

ISG

Interior Services Group plc

Interim Accounts

31 December 2002

ISG

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Financial Highlights

- Operating profit* up 12.7% to £3.12m (2001: £2.77m)
 - Profit before tax* up to £4.17m (2001: £4.14m)
 - Fee income up 7.8% to £29m (2001: £27m)
 - Value of work performed £270m (2001: £270m)
 - Earnings per share* up to 11.33p (2001: 11.18p)
 - Interim dividend up 14% to 2.5p (2001: 2.2p)
 - Net cash £30.4m (2001: £32.1m)
- (* before exceptional costs and goodwill)

Chairman's Statement

ISG's strategy is to create an integrated group offering a broad range of services to a wide ranging client base in both the commercial and public sectors. We are delighted to report that during the six months under review we have made significant progress.

The first half results demonstrate the strength and resilience of our diversified business with PBT (before exceptionals and goodwill) maintained at £4.17m (£4.14m 2001). I am especially pleased with these results as they have been achieved against a background of difficult market conditions, and after PFI bidding costs of £216,000.

After exceptional costs of £764,000 to cover the reorganisation of all our property and facilities business into one 'Occupancy' division, PBT (before goodwill) reduced 17.9% to £3.40m (£4.14m 2001). In view of current equity markets, and in line with our prudent accounting policies, the company has also written down its quoted investment in Stonemartin to current market value. This adjustment has been made through the balance sheet. The balance sheet remains strong with net cash of £30.4m.

Encouragingly, underlying operating profit before exceptionals increased 12.7% to £3.12m (£2.77m 2001) with operating margin before exceptionals increasing to 10.66% (10.19% 2001). Fee income increased 7.8% to £29m and EPS (before exceptionals and goodwill) increased to 11.33p (11.18p 2001), against a background of steady workload at £270m.

To reflect the ongoing performance of the business, a 14% increased dividend of 2.5p (2.2p 2001) will be paid on 23rd April '03 to shareholders who are on the register on 28th March '03.

Strategic Developments

The three key objectives of the last six months have been to:

- Create a single Occupancy division covering all of our property and facilities services. To rationalize and reorganize it to lower its cost base, and hence its breakeven, and to resource it to grow in the future.
- Continue the market and sector diversification in both our Occupancy and Facilities Creation activities away from the private sectors and our dependency on the London commercial office market towards a greater proportion of publicly funded work, including PFI, outside London.
- Develop growth opportunities for both Facilities Creation & Occupancy in Asia through our JV with CityAxis.

Progress has been made in all three areas:

- Occupancy is now running with a £400k p.a lower cost base and is now much closer to achieving 'critical mass'. With this unit now organised into four streams; Advisory, Property Management, Facilities Management & Service Delivery, it is much better placed to respond to its customers' collective needs.
- The proportion of publicly funded assignments in Facilities Creation (Interior & Exterior) has increased to 25% of order book. A further reduction in dependence on the Central London fit-out market was achieved, now representing only 36% (46% 2001) of the group's revenue. 50% of the order book is now accounted for by non commercial office sector clients. Having invested £216k this half in a number of 'LIFT' PFI schemes in the Health Sector; if successful, work on these schemes should start to be seen in the second half.
- With the acquisition by our JV company in Hong Kong of some of the North Asian businesses of Trammell Crow Savills in December; we now have over 200 staff offering project and facilities management in Asia, making a positive P&L contribution this half.

Trading

Our Facilities Creation business works for occupiers fitting out space and for owners refurbishing or building it.

As predicted, the occupier market has been weak, as indicated by Central London office take up being down 20% over the last twelve months. Interior as a leader in this market cannot avoid this decline but can offset it with growth in fit-out markets outside London where its penetration is lower. Interior continues to win a major share of the capital's significant new projects, including most recently the new HQ for Marks & Spencer in Paddington.

	Fee Income		Gross Value of Work Performed	
	6 months to Dec 02 £m	6 months to Dec 01 £m	6 months to Dec 02 £m	6 months to Dec 01 £m
London Fit-Out	10.9	12.5	106	155
Exterior/Refurb	8.6	7.4	101	74
Regional Fit-Out	2.2	2.0	32	20
Occupancy	5.3	4.0	16	15
Europe	1.2	1.2	6	6
Asia	1.0	-	9	-
	<u>£29.2m</u>	<u>£27.1m</u>	<u>£270m</u>	<u>£270m</u>

In group income terms, the reduction in London fit-out volume was 32%, but only 12% in fee income terms. This was partly offset by growth in the regions of 60% in volume and 10% in fee income terms.

