



HARRY SHERIDAN

Finance review

Results

The good growth in sales of 3.3%, in operating profits of 2.7% and in profit before tax of 6.6% has been highlighted elsewhere in the Annual Report. Record levels of both earnings and cash earnings per share have also been achieved. The key components of 2002 performance are analysed in Table 1.

Exchange translation effects

The average 2002 euro exchange rate was 5% stronger versus the US Dollar than in 2001 resulting in a net negative profit before taxation translation impact of €28 million. The profit and loss impact of other currency movements during 2002 was not significant.

Incremental impact of acquisitions

The incremental operating profit effect in 2002 of €34 million from acquisitions completed during 2001 principally reflects an additional seven-month contribution from our 25% joint venture investment in the Mashav Group, which owns Neshor Cement, Israel's sole cement producer, together with good contributions from 2001

acquisitions in our Products & Distribution Divisions in Europe and North America. The incremental benefit from 2001 acquisitions in the Americas Materials Division was, as expected, modestly positive despite first-time winter losses at Mount Hope Rock Products which was acquired in April 2001.

The €80 million operating profit impact of acquisitions completed during 2002 principally reflects a strong contribution from the EHL Group, Germany's leading producer of concrete paving and landscape walling products, which was acquired in May. We also benefited from strong initial contributions from Americas Materials Division acquisitions in Iowa, Utah, Idaho and Ohio as well as from deals completed by the Architectural Products and Distribution Groups across their operations in the United States.

Benefits of share issues

The incremental interest income in 2002 arising on the proceeds from the March 2001 Rights Issue amounted to €13 million.

Ongoing operations

In a very difficult year, ongoing operations suffered a decline at the sales and operating profit levels. The most severe setback was experienced by the Americas Materials Division which suffered from unseasonably wet weather in May and June and slower underlying second half demand. The Precast operations in the Americas Products & Distribution Division continued to be affected by the sharp decline in non-residential activity; however, the Architectural Products, Glass and Distribution activities combined reported an increase in operating profit. In Europe the Materials Division reported similar underlying profits before taking account of a €7 million rationalisation charge in its Polish operation. The Europe Products & Distribution Division reported a slight decline in underlying profits which was largely offset by a €3 million reduction in rationalisation costs compared with 2001.

Lower interest rates combined with the benefits of our strong free cash flow resulted

Table 1 Key components of 2002 performance

€ million	2001	Exchange translation effects	Incremental effect in 2002 of acquisitions & investments completed during		Disposed businesses	Benefits of 2001 Rights Issue	Incremental effect in 2002 of rationalisation costs charged in		Ongoing operations	2002
			2001	2002			2001	2002		
Sales	10,444	(390)	436	678	(45)	-	-	-	(329)	10,794
Operating profit	1,020	(38)	34	80	-	-	8	(12)	(44)	1,048
Goodwill amortisation	(61)	2	(6)	(5)	-	-	-	-	-	(70)
Profit on disposals	17	-	-	-	-	-	-	-	(1)	16
Profit before interest	976	(36)	28	75	-	-	8	(12)	(45)	994
Finance costs	(173)	8	(25)	(20)	-	13	-	-	59	(138)
Profit before taxation	803	(28)	3	55	-	13	8	(12)	14	856
Change		-3%	-	+7%	-	+1%	+1%	-1%	+2%	+7%

“Against a difficult market backdrop, the Group has again demonstrated its ability to maintain earnings at record levels while delivering a strong level of free cash flow and an active acquisition programme across its four product divisions. Our US\$1 billion Global Bond Issue completed in March 2002, combined with the benefits of the €1.1 billion Rights Issue of March 2001, places CRH in an exceptionally strong position to avail of attractive acquisition opportunities as they arise in our various geographic, product and sectoral markets.”

in a strongly positive finance cost impact from ongoing operations.

The strong growth in earnings and cash earnings per share and net dividend over a five and ten-year period are highlighted in Table 2.

Financial indicators

Some key financial indicators which, taken together, are a measure of performance and financial strength are set out in Table 3.

Lower interest rates resulted in further improvement in interest cover measures despite a continued strong acquisition spend. The Group regards interest cover based ratios as more meaningful measures of financial capacity than the ratio of debt to shareholders' funds as they match the earnings and cash generated by a business to the underlying funding costs.

While lower year-end debt levels resulted in a decline in the debt to shareholders' funds ratio compared with 2001, the debt to year-end market capitalisation ratio actually increased reflecting the decline in share price during the course of the year.

The reduction in return on average capital employed since 2000 reflects the challenging trading conditions experienced during 2001 and 2002 together with the impact of the larger acquisitions in recent years which have slightly diluted overall returns on total average capital employed.

The Group's return on average equity in 2002 and 2001 has also been affected by tougher trading conditions and by higher average equity levels following the March 2001 Rights Issue. A continuation of the good level of acquisition activity delivered in recent years should naturally lead to the increased use of the Group's debt capacity and improvements in return on equity.

