Chris Carney, Group Finance Director

15,275
Group completions including joint ventures

£4,082.0m
Revenue

£880.2m
Operating profit*

£656.6m
Profit for the year

Focused on driving **strong financial performance**

2018 Group results	UK	Spain	Group
Completions including joint ventures	14,933	342	15,275
Revenue (£m)	3,977.8	104.2	4,082.0
Operating profit* (£m)	851.0	29.2	880.2
Operating profit* margin (%)	21.4	28.0	21.6
Profit before tax and before exceptional items (£m)			856.8
Profit for the year (£m)			656.6
Basic earnings per share (p)			20.1
Adjusted basic earnings per share†† (p)			21.3
Total dividends paid per share (p)			15.3

More information on segmental reporting can be found in Note 5 to the consolidated financial statements on page 140.

Alternative Performance Measures

The Group uses Alternative Performance Measures (APMs) as key financial performance indicators to assess underlying performance of the Group. The APMs used are widely used industry measures, form the measurement basis of the key strategic KPIs (return on net operating assets** and operating profit* margin) and are linked directly to executive remuneration. All references to operating profit* throughout this report meet the definition of an APM.

Definitions of the APMs discussed throughout our Annual Report and Accounts, and a reconciliation to the equivalent statutory measure are detailed in the APM section on pages 178 to 180.

Our Group financial review is presented at Group level, which includes Spain, unless otherwise indicated. A short summary of the Spanish business follows.

Joint ventures are excluded from the operational review and are separated out in the Group financial review of operations, unless stated otherwise.

Group financial review of operations

Income statement

Group revenue increased by 2.9% to £4,082.0 million in 2018 (2017: £3,965.2 million). This increase was driven by increased completions both in the UK and in Spain, with completions (excluding joint ventures) increasing by 3.2% to 15,164 (2017: 14,688). Whilst UK selling prices for both private and affordable completions increased in the year, the average selling price of UK completions remained flat at £263.9k (2017: £264.4k), due to the greater proportion of affordable housing completions in 2018. The average selling price on UK private completions was £301.8k (2017: £296.4k).

The UK land cost per completed unit, at £41.7k, was 8.1% lower than prior year (2017: £45.4k). This reflected the greater proportion of affordable housing in 2018, an increased proportion of completions from strategically sourced land of 58% (2017: 53%), and a lower proportion of completions from the Central London business. Total UK land cost per completion as a percentage of selling price was 15.8% (2017: 17.2%).

Build cost per unit in the UK increased to £147.4k (2017: £143.7k), with the greater level of strategically sourced sites requiring higher infrastructure costs, together with marginal build cost inflation, regional mix and specification improvements. Underlying annual build cost inflation (excluding house type mix impact) was c.3.5% year on year (2017: c.3.5%), largely due to continued pressure on resources to deliver the higher level of homebuilding.

Direct selling expenses per unit decreased marginally to £5.9k (2017: £6.0k), due to sales efficiencies.

Whilst the average UK gross profit per private completion increased in the year, the average UK gross profit per completion was down marginally by 0.6% to £68.9k (2017: £69.3k), reflecting the higher proportion of affordable completions in the year.

Group gross profit of £1,074.5 million (2017: £1,031.8 million) increased by 4.1%, and included a positive contribution of £7.7 million (2017: £17.4 million). Positive contribution represents previously written down inventory allocated to a plot which has subsequently resulted in a gross profit on completion. This can be due to revenue outperformance, cost efficiencies or product mix improvements since the inventory was assessed for its forecast profitability. These amounts are stated before the allocation of overheads, which are excluded from the Group's net realisable value of inventory exercise.

In 2018, only 2% (2017: 5%) of the Group's UK completions were from sites that had been previously impaired. In Spain, 17 plots (2017: 35) were completed that had previously been impaired. The Group anticipates that c.2% of UK 2019 completions will come from sites that have been previously impaired.

During the year, completions from joint ventures were 111 (2017: 154), with new phases of existing sites, at Chobham Manor and Greenwich Millennium Village, starting to deliver completions in the second half of the year. The total order book value of joint ventures as at 31 December 2018 was £22 million (31 December 2017: £4 million), representing 58 homes (31 December 2017: 7), for 2019 completions. Our share of results of joint ventures in the period was a profit of £5.3 million (2017: £7.6 million).

