News Release

KIER GROUP

14 September 2006

KIER GROUP PLC

PRELIMINARY RESULTS FOR THE YEAR TO 30 JUNE 2006

- Pre-tax profits* up 23.6% to £59.1m (2005: £47.8m**)
- EPS before last year's exceptional items up 25.1% to 120.8p (2005: 96.6p)
- Full year dividend increased by 17.1% to 26.0p (2005: 22.2p)
- £96.6m of cash generated from operating activities
- Construction and Support Services order books at record levels
- Homes order book at 31 August 45% ahead of last year

*Pre-tax profits are stated after deducting joint venture tax of £1.4m (2005: £1.2m)

**Before exceptional items

Commenting on the results, John Dodds, Chief Executive said:

"The year to 30 June 2006 has seen the Group firing on all cylinders and our objective for the new financial year is to maintain this momentum and to continue to provide clients with a high quality service.

Our Construction order books at 30 June 2006 were at the highest level ever and, with a strong pipeline of virtually secure work, our Construction division is in an excellent position to grow further. In Support Services the market for local authority outsourcing contracts continues to expand. Our housing land bank contains sites of good quality in saleable locations and we anticipate an increase in unit sales for Kier Residential this year enhanced by the acquisition of Hugh Bourn Homes which provides us with a new operating area. Our Property portfolio contains a range of development sites that will continue to be enhanced in value, and in Infrastructure Investment we can see a number of good projects coming forward.

Against this backdrop, the prospects for the Group are excellent and I am confident that we will continue to deliver further growth in 2007 and thereafter."

ISSUED BY THE PUBLIC RELATIONS DEPARTMENT, TEMPSFORD HALL, SANDY, BEDFORDSHIRE SG19 2BD
TEL: 01767 640111 FAX: 01767 641710 email: info@kier.co.uk www.kier.co.uk

Chairman's Statement

Overview

I am pleased to report another record result for Kier Group plc for the year to 30 June 2006. Profits before tax have grown by 23.6% to £59.1m (2005: £47.8m before exceptional items); and earnings per share, after deducting the amortisation of intangible assets, have increased by 25.1% to 120.8p (2005: 96.6p before exceptional items), representing a compound annual growth rate of 23% since flotation some 10 years ago.

Activity across all of our divisions was high during the year and order intake was strong, resulting in a record £1.8bn of revenue for the year (2005: £1.6bn) and record year-end order books for Construction and Support Services of £2.7bn (2005: £2.2bn). Our Homes division had an excellent year with the number of unit sales 25% ahead of last year and order books at 31 August 45% ahead of the same time last year.

The cash performance, one of our key measures, was exceptionally strong, particularly within our Construction businesses, with £96.6m generated from operating activities during the year, despite special pension contributions of £31.5m in the period. The net cash balance at 30 June 2006 was £111.2m (2005: £58.1m).

This is the first set of full year results presented under International Financial Reporting Standards (IFRS) and comparative figures for the year to 30 June 2005 have been restated on this basis. The most significant impact of changes in accounting standards is on the Group's net asset position, which has reduced by £42.1m as a result of reflecting the net pension scheme deficit on the balance sheet.

The Board proposes a final dividend of 17.8p (2004: 15.2p) making 26.0p for the year (2005: 22.2p), an increase of 17.1% which is covered 4.6 times by earnings per share. The dividend will be paid on 5 December to shareholders on the register on 29 September 2006 and there will be a scrip dividend alternative.

Board appointments

I am very pleased to welcome Phil White to our Board as a non-executive director from 1 July 2006. Phil was Chief Executive of National Express for nearly 10 years transforming it into one of the UK's leading transportation groups. He is already playing a very constructive role on the Kier Board and, with his experience, will contribute significantly to the future growth of the Group.

I am delighted to announce that, with effect from 1 October 2006, Mick O'Farrell, managing director of Kier Residential, will be joining the Board. Mick, aged 45, joined the Group in May 2003 as managing director of Allison Homes and became managing director of Kier Residential in August 2005. Mick has many years of experience in housebuilding having held senior positions in other major housing businesses. Our housing activities contribute significantly to the results and the strength of the Group and Mick's position on the Board is well deserved – I wish him well.

Prospects

The record levels of revenue, cash generation and contracting order books provide a firm foundation for the future and we are therefore well placed for further profitable growth in 2007.

Operating and Financial Review

Chief Executive's Review

Overview

The year to 30 June 2006 has been another successful one for the Group. Activity levels have been high, with revenue across most of the divisions at record levels; cash generation has been strong and all of the divisions have seen increased operating margins. Our growth record in earnings per share has continued with a 25.1% increase on last year (excluding the impact of last year's exceptional items) and compound annual growth of 23% since flotation in 1996.

Good progress has been made this year on multi-skilled projects where two or more of the divisions within the Group are working together. This is an area in which Kier has a competitive advantage and which, I believe, will continue to strengthen our position in the marketplace.

Financial performance

Revenue for the year at £1,838.3m (2005: £1,623.2m) was 13.3% ahead of last year with strong growth from our Construction, Support Services and Homes divisions. Operating profit, after the amortisation of intangible assets and joint venture interest and tax, was 20.8% ahead of last year at £59.2m (2005: £49.0m) and profit before tax increased by 23.6% to £59.1m (2005: £47.8m before exceptional profits of £6.7m).

Adjusted earnings per share before the amortisation of intangible assets and last year's exceptional profits and tax increased by 24.4% to 124.8p (2005: 100.3p).

The trading result for the year was supported by strong cash generation. Overall there was an inflow of £53.1m resulting in a year end net cash balance of £111.2m (2005: £58.1m) after an outflow of £31.5m relating to special pension contributions to the Kier Group Pension Scheme in the last quarter of the financial year. The strong cash balance is a reflection of excellent cash management in the Construction and Support Services divisions and the timing of land expenditure within the Homes division including the purchase of a number of sites on deferred terms.

Group structure and strategic developments

Kier Group comprises five divisions: Construction; Support Services; Homes; Property Development and Infrastructure Investment (investment under the Private Finance Initiative (PFI)). The Group's management structure and segmental analysis for reporting purposes are based on the five divisions.

The Group has a well established business model that has underpinned its growth and development over a number of years providing both financial and operational synergies. Financially, the construction activities generate cash, albeit at relatively low operating margins whilst activities such as housebuilding and property require cash investment for growth but generate higher operating margins. By combining the cash generative construction activities with housebuilding and property, we have created an efficient financial model that achieves excellent returns on capital. Operationally the combined skills of our businesses are delivering a wide range of development schemes through a single source. Such schemes include regeneration projects, mixed-use schemes and PFI projects, bringing together cross-divisional expertise in a total in-house solution.

The Group strategy is to build on our skills and expertise and grow each of the divisions by maximising opportunities in the markets in which we operate. Much of our growth has occurred organically, particularly in the Construction division where our reputation for delivery and multi-skilled services has attracted a large number of opportunities. In Support Services our growth continues to emanate, largely, from new contracts in the local authority outsourcing sector through our Building Maintenance division.

Our Homes division is one in which we have generated growth both organically and through acquisition. We have continued this strategy with the acquisition, in July 2006, of Hugh Bourn Developments (Wragby) Limited (Hugh Bourn Homes) which has formed the basis for our fifth housing operation within the Group.

Our Property development business has also grown both organically and through acquisition including, in December 2005, the acquisition of a portfolio of nine properties to add to our existing holdings. The strategy for Infrastructure Investment continues to be to grow a portfolio of PFI projects yielding long-term income streams while providing a flow of negotiated construction contracts and operational facilities management contracts for the Group's other operating divisions.

Business review, markets and outlook

Construction

The Construction division comprises Kier Regional and Kier Construction. Kier Regional benefits from unrivalled UK regional construction coverage focusing largely on mid-range building contracts, and encompasses our affordable homes and major building projects operations. Kier Construction includes the Group's infrastructure and overseas business with rail, mining and remediation capability.

Revenue in the Construction division reached a record £1,218.1m for the year, 12.1% ahead of 2005's revenue of £1,086.3m. Growth within this division was fuelled by a strong market supported by a high level of public sector expenditure. Operating profit increased by 30.4% to £18.0m (2005: £13.8m) and the operating margin reached our short-term target of 1.5% compared with 1.3% last year.

Cash generation, one of our key performance measures, has been exceptionally strong, with cash balances at 30 June 2006 over £40m higher than the previous year end and average cash balances for the year £38m ahead. Contract awards were very strong during the year at £1,311m (2005: £1,372m), providing a record order book of £1,270m at 30 June 2006 (2005: £1,030m).

