CHIEF EXECUTIVE OFFICER'S REVIEW

"Polypipe's balanced exposure to the different elements of the UK construction market, together with its long-term growth drivers of legacy material substitution, legislative tailwinds, and its acquisition strategy to provide our customers with a 'one-stop shop' and geographic reach, delivered another record performance in 2018."

Martin Payne
Chief Executive Officer

I am pleased to report that Polypipe has delivered another record performance in 2018, with revenue from continuing operations 5.2% higher than the prior year at £433.2m (2017: £411.7m), underlying operating profit 1.9% higher at £74.0m (2017: £72.6m), and underlying basic earnings per share 4.4% higher at 28.4 pence per share. Against a background of mixed conditions in the UK construction market, the 'Beast from the East' in February and March 2018, and uncertainty around the nature and timing of the UK withdrawal from the EU, this performance shows the robust nature of the Polypipe business model and the strength of its long-term strategic drivers of legacy material substitution and continuing legislative tailwinds in water management and climate management.

Revenue from continuing operations was 5.2% higher than the prior year

As noted in last year's report, price increases had been implemented in early 2018 to mitigate inflationary effects seen in the second half of 2017. I am pleased to report that these increases were successfully implemented progressively through the first half of the year. In 2018 oil prices rose throughout most of the year, resulting in higher raw material costs as well as increases in energy and transport costs. Wage inflation continued to track consumer price inflation. While the Group does all it can to mitigate inflation through various cost reduction measures, the scale of the oil-related inflation meant that price increases were inevitable. Further price increases have been implemented in the first quarter of 2019 to reflect this, and I am confident that these increases will be successfully delivered.

The year has also seen a number of changes to the Group, all in line with the Group's strategy, which leave it well placed to capitalise on future opportunities in its chosen markets.

On 29 March 2018, the Group completed the sale of Polypipe France Holding SAS (Polypipe France), its French operations, to Ryb S.A., a France-based manufacturer and distributor of plastics in Europe for €16.5m on a debt and cash-free normalised working capital basis. Accordingly, the results for Polypipe France have been treated as discontinued. Completion of this transaction, which represented excellent value for shareholders, was a significant step forward in implementing our strategy, allowing the Group to concentrate on its higher margin product groups in plumbing, drainage and ventilation, in both our UK and overseas markets.

In May 2018, Polypipe presented its first Capital Markets Day since it listed in April 2014. This confirmed that, following an in-depth review, the Group would continue to drive profitable organic growth through exploiting legacy material substitution and legislative tailwinds in water and climate management. The Group continues to review bolt-on acquisition opportunities to accelerate growth. Our strategic priorities are to firstly add innovative solutions to our already market-leading offer in water and climate management, in order to provide our customers with a 'one-stop shop' and secondly to provide further geographic reach to leverage our skills, technical knowledge and IP across a wider market.

In line with this strategy, the Group announced two acquisitions in the second half of the year. Permavoid Limited

(Permavoid) was acquired on 31 August 2018 for an initial consideration of £4.0m on a debt and cash-free normalised working capital basis, with a further consideration of up to £12.5m depending on financial performance in the two years to September 2020. Manthorpe Building Products Holdings Limited (Manthorpe) was acquired on 25 October 2018 for a total cash consideration of £52.1m on a debt and cash-free normalised working capital basis. The strategic rationale for acquiring these businesses is strong, with both businesses providing innovative solutions to complement the Group's existing offer, and I am excited by the prospects for these businesses in the coming years within the Group. The integration of these businesses into the Group is progressing well and both businesses are performing in line with management expectations.

Polypipe continues to be highly cash generative, notwithstanding spending £42.5m on acquisitions (net of disposals) during the course of the year and capital expenditure of 1.5x depreciation in our existing businesses. This delivered Group leverage of 1.7x pro forma EBITDA (2017: 1.6x). The Group is well invested and well placed to continue to pursue selective bolt-on acquisitions where appropriate in line with the Group's strategy, while maintaining a strong balance sheet, and a disciplined approach to capital allocation.

The Group continues to take its responsibilities towards sustainability very seriously. Although product standards and certain applications do not permit use of recycled materials in some products, wherever possible we use recycled materials instead of virgin polymer. In 2018 we used 44,700 tonnes of recycled plastics, which represents 40.2% of our overall plastic usage compared to 34.0% in 2017. Of this recycled plastic, 16,000 tonnes were from recycled milk bottles and other polyethylene consumer liquid bottles which are sourced from recycling companies such as Veolia in bales and go through our 15-stage recycling process at our plant in Horncastle, Lincolnshire.

Our strong sustainability and recycling credentials continue to be something that are important not only to Polypipe but to our customers, investors and employees, and we will continue to explore opportunities to increase our usage of recycled material wherever we can.

