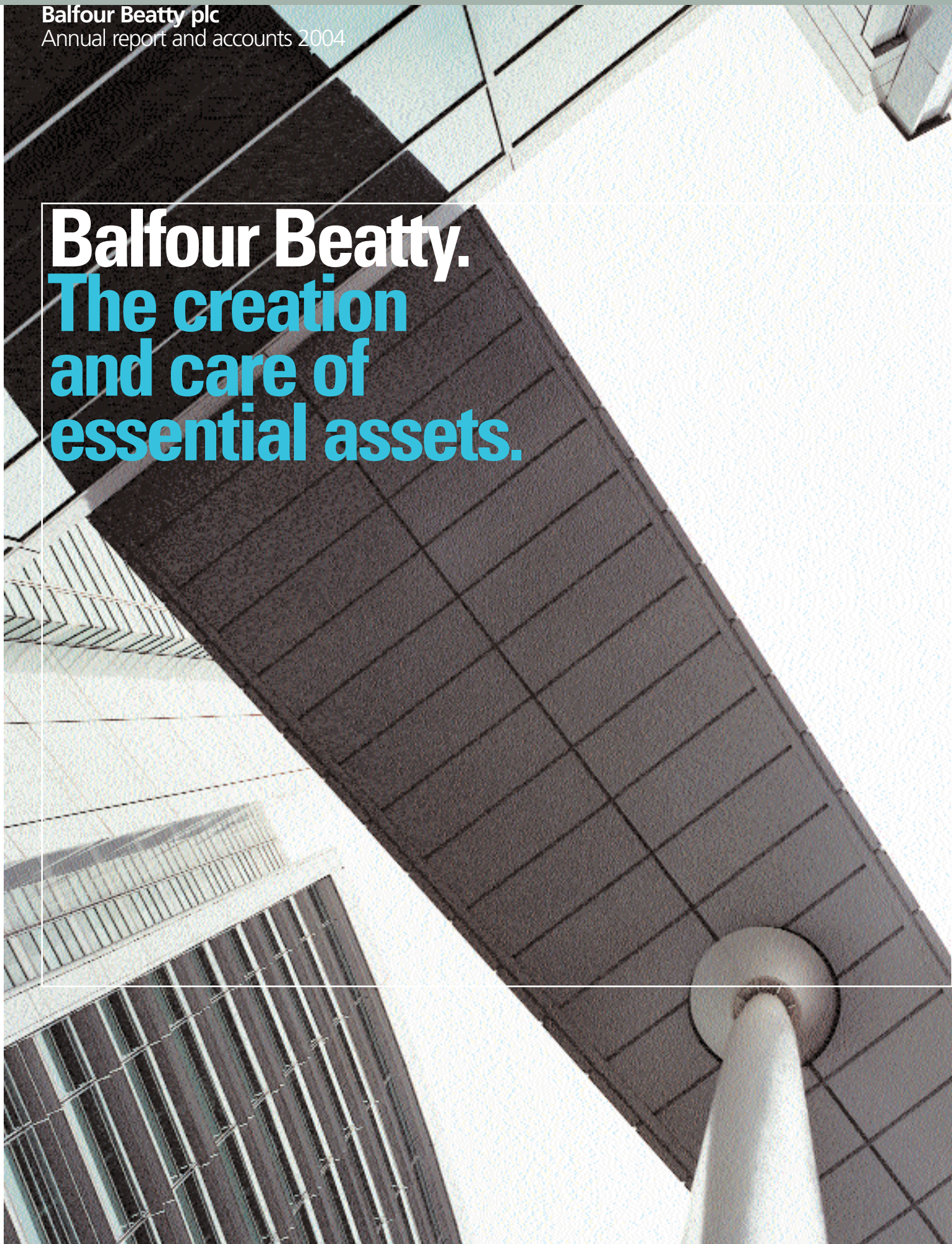


Balfour Beatty plc
Annual report and accounts 2004

Balfour Beatty. The creation and care of essential assets.



Balfour Beatty is a world-class engineering, construction and services group, well positioned in infrastructure markets which offer significant long-term growth potential.

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| Financial highlights | 2004 | 2003 | Change |
|---|----------------|---------|--------|
| Turnover (including joint ventures and associates) | £4,171m | £3,678m | 13% |
| Operating profits: | | | |
| – Before goodwill charges and exceptionals | £173m | £161m | 7% |
| – After goodwill charges and exceptionals | £280m | £149m | 88% |
| Pre-tax profit: | | | |
| – Before goodwill charges and exceptionals | £150m | £130m | 15% |
| – After goodwill charges and exceptionals | £257m | £118m | 118% |
| Earnings per share: | | | |
| – Adjusted* | 23.4p | 20.6p | 14% |
| – Basic | 43.8p | 16.9p | |
| Dividends per ordinary share | 6.6p | 6.0p | 10% |
| Financing: | | | |
| – Net cash before PPP subsidiaries | £311m | £127m | +£184m |
| – Net borrowings of PPP subsidiaries (non-recourse) | £(244)m | £(3)m | |

*before goodwill charges, exceptional items and the premium arising on buy-back of preference shares.

Highlights of the year

Five new PPP concessions at preferred bidder stage

Andover Controls sold for \$403m

Order book grows by 17% to £6.8bn

Gammon acquisition in Hong Kong creates strong base for Asian growth

Turnover by destination



US: £412m

South America:
£20m

UK: £3,261m

Europe: £263m

Africa, Middle East,
Near East: £65m

Asia Pacific: £150m

The Company

Balfour Beatty is a world-class engineering, construction and services group, well positioned in infrastructure markets which offer significant growth potential. Our partnerships with public and private customers generate secure, sustainable income. Our financial position, with significant net cash and with strong operating cash flows, offers continuing flexibility to add additional capacity and expertise to the business mix and to make appropriate investments in PPP and other long-term growth opportunities.

Against this background, we made further sound progress in 2004. Once again, we were able to both improve our profits and earnings and take important actions in developing the platform for the Group's continued long-term success.

Our financial progress was driven by a mixture of increasing returns on our equity investments, the benefits of acquisition and by organic growth. We anticipate continuing contributions from each of these three sources in 2005 and beyond.

In 2004, the disposal of Andover Controls, the acquisition of 50% of Gammon in Hong Kong and a number of smaller disposals and acquisitions to add to the acquisition of Mansell in late 2003 have improved the long-term earning power of the Group.

The leadership positions which we have in our core businesses were further reinforced with a wide range of major contract wins and PPP preferred bidder status awards.

Shareholders have become accustomed to seeing our cash flow fully back our profits. This was again true in 2004. The strong positive cash position which this gives us has been enhanced significantly this year through the disposal of Andover Controls. As a result, we now have even greater flexibility to move our business forward through further investment and acquisition.

You may rest assured that whatever changes we make to our business mix, all the component parts of the Group will continue to adhere to our core principles – careful bid selection, first-class project management, sound engineering judgements and close attention to cash management.



"The Group will continue to adhere to its core principles – careful bid selection, first-class project management, sound engineering judgements and close attention to cash management."

The Board

In August, we announced the retirement of Group Chief Executive, Mike Welton, from the Company and the Board. On 1 January 2005, he was succeeded by Ian Tyler, who has been Chief Operating Officer of the Group since 2002, having joined Balfour Beatty from Hanson plc as Finance Director in 1996.

Under Mike Welton's leadership as Chief Executive since 1996, Balfour Beatty has made enormous progress. During that time Balfour Beatty has been transformed from a traditional contracting organisation with sales of £1.7bn to a broadly-based engineering, construction and services company with sales of over £4bn and excellent future prospects. Mike was an outstanding leader and has left with the Board's sincere thanks and good wishes.

During this time, Mike Welton and Ian Tyler have worked closely together in taking and implementing decisions which have brought this transformation about. Ian is, thus, ideally placed to lead the Company forward in its next stage of development.

There were no other changes to the Board during 2004. The particular area of expertise of each of the Directors is shown at pages 38-39 and in the Directors' report.

Corporate governance

The Board continues to endorse and apply the principles of good corporate governance reflected in the Combined Code and is very substantially compliant.

Social responsibilities

The Group is committed to fulfilling its responsibilities to all of its stakeholders, including the wider communities in which it operates. Ian Tyler covers our approach to and record in safety matters in his review.

In respect of the environment, we measure our key impacts, work with our shareholders to minimise any potentially-negative outcomes and actively promote sustainable projects and processes both within the Group and with our customers.

We are making good progress in a number of areas in respect of our social responsibilities. For example, a new code of business ethics was published in the early part of 2005. The proportion of women and ethnic minorities employed by the Group has grown. A new charities policy has both increased the quantum of our corporate donations and focussed them more clearly on causes where we can most make a difference. We have contributed equipment, staff time and expertise as well as money to the current tsunami relief effort in Indonesia, where we have a joint venture company.

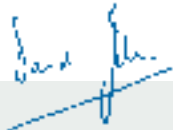
As Chairman of the Business Practices Committee, I continue to take a close personal interest in all of these matters, which will be fully reported in our fourth Safety, Environment and Social Report in May.

People

In the great majority of our businesses, we have established a position as the employer of choice and, as a result, can count on a strong cadre of talented, highly-motivated people dedicated to delivering our customers' requirements. I am sure shareholders will wish to join me in thanking all of our people for their efforts and achievements in 2004.

The way ahead

As creators of and carers for infrastructure, our work contributes directly to improving public services and amenities and enhancing the quality of life. Our people, disciplines and methods have proved successful in this task over many years and I believe will continue to do so in the future and, in doing so, continue to deliver growth in shareholder value.



Sir David John KCMG Chairman

A world-class company



Results

In 2004, pre-tax profits before goodwill charges and exceptional profits rose by 15% to £150m (2003: £130m).

Turnover was up 13% at £4,171m (2003: £3,678m). Earnings per share before goodwill charges, exceptional items and the premium arising on the buy-back of preference shares rose by 14% to 23.4p (2003: 20.6p).

£35m was charged to the profit and loss account in respect of goodwill amortisation arising from acquisitions (2003: £17m) including a £16m impairment charge in respect of Balfour Beatty Rail Inc.

There were a number of exceptional items, resulting in a net exceptional pre-tax profit of £142m. The sale of Andover Controls of the US, completed in July, brought an exceptional profit of £137m, with a number of other items netting to a further £5m credit (2003: £5m credit).

Profit before tax but after goodwill amortisation and exceptional items amounted to £257m (2003: £118m).

Operating cash flow was, once again, strong and year-end net cash stood at £311m (2003: £127m) before taking account of the consolidation of £244m of non-recourse net debt held in the PPP subsidiaries.

The year-end order book increased by 17% to £6.8bn (2003: £5.8bn). The Board recommends a final dividend of 3.75p per ordinary share making a total dividend for the year of 6.6p (2003: 6.0p), an increase of 10%.

£238m

PPP Investment

The Group will have a committed equity investment of £238m in 20 UK PPP schemes when the schemes at preferred bidder stage reach financial close.

23.4p

Earnings per share

Earnings per share before goodwill charges, exceptional items and the premium arising on the buy-back of preference shares have grown by almost 70% in the last three years.

£6.8bn

Order book

The Group's order book stood at a record £6.8bn at the end of 2004.

£4.2bn

Turnover

Balfour Beatty's sales exceeded £4bn for the first time in 2004.

Building on strength

Sector performance

Operating profits are stated before goodwill charges and exceptional items.

In **Building, Building Management and Services**, operating profits from the continuing businesses improved by 14% to £32m (2003: £28m). Mansell, which was acquired at the end of 2003, performed ahead of anticipated levels and continued to grow, particularly in social housing. Elsewhere in the building sector, performance was satisfactory and order intake continued at very good levels. A number of substantial contracts and preferred bidder positions were secured, including a number of major new PPP schools schemes and major acute healthcare projects. Andover Controls, which was sold in July, made profits of £8m (2003: £17m) and is accounted for as a discontinued business.

In **Civil and Specialist Engineering and Services**, operating profits improved by 10% to £23m (2003: £21m). Performance in the UK was good. Particularly encouraging progress was made in utilities contracting, where major new projects have been secured in both the gas and water sectors. Performance also improved significantly in road management and maintenance. In the US, however, further substantial losses were incurred.

Our US business has now been reorganised and the heavy marine engineering business is being closed. The associated costs of these actions have been fully accounted for in 2004. The acquisition of 50% of Gammon in Hong Kong and the accelerating development of the Dubai market, where we have a strong presence, provide further opportunities for long-term future growth.

In **Rail Engineering and Services**, operating profits rose by 5% to £43m (2003: £41m). The maintenance contracts taken in-house by Network Rail were settled on satisfactory terms. Our UK projects, plant and track systems businesses also performed well. A significantly larger share of the main line renewals programme was secured early in the year and the renewals workload for the London Underground is now increasing sharply. There were losses in Balfour Beatty Rail Inc in the US. The business has been reorganised and downsized as a result and its carrying value has been reduced by £16m. There was also some weakness in the German market, which led to reorganisation costs, but major projects in Italy, Portugal and the rest of the world progressed well.

In **Investments and Developments**, operating profits improved by 24% to £67m (2003: £54m) and pre-tax profits by 58% to £41m (2003: £26m). Progress was very satisfactory, largely as a result of the acquisition of 100% ownership of the Connect Roads A30/A35, A50 and M77/GSO concessions, a first full year of Metronet profits and a strong recovery in profits in Barking Power. In this latter context, a first dividend in respect of the administration of TXU Europe is anticipated during 2005. Preferred bidder status was achieved for five new PPP schemes – hospitals at Birmingham and Pinderfields in Yorkshire through Consort Healthcare, and schools schemes at North Lanarkshire, Nottinghamshire and Birmingham through Transform Schools.

Outlook

We have leading positions in a number of long-term growth markets which continue to offer us encouragement and opportunity.

We anticipate further improvement in the Building sector as the construction of our significant portfolio of major PPP projects proceeds and the market for social housing continues to develop. In Engineering, our expectations of a significantly better performance in the US should, amongst other factors, lead to good progress. In Rail, lower UK activity levels following the loss of the maintenance contracts and some continuing weakness in Germany will impact results. In Investments, there was a major step forward in 2004. This segment will see more modest growth in 2005 as substantial new PPP projects reach financial close and are mobilised.

Overall, we expect to make further progress in 2005 and to maintain our momentum thereafter.

Ian Tyler Chief Executive

“Our success in growing our underlying profits and earnings in recent years has been based on organic growth, and on creating and investing in businesses which have superior growth characteristics.”

How would you summarise 2004 for Balfour Beatty in the UK?

Our main markets, in healthcare, education, road and rail and utilities, were generally buoyant in 2004. Our financial results constituted a good performance in this environment, although, as ever, not everything went as we would have wished it to.

We were very successful in winning new work and our order book grew to £6.8bn – a new record – with a further £1.0bn at preferred bidder stage at the year-end.

Reliable earnings growth is underpinned by long-term alliance contracts. We already have many such contracts and have won more in 2004, including a £400m, five-year project to manage and maintain motorways and trunk roads in south-west England and a five-year contract likely to be worth approximately £500m for rail renewals on the mainline network. Early in 2005, we secured a £380m contract to work with National Grid Transco in replacing the gas mains in Greater Manchester over the next eight years.