<u>Kier Regional business review</u>

Kier Regional, with its wide network of UK construction businesses, continues to go from strength to strength and, once again, has achieved a number of records in the key performance measures of revenue, cash and new orders. Revenue, at £1,092.8m, was 14.5% ahead of 2005; year-end cash balances of £243.0m were £38.2m ahead; and contract awards of £1,216m were 19.4% ahead of 2005's £1,018m.

The high proportion of negotiated and repeat business from long-standing clients, as well as national framework agreements, has remained a constant theme across all regional businesses. Representing around 65% of work secured (2005: 59%), this provides us with a lower risk, more sustainable order book, particularly when combined with the fact that the average size of contracts within this business remains relatively low at £3.2m, (2005: £2.9m).

A number of the framework agreements and strategic alliances are with public sector clients including those designed to deliver an increasing number of social housing units. Of particular note are our framework agreements with Newlon Housing Trust and Dominion Housing Group, both Registered Social Landlords, which are providing high-rise affordable housing in London and which have contributed to the £180m of residential awards for the year. The continuing high level of public expenditure has led to an increase in public sector awards to 43% of the total compared with 41% in 2005.

Education has remained a very strong sector for Kier Regional, with over £350m of work secured this year, representing 29% of total awards (2005:24%). £95m has been awarded under the private finance initiative, including Norwich Schools and Oldham Schools both with Kier as an equity partner in the special purpose vehicle.

Our involvement with private sector clients continues through partnering style arrangements with food retailers including Tesco, Waitrose, Morrisons and Sainsbury's and developers such as Land Securities Trillium, for whom we are carrying out the multi-phased refurbishment of the DVLA headquarters in Swansea. From this contract, our relationship with Land Securities has strengthened.

As previously reported, in November 2005 our client Castlepoint announced the closure of a retail centre in Bournemouth due to concerns over health and safety. We, as main contractor, worked around the clock to install temporary props allowing the centre to fully reopen in mid January. We are discussing with Castlepoint the dismantling and rebuilding of the car park and the minimisation of any disruption on trading. The costs of this exercise are expected to be covered predominately by insurance, with no material effect anticipated on the Group's trading position.

Kier Construction business review

Revenue remained relatively stable in the year to 30 June 2006 at £125.3m (2005: £131.7m). In the UK, the civil engineering arm of Kier Construction saw the commencement of a rail framework for the renewal of railway structures in East Anglia under a five year agreement with Network Rail. The five year Asset Management Programme 4 for United Utilities, in joint venture, has successfully completed its first year of operation, albeit with a longer lead-in time than envisaged. Our major infrastructure projects capability continues with the successful completion of CTRL contract 103 and increasing activity at Milford Haven for South Hook LNG.

Our mining business had another productive year at our opencast coal site at Greenburn, East Ayrshire, with coal production having exceeded one million tonnes. 1.3m tonnes of coal have now been extracted to date and over 66% of that remaining in the ground has been forward-sold at favourable fixed prices.

Our remediation capability, where brownfield sites are re-developed for commercial, residential or mixed use, is being enhanced with a number of projects for other Group companies. In Peterborough, work has commenced on a former Anglian Water site for our Homes business and in Uxbridge, Kier Construction is working with Kier Property to remediate a British Gas site ahead of development of a mixed-use scheme.

Overseas, our activities in the Caribbean continue to perform well. Good progress has been made on a large transportation centre in downtown Kingston, Jamaica and the extension to Kingston's Norman Manley Airport has started well with certain areas expected to be ready for the cricket world cup next year. Our long-term alliance with Alcoa continues to provide extensive work on projects at aluminium refineries in Suriname and Jamaica.

Construction markets and outlook

In the UK demand for building remains high, both in the public and private sectors and there is an increasing emphasis on remediation projects. This demand can be satisfied by the combined skills of our Construction division and development expertise from elsewhere in the Group.

Our mining activities have good potential to contribute to future growth. The current area in which we are mining in Ayrshire is expected to continue production until 2009, however, extensions are being pursued and a new planning application has been made to operate an opencast mine at an adjacent site. If successful, this will extend the life of the mine into 2011.

Overseas, our established contacts are providing us with good opportunities, particularly in the Caribbean, with Alcoa, and in Romania, where we have recently secured a contract for a shopping mall and residential apartments with our joint venture partner. In Dubai, where construction activity is plentiful, we remain focused on our key area of expertise, infrastructure, and we have recently been awarded a new contract to build roads and infrastructure works for the new 'City of Arabia'.

Our Construction order books, represented by confirmed contracts in hand, are at the highest levels ever at £1,270m (2005: £1,030m), supported by a significant pipeline of contracts in the final stages of negotiation. With these strong, good quality order-books, we can expect further growth in our Construction activities in the new financial year.

Support Services

Support Services comprises four business streams: Kier Managed Services, providing facilities management services to public and private clients; Kier Building Maintenance, providing reactive and planned maintenance mainly to local authority clients, housing associations and Arms Length Management Organisations; Kier Building Services Engineers, a specialist mechanical and electrical design and installation and maintenance business; and Kier Plant, specialising in plant hire to Kier Group companies and external clients.

Support Services business review

Revenue in the Support Services division increased by 18.5% in the year to £281.3m (2005: £237.4m), driven largely by our Building Maintenance business. Operating profit, before deducting the amortisation of intangibles of £1.9m in both years, increased by 26.1% to £8.7m (2005: £6.9m), providing an operating margin of 3.1% (2005: 2.9%), slightly ahead of our short-term target of 3.0%. The cash performance within the division has been strong with £14.6m generated in the year to give a closing cash balance of £12.5m (2005: overdraft of £2.1m). Order books have also grown during the year to £1,396m at 30 June 2006 (2005: £1,204m).

In Managed Services volumes have remained steady. An increasing contribution to revenue arises from services provided under PFI; however, other private sector work has reduced in volume as we continue our focus on margin improvement. New services have begun during the year for the National Offenders Management Service in Newport and the Dogs Trust site in Hatfield; both achieved through introductions from our Construction division.

Good results were achieved by the Building Maintenance division, which now looks after around 185,000 homes for local authority clients including Sheffield City Council, Islington Borough Council and Leeds City Council. Revenue increased from £136.9m to £172.5m, mainly due to the inclusion of Decent Homes work and a whole year of revenue from the Leeds contract. During the year we secured a five year contract for the City of Lincoln which, whilst currently in the mobilisation phase, will provide £7m of revenue per annum under the Decent Homes initiative. Kier Sheffield, our partnership with Sheffield City Council, has achieved an increase in the volume of work carried out under the Decent Homes initiative. It continues to benefit from Sharrow Industries, a sheltered workshop run by Kier Sheffield which supplies and manufactures kitchens, windows and doors under an exclusivity agreement with all five contractors under the Decent Homes initiative in the City, one of which is Kier Sheffield. We were delighted that Sheffield City Council achieved Beacon status, the highest accolade a council can receive. Kier Sheffield's work was also influential in Sheffield's housing services being awarded a three star rating (the highest) by the Audit Commission.

Support Services markets and outlook

Whilst opportunities continue to emerge within the facilities management market for Kier Managed Services, we will continue to be selective in the contracts for which we bid.

In Building Maintenance both local authority expenditure, through housing repairs and maintenance budgets, and central government expenditure, through the Decent Homes initiative, are providing good potential for new work. A strong list of opportunities is emerging in the £10m to £40m per annum range and, although disappointingly, we were unsuccessful on a bid for Manchester, we have recently been confirmed as preferred bidder, subject to negotiations on the heads of terms, on a contract for Harlow. With a revenue stream of £17m per annum this contract will provide repairs and maintenance to housing stock, street scene works and grounds maintenance. In addition, we have been confirmed as preferred bidder on a £6.5m per annum contract in Southwark and have been short listed as one of three on a £35m per annum repairs and maintenance contract for Stoke.

With our proven ability to fulfil these higher value contracts, we are well placed to secure further work in this area.

Homes

Kier Residential, our housebuilding division, was structured through four companies during the year: Allison Homes, which operates throughout Lincolnshire and north Cambridgeshire; Bellwinch Homes, with sites in the south and south east; Kier Homes, operating across the central belt of Scotland; and Twigden Homes, with activities in East Anglia and the West Midlands. In July 2006 we acquired Hugh Bourn Homes operating in North Lincolnshire, which has formed the basis of a fifth operating area.

Homes business review

Kier Residential experienced a changed pattern to the timing of unit sales in the year to 30 June 2006 with a greater bias towards the second half of the year than in 2005. Overall we sold 1,522 homes in the year, a 25% increase over 2005's 1,215 homes achieved from an 11% increase in outlets. Average selling prices of £180,100 (2005: £181,700) provided revenue of £274.2m from housing sales (2005: £220.8m). A land disposal, of part of a large site, generated a further £3.7m of revenue at a nominal profit of £0.1m. The slight reduction in average selling prices reflects a 2% reduction in unit size and an increase in the proportion of affordable housing sales from 12% of total sales in 2005 to 16% in 2006. Operating profit from housing sales increased by 26.1% to £41.5m (2005: £32.9m) at a margin of 15.1% on housing turnover (2005: 14.9%) in line with our targets for this business.