During the year we have followed events in the UK and across Europe as the UK moves towards withdrawal from the EU on 29 March 2019 (Brexit). In doing this we have assessed the risks to our business likely to be caused by Brexit, although this has proved difficult due to the uncertainty of the nature and timing of the withdrawal. While we are not complacent, we have concluded that Polypipe is at the lower end of the risk spectrum with regard to the impact of Brexit. With approximately 90% of our revenues derived from, and manufactured in, the UK market, we have relatively little cross-border trade. Also, if material costs increase as a result of either increased tariffs or a devaluation of Sterling, we will look to recover these increased costs in selling prices, as we have done historically when faced with cost inflation. Where it is deemed appropriate however, proportionate mitigating actions have been and are being taken, such as building raw material and finished goods stocks to allow for some supply chain disruption at ports, accelerating the refinancing of our debt facility that would otherwise have needed to have been done in the summer of 2019, taking forward currency cover and providing support to our non-UK EU colleagues, who account for approximately 13% of our UK workforce, to register for settled status.

The impact of Brexit on our end markets is difficult to predict, especially given the uncertainty around the nature of the exit. However, we continue to monitor our lead indicators around the Group and remain vigilant to any changes.

The following tables set out Group revenue and underlying operating profit from continuing operations by operating segment:

REVENUE

	2018 £m	2017 £m	Change %
Residential Systems	**245.3**	223.5	+9.8
Commercial and Infrastructure Systems	**187.9**	188.2	-0.2
	433.2	411.7	+5.2

UNDERLYING OPERATING PROFIT

	2018 £m	2017 £m	Change %
Residential Systems	**46.3**	44.3	+4.5
Commercial and Infrastructure Systems	**27.7**	28.3	-2.1
	74.0	72.6	+1.9

The Group continues to show resilience by having a balanced exposure to the different elements of the UK construction market, all of which have different drivers and move at different paces, and again this year's performance perhaps more than most demonstrates this.

In 2018, we used 44,700 tonnes of recycled plastics, which represents 40.2% of our overall plastic usage

CHIEF EXECUTIVE OFFICER'S REVIEW

RESIDENTIAL SYSTEMS

Revenue in our Residential Systems segment, which is almost exclusively derived from the UK market, was 9.8% higher than the prior year at £245.3m (2017: £223.5m). The acquisition of Manthorpe on 25 October 2018 contributed £2.8m revenue in the year, leaving like-for-like growth of 8.5%. This is again considerably ahead of the market and represents a strong performance in a challenging environment.

Conditions in the UK residential markets continued in line with prior years, with growth in the new housebuild sector driven by a structural housing shortage in the UK, continued historically low mortgage rates, and demand side help for first time buyers through the Government's Help-to-Buy scheme. The Repair, Maintenance and Improvement (RMI) market, however, continues to be slow, with weak consumer confidence driven by uncertainty around the EU withdrawal process impacting private RMI, and continued austerity impacting public RMI. Within that limited public RMI spend, we have seen post-Grenfell diversion of expenditure towards fire risk-related projects impacting our performance within that segment.

Like-for-like **growth of 8.5%** *is considerably ahead of the market*

Despite these challenging conditions, our Residential Systems segment delivered a strong result for the year. The adverse weather conditions in February and March 2018 impacted first-half performance with year-on-year revenue growth at the half year of 5.9%. However, concerted efforts by the house developers to claw back some of the weather-related lost time aided by mild weather conditions during the autumn and winter, as well as a two-month contribution from Manthorpe, helped second-half revenue to grow 13.7% compared to the prior year. This exceptional level of growth presented a number of operational challenges in our businesses, with parts of the business operating at or near full capacity.

I am delighted that on 25 October 2018 the Group acquired Manthorpe, a leading designer and manufacturer of moulded and extruded plastic and metal products to the UK and Irish residential and RMI markets. It has performed in line with expectations since joining the Group and we are pleased with how the integration is progressing. As well as a strong cultural fit, the acquisition is a good strategic fit with Polypipe's Residential Systems offering in the water and climate management sectors, with differentiated, patented, value-adding products that will help us deliver a 'one-stop shop' for our customers. There are exciting operational and commercial synergies that have been identified and will be delivered during 2019 and beyond.

Manthorpe is a good strategic fit with Polypipe's Residential Systems offering

Residential Systems delivered an underlying operating profit 4.5% higher than the prior year at £46.3m (2017: £44.3m) representing an 18.9% margin (2017: 19.8%) with cost reduction activities being more than offset by the dilutive effect of price increases, the relative growth of lower margin new housebuilding volumes, and towards the end of the year, inefficiencies caused by operating at or near full capacity in certain areas. Investment in both new production equipment and yard expansion and layout improvements at our main Doncaster site are being made to alleviate these capacity bottlenecks and will provide for a return to efficient working during the current year.