Does that mean that your business is now moving more towards services?

We are strong in services, but the majority of our activity remains in engineering and construction. During the year, for example, we were selected to build the world's largest shopping mall in Dubai and the new 1,231 bed Birmingham Hospital and to manage and execute more than £400m of work at Heathrow Terminal 5.

And what about the equity investment side of your business?

We are a market leader in public private partnerships. During the year, we were appointed preferred bidder on five new concessions – Birmingham and Pinderfields Hospitals and North Lanarkshire, Bassetlaw and Birmingham Schools – with a total capital value of over £1bn. When these schemes reach financial close, very substantial construction and long-term service contracts will fall to Balfour Beatty companies.

In Andover Controls, you sold a very profitable company. Why?

Andover is a US building management systems specialist – a business quite unlike anything else in the Group. To sustain Andover's position in its markets would have required heavy expenditure on research and new product development. A number of companies whose principal business makes such investments appropriate wanted to buy Andover. As the company was becoming increasingly vulnerable to its competition, we decided to sell.

We were paid a good price and this has released funds to invest in our core businesses.

And what do you intend to do with the funds?

The Andover sale realised £218m net. We continued to generate cash in line with our profits and to manage working capital carefully. Our overall year-end net cash position (excluding PFI/PPP non-recourse net debt) was £311m, after having spent a net £56m on acquisitions.

The year's major acquisition was a 50% interest in Gammon, the leading construction company in Hong Kong, for a consideration of £33m. In addition to giving us pole position in an important local market, this creates a strong base from which to grow more generally in Asia.

We also bought out the minority in Connect to give us 100% ownership of this profitable portfolio of road concessions, added to our rail signalling expertise and strengthened our US project and programme management company.

We will continue to acquire in areas where the acquisition adds value. We will also continue to take equity stakes in PPP concessions where we are confident we can make good returns.

What is your position in the US?

We had a difficult year in the US, resulting in substantial losses, as indicated in the geographic analysis. We have, however, now made good progress in getting our interests there into the right shape to generate the consistent and growing earnings profile which is the hallmark of our businesses elsewhere.

We now have a sound organisation structure and sensible business models in each of our US markets. We have three strong regional civil engineering businesses in California, Texas and Pennsylvania, a rail transit and services operation and, in Heery, a well-established specialist in architecture, engineering and programme management.

Our primary objective is to deliver significant performance improvement in 2005 and 2006, on which basis we can build a larger presence in the longer term.

How would you summarise your strategy?

Our success in growing our underlying profits and earnings in recent years has been based on organic growth, and on creating and investing in businesses which have superior growth characteristics.

We have created a strong concession base in the private finance sector where good growth is built in to the concessions over their term. We have extended our life cycle presence in roads, rail, utilities and buildings so that we have earnings streams emanating from across the value chain from concept and design through to whole-life management and maintenance. In addition to the disposal of Andover Controls we have also sold businesses overseas where prospects of growth are poor in favour of a more substantial presence in a few growth markets.

During this period, procurement methods, particularly in the UK, have moved towards a greater emphasis on design and build, private finance, bundling of construction work into larger packages and outsourcing – all trends which either play to Balfour Beatty's existing strengths or into which we have moved successfully for example through the acquisition of our gas and water utilities business.

To continue to meet our growth objectives, we will be looking to add further new elements to the business mix. Having the cash to invest and acquire gives us flexibility in maintaining our forward momentum.



The Gammon acquisition

In August 50% of Gammon, Hong Kong's leading construction group, was acquired for £33m.



The Burj Mall

Dutco Balfour Beatty has been selected to build the world's largest shopping mall in Dubai.

What are you doing about safety?

The construction environment is, by its nature, hazardous and we regard it as a priority to keep our employees and the public safe. It is, therefore, important to maintain our momentum in improving our safety systems and performance. Following the 17% improvement in our accident rate in 2003, it is gratifying to be able to report a further 20% reduction in 2004.

Our accident frequency rate is significantly better than Health and Safety Executive norms, but this breeds no complacency. I have set new targets for further improvement this year. We have introduced an IT system which provides a single worldwide safety, environmental and health reporting and tracking system. This enables us to benchmark performance, identify trends and develop appropriate action plans. Health and Safety Forums for each major sector in the Group and a number of subject-specific Best Practice Groups have also been set up.

As the new Chief Executive, what changes are you planning to bring to the Company and its management?

You shouldn't expect sudden changes in direction from someone who has been at the centre of Balfour Beatty's affairs since 1996. We would be foolish to change what has made us successful in that period.

We have a number of strict management disciplines, covering, for example, what to bid for and how to bid it, how to manage our working capital, and when and how we recognise profit.

We have leading market positions, experienced management and a consistent management culture.

We have been blessed by procurement trends moving towards our preferred way of working, but we have also taken positive action to put ourselves in the way of such trends.

You can expect to see more of the same in the future, with close attention being paid to the further strengthening of all of our operations and new businesses being brought in to improve the mix.

I will, of course, be bringing my own personal perspective to bear on all this, but very much within the context of what has gone before.

PARTNER

Our aim is to create long-term shareholder value by providing engineering, construction and service skills to customers for whom infrastructure quality, efficiency and reliability are critical. We seek to operate safely and sustainably.

Group structure

RING

We work in partnership with sophisticated customers to create and care for first class infrastructure. Some examples of Balfour Beatty at work are featured in the operating review...

Building, Building Management and Services

Balfour Beatty is an international specialist in the design, construction, equipping, maintaining and management of buildings and selected aspects of their internal environment.

See pages 10-11

Civil and Specialist Engineering and Services

Balfour Beatty is a leading provider of civil and other specialist engineering, design and management services, principally in transport, energy and water.

See pages 16-17

Rail Engineering and Services

Balfour Beatty is an international leader in the design, construction, equipping, maintenance, management and renewal of rail assets and systems.

See pages 22-23

Investments and Developments

Balfour Beatty promotes and invests in privately funded infrastructure projects and developments in selected sectors.

See pages 28-31

Review of operations

Balfour Beatty Construction performed well in 2004. Some 50% of its business now derives from the PFI market. During the year, good progress was made on the construction programme for PFI schools schemes in Stoke, Rotherham and Calderdale and new hospitals for University College London and Blackburn. More than £1.2bn of work is now at preferred bidder stage through schools schemes at North Lanarkshire, Bassetlaw and Birmingham and hospitals in Birmingham and Pinderfields. A further £1bn of PFI work is expected to go through the bidding process in 2005.

Elsewhere in the health sector, two new Procure 21 schemes, at Moorfields and Whittington, were secured, a first LIFT project was completed and work progressed well on the medical research facility for the University of Edinburgh.

In education, the company was appointed as one of two construction partners in the Manchester "Building Schools for the Future" framework in a contract likely to be worth approximately £80m.

Successful completions were achieved on a number of complex projects, including at Waverleygate in Edinburgh, and for MoD accommodation at HMS Nelson, Marshwood and Thorney Island.

In London, the refurbishment business performed well, while the station refurbishment programme for Metronet under the London Underground PPP scheme is now gathering momentum after a slow start.

Mansell has proved to be a highly successful addition to the Group, with sales and profits ahead of our expectations at the time of the acquisition in December 2003. Mansell operates at the smaller project end of the market but with a clear strategic focus on selected sectors and a differentiated approach to its customers. A substantial proportion of its work is in long-term framework agreements. Balfour Beatty's strong position in the PFI market will offer it further growth opportunities.

Some 70% of Mansell's work is for the public sector, including a strong and improving position in the fast-growing social housing market for which the government has earmarked some £47bn of expenditure for upgrading and modernising work over the next six years. Mansell anticipates approaching £200m of annual sales from this market by 2007. Major current clients include Helena Housing, Perthshire Housing Association, Solihull Community Housing and Home Housing Group. A substantial amount of future work is now at preferred bidder stage and a new brand, Mansell Partnership Housing, was launched during the year.

Mansell has also very successfully targeted the defence sector, winning substantial new orders for the United States Air Force at Lakenheath and in the MoD Prime Contract for Scotland, and the education sector with major contracts for Unite (student accommodation), Norfolk Schools and Reading University.

Balfour Kilpatrick had a good year, with profits in line with those of 2003. The company's involvement in the PFI education schemes at Stoke, Calderdale and Rotherham, continued successfully. The company will also be carrying out the mechanical and electrical work on schools projects in North Lanarkshire, Bassetlaw and Birmingham once these PFI schemes reach financial close.

Both Balfour Kilpatrick's Cruickshank and Lounsdale operations, which specialise in power systems, had good years. There were high activity levels in upgrading London Underground's power supply and in sub-stations for Network Rail's Southern Region Power Upgrade programme. Projects for Scottish and Southern and for Scottish Power also progressed well.

In the multi-services business, a number of projects are underway for BNFL at Sellafield, for Conoco, the Ministry of Defence and AWE.

2004 saw the continuation of the very substantial design programme for the mechanical and electrical works in the tunnels, and stations and track transit system works at Terminal 5 for BAA. In the first half of 2005, in excess of £50m of work will enter the order book in this connection.

Haden Young had another very satisfactory year, with profits in line with the good results of 2003. Healthcare PFI schemes in which market it is the acknowledged leader, continue to be an important source of work for Haden Young. The company made good progress on PFI hospitals at University College London, Blackburn, Dudley and Romford. Some £300m of further M & E work is at preferred bidder stage for Birmingham and Pinderfields' hospitals.

The company has also been very successful in winning and executing work under the Procure 21 programme with five pilot projects completed and work under way on a further ten. It successfully completed a major project for the Meteorological Office. Progress was also good in the private sector, including work for Land Securities.

In Haden Building Management, profits were below their 2003 level. While the core businesses performed well, the major seven-year contract for the management and maintenance of the Royal Mail's entire building stock was revised to reflect a reduction in the size of the Royal Mail estate. Romec continues to deliver performance at the agreed output specification levels.

Building, Building Management and Services

Performance on other existing contracts was good, including long-term service relationships with the BBC, BAA, BT and Tesco, amongst others. Among new customers secured during the year were Chelsea and Westminster Hospital and the Millennium Centre in Cardiff.

Haden Building Management is the chosen long-term facilities management contractor for the Group's five PFI projects currently at preferred bidder stage and future prospects are encouraging.

Heery, the architectural, engineering and programme management business, performed well in the US. In the UK, some losses were incurred and this business has now been merged with Balfour Beatty Management. A substantial portion of Heery's work in the US is undertaken for the public sector, with a particularly strong position in education. Major long-term schools contracts progressed well, including projects in Florida, Houston, Massachusetts and Arizona.

Other particular Heery strengths include airports, with projects currently under way at Atlanta and Seattle, and Federal Government work in Washington. During the year, the business was strengthened through the acquisition of HLM, a recognised leader in the planning and design of healthcare projects. Early in 2005, two further small acquisitions were made in California.

Andover Controls, the US-based security and building management systems company, was sold to Schneider Electric of France in July amidst significant market consolidation, realising some \$403m. Its operating profits to July were £8m (2003: £17m).

Outlook

With record order books and substantial further work at preferred bidder stage, prospects in the sector are good. Each of the Balfour Beatty businesses in this sector are leaders in their field and bidding opportunities in our chosen sectors remain plentiful.

Companies

Balfour Beatty Construction
Balfour Kilpatrick
Haden Building Management
Haden Young
Heery International
Mansell

Andover Controls (sold July 2004)

Specialist areas

Design
Construction
Construction and Programme Management
Electrical Engineering
Mechanical Engineering
Building and Facilities Management
Refurbishment and Fit-out
Social Housing

Highlights

Over £1bn of PFI construction work at preferred bidder stage
Mansell performs ahead of expectations
Heery in the US strengthened through acquisitions
Major M and E works at Heathrow Terminal 5 get under way

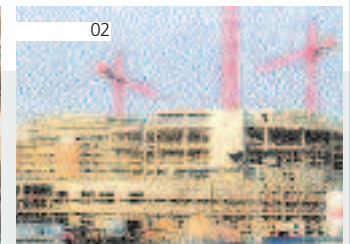
Financial summary

£1,586m
Turnover (2003: £1,093m)
£32m
Profit* (2003: £28m)

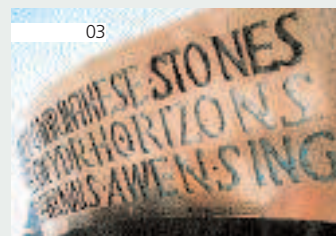
*before £4.3m goodwill amortisation and £1m exceptional profit



01



02



03

01 The first phase of the University College, London Hospital will commence operating in the first half of 2005.

02 Haden Young, leaders in healthcare M & E, are responsible for £30m of mechanical and electrical works at Romford Hospital.

03 In 2004, Haden Building Management won the contract for facilities management at the Millennium Centre in Cardiff.

2004 performance

Profits* in the continuing businesses in the Building, Building Management and Services sector rose by 14% to £32m. Mansell, acquired at the end of 2003, performed well as did the UK building and building services businesses overall. Confirmed order books and future workstreams held at preferred bidder stage grew substantially. In July 2004, Andover Controls was sold to Schneider Electric.

UPGRAD

Social housing to create sustainable communities.



Some other Balfour Beatty Customers Social Housing

| |
|---------------------------------------|
| Helena Housing |
| Places for People |
| Western Challenge Housing Association |
| Home Housing Group |
| Solihull Community Housing |
| Catalyst Housing Group |
| Perthshire Housing Association |

Mansell community housing

The UK government has directed that all public housing should meet the Decent Homes Standard by 2010, and allocated £47bn to fund the necessary improvements. Mansell Partnership Housing was the UK Partnering Contractor of the Year at the 2004 Housing Excellence Awards. It is a major national force in the affordable public sector homes market, where its excellent reputation for quality, efficiency and attention to customer need is bringing rapid growth. Over £250m of new build and refurbishment work was secured in 2004 alone as the money needed to bring the government's objectives to reality enters the system.

ING



01 Mansell developed these city-centre sheltered flats for Cotmer Housing Association mixing modern appeal with clever use of space.

02 Housing tenants in St Helens get their say on choices of fixtures and fittings.

03 Residents of Warden Housing Association sheltered accommodation enjoy their retirement in a homely environment.

Main picture: Marcia Edwards, Resident Liaison Officer, Mansell Partnership Housing.

TRANSFORM

Learning environments in the UK and US.



01



03



04



02

01 The development at Ferham School accommodates lottery funded space for sports and arts and a SureStart centre.

02 Partnership working ensures that sports facilities and community inclusion are built into the programme to maximise the use of school space.

03-07 Transform Schools worked closely with staff and pupils to help shape facilities at Clifton secondary school.