Group operating profit* increased by 4.3% to £880.2 million (2017: £844.1 million), delivering an operating profit* margin of 21.6% (2017: 21.3%). There was a slight reduction in margin from the net impact of market effects on selling and build cost inflation, which was more than offset through increased standardisation and operational efficiency and a small increase in our commercial property sales associated with our mixed use developments. Profit on ordinary activities before net finance costs increased by 17.3% to £828.8 million (2017: £706.5 million). This increase is driven by the increased operating profit* and a reduction in the exceptional charge in 2018.

Net finance costs for the period were £23.4 million (2017: £32.1 million). The reduction is primarily due to the lower notional interest charge of £1.1 million (2017: £5.9 million) on the defined benefit pension scheme deficit. This is a result of the deficit falling from £232.7 million in December 2016 to £63.7 million at December 2017, which drives the following period's notional interest charge. Unwind of the discount on land creditors and other items was £18.5 million (2017: £20.9 million), primarily due to a lower weighted average discount rate applied to land creditors. Interest on overdraft, bank and other loans decreased by £0.8 million year on year.

Profit before tax and exceptional items increased by 5.5% to £856.8 million (2017: £812.0 million). The pre-exceptional tax charge was £162.3 million (2017: £151.7 million) with an underlying tax rate of 18.9% (2017: 18.7%) that largely reflects the statutory tax rate in the UK. This resulted in a profit, before exceptional items, for the year of £694.5 million (2017: £660.3 million), 5.2% up on the prior year due to the improvement in the operational result and lower net finance costs.

Definitions

- * Operating profit is defined as profit on ordinary activities before net finance costs, exceptional items and tax, after share of results of joint ventures.
- ** Return on net operating assets (RONOA) is defined as rolling 12-month operating profit divided by the average of the opening and closing net operating assets, which is defined as net assets less net cash, excluding net taxation balances and accrued dividends.
- *** Return on capital employed is defined as rolling 12-month operating profit divided by average capital employed calculated on a monthly basis over the period.
- **** Operating cash flow is defined as cash generated by operations (which is before taxes paid, interest paid and payments related to exceptional charges).
- † Tangible net assets per share is defined as net assets before any accrued dividends excluding goodwill and intangible assets divided by the number of ordinary shares in issue at the end of the period.
- †† Adjusted basic earnings per share represents earnings attributed to the shareholders of the parent, excluding exceptional items and tax on exceptional items, divided by the weighted average number of shares in issue during the period.
- †* Net operating asset turn is defined as 12-month rolling total revenue divided by the average of opening and closing net operating assets.
- †** WIP turn is defined as total revenue divided by the average of opening and closing work in progress.
- ‡ Net cash / (debt) is defined as total cash less total financing.
- ‡‡ Cash conversion is defined as operating cash flow divided by operating profit on a rolling 12-month basis.
- ‡‡‡ Contribution margin is defined as revenue less direct build costs, less gross land costs and less direct selling expenses. Contribution margin excludes the impact of supplier rebates, land provision utilisation and discounting of deferred land commitments.
- ‡‡‡‡ Adjusted gearing is defined as adjusted net debt divided by net assets. Adjusted net debt is defined as net cash less land creditors.

The Group discloses material, financial impacts arising from events which are one-off or unusual in nature as exceptional items. An exceptional charge of £46.1 million was recognised in the year, which comprises two elements (2017: £130 million in relation to leasehold property matters and doubling ground rents). As previously reported, a charge totalling £30.0 million has been recognised for the removal of Aluminium Composite Material (ACM) cladding at a small number of sites. We have sought professional advice on each building and believe the £30.0 million exceptional provision to be an appropriate estimate of the final outcome. Further, following the landmark legal judgment in October last year, which ruled on the equalisation of guaranteed minimum pensions for men and women in UK defined benefit pension plans, we have reviewed our own position with our pension scheme Trustee. We estimate that the scheme's liabilities will increase by £16.1 million on an accounting basis and recognised this as an exceptional charge. The position will be kept under review, including the amount of the liability, pending any further clarification and Government guidance. An exceptional tax credit of £8.2 million was recognised in respect of the £46.1 million exceptional charge recognised in the year.