During the year £93.3m was spent on selective land purchases, including a significant amount on deferred terms, and at 30 June 2006 the land bank contained 5,863 units with planning consent (2005: 5,178 units) which, at 3.9 years worth of sales, is in line with our target holding of four years' unit sales. In addition to land with planning consent, we also hold approximately 12,000 units of strategic land, mostly under option. Strategic land is proving a valuable route for land acquisition as, historically, approximately 18% of our annual unit sales have originated from this process.

Continuing the theme of mixed-use and regeneration sites, Kier Residential is making good progress on remediating a former Anglian Water site near the centre of Peterborough. Kier Construction is carrying out the work, which, when completed, will provide a site for 550 residential units, comprising a combination of flats and houses. At Aylesbury, a former Kier Property site, sales targets are being achieved following remediation of the site adjacent to the station. Planning consent has now been granted at Poole Harbour, subject to signing the agreement for the Section 106 works, for redevelopment of a mixed-use site previously owned by Network Rail. Kier Construction will relocate the rail sidings and carry out other infrastructure works which, in time, will provide a development site for a new hotel, some 250 apartments, offices, shops and a new railway station.

In Sunbury, a development of 96 homes and a hotel is progressing on remediated land, in conjunction with Kier Property. Bellwinch is constructing three apartment blocks and Kier Property is building the 120 bedroom hotel. Our affordable housing business, Kier Partnership Homes, worked with Bellwinch to obtain a housing association contract for 48 units within the scheme.

On 31 July 2006 we acquired the shares in Hugh Bourn Homes for a total consideration of £53.3m, representing the market value of land, work in progress and other assets and liabilities. £20m was paid on completion, with the balance due in instalments on 2 July 2007 and 1 July 2008. Hugh Bourn Homes forms the foundation for a fifth trading division of Kier Residential, expanding its reach to the north of Allison Homes' operating area. The majority of the 1,197 residential plots we acquired with the business benefit from a combination of outline and detailed planning consent and included a small number of built and partially built units. In its first year of operation within Kier, Hugh Bourn Homes is expected to trade from 21 outlets.

Housing markets and outlook

The housing market saw its usual quietening during the holiday season in July and most of August, although there are clear signs that it has begun to pick up in recent weeks. Reservations during the new financial year, on a like for like basis, excluding the effects of the acquisition of Hugh Bourn Homes, are 46% ahead of the same period last year and, taking Hugh Bourn Homes into account, they are some 68% ahead of last year. This has given rise to an order book at 31 August 2006 some 45% ahead of the same time last year (38% excluding Hugh Bourn Homes).

We will be selling from approximately 27% more outlets during the year compared with last year and therefore we anticipate growth in unit sales for the full year of which 42% are already secure. Similar to 2006 we expect the balance of sales to be skewed towards the second half of the year.

We anticipate further land expenditure this financial year, in addition to the expenditure for Hugh Bourn Homes, in order to maintain our land bank at approximately four years' worth of sales.

Property

Our Property development business comprises activity across commercial, industrial, retail and mixed-use sectors largely on a non-speculative basis. It operates through Kier Ventures, a wholly owned subsidiary; and Kier Developments a joint venture with the Bank of Scotland.

Property business review

Kier Property has had another active year, cementing its position as one of the UK's leading commercial property developers. Despite the commercial property market in the UK experiencing high levels of investment demand, with investors chasing limited availability of stock, Kier Property acquired some 15 new sites during the year and crystallised considerable value on several existing properties through lettings, sales and obtaining planning consents.

Notwithstanding all this activity, the number of developments sold during the year fell resulting in a reduction in revenue from £62.2m in 2005 to £47.5m in 2006. Operating profit, similarly, reduced from £10.4m to £9.2m in the year, although operating margins moved ahead from 16.7% to 19.4%.

Kier Property has developed a portfolio that now totals over 5m sq ft of developments, with a prospective completed value of around £734m. The portfolio offers a diverse spread of office, retail and mixed-use schemes with a particular commitment to regeneration. In December 2005, we acquired a £10m portfolio including nine sites from Warner Estates. One of the sites, in Lincoln, has planning consent for residential use on which Allison Homes has commenced the infrastructure works for a major residential development. Remaining sites include a mixture of short-term and long-term developments across all sectors and we will work through the portfolio to maximise value.

During the year, Kier Property continued to augment its industrial portfolio, with the successful 'Trade City' brand as a platform. A 2.9 acre site on London's North Circular Road was acquired for a 115,000sq ft scheme, of which almost an acre is expected to be sold to a self-storage company. An 11 acre former British Gas site in Uxbridge was also purchased and is being remediated by Kier Construction ahead of a 215,000sq ft employment-led mixed-use scheme. At our Crown Road scheme in Enfield, the first phase was pre-let and completed during the year, comprising a 20,000sq ft Renault car showroom and a 50,000sq ft Selco builders' merchant. The scheme was then sold to a financial institution at a very satisfactory yield. We have now secured planning permission for a second, 80,000sq ft phase at the site and work will begin during the coming year.

At our Loughton development the prime site was sold to Sytner for a BMW car showroom and the remainder of the site was developed into a new office for Kier Regional's operating business, Kier London.

In the offices portfolio, Kier Property continued to establish itself as one of the foremost players in the pre-let development arena. During the year, Kier Property was selected as preferred developer to deliver a new head office for Ordnance Survey in Southampton. Kier Regional will build the new 145,000sq ft head office on a new site with Kier Building Services Engineers carrying out the mechanical and electrical installation. Kier Managed Services will then provide the facilities management services when it is complete. This will enable Kier Property to work up Ordnance Survey's existing twenty-five acre site into a major regeneration project comprising 10 acres of employment use and over 400 homes, to be developed with Kier Residential.

A further pre-let office scheme was signed during the year to develop a new 140,000sq ft head office campus for global IT company Electronic Data Systems. Work has begun on phase one of the £35m scheme with Kier Regional as the contractor.

On other regeneration projects, Kier Regional has begun work on a mixed-use redevelopment of the former Shippams food factory in Chichester. The scheme will include 45,000sq ft of retail space, most of which has been let to high street retailers, and a residential development of 165 flats the land for which has been sold to a house builder during the year.

In March 2006 we secured planning for a new 175,000sq ft produce and flower hall at the Western International Market near Heathrow. On completion of the new facility, we will develop a 300,000sq ft distribution scheme on the old market site.

Property markets and outlook

Looking ahead, major schemes such as the three-phase, 600,000 sq ft Reading Central office development and a 800 home regeneration site close to Ashford Town centre will gather pace and we anticipate further growth in the business through both acquisitions and enhancement of existing properties.

We are particularly pleased to have been selected as preferred bidder for the new UK Supreme Court in London's Parliament Square. Planning consent has recently been granted and work is expected to commence in spring 2007.

Infrastructure Investment

Kier Project Investment (KPI) manages the Group's interests procured under PFI. The core strength of KPI is the ability to bring together the diverse range of skills and resources within the Group and combine these with a financial package that will deliver high quality buildings and services to meet the public sector's needs.

Infrastructure Investment business review

This has been another successful year for KPI, bringing our committed equity investment in the government's PFI to £22.8m and securing a further £230m of future turnover for the Group through associated construction and facilities management contracts.

Three projects reached financial close during the year: one health scheme, the Garrett Anderson Centre, a significant addition to the existing Ipswich Hospital; and two schools schemes providing six schools in Norwich for Norfolk County Council and two schools, for Oldham Metropolitan Borough Council. Construction work with a combined value of £120m is now under way by Kier Regional. Facilities management services will be provided by Kier Managed Services on completion of the buildings.

A contract to provide a new headquarters building in Gravesend for Kent Police reached financial close in July 2006. This new £32m facility will be constructed by Kier Regional.

Construction was successfully completed on a number of projects during the year. Eleven schools including two in Tendring, seven in Waltham Forest and two in Sheffield; Hinchingbrooke Hospital and Oldham Library were all handed over on time and Kier Managed Services commenced facilities management operations on each of these new facilities. Construction continues on two further schools in Sheffield.

We were disappointed not to have been selected for either of the 'Building Schools for the Future' (BSF) projects for which we were bidding. BSF has been a costly exercise for us and we have written off costs of £2.2m in the two years to 30 June 2006. However, we are not ruling out BSF projects and our Construction companies remain keen to pursue the construction opportunities.