08 Thornhill Primary was handed over in April 2004 less than twelve months after the financial close of the project.

09 The new build Wath Comprehensive School is being constructed adjacent to the existing school.

Some other Balfour Beatty Customers Education

Stoke-on-Trent City Council

North Lanarkshire Council

Calderdale Metropolitan Borough Council

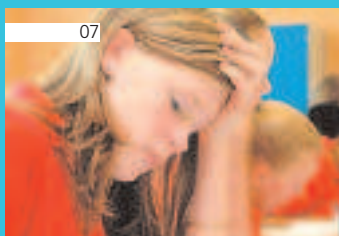
Manchester City Council

Houston Independent Schools District

Manroc County School Board

Nottinghamshire County Council

DRIVING



Rotherham Schools

Rotherham Council Education Authority is committed to creating the best possible learning environment for the children within its scope. Transform Schools is responsible, under a 31-year PFI concession, for building six new secondary and nine new primary schools and for maintaining them and providing a range of associated services. Balfour Beatty Construction, Balfour Kilpatrick and Haden Building Management all have critical roles to play, working in co-operation, to deliver the customer's requirements. Balfour Beatty is at work on many such schemes in the UK and the US.

Review of operations

Balfour Beatty Civil Engineering in the UK performed well, albeit with reduced volumes, as the Hong Kong activities whose profits were previously reported as part of its results were integrated into Gammon.

In the roads sector, a government review, late in 2004, saw our three principal Early Contractor Involvement schemes fall back in the Highways Agency's schedule. Early in 2005, however, we were awarded the £200m M1 Junctions 6A-10 widening scheme. The A120 in Essex was completed, as were the last elements in the M6 Tollway and the A1 between Dunbar and Haddington in Scotland.

The widening of the M25 between Junctions 12 and 15 progressed well and the M77, the Group's latest Design, Build, Finance and Operate road, progressed to completion in April 2005.

Tunnelling works on the Steg Raron rail projects in Switzerland progressed ahead of programme.

The regional civil engineering business continued to perform well, including on the long-term framework contracts for Cambridgeshire, Durham and Northumbria County Councils.

Balfour Beatty Civil Engineering is now in its third year of maintaining and upgrading the Forth Railway Bridge. Maintenance work at BAA's airports at Aberdeen, Glasgow and Edinburgh also progressed satisfactorily.

Stent, the Group's specialist foundations and piling business, performed well, in line with the previous year. Work on the new Wembley Stadium was successfully completed and good progress was made on the new Arsenal stadium in North London and on the major new development at White City in West London. The company has now entered the Dubai market in support of our main contracting business there.

In Hong Kong, the acquisition of a 50% interest in that territory's principal construction contractor, Gammon, was completed in August. This gives the Group a strong, established base in a regional market with excellent growth potential. The Group's existing civil engineering and mechanical and electrical engineering businesses have been integrated into Gammon.

Markets in Hong Kong are currently somewhat depressed and performance in the combined businesses reflected this. Current major projects include the Lok Ma Chau rail terminus and immigration hall, the elevated highway and bridge connection between Kowloon and Shenzhen and a number of public and private high-rise building developments.

Companies

| |
|----------------------------------|
| Balfour Beatty Civil Engineering |
| Balfour Beatty Construction Inc |
| Balfour Beatty Management |
| Balfour Beatty Power Networks |
| Balfour Beatty Utilities |
| Balfour Beatty Sakti (49%) |
| Dutco Balfour Beatty (49%) |
| Gammon (50%) |
| Lounsdale Electric |
| RCS |
| Stent Foundations |
| Devonport Management Ltd (24.5%) |

Specialist areas

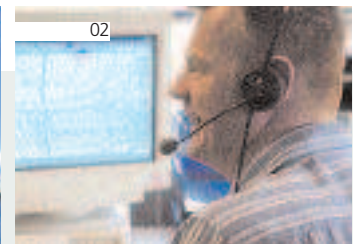
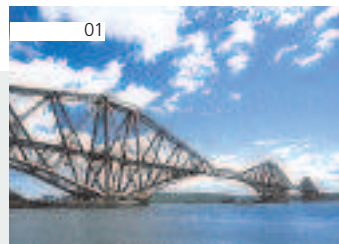
| |
|-------------------------------------|
| Design |
| Construction |
| Project Management |
| Foundations, Strengthening, Testing |
| Civil Engineering |
| Transmission Lines |
| Road Management and Maintenance |
| Utility Upgrade and Maintenance |
| Professional Services |

Highlights

| |
|--|
| Balfour Beatty Utilities wins substantial new gas and water infrastructure contracts |
| RCS extends its UK leadership in road maintenance |
| 50% interest acquired in Gammon, Hong Kong's leading construction company |
| Radical action taken to address US losses |

Financial summary

| |
|--|
| £1,443m |
| Turnover (2003: £1,393m) |
| £23m |
| Profit* (2003: £21m) |
| *before £5.0m goodwill amortisation and £4m exceptional charges. |



01 Balfour Beatty Civil Engineering's maintenance work on the Forth Railway Bridge entered its third year.
02 RCS's order book for road management and maintenance grew substantially during the year.
03 Gammon made good progress on the construction of the Deep Bay Link in Hong Kong.

Civil and Specialist Engineering and Services

In Dubai, **Dutco Balfour Beatty**, in which Balfour Beatty has a 49% interest, has a strong position in a fast-growing market and its sales and profits grew. To add to a range of projects already under way, in November the company secured the £400m contract to build Burj Mall, the world's largest shopping centre. **BK Gulf**, the M & E specialist, also had an excellent year, with major projects at Dubai Airport and a range of high-rise residential and commercial developments progressing well.

Balfour Beatty Sakti in Indonesia, in which the Group has a 49% interest, continued to undertake project work for PLN, the national power utility in both the generation and transmission sectors, most notably in a £28m contract at Muara Tawar Power Station. Balfour Beatty's interests in companies in Turkey and the Philippines were sold in the early part of 2004.

In the US, **Balfour Beatty Construction Inc** incurred further substantial losses, arising, principally, from its marine engineering business, and was subject to intensive management attention and reorganisation during the year. New management was appointed and a new business was created through the merger of NEC, acquired in 2001, and the central division, serving Ohio, Pennsylvania, Virginia and Maryland.

Balfour Beatty's marine engineering business has, in recent years, undertaken a number of technically and environmentally challenging projects. With all but one of these projects now largely completed, the business is being closed. The Texas Roads business, the California business which is largely focussed on the transportation market, and the Special Projects Division, with its tunnelling and multidisciplinary rail projects, performed well. The US\$150m Greenbush project, which will create a new commuter railway along the Boston South Shore, received final clearance to go ahead.

Order intake in the year has been very strong, including major projects for Caltrans, the Texas, Maryland, Ohio and Pennsylvania Departments of Transportation and the Central Puget Sound Regional Transit Authority.

In the utilities market, **Balfour Beatty Utilities**, which serves the gas and water sectors, had an excellent year following the reorganisation of the acquired businesses, John Kennedy and Kentons, and intensive bidding activity in 2003. Profits improved significantly and several very substantial new orders were secured.

The most notable success was the £380m Alliance with NGT to replace all the gas mains in the Manchester Area over an initial eight-year period, which was finalised early in 2005. This was won in conjunction with Balfour Beatty Management and involves the planning and management as well as execution of the major works programme.

New long-term contracts were also secured for Yorkshire Water, Anglian Water and Severn Trent Water.

Balfour Beatty Power Networks, the UK's leading specialist in the design and construction of power transmission and distribution networks, saw profits fall somewhat from their 2003 level as early

work on the Group's Sunderland Street Lighting PFI project proved more challenging than originally anticipated. Work for NGT continued at high levels. Late in the year, the company was awarded the largest single overhead line refurbishment contract ever let in the UK.

The transmission line across the Yangtze River in China, for which Balfour Beatty Power Networks built the world's tallest transmission towers, was opened during the year.

In road management and maintenance, **RCS**, had a very successful year, improving its profits and securing a growing future workload. Performance under the existing long-term Highways Agency contracts for Areas 2 and 3 in Kent, Sussex, Surrey and Hampshire was good.

In December 2004, the company won the "Enhanced Managing Agent" Contract for Area 2 in the West Country, with a potential value of up to £400m. RCS now maintains the motorways and trunk roads for the whole of southern England from the Kent coast to the far South-West. The company also won a five-year £65m contract to maintain roads, footpaths and street lights for Westminster City Council.

Performance in the company's major long-term local authority contracts in Worcestershire, Bedfordshire, Hampshire, North Yorkshire and Wokingham was satisfactory.

Balfour Beatty Management, the Group's professional services business formed in 2003, increased its resource base and subsumed the UK activities of Heery International during 2004.

It continued to provide project management services to London Underground and the Department for Transport in respect of the major rail developments at Kings Cross. In conjunction with Balfour Beatty Utilities, it was appointed by NGT for its £400m Manchester Alliance gas mains replacement contract. Bidding activity is intense.

Devonport Management Limited (DML), in which the Group has a 24.5% interest, continued to perform very well. The first nuclear submarine to have been refitted and refuelled in the new facility sailed for sea trials during the year with several more submarines due in during 2005 and subsequent years as the programme develops. In 2003, DML also became responsible for the management of the naval dockyard, in which workload continued to grow during 2004.

The refitting of surface ships remains a highly competitive market in which DML is a major player.

Outlook

Delays in the UK roads construction programme are unhelpful, but demand in the Group's other UK-based engineering businesses is strong and order books are substantial. Action taken in the US should provide further impetus to continuing performance improvement while the acquisition of 50% of Gammon and the accelerating development of the Dubai market provide further opportunities for long-term future growth.

2004 performance

Profits* in Civil and Specialist Engineering and Services improved by 10% to £23m in 2004. Performance in the UK was good. Particularly encouraging progress was made in utilities contracting and in road management and maintenance. In the US, further substantial costs were incurred on the residual positions of some contracts in the heavy marine engineering business, which largely offset the improvements elsewhere, and is being closed.

MODERN

The gas delivery infrastructure in Greater Manchester.

Some other Balfour Beatty Customers Utilities

| |
|------------------------|
| Anglian Water Services |
| South-West Water |
| Severn Trent Water |
| United Utilities |
| Northumbrian Water |
| Three Valleys Water |
| Yorkshire Water |



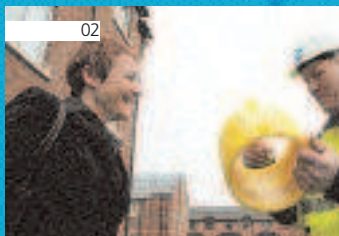
USING



01 Work is underway to replace Victorian metallic gas mains with 371kms of modern pipework systems.

02 More than 36,000 properties are to be disconnected and reconnected. Liaison with local residents is a key part of the programme.

Main picture:
Desmond Mulgrew, Gas Mainlayer Craftsman.

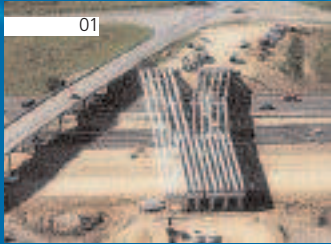


NGT Manchester Alliance

A comprehensive replacement programme for the gas mains system is needed in order to maintain safe and reliable gas supplies. In one of four such alliances, Balfour Beatty has been selected to work in partnership with NGT on their innovative approach to asset modernisation in Greater Manchester. Balfour Beatty Management will provide professional services to manage and deliver the scheme from concept to execution. Balfour Beatty Utilities will provide a complete contracting service, including investigation, design, construction and commissioning.

IMPROV

The traffic flows
in and around
Austin, Texas.



SH 130

Heavy congestion on the I-35 through Austin, one of the largest cities in the USA, is choking the flow of freight traffic en route to other destinations. Balfour Beatty Construction Inc is a major stakeholder and key contractor in Lone Star Infrastructure, a consortium of three engineering companies which has been chosen to design and construct SH 130, a 90-mile, \$1.3bn toll road through central Texas. Under the Exclusive Development Agreement, customer and contract designers and the construction team are working in partnership to maximise efficiencies and minimise costs.

ING



01 The first section of the project currently under construction involves building 114 new bridges of various sizes.

02 SH 130 will run 90 miles due south-north between Seguin and the I-35 at Georgetown.

03 SH 130 is the largest Texas DOT project to be built through undeveloped land since the 1960s.



Some other Balfour Beatty Customers Highway

- Highways Agency
- North Yorkshire County Council
- Hampshire County Council
- Caltrans
- Pennsylvania Department of Transportation
- The Dubai Municipality
- Hong Kong Highways Department

Review of operations

In **Infrastructure Services**, the year was dominated by the handover of the Kent and Anglia maintenance contracts to Network Rail and the achievement of a considerably increased market share in main line renewals following the award of new contracts in April. The transfer and handover of maintenance was achieved to plan. A financial settlement was reached with Network Rail on a satisfactory basis, including resolution of a number of issues outstanding from prior years' activities. It was also possible to reverse some exceptional provisions made in 2003 against costs which had the potential to fall to Balfour Beatty.

In April, new five-year contracts were awarded by Network Rail for main line renewals. The company was successful in securing the contracts for plain line renewals in the Anglia and Southern regions and switch and crossings renewals in London North-East, Southern and Anglia regions and in Scotland. This increased its annual sales under the new contracts from approximately £70m to over £100m. Performance under the new contracts is good and improving.

The **Projects** business had an extremely busy year, with increased sales and profits. The first phase of the overhead electrification work on the West Coast line was completed successfully, as were complex works for the Watford to Bletchley infrastructure upgrade project. Responsibility for the track replacement programme for Metronet falls to the Projects business. There was a substantial programme of renewals during 2004 which accelerated through the year despite the problems presented by the challenging working environment in the deep tube lines.

Prospects for major new UK rail projects are not encouraging in the short-term. Responsibility for major main line network upgrades will pass from the SRA to the Department for Transport. In the longer term, Crossrail, Thameslink and the East London line offer good work prospects.

In October, Balfour Beatty acquired Bombardier Transportation's UK Solid State Interlocking (SSI) signalling resources. This acquisition expanded the Group's signalling capability and substantially broadened the range of signalling-related services that it can offer to Network Rail and other customers.

2004 saw the major planning activity for the rail connections at Heathrow Terminal 5. Construction and installation work is now under way in a project with a total value of over £100m.

Rail Power Systems, the international electrification and power supply business had a mixed year in Germany, with largely positive developments elsewhere. Capital expenditure levels in Deutsche Bahn are depressed, making the German market difficult, and some reorganisation and downsizing was necessary during the year.

Progress on the three main German projects – Nürnberg-Ingolstadt, Ulmi Hahm and the Berlin Tunnel – was, however, good and the company's reputation as a supplier of choice for major projects in Germany was enhanced. We remain confident in the long-term prospects for the German market, but we do not expect recovery in 2005.

In Italy, the business performed well, principally on the early stages of the electrification of the line between Turin and Milan. The order book in Italy is substantial as the new high-speed inter-urban routes on the Italian Rail system are created.

In Portugal, having successfully completed the first phase of the Porto Metro to time and budget, the second phase has begun and is progressing well. In Spain and Sweden, we have strengthened our position with several new contract wins, most notably, in Sweden, for trackwork and associated system works in the north of the country and for electrification works on the East Coast.

Work progressed on the Rawang-Ipoh project in Malaysia and bidding activity in China continued.

Performance in **Track Systems**, the switches, crossings and components manufacturer, was in line with 2003. The weakness of the major project market and low levels of Network Rail investment expenditure in the short-term has led to some capacity reduction in 2004. The business's production facilities were further upgraded.