Demand from owners for Exterior & Interior refurbishment services was strong, with 36% growth in volume and in fee income the increase was 16%. This growth, mainly in London, included work for the Retail, Education and Residential sectors as well as for commercial office space.

Demand for Occupancy remained mostly strong, and especially in Property & Facilities Management. Demand for transactional property advice however continued to be weak. Following the reorganisation of the business, when some unprofitable contracts were terminated, volume increased by 7% to £16m. A more selective approach to business and growth in property management improved fee income by 31% from £4m to £5.3m, including for the first time income from the new Service Centres for Benchmark and Grosvenor.

Prospects

Whilst trading conditions generally are getting tougher, the key drivers for growth in our business remain valid.

Demand for outsourcing to improve service quality and reduce fixed overheads continues unabated. The government's use of PFI vehicles to deliver improvements in the Health Sector is well documented. Whilst demand for our new build and refurbishment services from commercial developers is still strong, any potential decline can be offset by increasing market share. Demand for publicly funded buildings is likely to increase. Demand for fit-out will continue to decline, especially in London, and will result in fit-out representing a smaller percentage of the total order book for 03/04. However, if vacancy rates amongst the portfolios of major occupiers continue to rise, it will not be long before this space is refitted to bring back to the letting market.

Like London, the outlook for fit-out in Europe also remains weak, especially in Germany. During the next six months we will review our operations in Europe in light of this easing. The outlook for Asia is more promising with our JV well placed to take advantage of growth, especially in China.

Although the business environment will undoubtedly become more challenging, we have a well motivated team. A team who helped the company be ranked 21st in the Sunday Times 100 Best Companies to work for. With the order book steady at £529m, the company is well placed to take advantage of the growth opportunities that do exist.

David King
Executive Chairman
18 March 2003

Consolidated profit and loss account

6 months ended 31 December 2002

Unaudited

		6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
	Notes			
Gross value of work performed	2	269,612	269,701	510,750
Less: relating to construction management share of joint ventures' turnover		(68,886) (2,664)	(47,192) (1,051)	(101,303) (3,008)
TURNOVER				
Group turnover - continuing operations		198,062	221,458	406,439
Cost of sales		(184,986)	(208,321)	(380,190)
Gross profit		13,076	13,137	26,249
Administrative expenses:				
Amortisation of goodwill		(537)	(484)	(1,020)
Exceptional reorganisation costs	3	(764)	-	-
Other administrative expenses		(9,423)	(9,887)	(19,590)
		(10,724)	(10,371)	(20,610)
OPERATING PROFIT				
Group operating profit - continuing operations		2,352	2,766	5,639
Share of operating (loss)/profit in joint ventures		(20)	(47)	53
Total operating profit		2,332	2,719	5,692
Profit on disposal of interest in joint venture		-	412	412
Net interest receivable and similar income	4	533	530	999
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	2	2,865	3,661	7,103
Tax on profit on ordinary activities		(1,053)	(1,295)	(2,443)
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION		1,812	2,366	4,660
Equity minority interests		(17)	(41)	(26)
PROFIT FOR THE FINANCIAL PERIOD/YEAR		1,795	2,325	4,634
Equity dividends paid and proposed	5	(621)	(566)	(1,674)
RETAINED PROFIT FOR THE FINANCIAL PERIOD/YEAR		1,174	1,759	2,960
Basic EPS	6	7.11p	9.25p	18.37p
Diluted EPS	6	7.02p	9.08p	18.01p
Adjusted EPS before amortisation of goodwill and exceptional administrative costs	6	11.33p	11.18p	22.41p
Dividend per share	5	2.50p	2.20p	6.50p