Infrastructure Investment markets and outlook

The PFI market continues to provide sensible opportunities for our businesses in the key sectors in which we operate. Our strategy continues to be to invest in PFI opportunities that provide the Group either with the construction work or the facilities management contracts, and preferably both. As a Group we can tackle a wide range of sectors from hospitals and schools to street services, which provides us with a broad market and plenty of scope for new projects.

KPI is currently short-listed, supported by other Group companies, on bids for the Three Counties Police Investigation Centres project in East Anglia and the Leicester Hospitals scheme.

Pensions

At 30 June 2006 the net pension deficit shown on the balance sheet, calculated as required by IAS 19 'Employee Benefits', is £42.1m (June 2005: £85.3m). The movement in the year includes special contributions, amounting to £31.5m, paid into the pension scheme in the last quarter of the financial year. These contributions form part of a schedule of payments designed to eliminate the pension scheme deficit over 10 years. A further £5.0m was contributed in July 2006 and the Group is making further special contributions of £0.5m per month. These contributions are in addition to a special contribution of £12.0m made in March 2005, bringing the total payments to the scheme, over and above normal contributions, to £43.5m in the two years to 30 June 2006.

The special contributions have no effect on the income statement for the year, but are shown as a reduction in cash and a reduction in the pension deficit.

Health & Safety

Kier has continued to build on the positive approach to health and safety valued in all of our employees and supply chain members. This approach, together with our "Don't Walk By" campaign and continuing focus on behavioural issues, has created a proactive approach identifying and correcting health and safety issues. By addressing the risk and not the symptom, Kier has brought about significant reductions in its Accident Incidence Rate, which now stands at 522 per 100,000 staff and subcontractors, comparing favourably with the Health & Safety Executive benchmark of 902.

In recognition, the Group received nine gold, two silver, and one bronze award from RoSPA and seven British Safety Council Awards.

Through their positive, proactive attitude, our staff and supply chain work tirelessly to reduce the potential for accidents to happen, and to protect the long-term health of those working on Kier sites. The roll-out of the ISO 18001/14001 registration programme has ensured that already high standards and levels of awareness continue to be raised and the third party audit carried out by BSI ensures that the Group continues to deliver best practice. This continuing improvement approach culminated in Kier Group being awarded the highly coveted Quality in Construction Health and Safety Management Award 2006.

People

The success and reputation of a business is a reflection of the quality of the people who work together to form it. We have many excellent, committed and enthusiastic people in this Group. Whether we are building a tunnel, servicing an office, changing a boiler or grappling with a complex planning issue, the wealth of talent in this Group to bring any project to fruition is immense. I am very proud of what this Group can achieve and I also sense a great pride in our employees: pride, not just for the work they are doing, but as employees of Kier. I should like to thank all of our employees for their continuing contribution to making Kier Group the success it is today.

Objectives and prospects

The year to 30 June 2006 has seen the Group firing on all cylinders and our objective for the new financial year is to maintain this momentum and to continue to provide clients with a high quality service.

Our Construction order books at 30 June 2006 were at the highest level ever and, with a strong pipeline of virtually secure work, our Construction division is in an excellent position to grow further. In Support Services the market for local authority outsourcing contracts continues to expand. Our housing land bank contains sites of good quality in saleable locations and we anticipate an increase in unit sales for Kier Residential this year enhanced by the acquisition of Hugh Bourn Homes which provides us with a new operating area. Our Property portfolio contains a range of development sites that will continue to be enhanced in value, and in Infrastructure Investment we can see a number of good projects coming forward.

Opportunities for our businesses to work together are becoming more prolific as complex planning issues continue to require resolution and clients' requirements become more intricate.

Against this backdrop, the prospects for the Group are excellent and I am confident that we will continue to deliver further growth in 2007 and thereafter.

Financial Review

International Financial Reporting Standards (IFRS)

These are the Group's first annual consolidated financial statements prepared in accordance with IFRS.

The Group's IFRS accounting policies have been applied in preparing the consolidated financial statements for the year to June 2006, the comparative information for the year to 30 June 2005 and the preparation of an opening IFRS balance sheet at 1 July 2004 (the date of transition from UK GAAP to IFRS).

Profit before tax

Profit before tax increased by 23.6% to £59.1m (2005: £47.8m). This is stated after deducting joint venture tax of £1.4m (2005: £1.2m) and before the exceptional profits of £6.7m recorded in the year to 30 June 2005. The exceptional profits in 2005 included: £0.8m on the sale of the Group's remaining interest in Kier Hong Kong Limited; £3.8m on the sale of a property fixed asset; and £2.1m on the sale of the Group's interest in a PFI concession.

Taxation

The Group's effective tax rate, including joint venture tax on joint venture profits, is 29.0%. This compares with an effective rate of 34.3% in 2005. However, the effective tax rate for the year to 30 June 2005 included £2.5m of exceptional tax relating to refinancing one of the Group's PFI concessions, for which no profit was recognised; and £1.8m relating to exceptional items. Disregarding the exceptional items, the 2005 effective rate, including joint venture tax on joint venture profit, was 30.2%.

The reduction to 29.0% largely reflects the utilisation of some brought forward capital losses and tax benefits relating to contaminated land remediation.

Interest and cash

The interest charge for the year comprises the following:-

	Years to 30 June	
	2006	2005
	£m	£m
Group interest receivable	5.3	4.0
Interest payable	(2.8)	(2.5)
Unwinding of discount	(2.6)	(2.7)
Share of joint venture interest	(2.6)	(3.1)
	(2.7)	(4.3)

The Group interest receivable arises from average treasury balances of £60m for the year. The charge of £2.6m relating to unwinding of discounts includes £2.0m relating to land creditor balances payable over a number of years (2005: £2.1m).

Net cash at 30 June 2006 was £111.2m (2005: £58.1m) after deducting £30.1m relating to loan notes. £96.6m was generated from operations during the year after deducting £31.5m in respect of the special pension contributions made during the year.

Cash, net of debt, at 30 June 2006, includes £37.6m (2005: £22.8m) of cash which is not generally available for Group purposes, including that held by joint arrangements, overseas and by the Group's captive insurance company. The liquid cash position is affected by seasonal, monthly and contract-specific cycles. In order to accommodate these flows the Group maintains a range of bank facilities which were increased by £40.0m during the year. The facilities at 30 June 2006, of £120.0m, comprise £12.5m of overdraft facilities, and £107.5m of committed, revolving credit facilities all on an unsecured basis. £15.0m of this expires in January 2007 and £92.5m expires in January 2011.

Treasury policy and risk management

The Group has a centralised treasury function which manages funding, liquidity and financial risks. The Group's policy is to use the cash generated by the Construction business to invest in the asset based homes and property businesses. This financial model is supplemented with bank facilities amounting to £120m and long term debt of £30m.

The Group's financial instruments comprise cash and liquid investments. The Group, largely through its PFI and Property joint ventures, enters into derivatives transactions (principally interest rate swaps) to manage interest rate risks arising from the Group's operations and its sources of finance. We do not enter into speculative transactions.

There are minor foreign currency risks arising from operations. The Group has a small number of branches and subsidiaries operating overseas in different currencies. Currency exposure to overseas assets is hedged through inter-company balances and borrowings, such that assets denominated in foreign currencies are matched, as far as possible, by liabilities. Where there may be further exposure to foreign currency fluctuations, forward exchange contracts are entered into to buy and sell foreign currency.

Balance sheet and shareholders' funds

The balance sheet at 30 June 2006 includes intangible assets of £14.8m of which £9.6m relates to the outsourcing contract at Sheffield which is being amortised over ten years, being the life of the contract, with £1.9m (2005: £1.9m) charged to profits in the year.

Shareholders' funds have more than doubled during the year to £108.5m (2005: £52.8m) arising from retained profits of £42.9, dividends of £(8.3)m, currency translation of £(0.3)m, movement in the share scheme reserve of £0.7m, movement in the net pension deficit of £21.0m, issue of shares of £2.1m and the introduction of IAS 32 and 39 this financial year, which has a £(2.4)m impact.

Pensions

The Group participates in two principal schemes, the Kier Group Pension Scheme, which includes a defined benefit section, and a defined benefit scheme on behalf of its employees in Kier Sheffield LLP. The financial statements reflect the pension scheme deficits and surpluses calculated in accordance with IAS 19. At 30 June 2006 the net deficit under the Kier Group Pension Scheme was £46.9m (2005: £86.6m). The market value of the schemes' assets was £467.0m (2005: £393.5m) and the net present value of the liabilities was £534.0m (2005: £517.2m). £31.5m of the movement in asset value related to the special contributions made to the pension scheme during the year.

Under the scheme relating to Kier Sheffield LLP there was a net surplus of £4.8m at 30 June 2006 (2005: £1.3m).