Profit on ordinary activities before tax increased by 18.9% to £810.7 million mainly as a result of higher operating profit* and lower exceptional charges (2017: £682.0 million). Profit for the year was £656.6 million, up by 18.2% on 2017 (2017: £555.3 million).

Basic earnings per share was 20.1 pence (2017: 17.0 pence). The adjusted basic earnings per share†† was 21.3 pence (2017: 20.2 pence), up 5.4%.

Balance sheet

Net operating assets** were £2,611.9 million (31 December 2017: £2,654.1 million). This reflects a net investment of £112.5 million (2017: £91.7 million) in the year in land and work in progress (WIP), funded by a £99.5 million increase in land creditors. In addition, there has been a £68.8 million increase in the retirement benefit obligations. Return on net operating assets** increased by 0.9 percentage points to 33.4% (2017: 32.5%), as a result of improved profitability and maintaining balance sheet discipline. Similarly, net operating asset turn†* remained at a strong 1.55 times (2017: 1.53 times). Asset turn has benefitted from the combination of on-going competitive land acquisition terms and strong revenues.

As at 31 December 2018, the UK short term landbank comprised 75,995 plots, with a net book value of £2.5 billion. Short term owned land comprised £2.3 billion (2017: £2.3 billion), representing 53,279 plots (2017: 56,619). The controlled short term landbank represented 22,716 plots (31 December 2017: 18,230). The value of long term owned land increased by 11% to £100 million (2017: £90 million), representing 32,354 plots (2017: 26,836), with a further total controlled strategic pipeline of 95,063 plots (31 December 2017: 90,409). Total potential revenue in the owned and controlled landbank increased to £50 billion in the period (31 December 2017: £47 billion), reflecting the increase in the scale of the strategic land pipeline.

Average WIP per UK outlet at 31 December 2018 increased by 12.5% to £5.4 million (2017: £4.8 million). UK WIP turn†** remained flat at 2.95 times (2017: 2.95 times).

As at the balance sheet date, the Group held certain land and work in progress that had been written down by £83.0 million (31 December 2017: £93.3 million) to a net realisable value of £73.8 million (31 December 2017: £87.7 million). The balance of previously written down land and work in progress in the UK was £46.6 million (31 December 2017: £69.9 million), following the associated write-downs of £38.7 million (31 December 2017: £46.9 million) and principally relates to eight locations.

As at 31 December 2018, in the UK, 86% of the short term owned and controlled landbank was purchased after 2009, 59% of which was sourced through our strategic pipeline. This results in a land cost to average selling price in the short term owned landbank of 15.2% (31 December 2017: 14.8%).

We continue to use land creditors as a way of funding land acquisitions where this results in better return on our investment for longer dated delivery schemes and is value-enhancing for the business. Land creditors increased to £738.6 million (31 December 2017: £639.1 million) and, combined with net cash‡, resulted in a low adjusted gearing‡‡‡ of 2.9% (31 December 2017: 4.1%). Included within the land creditor balance is £102.0 million of UK land overage commitments (31 December 2017: £117.0 million). £359.5 million of the land creditors is expected to be paid within 12 months and £379.1 million thereafter.

