Taylor Wimpey plc

Trading Update

Monday 11th January 2016

Pete Redfern, Chief Executive

Good morning everybody and thanks for joining us. I will give you some brief highlights from the statement and 2015 and then look ahead to 2016, and then we'll open up for questions. Ryan is heading towards us in a car at the moment, so he's on the line listening into the call and hopefully will be able to answer questions later on, but may find it difficult in the first few minutes.

Against a very strong market backdrop in 2015, with a housing market that performed better than we expected in the first half with the General Election, and then strengthened particularly in volume of demand terms in the second half of the year, with build costs under pressure in the earlier part of the year, but that softening towards the end of the year, particularly seeing labour, which had been under a lot of pressure early on in the year, starting to get into a more steady state sort of level, and with a land market which was benign, the business has delivered very strong results.

We set out I think nearly two years ago our targets for the three years, of which 2015 is the first, and we expect to meet or exceed all of those targets in the 2015 year. So it's particularly pleasing to achieve the 20% margin, which is a clear headline level, and to beat our 20% return on capital target with a level in 2015 of over 25% return on net assets. And we expect to deliver a cash conversion in the range of 64% to 66% with the fine tuning of our final accounts being needed to see whether we get to the 65% level for 2015 or not. We will be there or thereabouts.

It was clearly a year in which politics played a significant part in the industry, with a very benign backdrop, with the support from Help to Buy announced the previous year impacting on the whole of 2015. We saw new announcements with starter homes particularly in the second half of the year figuring high in the headlights. It's very difficult, as we say in the statement, for us to really give you a clear sense of the impact of the Starter Homes initiative because there is some real detail missing from that process. And it's not the usual detail isn't there so we can't quite call it; there's some really important detail that makes it very hard for us to say whether this is a positive policy that we can totally get behind or whether it has some real challenges, particularly for the affordable housing sector.

The planning backdrop to our environment has been easier but it still remains challenging. You may have seen my comments recently about government's overall targets. Planning has improved, and we applaud everything the government has done, but at the same time the act of getting outlets finally open remains difficult and remains particularly constrained by resources in local authorities.

As we look ahead to 2016 we expect another good year. We expect to deliver increased volume. We expect improvements in our margin and in our particularly strong order book at the end of 2015; we have margin improvements over the 2015 level. And again we expect another increase in average selling price over and above inflation, following the 8% increase in average selling price, 9% on private, that we saw in 2015.

We're also particularly pleased with the cash number at the end of 2015 which leaves us in a strong place, both to continue to invest sensibly in land, but particularly to deliver on the cash payments to the shareholders that we're committed to for 2016, and potentially to build further on them.

Can we open up for questions please?

Q&A session

Question 1

Aynsley Lammin, Canaccord Genuity Inc

Just firstly on the volume growth expectations for 2016, obviously you commented you expect more volume growth; should we expect that to be in line for what you've just delivered for 2015?

And then just on house price inflation, what was the mix versus underlying house price inflation for 2015? And again what trends are you seeing there?

Pete Redfern

On volume growth we expect it to be slightly below 2015. Same sort of order of magnitude but maybe a percent or so below.

On house price inflation, if we focus particularly on the private price, so where we've seen a 9% increase overall, around 5% to 5.5% has been actual house price inflation, which approximates to the level we think we see in January to December, with the balance being mix. And as ever it's really hard to split that mix between the specification quality of the individual units and the quality of the locations that we're operating on.

Aynsley Lammin

And would you expect to see much mix improvement in 2016?

Pete Redfern

We continue to expect mix improvements. As I say, we expect further selling price inflation over and above any market inflation. Will it be as high as the 8% overall for this year, with a mix element of about 3.5% to 4%? I think on the mix side at least that level. Obviously hard to call, but house price inflation level may be a little bit lower. But overall I think something in the order of 8% overall inflation, if we only see 2% to 3% house price inflation from here.

<u>Question 2</u>

Will Jones, Redburn

Three if I could please. First, just coming back on ASP more for the year finished, just to double check, slightly picky really but I think it came in at the lower end of the 8% to 9% range you talked about for the year. Was there anything there regarding timing issues on any sites just to be aware of for the year finished?

Second, I guess just on margin, really more of a general question: has anything changed in your thinking on margin development since you spoke a couple of months ago in mid-November, or is it as you were on expectations there?

And I guess just in terms of cash flow conversion, anything that can help us with the moving parts. Is it fair to say that relative to profits the land and work in progress requirements on the business from here are easing and therefore we should expect to see a useful step up in the cash flow conversion? Any detail on land and WIP expectations would be great, thanks.

Pete Redfern

I should definitely let Ryan come back on the cash flow movements.