Pension charges of £16.9m (2005: £15.3m) have been made to the income statement in accordance with IAS 19.

Consolidated income statement
for the year ended 30 June 2006

	Notes	**2006 £m**	2005 £m
Revenue - continuing operations			
Group and share of joint ventures	2	**1,838.3**	1,623.2
Less share of joint ventures		**(55.1)**	(50.2)
Group revenue		**1,783.2**	1,573.0
Cost of sales		**(1,623.7)**	(1,433.8)
Gross profit		**159.5**	139.2
Administrative expenses		**(103.5)**	(91.1)
Share of post tax profits from joint ventures		**3.2**	0.9
Profit from operations	2	**59.2**	49.0
Other non-operating income (exceptional items)	3	**–**	6.7
Finance income		**5.3**	4.0
Finance cost		**(5.4)**	(5.2)
Profit before tax	2	**59.1**	54.5
Income tax	4	**(16.2)**	(17.9)
Profit for the year		**42.9**	36.6
Earnings per ordinary share	6		
– basic		**120.8p**	103.4p
– diluted		**118.8p**	102.5p
Underlying earnings per ordinary share (excluding other non-operating income - exceptional items)			
– basic		**120.8p**	96.6p
– diluted		**118.8p**	95.8p

Consolidated statement of recognised income and expense
for the year ended 30 June 2006

	Notes	**2006 £m**	2005 £m
Foreign exchange translation differences		**(0.3)**	0.1
Fair value movements in cash flow hedging instruments		**4.1**	–
Actuarial gains and losses on defined benefit pension schemes		**30.0**	(41.5)
Deferred tax on items recognised directly in equity		**(10.2)**	12.5
Income and expense recognised directly in equity		**23.6**	(28.9)
Profit for the year		**42.9**	36.6
Total recognised income and expense for the year		**66.5**	7.7
Change in accounting policy			
Effect of adoption of IAS 32 and IAS 39 on 1 July 2005 (with June 2005 not restated) on cash flow hedge reserve		**(7.5)**	–
Deferred tax on above		**2.2**	–
		61.2	7.7

Consolidated balance sheet

at 30 June 2006

	Notes	2006 £m	2005 £m
Non-current assets			
Intangible assets		**14.8**	16.7
Property, plant and equipment		**78.5**	75.8
Investment in joint ventures		**20.8**	22.9
Retirement benefit surplus		**6.8**	1.8
Deferred tax assets		**20.9**	38.3
Other financial assets		**0.6**	–
Trade and other receivables		**16.1**	14.6
Non-current assets		**158.5**	170.1
Current assets			
Inventories		**377.8**	325.7
Other financial assets		**0.6**	–
Trade and other receivables		**258.4**	233.3
Cash and cash equivalents		**141.3**	93.5
Current assets		**778.1**	652.5
Total assets		**936.6**	822.6
Current liabilities			
Bank overdrafts and loans		**–**	(5.3)
Trade and other payables		**(670.5)**	(566.5)
Tax liabilities		**(2.7)**	(9.5)
Provisions		**(0.9)**	(1.2)
Current liabilities		**(674.1)**	(582.5)
Non-current liabilities			
Long-term borrowings		**(30.1)**	(30.1)
Trade and other payables		**(36.8)**	(17.2)
Retirement benefit obligations		**(67.0)**	(123.7)
Provisions		**(18.1)**	(16.3)
Deferred tax liabilities		**(2.0)**	–
Non-current liabilities		**(154.0)**	(187.3)
Total liabilities		**(828.1)**	(769.8)
Net assets	2	**108.5**	52.8
Equity			
Share capital		**0.4**	0.4
Share premium		**20.0**	17.9
Capital redemption reserve		**2.7**	2.7
Retained earnings		**88.0**	31.7
Cash flow hedge reserve		**(2.4)**	–
Translation reserve		**(0.2)**	0.1
Total equity	7	**108.5**	52.8

Consolidated cash flow statement

for the year ended 30 June 2006

		Notes	2006 £m	2005 £m
Cash flows from operating activities				
Profit before tax			**59.1**	54.5
Adjustments	Other non-operating income (exceptional items)		–	(6.7)
	Share of post tax profits from joint ventures		**(3.2)**	(0.9)
	Normal contributions to pension fund in excess of pension charge		**(0.2)**	(0.1)
	Share-based payments charge		**1.1**	0.6
	Amortisation of intangible assets		**1.9**	1.9
	Depreciation charges		**13.5**	12.3
	Profit on disposal of property, plant & equipment		**(1.1)**	(0.5)
	Net finance cost		**0.1**	1.2
Operating cash flows before movements in working capital			**71.2**	62.3
Special contributions to pension fund			**(31.5)**	(12.0)
(Increase)/decrease in inventories			**(49.3)**	19.7
Increase in receivables			**(26.7)**	(16.7)
Increase in payables			**131.8**	31.3
Increase in provisions			**1.1**	1.8
Cash inflow from operating activities			**96.6**	86.4
Interest received			**5.3**	3.7
Income taxes paid			**(11.3)**	(12.8)
Net cash generated from operating activities			**90.6**	77.3
Cash flows from investing activities				
Proceeds from sale of property, plant & equipment			**4.6**	6.0
Proceeds from sale of investments			**1.4**	5.8
Refinancing of PFI joint venture			–	8.1
Dividends received from joint ventures			**1.3**	0.4
Purchases of property, plant & equipment			**(23.2)**	(19.9)
Acquisition of subsidiaries			**(10.1)**	(16.5)
Investment in joint ventures			**(0.6)**	(1.5)
Net cash used in investing activities			**(26.6)**	(17.6)
Cash flows from financing activities				
Proceeds from the issue of share capital			–	0.2
Purchase of own shares			**(2.0)**	(0.4)
Interest paid			**(2.7)**	(2.6)
Dividends paid			**(6.2)**	(6.4)
Net cash used in financing activities			**(10.9)**	(9.2)
Net increase in cash and cash equivalents			**53.1**	50.5
Opening net cash and cash equivalents			**88.2**	37.7
Closing net cash and cash equivalents			**141.3**	88.2
Reconciliation of net cash flow to movement in net funds				
Net increase in cash and cash equivalents			**53.1**	50.5
Opening net funds			**58.1**	7.6
Closing net funds			**111.2**	58.1
Net funds consist of:				
Cash and cash equivalents			**141.3**	93.5
Overdrafts			–	(5.3)
Net cash and cash equivalents			**141.3**	88.2
Long-term borrowings			**(30.1)**	(30.1)
Net funds			**111.2**	58.1

Cash and cash equivalents includes £12.6m (2005: £6.2m) being the Group's share of cash held by joint arrangements and £25.0m (2005: £16.6m) of cash not readily available to the Group.

Notes to the Consolidated Financial Statements

1. Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards as adopted for use in the EU (IFRS).

As these are the first annual financial statements of the Group to be prepared under IFRS, the significant accounting policies that have been applied in the preparation of the financial statements are detailed in note 8.

2 Turnover, profit and segmental information

For management purposes the Group is organised into five operating divisions, Construction, Support Services, Homes, Property and Infrastructure Investment. These divisions are the basis on which the Group reports its primary segmental information.