Cash generation

The strong cash generation characteristics of the Group combined with a favourable translation adjustment, primarily as a result of a weaker US Dollar, resulted in a €184 million decrease in net debt despite spending a total of €1.36 billion on acquisitions, investments and capital projects. Table 4 (overleaf) summarises

CRH's cash flows for 2002 and 2001.

The €1 billion spend on acquisitions and investments in 2002 reflects the completion of 45 deals across the Group's operations.

The increased depreciation and amortisation charges reflect the impact of acquisitions completed in 2001 and 2002.

Proceeds from share issues principally reflect the take-up of shares in lieu of dividend under the Company's scrip dividend scheme augmented by issues under Group share option and share participation schemes. The comparative prior year figure reflects the March 2001 Rights Issue, which raised approximately €1.1 billion (net of expenses). Also in 2001 preference shares in a subsidiary company were issued on a non-recourse basis to a financial institution as part of the financing of our 25% investment in Mashav in Israel.

Once again in 2002, control of working capital levels remained a key priority for the Group. More normal US weather patterns in the final quarter resulted in a traditional

Table 2 Compound average growth rates

	5 year	10 year
Sales	21%	21%
Earnings per share	15%	21%
Cash earnings per share	20%	21%
Dividend per share	13%	13%

Table 3 Key financial indicators

	2002	2001	2000
Interest cover, excluding joint ventures			
– EBITDA basis (times)	11.3	8.5	6.7
– EBIT basis (times)	7.3	5.6	4.6
Debt to shareholders' funds ratio (%)	35.7	39.7	83.8
Debt to year-end market capitalisation ratio (%)	27.8	18.3	31.9
Tax as a percentage of pre-tax profit (%)	26.5	27.0	27.8
Return on average capital employed (%)*	13.3	14.0	16.3
Return on average equity (%)*	12.2	12.8	16.6

EBITDA = earnings (profit) before interest, tax, depreciation and goodwill amortisation

EBIT = earnings (profit) before interest and tax (i.e. trading profit)

** these returns are calculated after charging goodwill amortisation*

Finance review *continued*

seasonal run-down in working capital levels in contrast to 2001 when very favourable conditions resulted in higher than normal year-end working capital. This combined with ongoing intensive efforts at operational level resulted in a working capital reduction for the year as a whole.

Against a challenging market backdrop only

Table 4 Cash flow

€ million	2002	2001
Inflows		
Profit before taxation	856	803
Depreciation	456	436
Goodwill amortisation	70	59
Working capital	90	(61)
	<u>1,472</u>	<u>1,237</u>
Outflows		
Taxation	(162)	(79)
Dividends	(135)	(103)
Capital expenditure	(367)	(452)
Other	(21)	(29)
	<u>(685)</u>	<u>(663)</u>
Operating cash flow	787	574
Acquisitions and investments	(992)	(1,080)
Disposals	104	89
Share issues	37	1,108
Issue of preference shares in subsidiary to minority	-	109
Translation adjustment	248	(74)
	<u>184</u>	<u>726</u>
Decrease in net debt		

essential capital projects were undertaken resulting in a decline in such expenditure for the first time since 1991. Capital expenditure of €367 million represented 3.5% of sales (2001: 4.4%) and amounted to 0.81 times depreciation (2001: 1.04 times).

Taxation payments, which had been favourably impacted in 2001 by timing issues, reverted to more normal levels in 2002.

Exchange rate movements between end-2001 and end-2002 reduced the euro amount of net foreign currency debt by €248 million principally due to the 18% revaluation of the euro against the US Dollar.

Liquid resources

In March 2002, the Group completed a 10 year US\$1 billion Global Bond Issue, which substantially extended the maturity profile of the Group's net debt. This Bond Issue, which is rated BBB+ / Baa1 / A-, was significantly over-subscribed and represented a natural progression from previous fundings in the US Private Placement market undertaken by the Group over the period 1992 to 2000.

The Group finished the year in a very strong financial position with 98% of the Group's gross debt drawn under committed term facilities, 95% of which mature after more than one year. In addition, at year-end the Group held €621 million of undrawn committed facilities, which had an average maturity of two years.

The Group holds significant cash balances, which are invested on a short-term basis. At year-end 2002, 96% of the Group's cash, short-term deposits and liquid resources had a maturity of six months or less.

Pensions

Details of the Group's pension schemes and the disclosures required by Financial Reporting Standard 17 – Retirement Benefits (FRS 17) are set out in note 31 to the financial statements. FRS 17, which was issued by the

Accounting Standards Board in November 2000, represented a significant change in the method of accounting for pension costs relating to defined benefit pension schemes compared with the previous rules as set out in Statement of Standard Accounting Practice 24 (SSAP 24). A majority of the Group's employees are in defined contribution schemes.

Full implementation of the accounting rules prescribed by FRS 17 has been deferred by the Accounting Standards Board, except for the detailed disclosure required in the notes to the financial statements. The total pension charge for the Group in 2002, computed in accordance with SSAP 24, amounted to €107.9 million (2001: €95.8 million). Under FRS 17, the total pension charge for the year would have been €85.0 million. As at 31st December 2002, the net FRS 17 pension liability of the Group amounted to €130.0 million; this compares with an asset of €119.3 million as at 31st December 2001, and reflects primarily the decline, compared with year-end 2001, in the market value of the equity portion of the assets of the Group's various defined benefit pension schemes. The net liability as at year-end 2002 represents just 2% of the Group's market capitalisation at that date.