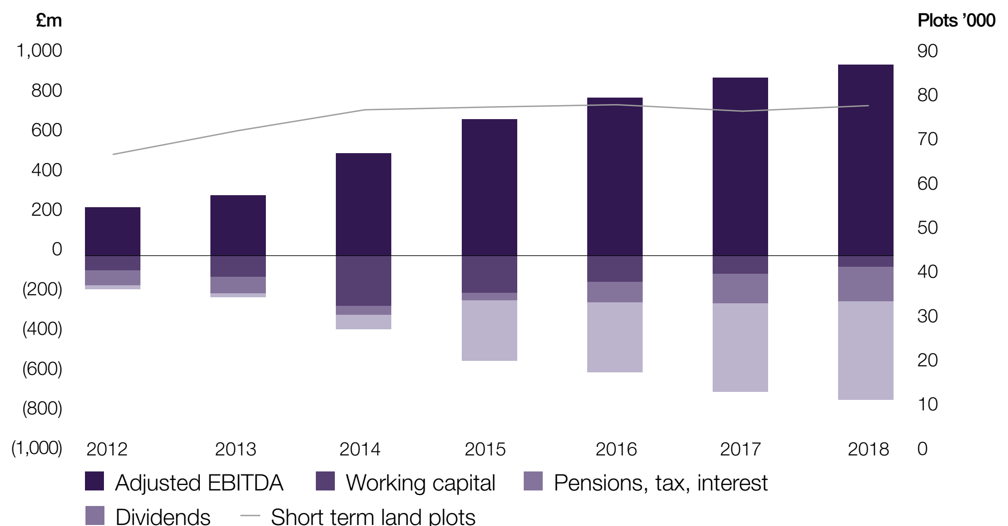
The mortgage debtor balance was £45.3 million at 31 December 2018 (31 December 2017: £63.1 million), with the decrease due to redemption receipts of £21.6 million.

Provisions increased to £170.3 million (31 December 2017: £161.6 million) following the recognition of the £30.0 million exceptional cladding provision in the year, offset by payments amounting to £25.5 million for the settlement with regard to the GRRAS.

Our net deferred tax asset of £40.7 million (31 December 2017: £29.3 million) relates to our pension deficit, employee share schemes and the temporary differences of our Spanish business, including brought forward trading losses.

Net assets at 31 December 2018 increased by 18.8% to £3,726.3 million before dividends paid in the year, and by 2.9% overall year on year to £3,226.8 million (31 December 2017: £3,137.3 million). The net asset increase from 31 December 2017 was driven by strong profitability in the year offset by the £499.5 million dividends paid and the pension actuarial assumptions and asset performance increasing the pension deficit year on year.

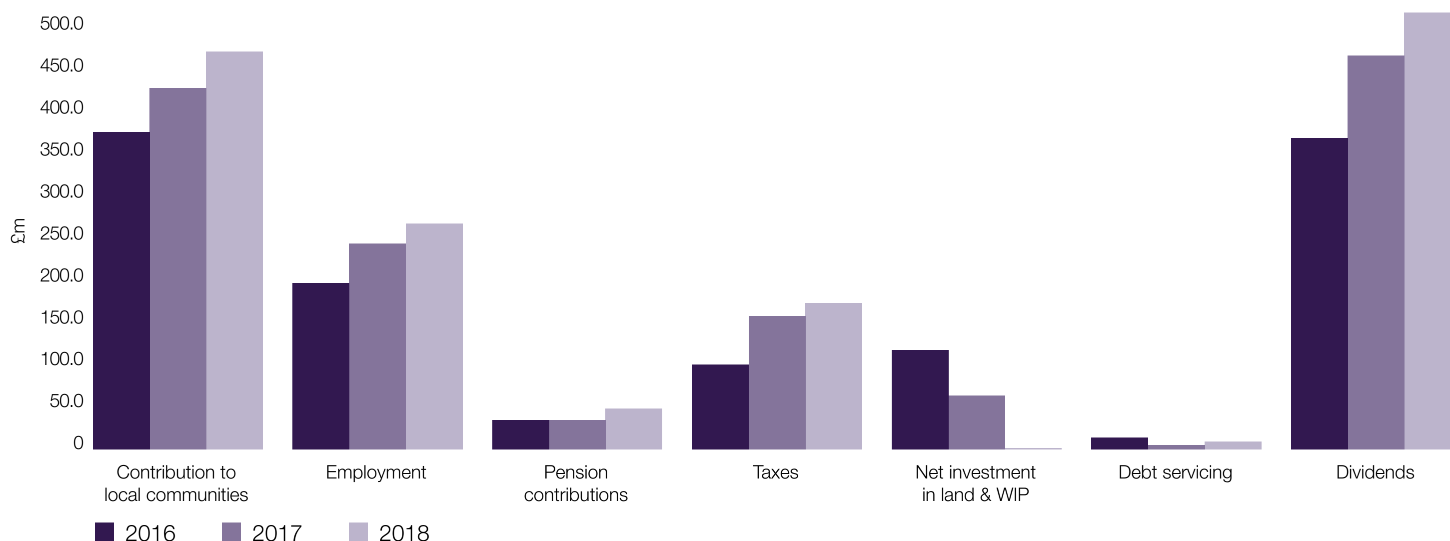
Turning Group profit into cash



Note: Excludes cash payments in respect of exceptional items

Value distributed during 2016-2018 (£m)

The chart demonstrates how value is distributed amongst stakeholders and invested in the business.