On the selling price movements, clearly the difference between 8% and 9%, we were 9% on private, when we tend to talk about selling price inflation we're generally talking about private, so I think it's more that than anything else. There was one block which we half-legalled in Central London, but I don't think you would have noticed the numbers on the dials to be honest in terms of impact on that movement.

Margin development, very much as we were. We don't expect to be delivering in 2016 and 2017 the same scale of year-on-year movement that we've been able to deliver over the last two to three years; clearly that gets increasingly difficult. I think at this point, whereas in the past we've guided you to 100 to 200 basis points at the beginning of the year as being a reasonable expectation, at this point that guidance is more 50 to 100 basis points, with a balance, depending on what house price inflation we see, particularly in the first five months of the year; which is what, with the length of order book we've got, tends to impact on this year's results.

But as I say, on the cash flow, I could answer the question, but I think I should let Ryan come back on that and any other cash questions when he joins us.

Ryan Mangold

On the cash flow conversion yes, we've made good progress on the medium-term targets of 65% over the three-year period. The balance sheet is at optimal scale. We've got probably a bit of growth on the outlets in terms of delivery of the volumes coming, but that's not a significant consumption of capital. We've gone through the relatively significant step-up in London in terms of the expansion in the Central London market, but we've got a little bit to go there in terms of working capital demand. But overall from a land perspective fairly balanced with a little bit of consumption on work in progress, but not as great.

Will Jones

Just to come back on the margin comment, Pete, the 50 to 100 basis points: did you say that was before you might see prices nudge up 2% to 3% or would that be including that for you?

Pete Redfern

No, I think that would assume about 2% inflation. There’s a bit of upside beyond that if prices move more than that, particularly if they move from that early.

Will Jones

Got you, thank you.

Question 3

Gregor Kuglitsch, UBS

I’ve got two questions. On landbank first, if I look correctly I think your landbank was broadly stable in the year. Could you maybe comment in the end for 2015 how that compares to your expectations? It looks to me as if you perhaps bought a little bit less. Perhaps it’s a timing question. And then if you could give us an outlook as we go into 2016 what your plans are with regards the short-term landbank?

The second question is, could you give us an update on your London business, how much broadly, I guess, from a revenue, profit or capital employed – I suspect those metrics are quite similar – where we are in that ramp up and when you expect it to reach full maturity?

Pete Redfern

If you look at the landbank, it’s slightly up year-on-year in the short-term landbank, with about half of the additions coming from the strategic landbank. That’s not far off what we expected. We’ve been talking about like-for-like replacement for the last 15 months or so, so it’s about in line with that. As we’ve talked about before we would be comfortable if the current level of 76,000 ended up anywhere between about 75,000 and about 78,000.

So if you focus too hard on one year-end target for that then you tend to take the wrong decisions. It could be a little bit higher in 2016, the land market remains benign so I wouldn't be surprised if it is, but we're not driving it to be that way, it just depends on the quality of opportunities that come through and the geographic spread of those opportunities. Obviously south east volume of plot numbers tend to be lower for the sites that seem appropriate, whereas you can actually make a big impact on landbank numbers if you buy an awful lot of plots in Wales and the north of England. So our buying has continued to be biased towards the southern half of the country so that maybe affects the numbers a little bit. But overall, very much in the sweet spot of what we think are the right level to fit at, and sticking to our principles of investing in the right quality of sites rather than chasing a number.

In terms of the London business, we tend to talk about the central London business specifically, and when we go through things at the Prelims and potentially we will have a Capital Markets' day in the later Spring and we can go through it in a little bit more detail. But the central London business has continued to grow. We delivered total completions from that business of about just over 300 units, so it's material when you look at the average selling price but it's not dominant in terms of its impact on the business. So it's growing very much in line with the plans that we set out where we did a full central London update going back 12 months or so.

<u>Question 4</u>

Andy Murphy, Bank of America Merrill Lynch

Just a quick one. Your reservation rate on the private's up from 0.64 to 0.73 looks like quite an impressive performance. I was just wondering whether that sort of level is sustainable and how you were dealing with that kind of pick up in reservations on the ground, whether you're finding it harder to build at a rate that is sufficient to maintain that kind of growth rate?

Pete Redfern

Yeah, it is a high reservation rate and it is above the level we'd have anticipated coming into the year, and if you roll the clock back three years or so and say what do we think is an underlying normal level of sales rate for us with this strategy and this cycle, it is above that, it's certainly at the upper end of the range. It seems to come from having a strong market and having the right sites and the right products in that market, and so we're very pleased with how that's happened. We certainly haven't had to force it, we've had very few sales and marketing led initiatives and no pricing initiatives through the course of the year, certainly at Group level but also actually at site level as well.

