MEARS

GROUP PLC

Unaudited Interim Report 2003

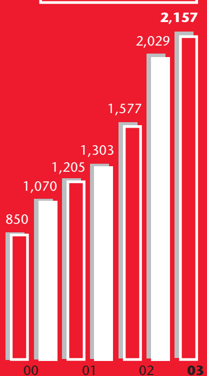
National provider of facilities and support services

Contents

Financial Highlights

Profit before tax

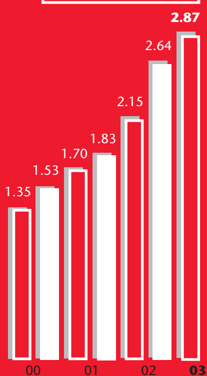
up 37%



profit before tax £'000

Earnings per share

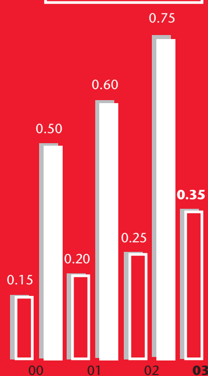
up 33%



earnings per share p
– normalised pre amortisation

Dividend per share

up 40%



dividend per share p

first half year second half year

Chairman's Statement

I am pleased to announce record results for the six months ended 30 June 2003. Profit before tax and the amortisation of goodwill increased by 40.0% to £2.31m (2002: £1.65m) on turnover up by 30.5% to £49.65m (2002: £38.06m). Profits have shown an annual compound growth rate of 42% since Mears was listed on the Alternative Investment Market in October 1996.

Earnings before amortisation of goodwill increased by 33.5% to 2.87p per share (2002: 2.15p).

Net profit margins increased again in the period to 4.3% up from 4.1% in the comparable period last year.

Excellent cash management again resulted in the generation of £1.70m of positive cash inflow from operating activities in the period.

The Group had no borrowings and cash in the bank of £6.41m at the end of June 2003.

The Board has declared an interim dividend of 0.35p per share (2002: 0.25p), an increase of 40%, payable on 10 November 2003 to shareholders on the register on 24 October 2003.

Acquisitions

I am also pleased to confirm the recent acquisition of SCION Group Limited (Scion) a multi-disciplined facility services group. Scion provides a range of facility services including grounds maintenance, building maintenance, mechanical and electrical services and facility and estate management to a wide range of customers in the public and private sectors. Mears has been in dialogue with Scion over many years and the industry trends of large public and private sector customers seeking to work with larger service providers, has encouraged Scion to find a partner who shared their views of customer focussed facility service partnership. I welcome Tony Southon and his team into the Group.

Full details of the Scion and other acquisitions are contained in the Financial review.

Trading review

Mears has continued its excellent progress in the period and has been awarded a number of new contracts, mostly on a long-term partnership basis. Contracts have been awarded with Tristar Homes, Stockport Metropolitan Council, Broomleigh Housing Association and Northampton Borough Council. The record order book of £400m stretches as far ahead as 2012.

It should be remembered that Mears provides 'essential support services' and is not subject in its core business to any aspect of discretionary spending from its customers.

Operations

Mears operates principally in five sectors.

Public sector services

By far the largest part of Mears, representing 60% of Group turnover, is the provision of a range of maintenance services to the social housing and central Government sectors. The Government has made a commitment to bring all council housing up to a decent standard by 2010. This is driven by the Decent Homes Standard initiative and will make a significant impact on the estimated £19 billion backlog of

Chairman's Statement (continued)

repair and improvement work required to local authority housing in England and Wales. Mears has been successful in the award of long-term partnering contracts to ensure that social housing providers comply with that standard. The contracts are typically for five years or longer and contain annual benchmarked spending requirements. Mears provides a mixture of both rapid response and planned maintenance, to deliver a total quality outsourced building maintenance service. The partnership ethos embraces the tenant, client, employee and every stakeholder in that process. As the contracts near the end of their term the Group has demonstrated an excellent record of contract renewal. The division has enjoyed buoyant trading conditions and continues to be recognised as a preferred supplier.

Mechanical and electrical services
This business provides mechanical and electrical services in the commercial, housing, education and healthcare sectors operating as Haydon Mechanical & Electrical. Haydon has performed well in the period. The business has expanded into new sectors and new geographical areas and is looking to strengthen its presence by the acquisition of a maintenance services business that will increase greatly the range and scope of services provided. The London based housing division has performed satisfactorily and is well placed to maximise other opportunities should the anticipated downturn in the housing market occur.