In **Plant**, performance was broadly in line with last year as the business adapted to its changing market environment. The in house market previously represented by the Group's maintenance contracts is no longer available, but the increasing demand for new and higher technology equipment offers considerable new opportunity. Network Rail is still developing its own strategic approach in this area.

Rail Engineering and Services

Companies

Balfour Beatty Rail
– Infrastructure Services
– Projects
– Power Systems
– Track Systems
– Plant
– Technologies
Balfour Beatty Rail Inc

Specialist areas

Design
Construction
Project Management
Maintenance
Track Renewals
Specialist Plant, Products and Systems
Electrification and Power Supplies
Signalling

Highlights

Satisfactory financial settlement of terminated UK maintenance contracts
Significant increase in UK renewals market share from new five-year contracts
Rationalisation of US and German businesses
Major Terminal 5 works in mobilisation

Financial summary

£803m
Turnover (2003: £873m)
£43m
Profit* (2003: £41m)

*before £24.6m goodwill amortisation and impairment and £8m exceptional profit.

In the **Technologies** division, the research and development of new systems and techniques, largely aimed at improved network safety, continued. Amongst its key projects in 2004 were a new method of stabilising old track through polymer injection, a new method for monitoring and stressing to prevent broken rails and new designs for switches and crossings.

It was a difficult year for **Balfour Beatty Rail Inc** in the United States. The urban transit market was depressed, with a great deal of planning and preparation by owners but very little release of funds for projects. No new work was secured from this source although the \$200m project at Greenbush on the Boston South Shore, secured in 2002, is now mobilising after some delay.

The rail businesses acquired in the US over the last four years were integrated into a single organisation and relocated to Jacksonville, Florida. There were significant rationalisation costs as a result. The largest current signalling project encountered problems and substantial losses were incurred as a result.

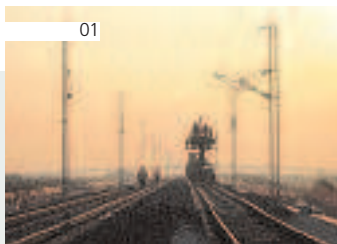
The downsized business is now being refocused on the growing rail services market, principally for the Class 1 freight railways and for industrial rail customers. Key target areas are rail replacement, maintenance, vegetation control and upgrading and operating rail spurs for industrial locations. A number of new regional offices to service this market were opened during the year, with more planned for 2005.

The potential for entry into the US rail power market is under investigation.

Outlook

2005 will be a year of transition for Balfour Beatty's rail businesses in the UK and the US, with market conditions elsewhere dictated by the short-term spending policies of network owners.

The potential to strengthen the Group's presence in this sector continues to be explored.



01



02



03

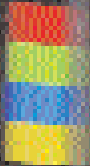
01 The €300m Milan-Turin electrification project progressed well.
02 Rail renewal work for Metronet on the London Underground accelerated in 2004.
03 A major phase of the West Coast main line electrification project was completed during the year.

2004 performance

Profits* in Rail Engineering and Services rose by 5% to £43m (2003: £41m). The maintenance contracts taken in-house by Network Rail in mid-year were settled on satisfactory terms and claims were settled from prior years' activity. Rail renewals activity increased following the award of a larger share of the main line market. There was also a sharp increase in the workload under the London Underground PPP. These factors and good performances in other UK activities and most of continental Europe were partially offset by the impact of market weakness and reorganisation costs in Germany and by losses and reorganisation costs in the US.

POWERI

Metro do Porto – Europe's largest new light rail transit system.



02



01



03



Metro do Porto

The need to relieve central Porto, a UNESCO world cultural heritage site, of growing congestion and pollution and provide a modern, urban transport system has created Europe's largest current light rail system development. Balfour Beatty Rail Power Systems is responsible for all the electrical and mechanical design and installation work for the new system which combines an underground metro, a surface tramway system and a suburban overground railway. The finished system will be transferred to the operator at the end of 2008.

MG



01 Balfour Beatty Rail Power Systems is responsible for the design and installation of the entire power delivery system.

02 The Blue Line was completed in 2002 and its extension in June 2004.

03 Balfour Beatty has introduced a number of new components and technical solutions to the system.

Some other Balfour Beatty Customers Railways

Network Rail

Deutsche Bahn AG

FS – Italian State Railways

MTA New York City Transit

Ministry of Railways – China

Banverket – Swedish National
Rail Administration

INTEGRA

Ground transport
for the world's most
successful airport
development.



Heathrow T5

Terminal 5 at Heathrow Airport is a critical element in meeting growing demand for air travel and in keeping London ahead of its European rivals. Balfour Beatty is managing and executing over £400m of work for BAA in integrated teams jointly dedicated to the project's successful delivery. The work, which comprises rail tunnels, rail station services, construction management, mechanical and electrical and other fit-out, the new track transit system, ancillary building works and the associated widening of the M25 motorway, involves five separate Balfour Beatty operating companies.

TING



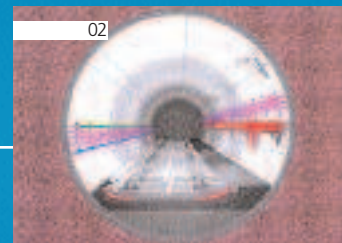
01 Balfour Beatty Construction is responsible for the delivery of the new railway station from concept design through to handover.

02 Balfour Beatty Rail Projects and Balfour Kilpatrick are designing and installing the mechanical and electrical services, track and rail systems and the track transit system.

03 Balfour Beatty Civil Engineering is widening Junctions 12-15 of the M25 to accommodate growing traffic flows.

Some other Balfour Beatty Customers Integrated Transport

| |
|---|
| London Underground |
| Hong Kong Airport Authority |
| Kowloon and Canton Railway Corporation |
| Massachusetts Bay Transit Authority |
| Puget Sound Regional Transit Authority |
| Singapore Land Transport Authority |
| California Department of Transportation |



The market

The PFI market remains strong. The Treasury recently reported that, by December 2004, 677 PFI projects with a combined capital value in excess of £42bn had been signed, with the 2004 tally comprising 45 projects and £2.8bn in capital value.

In Balfour Beatty's chosen markets, prospects remain very encouraging. In healthcare, for example, as well as the two bids already in preparation, there are 23 further major acute schemes in the pipeline with a total predicted capital value of over £5bn. In education, in addition to the current bids, there are 18 schemes scheduled for the next tranche with a total capital value of approximately £2.5bn. The introduction of the "Building Schools for the Future" initiative has provided further impetus for investment in the education sector.

In the roads sector, focus now rests on large-scale widening projects for the M25, M1 and M6 for which PPP may be the chosen procurement method.

There are a number of other infrastructure schemes likely to come to the market in the medium term.

Strategy

Balfour Beatty will continue to pursue opportunities in its existing markets, in all of which it now has clear competitive advantages and market leading positions. Projects will continue to be targeted whose size and complexity offer advantages arising from the Group's unique range of skills and experience. These projects will, typically, not only provide attractive investment opportunities – a real, post-tax internal rate of return of between 13% and 18% – but also trade on the proven strengths of and provide design, construction and service contracts for other parts of the Balfour Beatty Group.

Balfour Beatty has concentrated, to date, almost exclusively on the highly active UK market. However, as other national markets develop, their potential will be explored, with a preference given to territories where there is an existing Balfour Beatty contracting presence.

Its track record and the strengths of its market-specific brands, together with Balfour Beatty's role as both investor and contractor, provide potential customers with a high level of confidence that they will receive a high-quality, deliverable solution.

Outlook

With a number of PFI schemes due to become operational and to start contributing during the year and continuing satisfactory operational performance, further progress is anticipated in 2005.

Companies

| |
|-----------------------------------|
| Balfour Beatty Capital Projects |
| – Aberdeen Environmental Services |
| – Connect |
| – Consort Healthcare |
| – Health Management (UCLH) |
| – Metronet |
| – Powerlink |
| – Transform Schools |
| Balfour Beatty Property |
| Barking Power Ltd |

Specialist areas

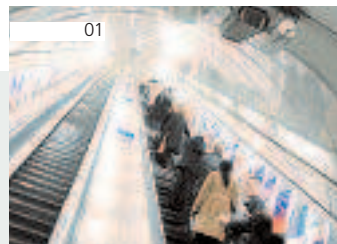
| |
|---------------------------------------|
| Roads |
| Rail |
| Accommodation – Healthcare, Education |
| Water |
| Integrated Transport |
| Power Systems |
| Property |

Highlights

| |
|---|
| Five new preferred bidder positions secured |
| Metronet performs to expectations |
| Good concession performance, particularly in roads |
| Significantly improved performance from Barking Power |

Financial summary

| |
|--------------------------------------|
| £288m |
| Turnover (2003: £216m) |
| £67m |
| Profit* (2003: £54m) |
| *before £0.3m goodwill amortisation. |



Investments and Developments

Review of operations

Overview

Balfour Beatty Capital Projects is a leader in the PPP/PFI market with 15 active concessions and five more at preferred bidder stage. A further eight bids have been submitted or are in preparation.

Barking Power is a leading independent power producer with a 1,000mW gas-fired station at Barking Reach.

01 Balfour Beatty is investing £70m in Metronet, which is modernising two-thirds of the London Underground.

02 The £220m Edinburgh Royal Infirmary became operational in April 2003.

03 The M77 in Scotland will move from construction to operational phase in the first half of 2005.

04 Profits from Barking Power Station improved significantly during the year.

Healthcare

| |
|--|
| Edinburgh Royal Infirmary: 42.5% |
| University Hospital of North Durham: 50% |
| University College London Hospital (UCLH): 33% |
| Blackburn: 50% |

| |
|--------------------------------|
| Birmingham: 50% [†] |
| Pinderfields: 50% [†] |

[†]Preferred bidder

Consort

Healthcare

Consort, the established Balfour Beatty business brand in the healthcare market, performed well in 2004, contributing profits and cash at anticipated levels.

Consort Healthcare's portfolio comprises interests in six major hospitals and represents a committed equity investment of £71m, £41m of which is in projects at preferred bidder stage.

North Durham and Edinburgh Royal Infirmary are already fully operational. The first phase of the University College London Hospital is nearing completion and will open to time and budget in May 2005. Blackburn Hospital is under construction, on schedule, and has an anticipated opening date in summer 2006. During 2004, Consort was appointed preferred bidder for two further hospitals. Birmingham Hospital, with an anticipated capital value of £521m, is expected to reach financial close during the summer of 2005. The Pinderfields and Pontefract Hospital scheme, with an anticipated capital value of £250m, should reach financial close in 2006.

Two bids are in preparation. These are for Northern Batched Hospitals and the Three Shires Mental Health Scheme and have an aggregate capital value of approximately £300m.

Consort Healthcare is now a clear market leader in PPP hospitals with a proven track record, a differentiated approach and high levels of client satisfaction.

2004 performance

Profits* in Investments and Developments improved by 24% to £67m in 2004. Pre-tax profit* was £41m (2003: £26m). Continuing growth in PFI concession income was augmented by the additional profits arising from our acquisition of the 32.2% minority shareholding in Connect Roads in January 2004 making Balfour Beatty the sole owner; a first full year of profits at anticipated levels from the Group's 20% interest in Metronet's concessions under the London Underground PPP; and a strong recovery in profits in Barking Power. During the year, preferred bidder status on five new PFI concessions was achieved.

Investments and Developments continued

Education

| |
|-------------------------|
| Stoke: 50% |
| Rotherham: 50% |
| North Lanarkshire: 50%* |
| Bassetlaw: 50%* |
| Birmingham: 50%* |

*Preferred bidder



Education

Transform Schools, the established Balfour Beatty brand in the education market, performed well and at anticipated levels in 2004. Its portfolio consists of major interests in five large-scale schools schemes and represents £29m of committed equity investment, of which £19m is at preferred bidder stage. The Stoke concession is the largest grouped schools scheme in England, covering 122 schools, and has been operational since October 2000. In 2004, Transform was awarded “Best Operational Educational Project” and “Best Overall Operational Project (all sectors)” in the Public Private Finance Awards.

The concession for Rotherham Schools became operational in June 2003 and is also highly successful. During the year, preferred bidder status was achieved for new schemes in North Lanarkshire, Bassetlaw in Nottinghamshire and Birmingham, with an aggregate capital value of £319m. Financial close for North Lanarkshire and Bassetlaw is expected during the first half of 2005 and, for Birmingham, in the third quarter.

Active bids are in hand for the schools schemes in Edinburgh and Oldham with an aggregate capital value of approaching £200m.

With five schemes, Transform Schools is now a market leader in the education sector, with high levels of customer satisfaction.

Roads

| |
|------------------------------------|
| M1-A1: 50% |
| A50 Stoke/Derby link: 100% |
| A30/A35: 100% |
| M77/Glasgow Southern Orbital: 100% |
| Sunderland Street Lighting: 100% |



Roads

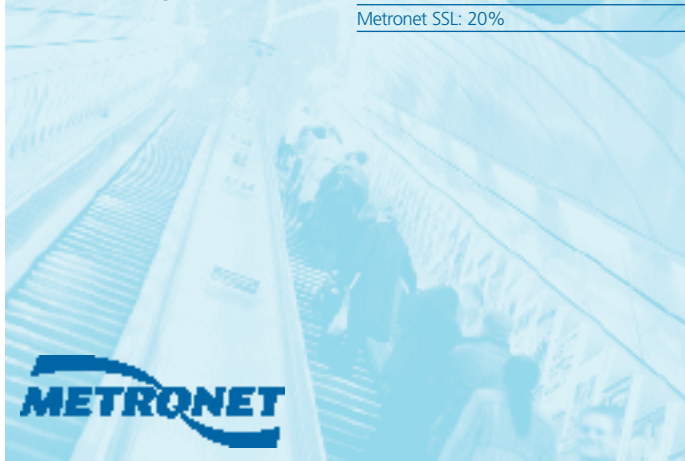
The profit and cash contribution from Connect Roads, Balfour Beatty's brand in the highways market, increased in 2004.

In January 2004, Balfour Beatty bought Atkins 32.2% minority interest in Connect Roads Ltd and Connect M77/GSO Holdings Ltd for £13m. The Connect portfolio covered by this transaction consists of the A30/A35 in Devon and Dorset, the A50 in Derbyshire and the M77 in Scotland. The first two of these projects are fully operational, having opened in 2000 and 1998 respectively. The M77 is due for completion and opening in April 2005. The Sunderland Street Lighting concession is also 100% Balfour Beatty owned and Connect branded and became operational in 2003.

With 100% ownership, results from these three road projects and the street lighting concession are now fully consolidated in the Group accounts. Connect M1/A1 near Leeds is 50% owned with a financial shareholder and has been operational since 1999. The underlying performance of the individual concessions was good.

In aggregate, Balfour Beatty has committed equity investment of £59m in these schemes. Active bids are in preparation for the Carlisle Northern Development Route, South Tyneside Street Lighting and Birmingham Highway Maintenance.

London Underground



Metronet BCV: 20%
Metronet SSL: 20%

The London Underground

Profits from the Group's 20% share in Metronet's concessions for the Bakerloo, Central and Victoria Lines and the Sub-Surface Lines for London Underground were significantly higher than last year, with a full 12 months of activity against the nine months in 2003 following financial close in early April of that year.