Consolidated balance sheet

6 months ended 31 December 2002

Unaudited

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Notes			
FIXED ASSETS			
Intangible assets	17,137	17,852	17,694
Tangible fixed assets	1,722	2,239	1,851
Investment in joint ventures:			
Share of gross assets	3,686	1,418	1,596
Share of gross liabilities	(3,326)	(1,219)	(1,234)
	360	199	362
Other investments	2,753	4,364	3,997
Total investments	3,113	4,563	4,359
TOTAL FIXED ASSETS	21,972	24,654	23,904
CURRENT ASSETS			
Stocks	278	321	315
Debtors	50,895	48,359	49,488
Cash at bank and in hand	36,771	38,120	36,619
	87,944	86,800	86,422
CREDITORS: amounts falling due within one year	(82,555)	(83,360)	(80,867)
NET CURRENT ASSETS	5,389	3,440	5,555
TOTAL ASSETS LESS CURRENT LIABILITIES	27,361	28,094	29,459
CREDITORS: amounts falling due after more than one year	(4,197)	(5,166)	(5,296)
PROVISIONS FOR LIABILITIES AND CHARGES	318	-	318
EQUITY MINORITY INTERESTS	(167)	(105)	(150)
TOTAL NET ASSETS	23,315	22,823	24,331
CAPITAL AND RESERVES			
Called up share capital	258	255	257
Share premium account	8 9,116	8,555	9,022
Other reserves	8 1,171	3,456	3,456
Profit and loss account	8 12,770	10,557	11,596
TOTAL EQUITY SHAREHOLDERS' FUNDS	7 23,315	22,823	24,331

Consolidated cash flow statement

6 months ended 31 December 2002

Unaudited

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Notes			
Net cash flow from operating activities	9 3,499	6,258	6,757
Dividends from joint ventures	-	-	105
Returns on investments and servicing of finance	526	530	984
Taxation	(1,170)	(765)	(2,567)
Capital expenditure and financial investment	(1,415)	(763)	(997)
Acquisitions and disposals	(112)	(239)	(660)
Equity dividends paid	(1,076)	(818)	(1,373)
Cash inflow before financing	252	4,203	2,249
Financing:			
Issue of shares (net)	4	53	99
Capital element of payments under hire purchase contracts	(13)	(5)	(21)
Long term debt	(200)	217	48
Net cash (outflow)/inflow from financing	(209)	265	126
Increase in cash for the period/year	43	4,468	2,375

Reconciliation of net cash flow to movement in net funds

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Increase in cash in the period/year	43	4,468	2,375
Cash outflow/(inflow) from decrease/(increase) in debt financing	213	(212)	(27)
Change in net debt resulting from cash flows	256	4,256	2,348
Change in net debt resulting from non-cash changes	43	-	(82)
Net cash brought forward	299 30,077	4,256 27,811	2,266 27,811
Net cash carried forward	30,376	32,067	30,077

Net cash carried forward of £30,376,000 is after overdrafts of £701,000, loans of £4,848,000, loan notes of £808,000 and hire purchase contracts of £38,000.

Notes to the accounts

Unaudited

1. Accounting Policies

The Interim Accounts, which are unaudited, have been prepared on the basis of the accounting policies set out in the 2002 group accounts.

2. Segmental Information

Gross value of work performed, turnover and profit before taxation may be analysed as follows:

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Gross value of work performed by origin and destination:			
United Kingdom	254,805	264,139	501,171
Europe	5,665	5,562	9,579
Asia	9,142	-	-
	<u>269,612</u>	<u>269,701</u>	<u>510,750</u>
Turnover by origin and destination:			
United Kingdom	193,319	217,988	402,563
Europe	5,665	4,521	6,884
Asia	1,742	-	-
	<u>200,726</u>	<u>222,509</u>	<u>409,447</u>
Less: Share of joint ventures' turnover	(2,664)	(1,051)	(3,008)
	<u>198,062</u>	<u>221,458</u>	<u>406,439</u>
Profit on ordinary activities before taxation:			
United Kingdom	2,495	3,381	6,682
Europe	299	280	421
Asia	71	-	-
	<u>2,865</u>	<u>3,661</u>	<u>7,103</u>
Fee income is derived as follows:			
Turnover	198,062	221,458	406,439
Trade contractor costs recharged	(169,489)	(195,009)	(353,359)
	<u>28,573</u>	<u>26,449</u>	<u>53,080</u>
Interest receivable	688	727	1,337
Less: Attributable to minority interests	(24)	(42)	(69)
	<u>29,237</u>	<u>27,134</u>	<u>54,348</u>

The majority of net assets are held in the United Kingdom.

The principal activity of the company and its subsidiaries is to provide occupancy support services to its customers throughout the Occupancy Life Cycle. The group has European operations based in Germany and France. The group's Asian operations are based in Hong Kong, Singapore and South Korea.

In accordance with industry practice, gross value of work performed includes £60,486,000 (December 2001 - £47,192,000; June 2002 - £101,303,000) in respect of the construction costs of projects on which the company acts as construction manager. These construction costs are billed directly to the client and are not invoiced via the group.