Vehicle collection and delivery
United Fleet Distribution (UFD) provides a collection and delivery service to large commercial customers who typically own a large vehicle fleet. UFD is the market leader in the single vehicle collection sector and holds some of the largest contracts for these services in the UK operating from a number of locations. The business performed well in the period.

Facility management (FM)
Mears FM provides a total building management service to its customers managing a large number of individual services. Since its formation in September 2001, the business has performed excellently and expanded significantly.

The recent award by Northampton Borough Council of a seven year partnership contract for the management of all white collar building management services has expanded the range of services offered by Mears FM and the Group in the public sector.

I look forward to bringing exciting news of this business in the future.

Painting and decorating services
In December 2002 the Group acquired M & T Group Limited with the aim of building a national painting and decorating services business. I am pleased with the performance of this business which is well ahead of our expectations. Mears has subsequently acquired two other small regional painting businesses and negotiations are at an advanced stage to acquire further businesses to increase its regional presence.

Strategy and expansion

Throughout Mears we operate a reward based culture with bonus and incentive arrangements in place at all levels. Of equal importance is the ethos of partnership, both within the Group and towards its customers. We are seen as an employer who is admired internally and externally, and I have been impressed by the number of our people who want to be a Mears employee for a very long time. In an age where loyalty is almost a forgotten word we have a management team who picks up every new challenge, embracing change, welcoming new colleagues into the Group and seeking to build long-term futures for all. Record profits reflect this approach with employees at all levels committed to a common ethos.

We are looking to embrace an even wider corporate social responsibility ethos by our commitment to 'working in the community for the community' and I am delighted to confirm that all our recent initiatives are working well. The paired reading scheme where employees of the Group visit a local school and are paired with a schoolchild, spending an hour a week with the child, has been a big success. Three employees have recently completed a sponsored walk in Iceland on behalf of a local based national charity. In addition we continue to support a large number of community based schemes with the emphasis on improving the local community for all.

It is, I believe, these types of initiatives which will continue to set Mears apart from its competitors. Success can and will be judged in different ways and the Group has been tremendously successful to date and can continue to improve with the commitment of all. I commend this commitment and support of staff at all levels.

Mears has a proven robust and sustainable business model upon which to expand both the size of the Group and the range of services provided. The demand for our services has never been stronger.

Our future earnings are highly visible whilst the excellent generation of cash from our operations allows us to seek out earnings enhancing acquisition opportunities. The record order book demonstrates a commitment to long-term partnership opportunities in stable market sectors.

Again my sincere thanks to everyone involved within the business, there are too many individuals to name here but they are all aware of my tremendous gratitude. I also extend a welcome to all the teams who have recently and will shortly be joining the Group.

I look forward to bringing further news of developments of Mears in the future.

Bob Holt
Chairman
2 September 2003

Financial Review

I am delighted to report another six months of significant progress across all aspects of the Group. Turnover in the six months to 30 June 2003 was up by 30.5% at just under £50m. This increase came primarily from the recent awards under the Government's Best Value initiative and new contract awards. Contract extensions under Partnering arrangements at Basildon, Croydon and Wycombe have further strengthened the quality of the order book which now stands at £400m of which £310m is at guaranteed net margins.

The Group's operating margin before goodwill amortisation rose to 4.5% up from 4.3% in the first half of 2002. Of particular note, however, is the growth in the core maintenance net margin which saw an increase from 3.5% up to 4.3%. This again highlights the value of having guaranteed margin business. The reduction in the vehicle collection and delivery net margin from 6.9% to 5.0% has been well signalled, and reflects in part a change in level of service required by the vehicle industry.

The increased interest credit reflects the continued emphasis on cash collection which has been a foundation of the Group's success. The cash inflow in the six months amounted to £0.84m (£1.56m in 2002). This is against a background of continued investment in management and the IT infrastructure to support the Group's development and after £0.48m was paid as a further instalment on the deferred consideration payable following the acquisition of the M & T Group in December 2002. Overall at 30 June 2003 our net funds position stood at £6.41m (2002: £4.17m).

Earnings per share before goodwill amortisation was up 33.5% at 2.87p (2002: 2.15p). The Group has been on a full tax charge for some time. Basic earnings per share at 2.61p (2002: 2.02p) represents an increase of 29.2%.

The Group has been active on the acquisitions front and the following transactions have taken place since June 2003.