The underlying operational performance of the infrastructure for which Metronet is responsible is on a steadily improving trend. Major station refurbishment and other elements of Metronet's capital works programme have been somewhat slow in getting under way as design, approvals and mobilisation processes have been developed and refined. The pace of activity is now accelerating rapidly.

The Group has committed £70m of equity investment in Metronet.

Other infrastructure



Powerlink: 10%
PADCO: Powerlink 25%
Aberdeen Environmental Services: 45%
Barking Power Ltd: 25.5%

Infrastructure

Other Infrastructure Concessions

The performance of the Group's two other infrastructure concessions, namely Powerlink and Aberdeen Environmental Services, was satisfactory. Powerlink, in which the Group has a 10% interest, is responsible for the upgrade and maintenance of London Underground's high voltage power system. Aberdeen Environmental Services is the concession responsible for waste water treatment in Aberdeen. The total equity committed to these concessions is £10m.

We are currently bidding three new infrastructure schemes with a combined capital value of approximately £550m.

Barking Power

Profits in Barking Power improved very substantially in 2004, following the initial adverse impact arising from the entry into administration of TXU Europe in late 2002. The 27% of the station's output which is sold on the wholesale market as a result of TXU Europe's demise attracted much better prices than in 2003, while the station also achieved higher levels of availability and reliability in 2004.

We now expect the first dividend from the administrators of TXU Europe at the end of March 2005.

DEVELO

A 21st century hospital for Birmingham.



Some other Balfour Beatty Customers Healthcare

- Lothian University Hospitals NHS Trust
- County Durham and Darlington Acute NHS Trust
- University College London Hospitals NHS Trust
- The Mid Yorkshire Hospitals NHS Trust
- Royal Free Hampstead NHS Trust
- East London LIFT Accommodation Services Ltd
- Blackburn, Hyndburn and Ribble Valley Healthcare NHS Trust

01 The new hospital involves a revolutionary design concept to increase efficiency and be sympathetic to its environment.

02 A plaza will link the hospital campus to a new transport interchange, providing much improved public access.

03 By beginning some design and construction activities ahead of financial close the construction programme can deliver the first phase of the hospital in 2009.

Main picture right to left: Ian Woosey, Bid Director, Balfour Beatty Capital Projects; Mark Britnell, Chief Executive; Mel Morris, Project Director and Dame Catherine Elcoat, Executive Chief Nurse, the University Hospital Birmingham Trust.

PING



Birmingham Hospital

Birmingham last had a new general hospital over 70 years ago. The University Hospital Birmingham Foundation Trust and the Birmingham and Solihull Mental Health Trust are procuring a 1,231-bed acute hospital and over 200 new mental health places through PPP. Consort, the Group's PPP healthcare concession specialist, is its chosen partner for the scheme, which will revolutionise healthcare design from both a building and service delivery perspective. Construction work is being undertaken by Balfour Beatty Construction and Haden Young with facilities management provided by Haden Building Management. Construction work has begun in advance of financial close, which is expected in the summer of 2005.

Results

Turnover in 2004 increased by 13%, principally as a result of the acquisition of Mansell in December 2003.

Operating profit* increased from £161m to £173m (7%), despite an increase of £6m in pension charges for the Balfour Beatty Pension Fund, which impacted the building, engineering and rail sector results. The UK building and building services businesses continued to perform well, with profits from Mansell which was acquired in December 2003 more than offsetting profits forgone as a result of the sale of Andover Controls, completed in July 2004. The civil and specialist engineering sector produced another strong performance in the UK, but further substantial losses were incurred in the US. In rail engineering and services, the maintenance contracts taken in-house by Network Rail were settled on satisfactory terms and our UK projects, plant and track systems businesses performed well, while our US business incurred losses. Our rail electrification business showed some weakness in Germany, but there was good progress on major projects in Italy, Portugal and the rest of the world. There has been very satisfactory progress in our PFI/PPP portfolio of investments, which benefited from the increase to 100% ownership of Connect Roads, a first full year's contribution from Metronet and a strong recovery in profits in Barking Power.

A more detailed analysis of performance in our operating businesses is contained in the Operating Review.

Acquisitions and goodwill

During 2004 the Group acquired a 50% interest in Gammon for a consideration of £34m, including costs, and the remaining 32% interest in Connect Roads for £13m, and made three smaller bolt-on acquisitions for a consideration of £8m. Goodwill arising on these acquisitions amounted to £35m.

Operating profits were after charging £35m in respect of goodwill amortisation arising from acquisitions, including a charge of £16m for impairments in relation to the Balfour Beatty Rail Inc businesses.

Andover Controls

In July 2004 the Group sold Andover Controls for a cash consideration of US\$403m (£226m). After £10m transaction and other costs and £12m tax, the disposal resulted in an exceptional gain of £137m, after charging £37m goodwill previously written off to reserves. As this goodwill element is added back directly to equity, the disposal of Andover Controls has increased shareholders' funds by £174m.

Exceptional items

In addition to the exceptional pre-tax gain of £137m on the sale of Andover Controls, the Group recorded a net exceptional credit of £5m, including £7m credit from the reversal of provisions for costs arising on the cancellation of Network Rail maintenance contracts and a £2m loss on the sale of tangible fixed assets. These exceptional items have given rise in aggregate to a £15m tax charge.

Taxation

The Group's effective tax rate in 2004 was 26% (2003: 23%) of profit before goodwill amortisation and exceptional items. This charge benefited from the recognition of previously written off Advance Corporation Tax (ACT) which will be utilised in future periods as well as against the current year's liability. The Group also benefited from the use of brought forward tax losses in the US which reduced the amount of tax arising on the sale of Andover Controls. We expect a higher effective tax rate in 2005 than 2004 as all previously written off ACT has now been recognised.

Pre-tax profits and earnings

Pre-tax profits* amounted to £150m, an increase of 15%, and earnings per share* were 23.4p, an increase of 14% on 2003. Pre-tax profits after goodwill charges and exceptional items were £257m (2003: £118m).

Cash and interest

The Group has again benefited from a strong cash flow from operations and improvements in working capital management.

| | 2004 £m | 2003 £m |
|---|------------|------------|
| Group operating profit | 67 | 68 |
| add back: goodwill amortisation and impairment | 33 | 15 |
| Group operating profit* | 100 | 83 |
| Depreciation | 50 | 43 |
| Exceptional items – cash receipts/(expenditure) | (6) | 5 |
| Other items | 1 | – |
| Working capital decrease | 26 | 39 |
| Net cash inflow from operations | 171 | 170 |

*Before goodwill amortisation and impairment £35m (2003: £17m) and exceptional items £142m credit (2003: £5m).

"The Group has again benefited from a strong cash flow from operations and improvements in working capital management."



Cash flow from operations and the net £218m cash proceeds from the disposal of Andover Controls provided further capacity to grow the Group's core activities. In 2004, the Group had a cash outflow of £56m on acquisitions, including the interests in Gammon (£34m outflow) and Connect Roads (£11m outflow). When Connect Roads became a wholly-owned subsidiary in January 2004, the £239m non-recourse net debt of its A30/A35, A50 and M77/GSO concessions was brought on to the Group balance sheet. The level of the Group's net cash at the end of 2004 increased to £311m (2003: £127m), before taking into account the consolidation of £244m (2003: £3m) of non-recourse net debt held in the wholly-owned PFI/PPP project companies.

Pensions Charges

Pension charges to the profit and loss account of £35m (2003: £28m) have been made in accordance with SSAP 24, including £24m for the Balfour Beatty Pension Fund, £3m for the Balfour Beatty section of the Railways Pension Scheme and £5m for the Mansell schemes.

Valuation

A formal actuarial valuation of the Balfour Beatty Pension Fund was carried out at 31 March 2004 and showed a funding position of 102%. The last formal actuarial valuation of the Railways Pension Scheme was carried out at 31 December 2001. The next formal actuarial valuation of the Railways Pension Scheme will be carried out as at 31 December 2004 and will take into account the effect of the transfer to the Network Rail section for those employees who so elect, following the transfer of the UK rail maintenance business. The last formal actuarial valuations of the Mansell schemes were at 31 March 2002 and 31 July 2002 for the Hall & Tawse Retirement Benefit Plan and the Mansell plc Pension Scheme respectively.

The position of each of the funds has been updated by the actuaries at 31 December 2004 to review ongoing funding levels. The Group has increased contributions to the Balfour Beatty Pension Fund to £30m for the year ended 31 December 2004 (2003: £16m). Note 23a details the funding position of the schemes and the cost of providing pensions in accordance with SSAP 24.

FRS 17

The way in which pension arrangements are reflected in the Group's earnings and net assets will change radically when the substantive requirements of FRS 17 "Retirement Benefits" are implemented. Note 23b details the funding position and the cost of providing pensions in accordance with FRS 17 principles. The differences for the principal funds between the deficits reported in accordance with FRS 17 and the positions calculated on an ongoing actuarial funding basis are due entirely to the different discount rates applied in the two valuation methods.

Public Private Partnerships (PPP) and the Private Finance Initiative (PFI)

During 2004, the Group invested £24m in a combination of equity in and shareholder loans to its PFI/PPP project companies, including the acquisition of the remaining 32% interest in the A30/A35, A50 and M77/GSO concessions of Connect Roads. At 31 December 2004, the Group had invested a total of £88m in equity in and subordinated loans to its 15 project companies and had committed to provide a further £90m over the period 2005 to 2009. The Group has also been appointed preferred bidder for a further five projects to which it is expected at financial close to commit to provide approximately £60m funding.

At 31 December 2004, the Group's share of non-recourse net debt within project companies amounted to £775m, comprising £531m in relation to the joint ventures and associates disclosed in Note 11 and £244m on the Group balance sheet in relation to wholly-owned project companies disclosed in Note 14.

Treasury

The Group's policy remains to carry no significant net debt, other than the non-recourse borrowings of project companies.

The Group's financial instruments, other than derivatives, comprise borrowings, cash and liquid investments. The Group enters into derivatives transactions (principally interest rate swaps and forward foreign currency contracts) to manage the interest rate and currency risks arising from the Group's operations and its sources of finance.

It is, and has been throughout the period under review, the Group's policy that no speculative trading in financial instruments shall be undertaken. Compliance with policy is monitored through regular reporting and internal and external audits. The Board reviews and agrees policies for managing each of these risks and they are summarised below.

Finance and liquidity risk

Balfour Beatty's cash and liquid investments comprise cash, term deposits and the use of liquidity funds. Counterparty risk is monitored regularly and mitigated by limiting deposits in value to reflect the credit rating of the counterparty. Additionally, the Group has a series of bilateral facilities which total £210m maturing in 2006 and has in issue US\$120m of fixed rate loan notes maturing in 2008. The purpose of the facilities is to provide liquidity from a group of core relationship banks and other institutions to support Balfour Beatty in its current and future activities.

Financial strength

Interest rate risk

The interest obligations under the US\$ fixed rate loan notes were swapped into floating rate sterling obligations to match the floating rate nature of the cash held by the Group. The impact of interest rate risk management has been to reduce fixed rate borrowings (excluding PFI/PPP non-recourse term loans) to 3% of borrowings (2003: 5%).

Currency risk

The Group's businesses hedge their known foreign currency transactional exposures by taking out forward foreign exchange contracts.

Balfour Beatty also faces currency exposures on the translation into sterling of the profits and net assets of overseas subsidiaries and associates, primarily in the US and Europe, and on its overseas trading transactions.

Balfour Beatty does not hedge these profit translation exposures as these are an accounting rather than cash exposure. However, the effect of volatile short-term currency movements on profits is reduced because the Group accounts for currency profits using average exchange rates.

Balfour Beatty's balance sheet translation exposure is managed by matching approximately 90% of significant net assets denominated in currencies other than sterling by way of currency borrowings and forward foreign exchange contracts. Details of the position and fair values at the year end are shown in Note 15.

International financial reporting standards

Under EU regulations, the Group is required to prepare its 2005 annual financial statements under International Financial Reporting Standards ("IFRS"). The interim financial statements will also adopt accounting policies in compliance with IFRS. We continue to monitor the development of those standards yet to be finalised, particularly in the area of accounting for PFI/PPP concessions. In June 2005, we plan to publish a restatement of the 2004 financial statements in accordance with IFRS. During 2004, we have completed our review and identified and evaluated those matters affecting the Group, implemented the changes needed to the Group's treasury functions and developed a training programme for all our businesses. The paragraphs below set out the principal changes to the Group's financial statements as a result of applying IFRS.

Preference shares

Under IFRS, the Company's convertible redeemable preference shares are classified as a compound instrument comprising equity and liability components. Shareholders' funds will be reduced by the amount of the liability component, which is expected to be approximately 80% of the current £136m value, while the liability component will be reported separately in creditors. Deferred tax will be provided on the excess of the base cost of the liability component over its carrying amount.

The preference dividend will be replaced in the income statement by a computed finance charge on the liability component, which will include any premium paid on the buy-back of preference shares.

Retirement benefits

Under IFRS, the pension obligation relating to defined benefit pension schemes, as measured under IAS 19, is recognised in the balance sheet. The Group already discloses the adjustments required from the figures reported under SSAP 24 to FRS 17 (see Note 23b), which include reductions in shareholders' funds and changes to the income statement. The methodology and assumptions used under FRS 17 are consistent with IAS 19 except that equities are valued using mid-market prices under FRS 17 whereas IAS 19 will require the use of bid prices. It is the Group's intention to recognise actuarial gains and losses in full in the period in which they occur in a statement of recognised income and expense rather than spreading the amounts over a longer period through the income statement.

Share-based payments

Under IFRS, employee services received in exchange for share-based payments are charged to the income statement over the vesting period. In accordance with the transitional arrangements for IFRS, the Group intends to extend the profit and loss account charges to include employee services in relation to share options granted since 7 November 2002 but not vested.

Goodwill

Under IFRS, goodwill on the Group's balance sheet is not amortised, but is instead subject to annual review for impairment. The Group does not intend to elect to apply IFRS 3 retrospectively to business combinations prior to 1 January 2004.

PFI/PPP concessions

The International Financial Reporting Interpretations Committee ("IFRIC") has recently brought forward draft guidance notes on how the Group's PFI/PPP project companies should account for the assets which they have constructed. IFRIC's guidance is that these assets are to be classified as financial assets rather than fixed or leased assets.

Many of these project companies have entered into swap contracts to match movements in interest and inflation rates on their contracted future income and costs. Under IAS 39, these swaps are required to be recognised at fair value, giving rise to substantial additional liabilities in the accounts of the PFI/PPP project companies. As the financial assets arising from the construction activities will be recognised at fair value, any movement in the carrying value of those financial assets is expected to offset the additional liabilities arising under the swap contracts.

We will continue to monitor IFRIC's proposals and expect to be able to confirm the accounting treatment of these issues on publication of the restatement of the 2004 financial statements in accordance with IFRS in June 2005.

Financial instruments

Under IFRS, all derivative financial instruments are accounted for at fair value, while other financial instruments are accounted for at amortised cost or fair value depending on their classification. Other than the related impacts on PFI/PPP concession companies discussed above, this change is not expected to have any material impact on the Group.

