Operational and financial review

Commercial Division

Following a record turnover in 2007, the commercial division produced a strong profit performance in 2008. The division delivered substantial forward sales and forward leases, including the construction of the first two properties for the Group's investment division. The commercial business sold 98,000ft^2 of commercial property, consisting of 18,000ft^2 of completed stock units and 80,000ft^2 of forward sales contracted and in build (2007: 60,000ft^2 of stock sales; 27,000ft^2 of forward sales). This is an impressive level of forward sales.

Artisan occupies part of Vantage House, one of the two investment properties, which now provides a useful showcase to demonstrate the appropriate quality of the product Artisan (UK) Developments is able to deliver to prospective clients. Turnover has been achieved because the division has taken steps over the past few years to build its land bank – there may be a slow down in trade at present, but land remains in short supply and the difficulties in obtaining suitable planning permission have not abated. A stock of units is available at each site other than our newest site. Further build of stock units will only be in response to sales progress.

The introduction of business rates on empty properties is a key issue for developers. Whilst in the short term it may drive down rental and sales values, at Artisan we regard it as a pernicious and inequitable scheme since empty properties do not need many of the services for which rates are largely charged. In the longer term we believe it will result in stock shortages (since developers will be discouraged from investing in speculative stock) and consequently drive up property values.

Residential Division

Rippon Homes has had to negotiate hard to complete every sale. Sales of 80 units at an average value of £186,300 (15 months to 30 June 2007: 160 units at an average value of £168,500) is, in current market conditions and we believe in comparison to our regional competitors, an encouraging result. The increase in sale price reflects improved sales of four bedroom units, a configuration which most of our competitors have progressively reduced building. Our view of likely market trends has proven to be correct, with customers favouring these larger units even in a difficult residential market.

A variety of incentives have been used to persuade customers to purchase our houses. The most effective selling tool has been the ability to deal in part exchange properties. However the key competitive advantage at Rippon Homes has been the quality of its product. Rippon Homes has over recent years avoided purchasing sites at prices that would require over-dense plot ratios or a high volume of three storey units to prove commercially viable. This policy has proven attractive to customers, many of whom are willing to purchase a Rippon Homes property, even in the face of some extreme discounts offered by a number of our competitors.

Part exchange stocks are carefully managed and our sales team have proved adept at selling these part exchange properties and not allowing excessive stock to accrue.

We have created new innovative schemes, such as rent to buy, which on the limited scale offered have so far proved popular to customers, to compensate for the limited availability of mortgage funds. This scheme allows occupiers to purchase the house after 12 months at an agreed price, using their rental and Rippon incentive as contributions towards the deposit required. However, a new disincentive to sales is becoming more apparent. Valuers are very nervous of valuing properties for mortgage purposes and are downgrading agreed sales prices. In the tight mortgage market this is causing many sales to collapse.

Investment Properties

Artisan (UK) Properties was pleased to receive the completed buildings for the first two investment properties from the commercial division. These were delivered on time and without difficulty. The properties are fully utilised with the tenants including Artisan in 3,000ft^2. At present the Group is concentrating on maintaining cash balances, and therefore no further investments are currently contemplated. Nevertheless they will be considered as opportunities arise.

Land stocks

As stated, we have been cautious in buying new land. This has been counter-balanced by slower sales rates. The land stock of owned or secured plots at Rippon Homes is 378 plots (2007: 337). The management at Rippon Homes have addressed a land bank shortage from earlier years and now have a balanced stock level, especially in light of current trading conditions.

Operational and financial review continued

The commercial operation currently holds land, owned or secured of 25,300m^2 (2007: 21,000m^2). By controlling sites, the development team is able to create sales opportunities which can lead to forward sales. Whilst Artisan (UK) Developments is able to demonstrate its track record in delivering finished items, it is important to show confidence in a site by developing speculative stock. This stock is also needed to fulfil short lead time demand for space.