It is sometimes hard to build to keep up with that, and we're not always trying to build to keep up with that because we don't believe it can be done sensibly and properly, although where we have large land assets then we are able to step up production where it makes sense in the balance between margin and return on capital. That's probably the toughest part of a growing industry. But such is life, and as we go through 2016 we don't expect to see that order book in terms of length grow any further. It may come back a bit, and certainly it gives us a strong position to manage price and to manage were the market to be a bit softer. A number of the journalists this morning ask about are we worried about interest rate movements. We're certainly not worried about the kind of interest movements we'd expect to see in 2016, but that long order book does give you a chance to manage through them if you get a bit of softness when movements actually happen.

Andy Murphy

Just in terms of that reservation rate, can you just give us a bit of a flavour for what you're seeing across the UK in terms of materials, but more importantly the direction and scale of labour inflation please?

Pete Redfern

We flagged at the beginning of 2015 we expected to see overall build cost inflation of about 5%. I think when we flagged it we thought the risk to that was on the upside. As we said to you during the course of the year the position sort of improved slightly and softened, and we thought 5% was a very, very solid guidance. I'd say actually when we go back and analyse historically the data for 2015 it's actually slightly below that, although very marginally, 4.5% or whatever. As we look at 2016 the labour component of that has definitely softened, the industry has generally adapted to the change in the scale, and although further growth all comes with some pressure, the scale of the bottlenecks we see in labour and saw previously in materials are definitely less. So looking ahead think 5% is the top end, sort of 3% is the probably the bottom end, somewhere in the 3-4% range overall, with most of that still coming from labour. And materials very flat, some coming down; net net you might even see a net reduction in materials. 3-4% overall with the majority of it coming from labour.

<u>Question 5</u>

Kevin Cammack, Cenkos Securities

Just one question really, very much focused on your comments on the starter homes' initiative. Quite some contrast, I think, in Persimmon the other day were saying obviously there's wrinkles to iron out, but effectively they were peering through that and saying almost whatever happens it’s going to be positive to them and frankly the private developers in general. Whereas I don't know, maybe I interpreted your remarks to be slightly more cautious than that. I'm just really trying to ask, I suppose, is there one or two things in particular that you're aware of are proving sticking points which arguably could be more negative, or is it just a case of you being somewhat more conservative than one of your other peers?

Pete Redfern

You know, Kevin, that I'll tell it you as a I see it, and if it were just niggly bits around we're not quite sure how it will work then I'd put it that way. We start from a place where we want the policy to work, and Government has been supportive of our industry and of first time buyers particularly over the last two or three years and so we want to work with them to help make it work. So there's no kind of we've got our hands in our pockets waiting to see what they do, we'd like to make it work and we'd like to work with them on it.

There are a couple of specific things that particularly concern me, and they're not about the impact on TW or the impact on new house builders, they're more about the scale at which the policy can work and the pace which it works, and particularly the impact on the affordable housing sector as well. Obviously I can't comment on the detail of discussions behind the scenes, it's not that I am desperately close to that but I do have some knowledge. But if you look at how a 20% pricing discount mechanism will actually be set in practice and how you manage that, and if you look at how you make sure that local authorities support the scheme and are engaged in producing it and don't feel they've lost out more from affordable housing than they've gained from starter homes over which they have less control, those are patently from the outside two big question marks to which there is not yet an answer. It's not that I don't think the policy can work, I think it can, but I think depending on what decisions get taken over the next few weeks, do we end up with a policy that you can really get behind and get engaged with, and a policy that it's quite hard to make it work in practice.

Kevin Cammack

Theoretically, if this sort of were to run along another, say, three months before any resolution be it good or bad was made, would it impact industry volumes at all do you think?

Pete Redfern

I don't think it will impact whilst it's in this sort of limbo. I think what it does do is put the volume targets that the government has set for it under ever increasing pressure because they've set a deadline date and if the starting date goes forward, and we're used to that happening day-by-day on the sites we operate in, that we've got a date when we want to get completions and yet the point at which we're actually able to start on site gets ever under pressure, and so that then puts government under more pressure. And I think if they're saying yes it's a wonderful policy but not actually saying but we need the details so we can actually work out how to resource it, how to structure it, how we're actually going to sell those homes, do we need any additional sales skills, all those sorts of things, then they all put that sort of target. So it's the success of the policy rather than its impact on us.

It's not that we're sitting there thinking either we have a huge risk or a huge opportunity, we just don't quite know yet.

But if government take longer and longer to come to conclusions on those issues, and you're still expected to deliver the same volume in an ever shortening period of time, that becomes increasingly difficult.

Kevin Cammack

I'm sorry to labour the point, but just in terms of your sort of larger strategic sites coming through, do they sort of get put on hold as a result of this or not?

Peter Redfern

We haven't put any sites on hold, certainly we haven't put any planning processes on sites on hold at this point. There is always a possibility you can come back and re-plan a site, because we don't quite know whether the policy is something that we can wholly get behind, or something about which we have concerns, we don't feel that the risk is significant enough to hold back on planning processes, on either large or small sites.