Scion Group Limited

A cash payment of £750,000 was made on 22 August 2003 to acquire 100% of the share capital of this business. A further £250,000 is payable upon the final receipt of certain monies due to the business. A two year earn-out arrangement based on profitability has been established which caps the total consideration at £6m. This will be payable after the results for the year ending December 2005. In the accounts to 31 March 2003, Scion Group Limited showed a profit before tax of £0.07m on turnover of £27.56m and had net assets of £0.70m which include debt of £3.98m.

Grogan Decorators Limited

This Company was formed on 28 July 2003 to acquire certain assets of a long standing painting business based in Halifax. A payment of £73,000 was made which included goodwill of £55,000. This is the first of what is scheduled to be a number of small regional painting and decorating services acquisitions to create a national network.

Sheffield Décor Services Limited

On 19 August 2003 Mears acquired 100% of the issued share capital of a painting and decorating business for a consideration of

£86,030. In addition an earn-out arrangement exists based on profits in the three years after completion with a total consideration capped at £220,000.

At 30 June 2003 the net assets of the Group stood at £10.86m up from £8.57m at 30 June 2002. The Group is currently making significant investment in its infrastructure to prepare a sound footing for the future growth of the Group. Key appointments are being made across all the disciplines in both operational and administrative functions.

David J Robertson
Finance Director
2 September 2003

"Order book stands at £400m of which £310m is at guaranteed net margins"

Unaudited Interim Profit & Loss Account

for the six months ended 30 June 2003

	Note	**6 months to 30 June 2003 £'000**	6 months to 30 June 2002 £'000	Year to 31 December 2002 £'000
Turnover	1	**49,652**	38,061	78,834
Cost of sales		**(37,166)**	(28,478)	(58,759)
Gross profit		**12,486**	9,583	20,075
Administrative expenses		**(10,396)**	(8,024)	(16,563)
Operating profit		**2,090**	1,559	3,512
Share of operating profit in associate		**3**	1	8
		2,093	1,560	3,520
Net interest received		**64**	17	86
Profit on ordinary activities before taxation		**2,157**	1,577	3,606
Tax on profit on ordinary activities	2	**(690)**	(473)	(1,112)
Profit on ordinary activities after taxation		**1,467**	1,104	2,494
Equity minority interests		**10**	23	35
Profit for the financial period		**1,477**	1,127	2,529
Dividends	3	**(200)**	(141)	(565)
Profit retained		**1,277**	986	1,964
Earnings per share	4			
Basic		**2.61p**	2.02p	4.51p
Basic pre amortisation		**2.87p**	2.15p	4.79p
Diluted earnings per share		**2.52p**	1.95p	4.36p

Unaudited Consolidated Balance Sheet

as at 30 June 2003

	Note	**As at 30 June 2003 £'000**	As at 30 June 2002 £'000	As at 31 December 2002 £'000
Fixed assets				
Intangible assets		**5,285**	2,518	5,433
Tangible assets		**1,705**	1,547	1,641
Investment in associate		**40**	31	37
Investments		**62**	56	62
		7,092	4,152	7,173
Current assets				
Stocks		**1,828**	1,241	1,266
Debtors		**16,627**	15,780	15,920
Cash at bank and in hand		**6,410**	4,168	5,566
		24,865	21,189	22,752
Creditors: amounts falling due within one year		**(19,362)**	(16,774)	(18,129)
Net current assets		**5,503**	4,415	4,623
Total assets less current liabilities		**12,595**	8,567	11,796
Provisions for liabilities and charges		**(1,735)**	—	(2,260)
		10,860	8,567	9,536
Capital and reserves				
Called up share capital		**569**	565	565
Share premium account		**3,023**	2,967	2,970
Profit and loss account		**7,301**	5,046	6,024
Equity shareholders' funds	8	**10,893**	8,578	9,559
Equity minority interests		**(33)**	(11)	(23)
		10,860	8,567	9,536

Unaudited Consolidated Cash Flow Statement

for the six months ended 30 June 2003

	Note	**6 months to 30 June 2003 £'000**	6 months to 30 June 2002 £'000	Year to 31 December 2002 £'000
Net cash inflow from operating activities	5	**1,695**	1,717	4,743
Returns on investments and servicing of finance				
Interest received		**65**	19	86
Interest paid		—	(3)	(3)
Net cash inflow from returns on investments and servicing of finance		**65**	16	83
Taxation (paid)/received		**(146)**	5	(538)
Capital expenditure				
Purchase of tangible fixed assets		**(352)**	(403)	(731)
Sale of tangible fixed assets		—	2	17
Purchase of investment		—	(30)	(36)
Net cash outflow from capital expenditure		**(352)**	(431)	(750)
Acquisitions				
Purchase of subsidiary undertakings		**(475)**	—	(837)
Net cash acquired with subsidiary undertakings		—	—	479
Net cash outflow from acquisitions		**(475)**	—	(358)
Equity dividends paid		—	—	(479)
Financing				
Issue of shares		**57**	248	252
Net cash inflow from financing		**57**	248	252
Increase in cash	6	**844**	1,555	2,953

Unaudited Notes to the Financial Statements

for the six months ended 30 June 2003

1. Turnover and profit on ordinary activities before taxation

Turnover and profit on ordinary activities before taxation are attributable to the following activities carried out entirely within the UK.