	Construction £m	Support Services £m	Homes £m	Property £m	Infrastructure Investment £m	Centre £m	Group £m
Year to 30 June 2006							
Revenue							
Group and share of joint ventures	**1,218.1**	**281.3**	**277.9**	**47.5**	**13.5**	**–**	**1,838.3**
Less share of joint ventures	(2.6)	–	–	(40.0)	(12.5)	–	**(55.1)**
Group revenue	1,215.5	281.3	277.9	7.5	1.0	–	**1,783.2**
Profit							
Group operating profit	17.2	6.8	41.6	4.2	(2.1)	(11.7)	**56.0**
Share of joint ventures' operating profit	0.8	–	–	5.0	1.4	–	**7.2**
Group and share of joint ventures	**18.0**	**6.8**	**41.6**	**9.2**	**(0.7)**	**(11.7)**	**63.2**
Share of joint ventures – finance cost	–	–	–	(2.1)	(0.5)	–	**(2.6)**
– tax	(0.1)	–	–	(0.8)	(0.5)	–	**(1.4)**
Profit from operations	17.9	6.8	41.6	6.3	(1.7)	(11.7)	**59.2**
Finance income/(cost)	13.7	(0.5)	(13.1)	(0.9)	1.2	(0.5)	**(0.1)**
Profit before tax	**31.6**	**6.3**	**28.5**	**5.4**	**(0.5)**	**(12.2)**	**59.1**
Balance sheet							
Investment in joint ventures	–	–	–	21.7	(0.9)	–	**20.8**
Other assets	281.3	77.3	351.1	22.9	0.8	41.1	**774.5**
Total liabilities	(496.6)	(78.2)	(112.3)	(5.2)	(3.2)	(102.5)	**(798.0)**
Net operating assets/(liabilities)	(215.3)	(0.9)	238.8	39.4	(3.3)	(61.4)	**(2.7)**
Cash, net of debt	298.7	12.5	(165.8)	(23.8)	(3.8)	(6.6)	**111.2**
Net assets	**83.4**	**11.6**	**73.0**	**15.6**	**(7.1)**	**(68.0)**	**108.5**
Year to 30 June 2005							
Revenue							
Group and share of joint ventures	1,086.3	237.4	225.5	62.2	11.8	–	1,623.2
Less share of joint ventures	(7.3)	–	–	(32.0)	(10.9)	–	(50.2)
Group revenue	1,079.0	237.4	225.5	30.2	0.9	–	1,573.0
Profit							
Group operating profit	14.2	5.0	32.9	5.6	(1.7)	(7.9)	48.1
Share of joint ventures' operating profit	(0.4)	–	–	4.8	0.8	–	5.2
Group and share of joint ventures	13.8	5.0	32.9	10.4	(0.9)	(7.9)	53.3
Share of joint ventures – finance cost	–	–	–	(2.2)	(0.9)	–	(3.1)
– tax	0.1	–	–	(0.8)	(0.5)	–	(1.2)
Profit from operations	13.9	5.0	32.9	7.4	(2.3)	(7.9)	49.0
Other non-operating income (exceptional items)	0.8	–	–	–	2.1	3.8	6.7
Finance income/(cost)	11.5	(1.1)	(11.5)	(0.6)	1.1	(0.6)	(1.2)
Profit before tax	26.2	3.9	21.4	6.8	0.9	(4.7)	54.5
Balance sheet							
Investment in joint ventures	1.6	–	–	20.1	1.2	–	22.9
Other assets	243.5	77.3	320.2	11.5	0.6	53.1	706.2
Total liabilities	(431.2)	(66.2)	(74.6)	(7.2)	(3.5)	(151.7)	(734.4)
Net operating assets/(liabilities)	(186.1)	11.1	245.6	24.4	(1.7)	(98.6)	(5.3)
Cash, net of debt	258.2	(2.1)	(185.5)	(12.6)	(2.0)	2.1	58.1
Net assets	72.1	9.0	60.1	11.8	(3.7)	(96.5)	52.8

2 Turnover, profit and segmental information continued

The 30 June 2005 segmental information for Construction and Support Services has been restated to reflect the reclassification of Kier Plant from Construction to Support Services to align segmental reporting with the Group's management and internal reporting structure. This has increased revenue by £9.9m and operating profit by £1.8m in Support Services with a corresponding reduction in Construction.

Net operating assets represent assets excluding cash, bank overdrafts, long-term borrowings and interest-bearing inter-company loans.

3. Other non-operating income (exceptional items)

For the purpose of these financial statements the term other non-operating income and exceptional items are interchangeable where they relate to the prior year.

Exceptional items for the year to 30 June 2005 arose from the following:

	Profit before tax £m	Tax £m	Net profit/(loss) £m
Disposal of investment in Kier Hong Kong Limited	0.8	–	0.8
Disposal of investment in a PFI joint venture	2.1	(0.6)	1.5
Refinancing of a PFI joint venture	–	(2.5)	(2.5)
Disposal of a property held in property, plant and equipment	3.8	(1.2)	2.6
	6.7	(4.3)	2.4

4. Income tax

Recognised in the income statement

	2006 £m	2005 £m
Current tax expense		
UK corporation tax : current year on profit before exceptional items	**7.6**	11.7
: on exceptional items	**–**	4.3
Overseas tax	**0.8**	0.3
Adjustments for prior years	**(3.9)**	0.4
Total current tax	**4.5**	16.7
Deferred tax expense		
Origination and reversal of temporary differences	**7.2**	1.6
Adjustments for prior years	**4.5**	(0.4)
Total deferred tax	**11.7**	1.2
Total income tax expense in the income statement	**16.2**	17.9
Reconciliation of effective tax rate		
Profit before tax	**59.1**	54.5
Add : tax on joint ventures	**1.4**	1.2
Underlying profit before tax	**60.5**	55.7
Income tax at UK corporation tax rate of 30%	**18.2**	16.7
Tax on refinancing of a PFI joint venture	**–**	2.5
Non deductible expenses	**0.5**	0.5
Tax reliefs not recognised in the income statement	**(1.4)**	–
Capital items not taxable	**–**	(0.5)
Effect of tax losses utilised	**–**	(0.2)
Effect of tax rates in foreign jurisdictions	**–**	0.1
Under provision in respect of prior years	**0.3**	–
Total tax (including joint ventures)	**17.6**	19.1
Tax on joint ventures	**(1.4)**	(1.2)
Group income tax expense	**16.2**	17.9

Notes to the Consolidated Financial Statements continued

5. Dividends

Amounts recognised as distributions to equity holders in the year.

	2006 £m	2005 £m
Final dividend for the year ended 30 June 2005 of 15.2 pence (2004: 13.0 pence)	**5.4**	4.6
Interim dividend for the year ended 30 June 2006 of 8.2 pence (2005: 7.0 pence)	**2.9**	2.5
	8.3	7.1

The proposed final dividend of 17.8 pence (2005: 15.2 pence) had not been approved at the balance sheet date and so has not been included as a liability in these financial statements. The dividend totalling £6.3m will be paid on 5 December 2006 to shareholders on the register at the close of business on 29 September 2006. A scrip dividend alternative will be offered.

6. Earnings per share

A reconciliation of profit and earnings per share, as reported in the income statement, to underlying and adjusted profit and earnings per share is set out below. The adjustments are made to illustrate the impact of exceptional items and the amortisation of intangible assets.

	2006		2005	
	Basic £m	**Diluted £m**	Basic £m	Diluted £m
Profit for the year	**42.9**	**42.9**	36.6	36.6
Less : exceptional items	**–**	**–**	(6.7)	(6.7)
Add : tax on exceptional items	**–**	**–**	4.3	4.3
Underlying profit	**42.9**	**42.9**	34.2	34.2
Add : amortisation of intangible assets	**1.9**	**1.9**	1.9	1.9
Less : tax on amortisation of intangible assets	**(0.5)**	**(0.5)**	(0.6)	(0.6)
Adjusted profit	**44.3**	**44.3**	35.5	35.5
	million	**million**	million	million
Weighted average number of shares	**35.5**	**35.5**	35.4	35.4
Weighted average number of unexercised options – dilutive effect	**–**	**0.3**	–	0.1
Weighted average impact of LTIP	**–**	**0.3**	–	0.2
Weighted average number of shares used for EPS	**35.5**	**36.1**	35.4	35.7
	pence	**pence**	pence	pence
Earnings per share	**120.8**	**118.8**	103.4	102.5
Underlying earnings per share (excluding exceptional items)	**120.8**	**118.8**	96.6	95.8
Adjusted earnings per share (excluding exceptional items and amortisation of intangible assets)	**124.8**	**122.7**	100.3	99.4

7. Reconciliation of changes in shareholders equity

	2006 £m	2005 £m
Opening shareholders' equity	**52.8**	51.2
Adjustments on adoption of IAS 32 and IAS 39 on 1 July 2005 (net of tax)	**(5.3)**	–
Restated opening shareholders' equity	**47.5**	51.2
Recognised income and expense for the year	**66.5**	7.7
Dividends paid	**(8.3)**	(7.1)
Issue of own shares	**2.1**	0.8
Purchase of own shares	**(2.0)**	(0.4)
Share-based payments	**1.1**	0.6
Deferred tax on share-based payments	**1.6**	–
Closing shareholders' equity	**108.5**	52.8

8. Significant accounting policies

Kier Group plc (the 'Company') is a company domiciled in the United Kingdom (UK). The consolidated financial statements of the Company for the year ended 30 June 2006 comprise the Company and its subsidiaries (together referred to as the 'Group') and the Group's interest in jointly controlled entities.

Statement of compliance
The Group's consolidated financial statements have been prepared in accordance with IFRS.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance, and cash flows of the Group, and reconciliations of total equity and profit for the comparative period reported under UK Generally Accepted Accounting Practice (GAAP) to those reported under IFRS was published in the 2005 Annual Report and is available on the Group's website at www.kier.co.uk.

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Group's financial statements with the exception of certain policies subject to the transitional arrangements of IFRS, as detailed below.

8. Significant accounting policies continued

The financial statements are presented in pounds sterling. They have been prepared on the historical cost basis except for derivative financial instruments which are stated at their fair value and certain payables on extended terms which are stated at discounted cost.