Debt and Banking

The Group has net borrowings of £19.7m (2007: £10.8m) resulting from the new investment property loan of £4.5m and the balance resulting from increased investment in work-in-progress. The Group has drawn bank debt of £32.6m (2007: £24.1m) resulting in substantial cash balances continuing to be available. The trading conditions have placed a strain on the Group's profitability and our banking arrangements have been re-negotiated since the year end to

Results

	Residential £m	Commercial £m	Investment £m	Central £m	Total £m
Turnover					
2008 (12 months)	**15.1**	**10.7**	**0.2**	**(2.6)**	**23.4**
2007 (15 months)	26.9	15.6	–	(1.5)	41.0
Operating profit before group management charges					
2008 (12 months)	**–**	**1.7**	**1.5**	**(1.3)**	**1.9**
2007 (15 months)	2.6	2.4	0.3	(1.6)	3.7

The divisional analysis of profit is before Group management charges. The central column deducts the inter segment trading.

The tax credit for the year is £0.1m resulting in an effective tax rate of (18.5)% (2007: 24.1%). The reduction to standard rate resulting in a recovery of tax is primarily due to the surplus on investment property not being chargeable to tax in the current period and the utilisation of tax losses brought forward.

The net assets have grown 2.8% from £20.9m to £21.4m as a result of the retained profit for the year. There have been no significant changes to share capital during the year.

reflect this and the market conditions affecting the supply and pricing of credit. Our revised bank facility is split between a LIBOR based facility and a Base Rate based facility. The Base Rate interest margin is adjustable to reflect the LIBOR based cost of funding, but this element of the facility allows positive bank balances in the Group to be offset against drawdown funds for the purposes of interest calculation allowing for an effective management of funding. The gearing ratio is now 91.9%, or 71.1% excluding the new investment property loan (2007: 51.5%).

On 1 August 2008 the Group issued £1.75m of convertible loan note to Aspen Finance Limited. As disclosed in this report and accounts Michael W Stevens has a beneficial interest in the shares held by Aspen Finance Limited. The issue of the Loan Notes fulfils an existing commitment agreed in 2007 on the part of Artisan to its bankers to support new funding for the Artisan Group's investment property. Although this was originally envisaged as equity funding, the Directors believed that the current market conditions were not conducive to equity fund raising and a convertible loan note structure was agreed as an alternative.

The Loan Notes are convertible at any time, at the holder's option, into ordinary shares of 20p each in the capital of the Company ("Ordinary Shares"). The conversion price is:

(1) until 30 June 2009. 34.125p per Ordinary Share, being the average mid-market closing price of the Ordinary Shares over the previous ten dealing days;
(2) from 1 July 2009 to 30 June 2010, 80p per Ordinary Share;
(3) from 1 July 2010 to 30 June 2011, 85p per Ordinary Share; and
(4) after 1 July 2011, 90p per Ordinary Share.

The loan notes are subordinated to the banking facilities provided by National Westminster Bank plc, as part of The Royal Bank of Scotland plc, to the Company, but are otherwise repayable on 1 July 2012. In the meantime, the Loan Notes carry interest at a rate 1.25% above the National Westminster Bank plc Base Rate, from time to time, the same rate of interest as payable by the Group in respect of its investment property bank funding.

If, as a result of converting the Loan Notes, Aspen Finance Limited acquired 30% or more of the voting rights in relation to the Company, it would be obliged to make an offer to the other shareholders to acquire their shares in accordance with Rule 9 of the Takeover Code.

Work in Progress

Work-in-progress has increased from £34.8m to £39.1m at the year end reflecting continued investment in both residential and commercial stocks. As indicated in the segmental analysis within the notes to the accounts, the larger part of the Group assets are invested in the residential activities reflecting the greater volume of trade and the greater cost of residential land. In addition, the commercial operations are able to negotiate some of their sales on a forward basis, which can reduce the level of investment required. The nature of the residential market is that, more than ever, customers wish to view their potential purchase prior to commitment and it is therefore essential to maintain a stock of finished properties with sufficient range of product types across the various sites.

Chris Musselle
Chief Executive
15 October 2008