Pensions

As previously announced, further to our 31 December 2016 triennial valuation, we agreed a funding plan with the Trustee to December 2020. This included a contribution mechanism, tested quarterly, such that should the Taylor Wimpey Pension Scheme (TWPS) reach a technical provisions surplus, further contributions would be suspended and only recommence if the funding level fell below 96%. The first quarterly test as at 29 March 2018, identified a deficit of £23.0 million which was paid in April 2018. The subsequent quarterly tests to 30 September 2018 resulted in a small deficit. However, as the TWPS remained 99% funded, regular contributions were suspended through the remainder of the year.

The quarterly test for 31 December 2018 showed that the TWPS funding had declined to 94%, following a fall in global equity valuations and other related financial markets in Q4 2018. A result of this latest quarterly test, the Group will recommence regular contributions from January 2019, until the earlier of full funding or Q4 2020. In addition, the Group will continue to cover scheme expenses and make contributions via the Pension Funding Partnership. Total scheme contributions totalled £34.1 million in 2018 (2017: £23.1 million). Payments are expected to increase to £47.1 million per annum from 2019, assuming the TWPS remains less than 100% funded.

As 31 December 2018, the IAS 19 valuation of the scheme remained in surplus at £30.9 million. Due to the rules of the TWPS, this surplus cannot be recovered by the Group and therefore a deficit has been recognised on the balance sheet under IFRIC14. This deficit is equal to the present value of the remaining committed payments under the 2016 triennial valuation. Total retirement benefit obligations of £133.6 million at 31 December 2018 (31 December 2017: £64.8 million) comprise a defined benefit pension liability of £133.0 million (31 December 2017: £63.7 million), with the increase reflecting the new pension funding plan, and a post-retirement healthcare liability of £0.6 million (31 December 2017: £1.1 million).

The Group continues to work closely with the Trustee in managing pension risks, including management of interest rate, inflation and longevity risks. The underlying volatility of the TWPS remains low due to the c.£200 million buy-in completed in 2014 (c.10% of the liabilities), combined with c.90% liability hedging against interest rates and inflation risk exposure on the scheme's long term, 'self-sufficiency' basis.

Cash flow

Net cash‡ increased to £644.1 million at 31 December 2018 from £511.8 million at 31 December 2017. This is despite returning £499.5 million to shareholders by way of dividends in the year (2017: £450.5 million) and paying £25.5 million in relation to the GRRAS set up to assist certain of our customers to move their ground rent escalating terms to less expensive terms. This improvement in net cash‡ is largely as a result of strong performance in underlying trading and maintaining balance sheet discipline.

Net land spend, including the payment of land creditors, was £581.4 million (2017: £645.6 million) and we invested £2,406.6 million in work in progress (2017: £2,386.7 million). In 2018, we paid £8.6 million in interest costs (2017: £5.1 million) and £139.6 million in corporation tax (2017: £126.7 million). £8.3 million was paid for the car fleet and certain office properties capitalised under IFRS 16. £9.9 million was spent during the year to acquire shares for satisfying future share scheme awards (31 December 2017: £13.3 million).

In the 12 months to 31 December 2018 we converted 92.6% of operating profit* into operating cash flow**** (2017: 87.2%).

Financing structure

At 31 December 2018 our committed borrowing facilities were £640 million of which £550 million was undrawn. Average net cash‡ for 2018 was £259.6 million (2017: £186.5 million net cash‡).

During the year, we completed an amendment and extension of the £550 million revolving credit facility to mature in 2023 on improved terms with an option to extend for a further two years. At the start of 2019 we extended the facility by a further year to 2024. This extends the average maturity of the committed borrowing facilities to 5.0 years.