Basis of preparation
In March 2005, the International Financial Reporting Interpretations Committee (IFRIC) issued draft guidance on accounting for service concession arrangements (drafts D12 to D14). IFRIC are currently considering the comments received on this draft guidance, with the final guidance expected to be issued in late 2006. Until the final guidance is issued and endorsed by the EU and in absence of specific guidance within IFRS, the Group has continued to account for Private Finance Initiative (PFI) assets in the same way as previously accounted for under UK GAAP. This measures PFI contract assets (i.e. property, plant and equipment and finance debtors) on the basis of historical cost. However following the introduction of IAS 32 'Financial Instruments: Disclosure and Presentation' and IAS 39 'Financial Instruments: Recognition and Measurement', the interest rate swaps held by the PFI joint ventures for the purpose of hedging floating rate liabilities are measured at fair value both initially and subsequently. If the IFRIC draft interpretations are finalised in the current form, to the extent that PFI contract assets are recognised as financial assets (finance debtors) they also may be measured initially and subsequently at fair value.

In addition at the date of issue of these financial statements the following standards and interpretations, which have not been applied in these financial statements, were in issue but not yet effective:

IFRS 6	Explorations for and Evaluation of Mineral Resources.
IFRS 7	Financial Instruments: Disclosures: and the related amendments to ISA 1 'Presentation of Financial Statements' on capital disclosures.
IFRS 39	Amendments to fair value option, forecast intra-group transactions and financial guarantee contracts.
IFRIC 4	Determining whether an Arrangement contains a lease.
IFRIC 5	Right to Interest Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds.
IFRIC 8	Scope of IFRS 2
IFRIC 9	Reassessment of Embedded Derivatives

The directors anticipate that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements of the Group, except for additional disclosures on capital and financial instruments when the relevant standards come into effect for periods commencing on or after 1 January 2007.

Transition to IFRS
IFRS 1 'First-time Adoption of International Financial Reporting Standards' sets out the procedures that the Group must follow when it adopts IFRS for the first time as the basis for preparing its consolidated financial statements.

The Group is required to establish its IFRS accounting policies as at 30 June 2006 and, in general, apply these retrospectively to determine the IFRS opening balance sheet at its date of transition, 1 July 2004.

IFRS 1 provides a number of optional exemptions to this general principle. The most significant of these are set out below together with a description, in each case, of the exemption adopted by the Group.

Business combinations that occurred before the opening IFRS balance sheet date
The Group has elected not to apply IFRS 3 'Business Combinations' retrospectively to business combinations that took place before the date of transition. As a result, in the opening balance sheet, goodwill arising from past business combinations of £5.2m remains as stated under UK GAAP at 1 July 2004.

Employee benefits – actuarial gains and losses
The Group has elected to recognise all cumulative actuarial gains and losses in relation to employee benefit schemes at the date of transition. The Group has chosen to early adopt the amendments to IAS 19 'Employee Benefits' and has recognised actuarial gains and losses in full directly to reserves via the statement of recognised income and expense in the period in which they occur.

Share-based payments
The Group has elected to apply IFRS to relevant share-based payment transactions only where rights were granted after 7 November 2002 and not vested as at 1 January 2005.

Financial instruments
The Group has taken advantage of the exemption in IFRS 1 that enables the Group to apply IAS 32 and IAS 39 from 1 July 2005 only, with no restatement for prior periods. A reconciliation of total equity at 1 July 2005 following the adoption of IAS 32 and IAS 39 is given in note 7.

Cumulative translation differences
The Group has elected to set the previously accumulated translation differences relating to investments in overseas subsidiaries to zero at 1 July 2004.

Basis of consolidation
(a) Subsidiaries
The consolidated financial statements comprise the financial statements of the Company and subsidiaries controlled by the Company drawn up to 30 June 2006. Control exists when the Group has direct or indirect power to govern the financial and operating policies of an entity so as to obtain economic benefits from its activities. Subsidiaries are included in the consolidated financial statements from the date that control transfers to the Group until the date that control ceases. The purchase method is used to account for the acquisition of subsidiaries.

(b) Joint ventures
A joint venture is a contractual arrangement whereby the Group undertakes an economic activity that is subject to joint control with third parties.

The Group's interests in jointly controlled entities are accounted for using the equity method. Under this method the Group's share of the profits less losses of jointly controlled entities is included in the consolidated income statement and its interest in their net assets is included in investments in the consolidated balance sheet. Where the share of losses exceeds the Group's interest in the entity and there is no obligation to fund these losses the carrying amount is reduced to nil and recognition of further losses is discontinued, future profits are not recognised until unrecognised losses are extinguished. Interest in the entity is the carrying amount of the investment together with any long-term interests that, in substance, form part of the net investment in the entity.

Where a Group company is party to a jointly controlled operation, that company accounts for the assets it controls, the liabilities and expenses it incurs and its share of the income. Such joint arrangements are reported in the consolidated financial statements on the same basis.

8. Significant accounting policies continued

Basis of consolidation continued

Goodwill and other intangible assets

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary or jointly controlled entity at the date of acquisition.

Goodwill is recognised as an asset and reviewed for impairment at least annually. Any impairment is recognised immediately in the income statement and is not subsequently reversed. Negative goodwill is recognised in the income statement immediately. On disposal of a subsidiary or jointly controlled entity, the attributable carrying amount of goodwill is included in the determination of the profit or loss on disposal.

Goodwill arising on acquisitions before 1 July 2004, being the date of transition to IFRS, has been retained at the previous UK GAAP amounts at 1 July 2004 subject to being tested for impairment. Goodwill written off to reserves under UK GAAP prior to 1998 has not been reinstated and is not included in determining any subsequent profit or loss on disposal.

Other intangible assets which comprise contract rights are stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to the income statement on a straight line basis over the relevant contract period.

Revenue and profit recognition

Revenue comprises the fair value of the consideration received or receivable, net of value added tax, rebates and discounts and after eliminating sales within the Group. It also includes the Group's proportion of work carried out under jointly controlled operations.

Revenue and profit are recognised as follows:

a) Private housing and land sales

Revenue from housing sales is recognised at the fair value of the consideration received or receivable on legal completion, net of incentives. Revenue from land sales and land exchanges is recognised on the unconditional exchange of contracts. Profit is recognised on a site by site basis by reference to the expected out-turn result from each site. The principal estimation technique used by the Group in attributing profit on sites to a particular period is the preparation of forecasts on a site by site basis. These focus on revenues and costs to complete and enable an assessment to be made of the final out turn on each site. Consistent review procedures are in place in respect of site forecasting.

b) Property development

Revenue in respect of property developments is taken on unconditional exchange of contracts on disposal of finished developments. Profit taken is subject to any amounts necessary to cover residual commitments relating to development performance. Provision is made for any losses foreseen in completing a development as soon as they become apparent.

Where developments are sold in advance of construction being completed, revenue and profit are recognised from the point of sale and as the significant outstanding acts of construction and development are completed.

(c) Construction contracts

Revenue arises from increases in valuations on contracts and includes the Group's share of revenue from joint arrangements, and goods and services provided.

Revenue is normally determined by external valuations and is the gross value of work carried out for the period to the balance sheet date (including retentions) but excludes claims until they are actually certified.

Profit on contracts is calculated in accordance with accounting standards and industry practice and may not relate directly to revenue. The principal estimation technique used by the Group in attributing profit on contracts to a particular period is the preparation of forecasts on a contract by contract basis. These focus on revenues and costs to complete and enable an assessment to be made of the final out-turn on each contract. Consistent contract review procedures are in place in respect of contract forecasting.

The general principles for profit recognition are:

- Profits on short duration contracts (generally less than 12 months) are taken when the contract is complete;
- Profits on other contracts are recognised on a percentage of completion basis when the contract's outcome can be foreseen with reasonable certainty;
- Provision is made for losses incurred or foreseen in bringing the contract to completion as soon as they become apparent; and
- Claims receivable are recognised as income when received or certified for payment except that, in preparing contract forecasts to completion, a prudent and reasonable evaluation of claims receivable may be included to mitigate foreseeable losses but only to the extent that there is reasonable assurance of recovery.

Percentage completion is normally calculated by taking certified value to date as a percentage of estimated final value unless the adjusted value is materially different in which case the adjusted value is used.

Pre-contract costs

Costs associated with bidding for contracts are written off as incurred (pre-contract costs). When it is probable that a contract will be awarded, usually when the Group has secured preferred bidder status, external costs incurred from that date to the date of financial close are carried forward in the balance sheet.

When financial close is achieved on PFI or Public Private Partnership (PPP) contracts, external costs are recovered from the special purpose vehicle and pre-contract costs within this recovery that were not previously capitalised are credited to the income statement, except to the extent that the Group retains a share in the special purpose vehicle. The amount not credited is deferred and recognised over the life of the construction contract to which the costs relate.

