was secured from the Royal Society for the Prevention of Accidents to complement the Bronze Award of last year. Further reductions in our Accident Incidence Rate and the number of injuries reported under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations were achieved. In terms of Health and Safety Executive action, as in the previous year, there was only one prohibition notice issued and no prosecutions were made or improvement notices issued.

Outlook

In the short term we are focused on the maximisation of sales values and protecting our margins, increasing our outlets, maintaining the quality of our land bank, enhancing the effectiveness of our product and controlling cost. Reservations in the first 10 weeks of the new financial year are 10% ahead of the corresponding period last year from just over 10% more outlets, albeit the market has remained competitive and deal led in the seasonally weaker months of July and August. Whilst we anticipate a normal seasonal upturn in activity levels during the Autumn, it is too early to conclude whether the current levels of incentives will continue through the balance of the calendar year. The degree of competitiveness or otherwise within the market will have a significant impact on the outturn for the first half. Looking ahead, consumer confidence will be a key factor in determining the strength of the housing market in 2006.

Redrow has been positioned to manage the period of adjustment to a normal housing market. In the medium term it has opportunities to deliver organic growth through its regional structure, mixed use and regeneration capability, the incremental benefits of Debut and by continuing to build relationships with other stakeholders. These opportunities, together with a high quality land bank, effective product range and strong management team, position Redrow to be capable of delivering shareholder value into the future.

Neil Fitzsimmons
Chief Executive