COMMERCIAL AND INFRASTRUCTURE SYSTEMS

We had a particularly challenging first half in this segment, with tough market conditions and the adverse weather resulting in first-half revenue being 6.6% lower than the prior period. However, with performance significantly improving in the second half, largely through self-help measures and marginal market improvements, revenue grew 6.7% or 5.3% on a like-for-like basis, excluding the impact of the £1.3m revenue associated with the Permavoid acquisition on 31 August 2018. This resulted in full year revenue in our Commercial and Infrastructure Systems segment of £187.9m (2017: £188.2m), 0.2% lower than the prior year on a reported basis, and 0.9% lower on a like-for-like basis excluding Permavoid.

UK revenue, which accounts for 81% of the overall segment revenue, was 0.2% higher than the prior year. UK Commercial and Infrastructure markets remained difficult, particularly through the first half, with some small improvements in the second-half as road programmes, both smart motorway upgrades and new road projects, began to gather momentum. Successful product launches also helped drive second half performance. The Fuze range of HDPE electrofusion soil stacks launched by our Building Services business in the second half of 2017 has been extremely successful, complemented by the successful launch of a fabrication service supplying fully assembled soil stacks to site. The £5.0m investment in a large-diameter continuous corrugator in our Civils factory at Horncastle, which came on-stream in the first quarter of 2018, has also had encouraging early results and contributed to the second-half performance, along with the successful launch of Nuaire's IAQ-Valve and expansion of the XBC range of heat recovery ventilation units. It is encouraging to note that the development of these products is squarely in line with the Group's strategic growth pillars of legacy material substitution (for example, Fuze replacing cast iron, continuous corrugator replacing concrete) and legislative tailwinds (for example, Nuaire IAQ-Valve and XBC range driven by air quality and building energy efficiency).

Export revenue, which accounts for approximately 19% of overall segment revenue, was 1.6% lower than the prior year, with lower revenue in the Middle East driven by difficult market conditions, more than offsetting improved performance in Continental Europe. The alternative manufacturing strategy in the Middle East, announced last year, has been successfully implemented. The first production run of Permavoid product using our tooling with local subcontract injection moulders was successfully completed and sold in the second half of the year, and the closure of our Dubai manufacturing facility and transfer of production machinery back to the UK was also completed during the year.

Fuze HDPE soil stack range successfully launched

On 31 August 2018, we acquired Permavoid, a specialist designer and supplier of plastic surface water management solutions in commercial, residential and sports pitch applications. This is a great strategic fit with the Group, providing unique patented products that enhance our water management solutions offer in sustainable urban drainage systems, green infrastructure, Blue-Green roofs, podium decks and sports surface applications, as well as some exciting geographic reach opportunities. Permavoid has been used in applications throughout Europe including the redevelopment of Orlysquare in Amsterdam, the Maankwartier Heerlen development in Holland and the redevelopment of Liverpool Football Club's Anfield stadium. Through its US licensing partner, Permavoid is also beginning to see increased demand for its products in the US, an exciting development that will continue into 2019 and beyond.

Permavoid acquisition provides unique patented products that enhance our water management solutions offer

Commercial and Infrastructure Systems delivered an underlying operating profit of £27.7m (2017: £28.3m) and represents a 14.7% margin (2017: 15.0%). While the closure of our Middle East manufacturing facility improved profitability, this was more than offset by higher costs associated with the adverse weather in the first half of 2018 and again the dilutive effects of price increases.

OUTLOOK

Polypipe has made significant strategic progress in 2018. The disposal of Polypipe France and the acquisition of Permavoid and Manthorpe have all been firmly in line with the Group's strategy. Organic growth ahead of the UK market and strong cash generation has continued to demonstrate the robust nature of the Group.

I look forward to another year of progress in 2019

While the political and economic uncertainty associated with the UK's withdrawal from the EU may impact markets in the short term, we believe that the fundamentals of our markets remain robust. Government and opposition both understand the structural housing shortage in the UK and recognise the need to increase the housing stock further, and with Help-to-Buy now extended until 2023, historically low interest rates and good mortgage availability, the medium-term fundamentals for new housebuilding remain sound.

While RMI, commercial and infrastructure markets have been and will continue to be challenging, the balanced exposure that Polypipe has to these different sectors of the construction industry positions the Group well.

As we look into 2019 and beyond, the opportunities for growth through legacy material substitution, legislative tailwinds in water and climate management are still as strong as ever, and together with helpful emerging trends in green infrastructure and appropriate acquisition opportunities to broaden our product and solutions offer, I am confident the fundamentals for the Group remain strong. While we remain vigilant to the short-term impacts of economic and political uncertainty in our markets, I look forward to another year of progress in 2019.

Martin Payne
Chief Executive Officer