Share price

In a very turbulent year for Stock Markets and building materials stocks, the Company's Ordinary Shares traded in the range €11.10 to €20.70. The year-end share price was €11.75 (2001: €19.83). Shareholders recorded a gross negative return (dividends and capital depreciation) of -39% during 2002 following a return of +11% in 2001, -6% in 2000, +47% in 1999 and +43% in 1998.

CRH is one of six building materials companies included in the FTSE Eurotop 300, a market capitalisation weighted index of Europe's largest 300 companies. At year-end 2002 CRH's market capitalisation of €6.2 billion (2001: €10.3 billion) placed it among

the top 4 building materials companies worldwide.

Financial risk management

The Board of Directors sets the treasury policies and objectives of the Group, which include controls over the procedures used to manage currency, interest rate and credit risk. The approach to managing risk is set out below. The Group uses financial instruments throughout its businesses: *borrowings, cash and liquid resources* are used to finance the Group's operations; *trade debtors and creditors* arise directly from operations; and *derivatives*, principally interest rate and currency swaps and forward foreign exchange contracts, are used to manage interest rate risks and to achieve the desired currency profile of borrowings. The Group does not trade in financial instruments nor does it enter into any leveraged derivative transactions.

The Group's policy is to fix interest rates on a proportion of the Group's medium to long-term net debt exposure in individual currencies. Underlying borrowings are arranged on both a fixed rate and a floating rate basis and, where appropriate, the Group uses interest rate swaps to vary this mix and to manage the Group's interest rate exposure. In recent years the Group's target has been to fix interest rates on approximately 50% of Group net debt. At the end of 2002, 52% of the Group's net debt was at interest rates, which were fixed for an average period of 4.9 years. US Dollars accounted for approximately 67% of net debt at the end of 2002 and 44% of the Dollar component of net debt was at fixed rates.

CRH's activities are conducted principally in the local currency of the country of operation and the Group faces currency risk principally on its net assets, most of which are in currencies other than the euro. Currency movements can therefore have a significant effect on the Group's balance sheet when translating these foreign

currency assets into euro. The Group's policy is to spread its net worth across the currencies of its different operations so as to limit its exposure to any individual currency. We believe that this is an appropriate policy for an international Group with international shareholders. In order to achieve this the Group manages its borrowings, where practicable and cost effective, to hedge its foreign currency assets. Where possible, hedging is done using direct borrowings in the same currency as the assets being hedged or through the use of other hedging methods such as currency swaps.

The bulk of the Group's net worth is denominated in the world's two largest currencies – the US Dollar and the euro – which accounted for 55% and 32% respectively of the Group's net worth at end-2002.

The strengthening of the euro during 2002 resulted in a negative €514 million currency translation effect on foreign currency net worth mainly arising on US Dollar net assets. This negative effect is stated net of a €248 million favourable translation impact on net foreign currency debt.

Cash deposits and other financial instruments give rise to credit risk on amounts due from counterparties. Credit risk is managed by limiting the aggregate amount and duration of exposure to any one counterparty primarily depending on its credit rating and by regular review of these ratings. The possibility of material loss in the event of non-performance by a counterparty is considered unlikely by management.

Note 20 to the financial statements provides a detailed breakdown of debt, cash and capital employed by currency together with additional treasury-related information.

Interest and currency sensitivity

The Group monitors its exposure to changes in interest and exchange rates by estimating the impact of possible changes on reported

profit before taxation and net worth. The Group accepts interest rate and currency risk as part of the overall risks of operating in different economies and seeks to manage these risks by following the policies set out above.

Based on the Group's 2002 year-end level and composition of net debt, an increase in average interest rates of one per cent per annum would result in a decrease in future earnings, before taxation, of €8.3 million per annum (2001: €6.7 million).

A strengthening of the euro by 10% against all the other currencies the Group operates in would, when reported in euro, reduce the Group's year-end 2002 net worth by an estimated €293 million and year-end 2002 net debt by €163 million.

Legal proceedings

Group companies are parties to various legal proceedings, including some in which claims for damages have been asserted against the companies. The final outcome of all the legal proceedings to which Group companies are party cannot be accurately forecast. However, having taken appropriate advice, we believe that the aggregate outcome of such proceedings will not have a material effect on the Group's financial condition, results of operations or liquidity.

Summary

Against a difficult market backdrop, the Group has again demonstrated its ability to maintain earnings at record levels while delivering a strong level of free cash flow and an active acquisition programme across its four product divisions. Our US\$1 billion Global Bond Issue completed in March 2002, combined with the benefits of the €1.1 billion Rights Issue of March 2001, places CRH in an exceptionally strong position to avail of attractive acquisition opportunities as they arise in our various geographic, product and sectoral markets.