Dividends

As announced in May 2018, subject to shareholder approval each year, the Company will pay an ordinary dividend of approximately 7.5% of Group net assets from 2019, which will be at least £250 million per annum. This is intended to provide a reliable minimum annual return to shareholders throughout the cycle and will be paid equally as a final dividend (in May) and as an interim dividend (in November). This Ordinary Dividend Policy was subject to prudent and comprehensive stress testing against various downside scenarios, which also included a reduction of 20% in average selling prices and a 30% reduction in volumes.

The payment of ordinary dividends will continue to be supplemented by additional significant special dividends at appropriate times in the cycle. Our Special Dividend Policy will pay out to shareholders the free cash generated by the Group after land investment, all working capital, taxation and other cash requirements of the business in executing our strategy in the medium term, and once the Group's ordinary dividends have been met.

Subject to shareholder approval at the AGM scheduled for 25 April 2019, the 2018 final ordinary dividend of 3.80 pence per share will be paid on 17 May 2019 to shareholders on the register at the close of business on 5 April 2019 (2017 final dividend: 2.44 pence per share). In combination with the interim dividend of 2.44 pence per share (2017 interim dividend: 2.30 pence per share) this gives a total ordinary dividend for the year of 6.24 pence (2017 ordinary dividend: 4.74 pence per share).

This dividend will be paid as a cash dividend, and shareholders are once again being offered the opportunity to reinvest all of their ordinary dividend under the Dividend Re-Investment Plan (DRIP), details of which are available from our Registrar and on our website. Elections to join the Plan must reach the Registrar by 25 April 2019 in order to be effective for this dividend. Further details can be found on our website www.taylorwimpey.co.uk/corporate

In addition, on 13 July 2018, we returned £340.0 million to shareholders by way of a special dividend, equating to 10.40 pence per ordinary share. As previously announced in May 2018 we intend to return c.£350 million to shareholders in July 2019, equating to 10.7 pence per ordinary share, subject to shareholder approval at the AGM. This is proposed to be paid on 12 July 2019 as a cash dividend to all shareholders on the register at close of business on 7 June 2019. Shareholders will be offered the opportunity to reinvest all of their 2019 special cash dividend under the DRIP, for which elections to join the Plan must reach the Registrar by 21 June 2019.

The Board continues to keep the mechanics of how the Company will pay special dividends, including the merits of undertaking a share buyback at some point in the future should it become appropriate to do so, under regular review.

Spain

The Spanish housing market remained positive throughout 2018. We completed 342 homes in 2018 (2017: 301) at an average selling price of €344k (2017: €352k). The total order book as at 31 December 2018 was 284 homes (31 December 2017: 329 homes).

The Spanish business delivered an improved operating profit* of £29.2 million for 2018 (2017: £26.8 million) and an operating profit* margin of 28.0% (2017: 28.5%). Looking ahead, we believe the business is well positioned for further growth in 2019.

Going concern

The Directors remain of the view that the Group's financing arrangements and balance sheet strength provide both the necessary facilities and covenant headroom to enable the Group to conduct its business for at least the next 12 months. Accordingly, the consolidated financial statements are prepared on a going concern basis.

Accounting standards

During the period, the Group adopted three new accounting standards, being IFRS 9 – 'Financial Instruments'; IFRS 15 – 'Revenue from Contracts with Customers'; and IFRS 16 – 'Leases'. Although there is limited impact to the financial statements from their adoption, IFRS 16 has the greatest impact, with the recognition of £27.1 million of leased cars, office properties and other smaller items as assets at 31 December 2018, with a corresponding lease liability. In addition, with the adoption of IFRS 16, the cash spend on cars and leased property has moved from Net Cash from Operating Activities to Financing Activities (see page 134). The 2017 financial statements have been restated for IFRS 9 and IFRS 15. They have not been restated for IFRS 16 as it has been applied from 1 January 2018 using the 'modified retrospective' approach, as outlined in the standard.

Chris Carney
Group Finance Director

For our Viability statement see page 51

Approval of the Strategic Report

This Strategic Report was approved by the Board of Directors and signed on its behalf by

Pete Redfern
Chief Executive