Deferred taxation

Under IFRS, deferred taxation is provided under the temporal method and requires additional provisions in relation to the retained profits of overseas subsidiaries and fixed asset revaluations. This change is not expected to reduce the Group's shareholders' funds materially.

Post balance sheet events

Dividends declared after approval of the financial statements are not recognised under IFRS. The effect of this change will be to increase the Group's shareholders' funds.

Format of financial statements

The change to IFRS will result in a number of changes to the format and presentation of the figures within the Group's financial statements. The Group intends to continue to equity account for joint ventures but their results, along with those of associates, will be disclosed under IFRS on the income statement, net of tax. The Group's segmental analysis will also be modified to reflect IFRS requirements. Under IFRS, the financial statements will include additional disclosure on the gross values of the Group's construction contracts, but the Group's revenue recognition policies are expected to remain substantially unaltered.

Going concern

The Directors, having made appropriate enquiries, consider it reasonable to assume that the Group and the Company have adequate resources to continue for the foreseeable future and, for this reason, have continued to adopt the going concern basis in preparing the accounts.



Anthony Rabin Finance Director

Sir David John KCMG

Chairman

Age 66



Appointed a Director in 2000 and became Chairman in 2003. He is chairman of Premier Oil Group and The BSI Group, and immediate past chairman of The BOC Group. Formerly a director of Inchcape plc, he is a member of the CBI International Advisory Board, and a governor of the School of Oriental and African Studies.

Ian Tyler

Chief Executive

Age 44



A chartered accountant. A Director since 1999, he became Chief Executive on 1 January 2005, having been Chief Operating Officer since 2002 and prior to that, Finance Director. He joined Balfour Beatty in 1996 from the Hanson Group where he was finance director of ARC Ltd, one of its principal subsidiaries.

Anthony Rabin

Finance Director

Age 49



A chartered accountant and a barrister. A Director since 2002, he was previously managing director of Balfour Beatty Capital Projects, the arm of the Group responsible for the development and management of its PPP concession operations. Prior to joining Balfour Beatty, he was a partner at Coopers and Lybrand and before that, a senior assistant director at Morgan Grenfell.

Peter Zinkin

Planning and Development Director

Age 51



Joined the Group in 1981 and became Planning and Development Director in 1991 after a series of senior positions in the finance function. Prior to joining Balfour Beatty he worked at the London Business School and UMIST.

Jim Cohen

Managing Director,
Rail Engineering and Services,
Investments and Developments

Age 63



An economist. A Director since 2000 having joined the Group in 1993. Prior to joining Balfour Beatty, he held senior management positions with GTE and GEC and prior to those was a senior civil servant at the Department of Energy. He is a non-executive director of office2office plc, the office solutions and supplies group.

Alistair Wivell CBE

Managing Director,
Building and Building Services

Age 59



A civil engineer and a Fellow of the Chartered Institute of Building. A Director since 2002, he joined Balfour Beatty in 1966, and was previously managing director of Balfour Beatty Construction Limited, the Group's UK regional building and civil engineering business. He received a CBE for services to the construction industry in 1998.

Remuneration Committee

Robert Walvis (Chair)
Chalmers Carr
Richard Delbridge
Christoph von Rohr

Audit Committee

Richard Delbridge (Chair)
Chalmers Carr
Christoph von Rohr
Gordon Sage
Sir David Wright

Nomination Committee

Sir David John (Chair)
Gordon Sage
Ian Tyler
Robert Walvis
Sir David Wright

Business Practices Committee

Sir David John (Chair)
Chalmers Carr
Christoph von Rohr
Gordon Sage
Robert Walvis
Sir David Wright

Chalmers Carr

Non-executive Director

Age 67



Appointed a Director in 2003. He is a solicitor who is a legal adviser to Standard Chartered plc, having previously been general manager and group legal adviser to HSBC Holdings plc for eight years. His career experience also includes senior legal and other management positions with Coutts & Co, the Central Electricity Generating Board, Bridon plc and GKN plc.

Richard Delbridge

Non-executive Director

Age 62



Appointed a Director in 2002. A Fellow of the Institute of Chartered Accountants, he was formerly group finance director of HSBC Holdings plc and then a director and group chief financial officer of National Westminster Bank plc until 2000. He is currently a non-executive director of Tate and Lyle PLC, Cazenove Group plc, Fortis Group and Gallaher Group Plc.

Gordon Sage

Non-executive Director

Age 58

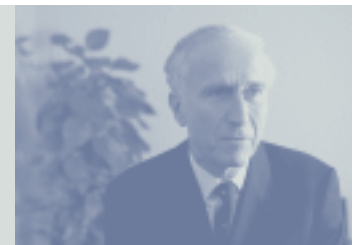


Appointed a Director in 2003. A chemical engineer, he is deputy chairman of ERM Holdings Ltd, the environmental services consultancy, and a non-executive director of Merrill Lynch World Mining Trust plc. Between 1970 and 2001 he held a series of increasingly senior positions in Rio Tinto plc, finally as executive director responsible for its industrial minerals and diamonds businesses.

Hans Christoph von Rohr

Non-executive Director

Age 65



Appointed a Director in 2003. He is a partner of the international law firm TaylorWessing and a board member of several corporations. He is also chairman of the German Institute for Market Economy and Competition. Previously, he was chairman of the Industrial Investment Council and also chief executive officer of the German manufacturing group, Klöckner-Werke AG.

Robert Walvis

Non-executive Director

Age 58



Appointed a Director in 2001. Previously with the Shell Group, latterly as chairman of the Corporate Centre of the Royal Dutch Shell Group of Companies. He is a non-executive director of Johnson Matthey plc. He is the senior independent Director.

Sir David Wright GCMG, LVO

Non-executive Director

Age 60



Appointed a Director in 2003. Currently vice Chairman of Barclays Capital, he retired as group chief executive of British Trade International in 2002, and was previously Ambassador to Japan for three and a half years. He is vice-president of the China-Britain Business Council, a member of the International Advisory Board of All Nippon Airways, and a Governor of the Royal Shakespeare Company.

Activities

The Chairman's statement and Chief Executive's review on pages 2 to 7, the Operating review on pages 10 to 33 and the Financial review on pages 34 to 37, report on the principal activities of the Group, its operations during 2004 and future developments in its businesses.

Dividends

The Directors recommend a final dividend on ordinary shares of 3.75p (net) per share, making, with the interim dividend of 2.85p, a total dividend for 2004 of 6.6p (net). Preference dividends totalling 10.75p (gross) per preference share have been paid for 2004.

Directors' interests

No Director had any material interest in any contract of significance with the Group during the period under review. The interests of Directors in the share capital of the Company and its subsidiary undertakings and their interests under the long-term incentive scheme (the Performance Share Plan 2001), and in respect of options, are set out in the tables in the Remuneration report beginning on page 44.

Share capital and major shareholders

Details of the share capital of the Company as at 31 December 2004 are set out in Note 18 on page 69. During the year to 31 December 2004 no ordinary shares were repurchased for cancellation and 13,710,755 preference shares (representing 9.2% of the preference share capital) were repurchased for cancellation for a total consideration of £19,859,291 at an average price of 144.6p. 1,696,608 ordinary shares were issued following the exercise of options held under the Company's Savings-Related Share Option Scheme and 1,779,667 ordinary shares were issued following the exercise of options held under the Company's Executive Share Option Schemes. No other shares were issued during the year.

At 31 December 2004, the Directors had authority, under the shareholders' resolutions of 13 May 2004, to purchase through the market 42,051,764 ordinary shares and 8,737,924 preference shares at prices set out in those resolutions. This authority expires at the conclusion of the 2005 Annual General Meeting.

As at 8 March 2005, the Company had been notified in accordance with Sections 198 to 208 of the Companies Act 1985 of the following interests in its ordinary share capital:

| | |
|--|-------|
| Aviva plc | 5.99% |
| Morley Fund Management Ltd (included in the interest of Aviva plc above) | 5.99% |
| Royal & Sun Alliance Insurance Group plc | 4.05% |
| Standard Life Investments Ltd | 3.83% |
| Prudential plc | 3.49% |
| Legal and General Group plc | 3.02% |

Corporate Social Responsibility

Safety, Environment and Social Report

For the fourth year we are publishing a separate Safety, Environment and Social Report. A copy will be available to shareholders attending the Annual General Meeting and to preference shareholders attending the separate class meeting.

Group policies

Our published policies on Health & Safety, the Environment, Ethics and Human Rights remain in place. Our continued progress in the areas of Health & Safety and the Environment is described in the Safety, Environment and Social Report.

Employment

As the Group operates across a number of business sectors in different environments it has a decentralised management structure, with employment policies designed to suit the needs of individual businesses. However, each employing company is expected to comply with certain key principles in its design and practice of employment policy.

These are:

- to provide an open, challenging and participative environment;
- to enable all employees to utilise their talents and skills to the full, through appropriate encouragement, training and development;
- to communicate a full understanding of the objectives and performance of the Group and the opportunities and challenges facing it;
- to provide pay and other benefits which reflect good local practices and reward individual and collective performance; and

- to ensure that all applicants and employees receive equal treatment regardless of origin, gender, disability, sexual orientation, marital status, religion or belief.

Individual businesses use a variety of methods to communicate key business goals and issues to employees and also consult and involve their employees through local publications, briefing groups, consultative meetings, training programmes and working groups to assist the process of continuous improvement in the way they operate and do business. Regular publications inform employees of major business and technical achievements. Most of our UK based businesses have either attained or have committed to attain the UK Investors in People standard.

Regular communication is maintained with the in-service and pensioner members of the Balfour Beatty Pension Fund, and during 2004 a series of roadshows were arranged to update pensioners on pension fund matters.

Donations

In 2004 the Group contributed approximately £75,000 to charitable organisations or for charitable purposes.

As foreshadowed in the 2003 Annual Report, following a review of policy, a charities committee was formed in the early part of 2004 comprised of employees from around the Group's operating companies. This committee, which has met on a number of occasions during the year, now determines the direction of the Group's charitable support. For 2004/2005 this support has been directed to three main charities: Groundwork, which carries out urban regeneration projects, Marie Curie, the cancer charity, and the Construction Industry Trust for Youth (C.I.T.Y.), which is active in seeking to support young people in acquiring basic skills through the medium of the construction industry.

At the time of writing, funding of £5,000 has been provided to CITY and an agreement has been signed with Marie Curie to match funds raised by employees during 2004/2005 up to a limit of £25,000. Groundwork has provided the committee with details of projects for possible support, out of which the committee has agreed that three, one in each of Birmingham, Blackburn and Wakefield, should benefit from funding provided by the Company of £10,000 per project.

Around the Group, individual operating companies are encouraged to provide charitable support on their own initiative. Thus, during 2004 Balfour Beatty Utilities Ltd donated £1,000 to Marie Curie and Raynesway Construction Services Ltd has agreed to fund 50% of the time off necessary for an employee to attend meetings of the leading charity Diabetes UK, of which he has been elected a trustee.

The Group has also provided material assistance in kind, to an estimated value of £0.1m, for the charitable organisation Engineers Against Poverty, which carries out small engineering projects in developing countries. The Group continues to enable UK employees to donate through the Give-as-you-Earn scheme to various charities of their choice.

Following the Asian earthquake and tsunami on 26 December 2004 and its devastating consequences, the Group provided considerable assistance both in practical terms and in cash for the relief of those affected. This has been channelled through the Group's long established joint venture company in Indonesia and subsidiary company in Sri Lanka.

Taxation status

The Company is not a close company for taxation purposes.

Post balance sheet events

Details of post balance sheet events are set out in Note 26 on page 76.

Research and development

The Group continues to be committed to investment in research and development in all its areas of activity. This covers new products and processes and innovation in areas such as information technology and asset management systems.

We continue to undertake a range of development initiatives throughout our businesses which are supported by links with selected universities.

Details of the Group's 2004 research and development expenditure are given in Note 3 on page 58.

Payment of creditors

In the UK, the Company's policy is to settle the terms of payment with suppliers when agreeing the terms for each transaction or series of transactions; to seek to ensure that suppliers are aware of the terms of payment; and to abide by these terms of payment as and when satisfied that the supplier has provided the goods or services in accordance with the agreed terms. At 31 December 2004 the year end creditors' days of the Company were 19 (2003: 27).

Statement of Directors' responsibilities

The following statement, which should be read in conjunction with the Independent auditors' report on page 51, is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the auditors in relation to the financial statements.

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year and of the profit or loss of the Group for the financial year. The Directors consider that, in preparing the financial statements and related notes on pages 52 to 79, the Company and the Group have used appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all applicable accounting standards have been followed.

The Directors have responsibility for ensuring that the Company and the Group keep accounting records which disclose with reasonable accuracy at any time the financial position of the Company and the Group and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and the Group and to prevent and detect fraud and other irregularities.

Auditors

Deloitte & Touche LLP have indicated their willingness to continue as auditors to the Company and a resolution for their reappointment will be proposed at the Annual General Meeting.

Annual General Meeting

Sir David John, who chairs the Nomination and Business Practices Committees, Richard Delbridge, who chairs the Audit Committee and Robert Walvis, who chairs the Remuneration Committee, will be available at the Annual General Meeting to answer any questions arising from the work of these Committees. The Board regards the Annual General Meeting as an important occasion on which to communicate with shareholders, and research into subjects of likely interest to shareholders is undertaken so that questions can be answered during the meeting for the benefit of all shareholders present. Shareholders may also put questions in advance of the Annual General Meeting by writing to the Company Secretary.

The business to be put to the Annual General Meeting is set out in the separate circular to shareholders.

Directors' report

Signed by order of the Board

C R O'N Pearson

Secretary
8 March 2005

Corporate governance and the Combined Code

Overview

The Board continues to endorse and apply the principles of good corporate governance reflected in the Combined Code (the "Code"), as appended to the Listing Rules of the UK Listing Authority.

The governance of the Company in the light of the principles and supporting principles and provisions of the Code is described in the following paragraphs. At the date of this report, and unless otherwise explained in the text, the Company is fully compliant with the provisions of the Code.

Honorary President

Viscount Weir is Honorary President of the Company, having been appointed to this position in May 2003, following his retirement as Chairman.

The Board

The Board currently comprises twelve Directors, of whom seven, including the Chairman, are non-executive. Throughout 2004, the Board comprised thirteen directors, with six executive Directors including Michael Welton as Chief Executive and seven non-executive Directors. With Mr Welton's retirement at the end of 2004, the number of executive Directors reduced to five. The Directors believe that the Board continues to include an appropriate balance of skills and, with them, the ability to provide effective leadership for the Group.

The Board operates both formally, through Board and Board Committee meetings, and informally through regular contact between Directors as required. Decisions on a list of specific matters, including strategy, approval of financial statements, risk management and treasury policy, major capital expenditure, acquisitions and disposals are reserved to the Board or Board Committees. Matters falling outside the list are delegated to management.

Meetings of the Board are normally held in London, but meetings are on occasions held in other parts of the UK and overseas to enable Directors to visit the Group's businesses at the same time. In 2004, the April meeting was held near Derby and Directors visited Balfour Beatty businesses in Derby and Nottingham following the meeting. The October meeting was held near Munich, and combined with a visit to a rail electrification project in Germany in which the Group is engaged.