But where we are looking at significant site new investments that have a heavy weighting towards first time buyer homes, then we are looking at them, thinking we're now getting into an area where we're not quite as sure as we were that we've got all the information we need to take a decision. And of course, with a strong land bank, that's a decision that we can take, but if we were shorter on land it would be a lot tougher. But it is getting to that point where actually you start to think actually, do I really want to put this money in until I really know what this policy is going to say and what impact it will have on affordable housing levels and first time buyer homes on that particular development.

<u>Question 6</u>

Peter Tester, One Investments

Just a couple of questions please. One was on your margin points and the other was on the units opened.

If you look at the margin points, you highlight on a same 2% inflation environment a slightly less optimistic view on margins this year going in than at the start of the last couple of years. And just harking back, you made some comments last year that the better market in H2 would largely be reflected in profitability more in 2016 than in 2015. And you've talked today about build costs, inflation coming down, and still the strategic land mix is strong, London should be making more of an impact on your business in 2016 and 2015. So with those sorts of things in mind, can you give some sort of sense as to what's pushing back on the margins at this stage versus the previous periods around this time of the year?

Peter Redfern

It's probably a question that we can answer most effectively and most fully with the Prelims, Peter, because we'll go through, as we have over the past couple of years, and show you the movements on the margin in the past, and that gives us the backdrops talk about the forecast. But it's not that there's something that's pushing back on that specifically, it's simply the dynamic over the last three years, that we have had stronger house price inflation than the 2% that I've just talked about.

We've had a bigger new impact from increasing strategic land and the working out of old pre-downturn land. All of those impacts are still there and all of them are positive, but if you look at the level of margin increase we've had in 2015, and particularly in 2014, then that level of increase is always going to be difficult to sustain. But we still expect, and I wouldn't necessarily see it as less optimistic, we still expect a higher margin in 2016 than we got in 2015 and a new record, it's just the rate of increase will start to taper off as those impacts get balanced up, because they're already in the base number.

Peter Tester

Right, and if you think about the better market in the second half of last year earning itself through and the London mix earning itself through as, say, positives versus coming into the 2015 year, can you give some thoughts as to those relative impacts?

Peter Redfern

Yes, they will have an impact, but sat here today I'm not going to give you the breakdown of all that balance, because we need to work through it in some detail ourselves to be able to give you that kind of reconciliation. At this point of the year it's a bit too early to do that.

We did see more positive margins in the order book at the end of 2015 than we saw during the year and at the end of 2014, but there's a whole variety of different impacts and old sites drop out and new sites come in, so we need to work through all of those. And as I say, we will break it down, as we have done in the past, at the Prelims, but it's not something we've got down in detail for you today.

Peter Tester

Right, but just conceptually, exiting 2014, the market flattened off, exiting 2015, the market had picked up again and London comes through, those should be net positive?

Peter Redfern

Yes, that's true.

Peter Tester

Okay, fine.

And the other question was just on unit pull through. You made the point earlier that you don't necessarily build to the pace at which you sell and units come through as they're supposed to and not on a projected basis.

Can you give some views on how you see units coming through during 2016 based upon your discussions at the local authority level now and based upon your planning? Would you expect units to pick up through H1?

Peter Redfern

A lot of it depends on the sales rate rather than just the planning position. I mean our delivery of new outlets in 2015 was pretty much bang on what we'd planned it to be at the beginning of the year, but with the faster sales rates, you obviously close more, so that compresses the outlet number. If we see sales rates at the same level that will keep that outlet number low with the balance being in a high order book. If the sales rate slackens off a bit, the outlet number will go up, but the order book won't be quite so strong.

Overall, we feel the balance of the two is in a pretty healthy place. We could end the year anywhere between 300 outlets and 325, depending on the sales rate mix and that outlet opening mix.

Peter Tester

Yeah, sure, I guess I was thinking for the first half of the year, where you're largely pre-sold, the extent to which you feel that it's based on local authority level, you see the outlets coming through to pull that through during the first part of the year?

Peter Redfern

Yeah, but the sales rate will still impact, because although we won't be selling plots for the first half of the year, we'll be selling the plots for the second half of the year. I still think it will probably come up a little, but it's very hard to call. And to be honest, we are fairly indifferent about balance, between whether the sales sit as reservations in the order book or whether they sit as open outlets that might otherwise have been sold out.

Peter Tester

Sure. Okay, fine, thanks very much.

Peter Redfern

Okay, if we wrap up there.

Thank you very much for all of your questions and your time this morning. Clearly, we're very pleased with the 2015 performance, but as ever, we're very much focused already on 2016 and adding to the performance that we've seen and continuing to beat those three-year targets that we've set.

Thank you very much.