8. Significant accounting policies continued

Property, plant and equipment and depreciation

Depreciation is based on historical or deemed cost, less the estimated residual value, and the estimated economic lives of the assets concerned. Freehold land is not depreciated. Other tangible assets are depreciated in equal annual instalments over the period of their estimated economic lives, which are principally as follows:

Freehold buildings	25-50 years
Leasehold buildings and improvements	Period of lease
Plant, equipment and vehicles	3-10 years

Assets held under finance leases are depreciated over the shorter of the term of the lease or the expected useful life of the asset.

Leases

Operating lease rental charges are charged to the income statement on a straight-line basis over the life of each lease.

Employee benefits

(a) Retirement benefit obligations

For defined contribution pension schemes operated by the Group, amounts payable are charged to the income statement as they fall due.

For defined benefit pension schemes, the cost of providing benefits is calculated annually by independent actuaries using the projected unit credit method. The charge to the income statement reflects the current and past service costs of such obligations, and the interest cost on scheme liabilities less the expected return on plan assets.

The retirement benefit obligation represents the difference between the fair value of scheme assets and the present value of scheme liabilities. It is determined bi-annually by independent actuaries and recognised in full in the balance sheet. Differences between the actual and expected returns on assets and experience gains and losses arising on scheme liabilities during the year, together with differences arising from changes in assumptions, are recognised in full directly to reserves via the statement of recognised income and expense in the year. In accordance with the transitional provisions of IFRS 1 cumulative actuarial gains and losses at 1 July 2004 are presented within the opening retained earnings reserve at that date.

The Group’s contributions to the schemes are paid in accordance with the rules of the schemes and the recommendation of the actuary.

(b) Share-based payments

In accordance with the transitional provisions, IFRS 2 ‘Share-based payments’ has been applied for all payments granted after 7 November 2002. This requires that share-based payments granted after that date, but not vested, should be valued at the fair value of the shares at the date of grant. This affects the Sharesave and Long-Term Incentive Plan (LTIP) schemes. The fair value of these schemes at date of award is calculated using the Black Scholes model.

The cost to the Group of awards to employees under the LTIP scheme is spread on a straight line basis over the relevant performance criteria period. The scheme awards to senior employees a number of shares which will vest after three years if particular criteria are met. The award may be taken either as shares or as a combination of shares and cash based on the share price prevailing when the shares vest. The cost of the share-based payment element of the scheme is based on the market value of the shares at the date the options are granted, and the cost of the cash based payment element is based on the market value of the share options at the balance sheet date.

Shares purchased and held in trust in connection with the Group’s share schemes are deducted from retained earnings. No gain or loss is recognised within the income statement on the market value of these shares compared to the original cost.

Finance income and costs

Interest receivable and payable on bank deposits is credited or charged to the income statement as incurred.

Borrowing costs are capitalised where the Group constructs qualifying assets and has separately identifiable funding. All other borrowing costs are written off to the income statement as incurred.

Borrowing costs incurred within the Group’s jointly controlled entities relating to the construction of assets in PFI and PPP projects are capitalised until the relevant assets are brought into operational use.

Notional interest payable, representing the unwinding of the discount on long-term liabilities, is charged to finance costs.

Infrequently a long-term land creditor arises for a parcel or parcels of land where the Group has exchanged unconditional contracts, and so recognised the creditor and the land inventory, but in practice does not have title or access to the land. In these few cases the notional interest payable already charged to finance costs is then credited to finance costs and added to the cost of inventory in accordance with IAS 23 ‘Borrowing Costs’ and IAS 2 ‘Inventories’. In no circumstances will the cost of such land inventory exceed the contracted sum payable.

Taxation

Income tax comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is also recognised in equity.

Current tax is the expected tax payable on taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

8. Significant accounting policies continued

Foreign currencies
Transactions denominated in foreign currencies are recorded at the exchange rates in effect when they take place. Resulting foreign currency denominated assets and liabilities are translated at the exchange rates ruling at the balance sheet date. Exchange differences arising from foreign currency transactions are reflected in the income statement.

The assets and liabilities of overseas subsidiary undertakings are translated at the rate of exchange ruling at the balance sheet date. Trading profits or losses are translated at average rates prevailing during the accounting period. Differences on exchange arising from the retranslation of net investments in overseas subsidiary undertakings at the year-end rates are recognised in the translation reserve. All other translation differences are reflected in the income statement.

In accordance with the transitional provisions of IFRS 1 the Group has elected to set the previously accumulated translation differences relating to investments in overseas subsidiary undertakings to zero at 1 July 2004.

Mining assets
Opencast expenditure incurred prior to the commencement of operating opencast sites is capitalised and the cost less the residual value is depreciated over the coaling life of the site on a coal extraction basis. The total cost of restoration is recognised as a provision as soon as the mine becomes operational. The amount provided represents the present value of the anticipated costs. Costs are charged against the provision as incurred and the unwinding of the discount is included within interest costs. A tangible asset is created for an amount equivalent to the initial provision and depreciated on a coal extraction basis over the life of the asset.

Inventories
Inventories and work in progress, including land held for and in the course of development, are valued at the lower of cost and net realisable value. Cost comprises direct materials and, where appropriate, labour and production overheads which have been incurred in bringing the inventories and work in progress to their present location and condition. Cost in certain circumstances also includes notional interest as explained in the accounting policy for finance income and costs. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Construction work in progress is included within inventories in the balance sheet. It is measured at cost plus profit less losses recognised to date less progress billings. If payments received from customers exceed the income recognised, the difference is included withiin trade and other payables in the balance sheet.

Land inventory is recognised at the time a liability is recognised - generally after exchange of unconditional contracts.

Property inventory, which represents all development land and work in progress, is included at cost less any losses foreseen in completing and disposing of the development less any amounts received or receivable as progress payments or part disposals. Where a property is being developed, cost includes cost of acquisition and development to date, including directly attributable fees, expenses and finance charges net of rental or other income attributable to the development. Where development property is not being actively developed, net rental income and finance costs are taken to the income statement.

Share capital
The ordinary share capital of the Company is recorded at the proceeds received, net of directly attributable incremental issue costs.

Provisions
Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event, and where it is probable that an outflow will be required to settle the obligation and the amount can be reliably estimated.

Financial instruments
Financial assets and financial liabilities are recognised in the Group’s balance sheet when the Group becomes a party to the contractual provisions of the instrument. The principal financial assets and liabilities of the Group are as follows:

(a) Trade receivables and trade payables
Given the varied activities of the Group it is not practicable to identify a common operating cycle. The Group has therefore allocated receivables and payables due within 12 months of the balance sheet date to current with the remainder included in non-current.

Trade receivables do not carry interest and are stated at their initial value reduced by appropriate allowances for estimated irrecoverable amounts.

Trade payables on normal terms are not interest bearing and are stated at their nominal value. Trade payables on extended terms, particularly in respect of land purchases, are discounted and recorded at their fair value.

(b) Cash and cash equivalents
Cash and cash equivalents in the cash flow statements comprise cash at bank and in hand, including bank deposits with original maturities of three months or less, net of bank overdrafts. Bank overdrafts are included within financial liabilities in current liabilities in the balance sheet.

(c) Bank and other borrowings
Interest bearing bank and other loans are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis in the income statement using the effective interest method and are added to the carrying value of the instrument to the extent that they are not settled in the period in which they arise.

(d) Derivative financial instruments
Derivatives are initially recognised at fair value on the date that the contract is entered into and subsequently re-measured in future periods at their fair value. The method of recognising the resulting change in fair value is dependent on whether the derivative is designated as an effective hedging instrument.

A number of the Group’s PFI joint ventures have entered into interest rate derivatives as a means of hedging interest rate risk under cash flow hedges, which are initially recognised at fair value. The effective part of the change in fair value of these derivatives is recognised directly in equity. Any ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are recycled to the income statement in the periods when the hedged items will affect profit or loss. The fair value of interest rate derivatives is the estimated amount that the Group would receive or pay to terminate the derivatives at the balance sheet date.

8. Significant accounting policies continued

The Group also enters into forward contracts in order to hedge against transactional foreign currency exposures. In cases where these derivative instruments are significant, hedge accounting is applied as described above. Where hedge accounting is not applied, changes in fair value of derivatives are recognised in the income statement. Fair values are based on quoted market prices at the balance sheet date.

9. Statutory Accounts

The financial information set out above does not constitute statutory accounts for the years ended 30 June 2006 or 2005 but is derived from those accounts.

Statutory accounts for 2005 have been delivered to the Registrar of Companies and those for 2006 will be delivered following the Company's Annual General Meeting. The auditors have reported on those accounts, their reports were unqualified and did not contain statements under section 237 (2) or (3) of the Companies Act 1985.