Papers for Board meetings are generally sent out at least three days in advance of the meeting. These include a written report from each of the Chief Executive, the Finance Director, the director of Health, Safety and the Environment, the group managing directors, and the chief executive officer of Balfour Beatty Inc. At Board meetings, oral reports are made on issues arising from the written reports, and both those and other matters of immediate interest or concern are discussed by the Board. Apart from the Board meetings that approve the interim and final results respectively, and the Board meeting prior to the Annual General Meeting ("AGM"), a separate presentation on a topic of interest or concern, such as strategy or the operations of a particular business, is normally made to the Board. Each meeting lasts about four hours, but can be longer.

The Board met on nine occasions in the course of 2004. A table showing attendance at these meetings and at meetings of the Audit Committee, the Nomination Committee, the Remuneration Committee and the Business Practices Committee, is on page 43.

The Chairman of the Board is Sir David John, and the Chief Executive is Ian Tyler, who succeeded Michael Welton on 1 January 2005. The senior independent Director is Robert Walvis, who was appointed a non-executive Director in 2001. The Chairman of the Audit Committee is Richard Delbridge, of the Nomination Committee, Sir David John, and of the Remuneration Committee, Robert Walvis. Sir David John also chairs the Business Practices Committee.

Chairman

Sir David John became Chairman in May 2003. He joined the Board in August 2000. Normally, Sir David spends two days per week on the business of the Company. He has other significant commitments as non-executive chairman of The BSI Group and of Premier Oil plc. The Board considers that his other commitments are not of such a nature as to hinder his activities as Chairman of the Company and of the Nomination and Business Practices Committees.

Directors

Brief biographical details of the Directors, including the Chairman, are given on pages 38 and 39. All the Directors shown served throughout the year. Michael Welton, who is not shown, served as Chief Executive throughout the year and retired on 31 December 2004 after 26 years with the Group. The Board considers that all the non-executive Directors continue to be independent.

From September 2003, non-executive Directors have been appointed for specific three year terms, and it is part of the terms of reference of the Nomination Committee to review all appointments of non-executive Directors at three year intervals and make recommendations to the Board accordingly.

Rotation of Directors, election and re-election

The Articles of Association of the Company currently provide that at each AGM one third, or the nearest number to one third, of the Directors who are subject to retirement by rotation shall retire from office and shall be eligible for re-election. This year, all the Directors are subject to such retirement and four Directors are, therefore, retiring by rotation. They are Jim Cohen, Richard Delbridge, Anthony Rabin and Alastair Wivell. Each is seeking re-election.

Board Committees

The main Board Committees, the membership of which is either wholly or substantially comprised of non-executive Directors, are the Audit Committee, the Nomination Committee, the Remuneration Committee and the Business Practices Committee.

Reports on the workings of these Committees are set out below.

The report of the Remuneration Committee can be found in the Remuneration Report beginning on page 44.

– The Audit Committee

The membership of this Committee currently comprises Richard Delbridge (the Committee chairman), Chalmers Carr, Christoph von Rohr, Gordon Sage and Sir David Wright. Christopher Pearson, the Company Secretary, continues as secretary of the Committee. The membership of the Committee has not changed during 2004. All of the members have extensive experience of management in large international organisations. The Committee chairman, Richard Delbridge, is a chartered accountant and a former group finance director of a FTSE 100 company.

The terms of reference for the Committee, based on the report by Sir Robert Smith in January 2003 and the requirements of the Code, were approved by the Board in October 2003 and remain unchanged. They are available on the Company's website at www.balfourbeatty.com. The main responsibilities of the Audit Committee are as stated in last year's report: to monitor the integrity of the financial statements of the Group and any formal announcements relating to the Group's financial performance; to review the Group's internal financial controls established to identify, assess, manage and monitor financial risks and receive reports from management on the effectiveness of the systems they have established and the conclusions of any testing carried out by the internal and external auditors; to monitor and review the effectiveness of the internal audit function; to make recommendations to the Board in relation to the appointment of the external auditor and to approve the remuneration and terms of engagement of the external auditor; to assess the independence, objectivity and effectiveness of the external auditor and to develop and implement policy on the engagement of the external auditor to supply non-audit services; and to review arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting.

Appointments to the Committee are made by the Board for a period of up to three years, extendable by no more than two additional three year periods, so long as members continue to be independent. Any additional remuneration of members of the Committee is set by the executive Directors and the Chairman. At the Board meeting following each meeting of the Committee, the Committee chairman provides an oral report on the work of the Committee and any significant issues that may have arisen. The minutes of Committee meetings are circulated to all members of the Board.

In May 2003 it was decided to increase the number of regular meetings each year from three to four, and four meetings were held in 2004. A fifth (short) meeting was also held in May. At the invitation of the Committee, partners from the external auditor, the Head of Internal Audit, the Finance Director and the Chairman regularly attend each meeting. In addition, any independent non-executive Director who is not a member has an open invitation to attend meetings.

The Committee met prior to the Board meetings at which the interim financial statements and the annual report and accounts were approved. The Committee reviewed significant accounting policies, financial reporting issues and judgements and, in conducting these reviews, considered reports from the external auditor, finance management and internal audit.

At each of its meetings, the Committee reviewed and considered reports on the status of the Group's risk management processes, findings from the internal audit reviews of internal controls and reports on the status of the correction of any weaknesses in internal controls identified by the internal or external auditors. The Committee also reviewed the external auditor's Group management letters on accounting procedures and the systems of internal financial control.

During 2004 the Committee reviewed the effectiveness of the external audit process, the audit strategy and plans and qualifications, expertise and resources of the external auditor. It also reviewed and approved the proposed audit fee and terms of engagement for the 2004 audit and recommended to the Board that it propose to shareholders that Deloitte & Touche LLP continue as the Company's external auditor.

In August 2004 the Committee reviewed the independence procedures of Deloitte & Touche LLP, and at the March 2005 meeting received a letter from them confirming that, in their opinion, they remained independent. A policy, proposed by the Committee, on non-audit work by the external auditor was approved by the Board in June 2003 and remains essentially unchanged.

The policy, which includes audit partner rotation, is designed to ensure that the independence of the external auditor will not be compromised by any non-audit work they carry out for the Group by specifying (a) services from which they are excluded; (b) services for which they can be engaged without referral to the Committee; and (c) other services for which a case-by-case decision by the Committee is required. An analysis of non-audit fees incurred in 2004 is set out in Note 3 c) on page 58.

At the start of the year, the Committee and management commissioned a review of the internal audit function which resulted, inter alia, in the enhancement of existing practices within the department and confirmation of its remit. A new head of internal audit was appointed in September.

During the year, the Committee continued to receive regular reports on the work of the internal audit function and has reviewed the effectiveness of the department. The Head of Internal Audit has direct access to the Audit Committee and the Committee has, during the year met, separately, at each Committee meeting, the Head of Internal Audit, the Finance Director and external auditors.

– The Nomination Committee

The Committee was established by the Board in November 2003. Its terms of reference are available on the Company's website.

The Committee continues to be chaired by Sir David John. Its other members are Gordon Sage, Robert Walvis, Michael Welton (Ian Tyler since 1 January 2005) and Sir David Wright. The secretary of the Committee is Peter Johnson, director of personnel.

The Committee met on one occasion in 2004.

– The Remuneration Committee

Information about the working and membership of this Committee is contained in the Remuneration report beginning on page 44.

– The Business Practices Committee

The Business Practices Committee is chaired by Sir David John, and has as its other members Chalmers Carr, Christoph von Rohr, Gordon Sage, Robert Walvis and Sir David Wright. The Secretary is Christopher Pearson, the Company Secretary. It meets three or four times a year and its current terms of reference cover matters of business conduct, ethics, reputation, health, safety and the environment and matters of corporate social responsibility generally. It is also charged with reviewing the effectiveness of the whistle-blowing procedures established in the Group. In placing this last responsibility with the Business Practices Committee, the Company has not complied with the Code, which requires the Audit Committee to carry out the function. The reason for adopting a different approach in this respect is that the Board believes that, based on experience, the great majority of whistle-blowing complaints are likely to arise out of non-financial matters. Arrangements whereby concerns may be raised about possible financial impropriety will, as already stated, continue to be the concern of the Audit Committee.

The Committee met on four occasions during 2004. Among matters considered by the Committee in 2004 were the final draft of the Safety, Health and Environmental report (published in April), the health & safety statistics from around the Group, reports from the charities committee, the progress of Tr@ction, the incident reporting system, and the Group's whistle-blowing policy.

Details of the number of meetings of, and attendances at, the Board and the Audit, Nomination, Remuneration and Business Practices Committees during the year are set out in the table below. The relevant total number of meetings held in 2004 in each case is included in brackets after the name of the Board or Committee.

| Name of Director | Board (9) | Audit (5) | Nomination (1) | Remuneration (8) | Business Practices (4) |
|-----------------------------|-----------|-----------|----------------|------------------|------------------------|
| C Carr | 9 | 5 | | 7 | 4 |
| J L Cohen | 9 | | | | |
| R Delbridge | 7 | 5 | | 7 | |
| Sir David John ¹ | 8 | | 1 | 6 | 4 |
| A L P Rabin | 8 | | | | |
| Dr H C von Rohr | 8 | 4 | | 6 | 3 |
| G H Sage | 8 | 4 | 1 | | 3 |
| I P Tyler | 9 | | | | |
| R J W Walvis | 9 | | 1 | 8 | 4 |
| M W Welton | 9 | | | | |
| A J Wivell | 9 | | | | |
| Sir David Wright | 8 | 3 | 1 | | 3 |
| P J L Zinkin | 8 | | | | |

¹ resigned from Remuneration Committee with effect from 1 February 2005.

Board, Committee and individual director evaluation

The Board's responsibilities are listed in a schedule of matters reserved for its attention which the Board keeps under review.

Against this background, pursuant to the Code, the Directors considered during 2004 a number of different alternatives for evaluation of the Board itself and its Committees. In the end, they elected to use an independent and objective questionnaire-based process developed by an external consultant.

The consultant produced a written report in late October, from which an agreed set of actions has been developed and is being implemented during the course of 2005 and beyond.

The Board sees individual Director evaluation as very much the second stage of a two stage process, the first being Board and Board Committee evaluation, because it believes that individual evaluation is more likely to be of benefit when the Directors have had more time to work together as a board. Accordingly, a process of individual evaluation will be carried out when the Directors judge that sufficient time has passed to make the exercise worthwhile.

Dialogue with shareholders

The Company has a long-established programme of regular communication with institutional investors and brokers. Presentations are made to brokers' analysts, the press and institutional investors at the time of the announcement of final and half-year results and there are regular meetings with analysts and investors throughout the year, which are organised through the Company's brokers, so that the investment community can be kept informed of longer-term strategic matters and can communicate their views to the Board. We expect to continue this programme, within the constraints of relevant legislation and practice. The Group's website is at www.balfourbeatty.com and is a regular channel of communication with shareholders and others.

Regular reports are made by executive Directors to the Board on meetings and other contact with major shareholders or their representatives. The Chairman on occasion attends meetings with shareholders. The non-executive Directors believe that, by having direct and ready access to the Chairman at all times, through the senior independent Director and by reports given at Board meetings, they are kept fully aware of the views of the larger shareholders and the wider investment community. It is open to them or any of them to attend or arrange meetings with investors if they wish to do so.

During the first six months of 2004 a number of meetings were held by the Chairman and the senior independent Director with institutional shareholders, as a result of an offer made by the Chairman and senior independent Director to meet major shareholders in late 2003. The main topics covered in the meetings were, as might be expected, corporate governance, remuneration and safety, health and environmental issues. The meetings provided a good opportunity for the Board to further its understanding of the views of institutional shareholders.

Risk management

The Board takes ultimate responsibility for the Group's systems of risk management and internal control and reviews their effectiveness. The Board has conducted an assessment of the effectiveness of the risk management processes and internal controls during 2004 and in 2005 up to the date of this report. The review was based on reports to the Board, the Audit Committee and the Business Practices Committee on the following:

- results of internal audit's reviews of internal financial controls;
- a Group-wide certification that effective internal controls had been maintained, or, where any significant non-compliance or breakdown had occurred with or without loss, the status of corrective action; and
- a paper prepared by management on the nature, extent and mitigation of significant risks and on the systems of internal controls.

The Group's systems and controls are designed to ensure that the Group's exposure to significant risk is properly managed, but the Board recognises that any system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. In addition, not all the material joint ventures in which the Group is involved are treated, for these purposes, as part of the Group. Where they are not, systems of internal control are applied as agreed between the parties to the venture.

Central to the Group's systems of internal control are its processes and framework for risk management. These accord with the Turnbull Guidance on internal controls and were in place throughout the year and up to the date of signing this report.

The Group's systems of internal control operate through a number of different processes, some of which are interlinked. These include:

- the annual review of the strategy and plans of each operating company and of the Group as a whole in order to identify, inter alia, the risks to the Group's achievement of its overall objectives and, where appropriate, any relevant mitigating actions;
- monthly financial reporting against budgets and the review of results and forecasts by executive Directors and line management, including particular areas of business or project risk. This is used to update both management's understanding of the environment in which the Group operates and the methods used to mitigate and control the risks identified;
- individual tender and project review procedures commencing at operating company level and progressing to Board Committee level if value or perceived exposure breaches certain thresholds;
- regular reporting, monitoring and review of health, safety and environmental matters;
- the review and authorisation of proposed investment, divestment and capital expenditure through the Board's Committees and the Board itself;
- the review of specific material areas of Group-wide risk and the formulation and monitoring of risk mitigating actions;
- the formulation and review of properly documented policies and procedures, updated through the free and regular flow of information to address the changing risks of the business;
- specific policies set out in the Group Finance Manual, covering the financial management of the Group, including arrangements with the Group's bankers and bond providers, controls on foreign exchange dealings and management of currency and interest rate exposures, insurance, capital expenditure procedures, application of accounting policies and financial controls;
- a Group-wide risk management framework which is applied to all functions in the Group, whether operational, financial or support. Under it, the key risks facing each part of the Group are regularly reviewed and assessed, together with the steps to avoid or mitigate those risks. The results of those reviews are placed on risk registers and, where necessary, specific action plans are developed;
- reviews and tests by the internal audit team of critical business financial processes and controls and spot checks in areas of perceived high business risk; and
- the Group's whistle-blowing policy.

Remuneration Committee

The Remuneration Committee of the Board ("RemCo") is primarily responsible for determining the remuneration policy and conditions of service for the executive Directors and Chairman of the Company. It also reviews and monitors the level and structure of remuneration for senior management immediately below the level of the Board. The terms of reference of the RemCo can be found on the Company's website and are available on request from the Company Secretary.

The RemCo is chaired by Robert Walvis. Its other members are Chalmers Carr, Richard Delbridge and Christoph von Rohr, all of whom are independent non-executive Directors. Sir David John was a member of the RemCo until 1 February 2005 when he resigned from this committee. In future he will attend by invitation, when appropriate. No member of the RemCo has any personal financial interest, other than as a shareholder, in the matters to be decided by the RemCo, nor potential conflicts of interest arising from cross-directorships, and no member of the RemCo has any day-to-day involvement in the executive management of the Group.