	Turnover		Profit before taxation		Net assets	
	6 months to 30 June 2003 £'000	6 months to 30 June 2002 £'000	**6 months to 30 June 2003 £'000**	6 months to 30 June 2002 £'000	**As at 30 June 2003 £'000**	As at 30 June 2002 £'000
Maintenance, mechanical and electrical services	**43,138**	30,880	**1,834**	1,083	**9,485**	7,326
Vehicle collection and delivery	**6,514**	7,181	**323**	494	**1,375**	1,241
	49,652	38,061	**2,157**	1,577	**10,860**	8,567

2. Taxation

The tax charge for the six months ended 30 June 2003 has been based on the estimated tax rate for the full year.

3. Dividends

	6 months to 30 June 2003 £'000	6 months to 30 June 2002 £'000
Ordinary shares		
– interim dividend of 0.35p (2002: 0.25p) per share payable on 10 November 2003	**200**	141

4. Earnings per share

Basic earnings per share is based on equity earnings of £1.48m (2002: £1.13m) and 56.64m (2002: 55.77m) ordinary shares of 1p each, being the average number of shares in issue during the period.

Basic pre amortisation earnings per share is based on equity earnings before charging for the amortisation of goodwill of £1.63m (2002: £1.20m).

For diluted earnings per share the average number of shares in issue is increased to 58.54m (2002: 57.83m) to reflect the potential diluting effect of employee share schemes.

Unaudited Notes to the Financial Statements

for the six months ended 30 June 2003

5. Net cash inflow from operating activities

	6 months to 30 June 2003 £'000	6 months to 30 June 2002 £'000	Year to 31 December 2002 £'000
Operating profit	**2,090**	1,559	3,512
Depreciation and amortisation	**436**	281	610
Loss on disposal of fixed assets	**—**	2	6
(Increase) in stocks	**(562)**	(9)	(29)
(Increase)/decrease in debtors	**(708)**	(41)	575
Increase/(decrease) in creditors	**439**	(75)	69
Net cash inflow from operating activities	**1,695**	1,717	4,743

6. Reconciliation of net cash flow to movement in net funds

	6 months to 30 June 2003 £'000	6 months to 30 June 2002 £'000	Year to 31 December 2002 £'000
Change in net funds resulting from cash flows and movement in net funds in the period	**844**	1,555	2,953
Net funds at start of period	**5,566**	2,613	2,613
Net funds at end of period	**6,410**	4,168	5,566

7. Analysis of changes in net funds

	At 1 January 2003 £'000	Cash flow £'000	**At 30 June 2003 £'000**
Funds – cash at bank and in hand	5,566	844	**6,410**

Unaudited Notes to the Financial Statements
for the six months ended 30 June 2003

8. Reconciliation of movements in equity shareholders' funds

	6 months to 30 June 2003 £'000	6 months to 30 June 2002 £'000	Year to 31 December 2002 £'000
Profit for the financial period	**1,477**	1,127	2,529
Dividends	**(200)**	(141)	(565)
	1,277	986	1,964
Issue of shares	**57**	597	600
Net increase in equity shareholders' funds	**1,334**	1,583	2,564
Equity shareholders' funds at start of period	**9,559**	6,995	6,995
Equity shareholders' funds at end of period	**10,893**	8,578	9,559

9. Preparation of interim financial information
The interim financial statements have been prepared on a basis consistent with the accounting policies disclosed in the Annual Report and Accounts for the year ended 31 December 2002.

The consolidated results for the year ended 31 December 2002 have been extracted from the financial statements for that year and do not constitute full statutory accounts for the Group.
The Group accounts for the year ended 31 December 2002 received an unqualified audit report and did not include a statement under section 237 (2) or (3) of the Companies Act 1985 and have been filed with the Registrar of Companies.

10. Interim financial statements
Further copies of the interim statements are available from the registered office of Mears Group PLC at The Leaze, Salter Street, Berkeley, Gloucestershire GL13 9DB, or www.mearsgroup.co.uk.

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