The operating margin is defined as the ratio of operating profit to fee income.

3. Exceptional items

Exceptional administrative costs relate to the reorganisation of seven Facilities Management and Operation businesses into one new division, ISG Occupancy.

4. Net interest receivable and similar income

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Group:			
Bank interest receivable	690	727	1,328
Other interest (payable)/receivable	(2)	-	9
Bank loans and overdrafts	(160)	(195)	(348)
Finance charges on hire purchase contracts	(2)	(2)	(5)
Joint ventures:			
Group share of interest receivable	7	-	15
	<u>533</u>	<u>530</u>	<u>999</u>

5. Equity dividends paid and proposed

	6 months ended 31 December 2002 pence	6 months ended 31 December 2001 pence	(Audited) 12 months ended 30 June 2002 pence
Ordinary dividends per share	2.50p	2.20p	6.50p
	<u>£'000</u>	<u>£'000</u>	<u>£'000</u>
Ordinary dividends	621	566	1,674

The interim dividend of 2.50p per share will be paid on 23 April 2003.

6. Earnings per share

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Profit on ordinary activities after taxation and minority interests	1,795	2,325	4,634
Basic and diluted earnings attributable to ordinary shareholders	1,795	2,325	4,634
Amortisation of goodwill	537	484	1,020
Post-tax exceptional reorganisation costs	528	-	-
Adjusted earnings attributable to ordinary shareholders	2,860	2,809	5,654
	Number '000	Number '000	Number '000
Weighted average number of ordinary shares	25,245	25,129	25,231
Dilutive share options	311	470	501
Diluted weighted average number of ordinary shares	25,556	25,599	25,732

7. Reconciliation of movements in consolidated shareholders' funds

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Profit for the financial period/year	1,795	2,325	4,634
Equity dividends	(621)	(566)	(1,674)
	1,174	1,759	2,960
Unrealised (loss)/gain arising on investments	(2,285)	3,456	3,456
Cost of shares to be allocated in the group Qualifying Employee Share Trust	-	-	(301)
Proceeds from share issue	95	272	741
Net (reduction)/addition to shareholders' funds	(1,016)	5,487	6,856
Opening shareholders' funds	24,331	17,336	17,475
Closing shareholders' funds	23,315	22,823	24,331

The unrealised loss arising from the fall in the market value of the group's investment in Stonemartin plc has been accounted for through the Statement of Total Recognised Gains and Losses. This is consistent with the treatment of the unrealised gain arising from the original transaction during the year ended 30 June 2002.

8. Group reserves

	Share premium £'000	Other reserves £'000	Profit and loss account £'000
Balance at 1 July 2002	9,022	3,456	11,596
Profit for the period	-	-	1,795
Equity dividends	-	-	(621)
Share premium arising on issue of shares	94	-	-
Unrealised loss arising on investments	-	(2,285)	-
Balance at 31 December 2002	9,116	1,171	12,770

The movement on Other reserves has arisen as a result of the fall in market value of the investment in Stonemartin plc.

9. Reconciliation of operating profit to operating cash flow

	6 months ended 31 December 2002 £'000	6 months ended 31 December 2001 £'000	(Audited) 12 months ended 30 June 2002 £'000
Operating profit	2,352	2,766	5,639
Depreciation charges	503	545	1,212
Amortisation of goodwill	537	484	1,020
(Profit)/loss on sale of tangible fixed assets	-	(2)	7
Decrease/(increase) in stocks	37	(70)	(64)
(Increase)/decrease in debtors	(1,407)	8,173	7,069
Increase/(decrease) in creditors	1,477	(5,638)	(8,126)
Net cash inflow from operating activities	3,499	6,258	6,757

10. Approval of interim accounts

The Interim Accounts were approved by the Board of Directors on 28 February 2003.

11. Status of financial information in this announcement

The financial information contained in this report does not constitute statutory accounts within the meaning of section 240 of the Companies Act 1985. The financial information for the six months to 31 December 2002 and the six months to 31 December 2001 is unaudited and has not been reviewed by the group's auditors. The year ended 30 June 2002 comparative figures have been extracted from the audited accounts. The accounts for the year ended 30 June 2002, on which the auditors issued an unqualified audit report and which did not contain a statement under either section 237 (2) or (3) of the Companies Act 1985, have been delivered to the Registrar of Companies.