During 2004 the Chief Executive, Michael Welton, was invited to join meetings of the RemCo whenever appropriate, and the practice of inviting the Chief Executive to join meetings has continued with Ian Tyler as Chief Executive. Peter Johnson, the director of personnel, continues to act as secretary of the RemCo. No Director has any involvement in discussions relating to his own remuneration.

Advice and assistance have been provided to the RemCo throughout the year by the Monks Partnership ("Monks"), New Bridge Street Consultants LLP ("NBSC") and Peter Johnson.

Monks and NBSC were each appointed by the RemCo to provide independent advice and assistance to it, and their terms of reference are available on the Company's website and on request from the Company Secretary. Monks has also provided data and advice to the Company regarding the remuneration of senior management below Board level.

Executive Directors' remuneration

General policy

It is the policy of the RemCo to provide an overall remuneration package that is competitive and fair to senior management and which facilitates the recruitment and retention of high calibre management. The annual and long-term incentive plans make up an important part of each executive Directors' remuneration and are structured so as to motivate senior managers to deliver high standards of performance, without encouraging excessive risk taking. It is intended that the share-based elements of the package will not only drive performance over the long term but will also assist in aligning the interests of management with those of shareholders.

During the course of 2004, the RemCo has carried out a review of the existing remuneration package and, as a result, believes that certain changes could be made which will make the package more effective in supporting the RemCo's remuneration policy. Although not requiring shareholder approval, these changes have been discussed with our major shareholders and are described in the relevant sections below. They will be implemented in 2005 and will continue in 2006, subject to review. If target performance is achieved, basic salary will represent around one half of total earnings. If maximum is achieved, which would involve a superior level of performance substantially in excess of business plan, basic salary will represent around one third of total earnings.

Executive Directors can join the Balfour Beatty Pension Fund. The RemCo is actively considering the policy it will adopt regarding pension provision after April 2006 in the light of the government's changes to pension taxation.

Basic salaries

It is the policy of the RemCo to set basic salaries at levels which it believes are competitive given the size and complexity of the Company, as well as the broad business sectors in which it operates. To assist in this, Monks and NBSC provide data and independent advice on remuneration levels in companies considered to be comparable in terms of annual sales, market capitalisation and industry sector. The RemCo does not specifically aim to set basic salaries at a stated point relative to the market, rather it uses this data in conjunction with its own judgement of the performance of the Group's businesses and the performance of individual Directors when setting basic salaries. The RemCo intends to continue to use this approach in the foreseeable future.

The basic salaries of executive Directors are reviewed annually at 1 July and the basic salaries following the review at 1 July 2004 are shown in the table below. The average increase was 6.5%.

| Name of Director | Salary at 1 July 2004 |
|------------------|--------------------------|
| J L Cohen | £300,000 |
| A L P Rabin | £305,000 |
| I P Tyler | £350,000 |
| M W Welton | £485,000 |
| A J Wivell | £300,000 |
| P J L Zinkin | £325,000 |

The RemCo subsequently agreed a basic salary of £440,000 for Ian Tyler which took effect on his appointment as Chief Executive on 1 January 2005.

Annual incentive plan

Each executive Director participates in an annual incentive plan, under which predetermined financial targets must be achieved before any payment is earned. The maximum potential bonus which could have been earned by executive Directors for 2004 was 50% of basic salary and the performance indicator chosen was profit before tax, exceptional items and goodwill amortisation ("profit"). A bonus of 25% of basic salary would have been earned for the achievement of performance in line with target. The actual profit for the year ended 31 December 2004 resulted in a bonus of 32.6% of basic salary for each executive Director. Precise figures are shown in the first table on page 46. These bonuses are payable in cash, after deduction of tax, and are non pensionable.

For 2005 a revised annual incentive plan will operate. Under the revised plan, the maximum potential bonus available to executive Directors and key senior managers will be 80% of basic salary. However, one third of any bonus earned will be deferred in the form of ordinary shares in the Company, which will be released after three years, providing the individual is still in the Company's employment at that time. The remaining two thirds of any bonus payment will be made immediately in cash after the deduction of tax.

The RemCo has decided to increase the maximum potential bonus because it believes that it is essential to have in place a competitive annual incentive which drives short-term performance and also ensures that the Company continues to attract and retain executive Directors and key senior managers who can deliver sustainable earnings growth in the future.

In designing the new structure, the RemCo also wanted to improve the link between annual and long-term performance and further strengthen the alignment of the interests of management with those of shareholders. For this reason there will now be a significant element of bonus deferral in the form of shares. Payment under the annual incentive plan will continue to occur only on the achievement of predetermined financial targets and payments will be non pensionable. In future, the RemCo will continue to review the competitiveness and structure of the annual incentive plan.

Long-term incentive scheme

In 2001 the Company obtained shareholder approval for a Performance Share Plan ("Plan"), a long-term incentive scheme which is entirely performance related. Under the Plan, executive Directors and key senior managers may receive ordinary shares in the Company up to a maximum number equivalent in market value to their basic salaries at the date of award. Details of awards to executive Directors are shown in the table on page 47. These shares will only vest to the extent that an earnings per share growth target is met over a three year performance period. The growth in earnings per share is determined following independent verification of the calculations made internally.

Growth in earnings per share before exceptional items, goodwill amortisation and appropriations arising on the buy-back of preference shares ("EPS") was chosen as the performance measure because it was, and remains, a key objective, since continuing growth in the Company's EPS should logically be reflected in growth in the share price and dividends and, therefore, increased returns to shareholders. The Directors and those other senior managers who participate in the Plan are positively motivated by it and fully understand the importance of EPS growth. The RemCo is aware of the impact of the introduction of International Financial Reporting Standards ("IFRS") on EPS and is considering how it will ensure consistency when assessing the achievement of performance targets for awards which have already been made, where performance periods span the introduction of IFRS.

The performance period for the conditional awards made in April 2002 was completed on 31 December 2004. The performance target for this award was such that the maximum number of shares would only vest if growth in EPS over the three year performance period was 100% or more. No shares would vest if EPS growth was below 30%. At a level of EPS growth of 30%, the minimum vesting of 30% of the maximum number of shares would occur, with levels of vesting pro rata to actual EPS growth between 30% and 100%. The growth in EPS for the period 1 January 2002 to 31 December 2004 was 65.96% and as a result, 65.96% of each participant's conditional award will vest on 17 April 2005.

Conditional awards were again approved by the RemCo and made under the Plan in 2004. In previous years the maximum award under the Plan was linked to an EPS growth target of 100%. In establishing performance targets for 2004, the RemCo considered the earnings growth achieved in recent years, future business prospects, and the requirement that targets going forward should continue to be demanding but also achievable. The RemCo concluded that to continue to link the minimum and maximum levels of vesting to EPS growth targets of 30% and 100% would not be effective in incentivising the participants to perform to the high standards required and that shareholders expect. As a result, the maximum award of shares in respect of the 2004 award will only vest if growth in the Company's EPS is at least 70% over the three year period ending 31 December 2006. If EPS growth is 25% over the period, participants will be entitled to 30% of the maximum award of shares. If EPS growth is between 25% and 70%, the number of shares vesting will

be pro rata to actual growth. No shares will vest if EPS growth is less than 25% and there is no provision for retesting the performance condition. The RemCo believes that the range of EPS targets established in 2004 remains amongst the most challenging in the sector and the market generally.

Unless circumstances change significantly, the RemCo intends to make further conditional awards under the Plan in 2005 and will again set similarly demanding targets which are consistent with the objectives of the Company and will motivate the participants to achieve earnings growth.

The Plan was approved at the 2001 Annual General Meeting for a period of five years and it is intended to submit proposals for future long-term incentive arrangements to shareholders for approval no later than the 2006 Annual General Meeting.

Share ownership guidelines

To further align the interests of senior management with those of shareholders, the RemCo has introduced share ownership guidelines which will apply to all participants in the Plan. Executive Directors will be required to build up a holding in shares of the Company to the value of one times basic salary. In order to achieve this, they will be expected to retain at least half of the shares (after payment of any taxes due) which vest from future awards made under the Plan and from the revised annual incentive plan.

Executive share options

Since the introduction of the Plan in 2001, it has been the RemCo's policy only to make grants of executive share options to participants in the Plan in exceptional circumstances, for example, to recruit a high calibre individual. Grants of options over ordinary shares were made to executive Directors before this time, some of which remain valid and unexercised and are detailed in the table on page 48. Certain managers below the level of those participating in the Plan have been granted options under the Executive Share Option Scheme 2001. In future, selected managers will participate in an annual incentive plan with a deferred share element similar to that described above, but with lower levels of maximum bonus. It is intended that no further grants of executive share options will be made to any level of management, except when it is necessary to facilitate the recruitment of an outstanding individual.

Savings-related share option scheme

The Company continues to operate an Inland Revenue approved savings-related share option scheme ("SAYE") under which employees are granted an option to purchase shares in the Company in either three or five years time, dependent upon their entering into a contract to make monthly contributions to a savings account over the relevant period. These savings are used to fund the option exercise. The exercise price for the SAYE options granted in 2004 was at a 20% discount to market value at the date of invitation. This scheme is open to all employees based in the UK, including executive Directors, and performance conditions are not applied to the exercise of SAYE options.

Executive Directors: Notice periods

Since 1999, it has been the Company's policy and practice to include in executive Directors' contracts a 12 month rolling notice period from the Company and six months' notice on the part of the Director. This policy will continue in the future.

Details of the service contracts of the executive Directors are shown in the table below.

| Name of Director | Date of contract | Notice period from Company (months) |
|------------------|-------------------|-------------------------------------|
| J L Cohen | 11 February 2000 | 12 |
| A L P Rabin | 28 August 2002 | 12 |
| I P Tyler | 22 December 2004 | 12 |
| M W Welton* | 12 September 1996 | 12 |
| A J Wivell | 23 July 2002 | 12 |
| P J L Zinkin | 10 December 1991 | 12 |

*Retired from the Company on 31 December 2004

Service contracts of executive Directors do not include provision for specific payment in the event of early termination, nor do they provide for extended notice periods in the event of a change of control. It is not the RemCo's intention to introduce such provisions. If any existing contract of employment is breached by the Company in the event of termination, the Company would be liable to pay, as damages, an amount approximating to the net loss of salary and contractual benefits for the unexpired notice period. The RemCo will seek to ensure that the Director fulfils his obligation to mitigate his losses and will also give consideration to phased payments where appropriate.

External appointments

The RemCo recognises that benefits can arise from allowing executive Directors to take a non-executive role elsewhere. With approval of the Board in each case, executive Directors may therefore accept one external appointment and retain any related fees. Jim Cohen was appointed as a non-executive Director of office2office plc on 29 June 2004 and fees of £16,500 were paid to him for his services during the year ended 31 December 2004.

Non-executive Directors

Non-executive Directors are appointed by the full Board following recommendations from the Nomination Committee. The Chairman's terms of service fall within the remit of the RemCo and the Board determines the terms on which the services of other non-executive Directors are provided. All non-executive Directors are elected for a term of three years unless required earlier to submit for re-election under the rotational provisions of the Articles of Association of the Company. They are not eligible to join the Balfour Beatty Pension Fund and cannot participate in any of the Company's share option, annual incentive or long-term incentive schemes. None of the appointment letters for non-executive Directors contain provision for specific payment in the event of termination for whatever cause.

The dates of the letters of appointment or last election of the non-executive Directors are shown in the table below.

| Name of Director | Date of appointment or last election | Unexpired period at 31 December 2004 (months) |
|------------------|--------------------------------------|---|
| C Carr | 13 May 2004 | 29 |
| R Delbridge | 15 May 2003 | 17 |
| Sir David John | 13 May 2004 | 29 |
| G H Sage | 13 May 2004 | 29 |
| Dr H C von Rohr | 13 May 2004 | 29 |
| R J W Walvis | 13 May 2004 | 29 |
| Sir David Wright | 15 May 2003 | 17 |

During the year, the executive Directors agreed that, in view of the increasing demands placed on the non-executive Directors, the basic annual fees payable to them (excluding the Chairman) should be increased by £3,000 to £33,000 with effect from 1 July 2004.

At the same time the RemCo agreed that the annual fees payable to the Chairman should be increased by £8,000 to £173,000 with effect from 1 July 2004. The Chairman was not in attendance when this matter was discussed.

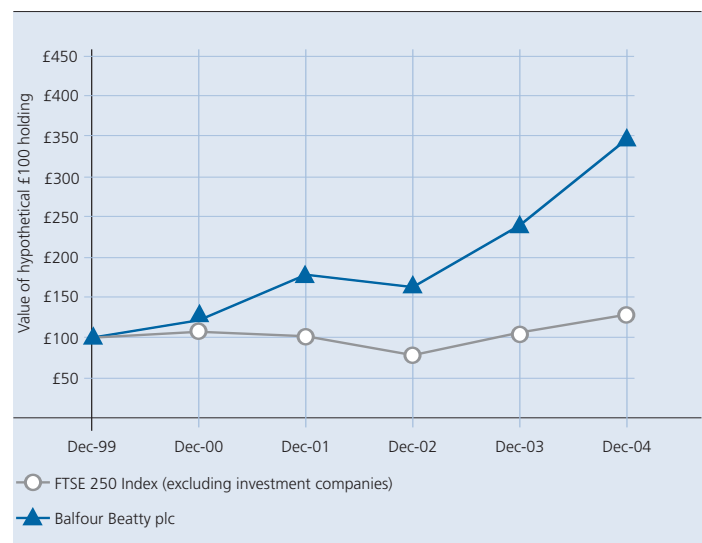
Additional fees of £6,000 per annum are payable to Robert Walvis and Richard Delbridge for their chairmanship of the RemCo and Audit Committees respectively, and a fee of €30,000 per annum is payable to Christoph von Rohr for his chairmanship of the supervisory board of Balfour Beatty Rail GmbH.

Performance graph

The graph below shows Balfour Beatty's Total Shareholder Return ("TSR") performance compared to the FTSE 250 Index (excluding investment companies) TSR over the five financial years ended 31 December 2004.

The values indicated in the graph show the share price growth plus reinvested dividends from a £100 hypothetical holding of ordinary shares in Balfour Beatty plc and in the index at the start of the period and have been calculated using 30 trading day average values.

The RemCo has elected to compare the TSR on the Company's ordinary shares against the FTSE 250 Index (excluding investment companies) principally because this is a broad index of which the Company is a constituent member.



The detailed information about the Directors' remuneration, set out on pages 46 to 50, has been audited by the Company's independent auditors, Deloitte & Touche LLP.

Directors' remuneration earned in 2004

| Name of Director | Basic salary £ | Fees £ | Benefits in kind £ | Annual bonus £ | Compensation for loss of office £ | Total remuneration 2004 £ | Total remuneration 2003 £ |
|----------------------------|-------------------|----------------|--------------------------|----------------------|--|------------------------------------|------------------------------------|
| C Carr | – | 31,500 | – | – | – | 31,500 | 10,000 |
| J L Cohen | 292,500 | – | 16,179 | 97,800 | – | 406,479 | 373,085 |
| R Delbridge | – | 37,500 | – | – | – | 37,500 | 33,750 |
| Sir David John | – | 169,000 | – | – | – | 169,000 | 114,375 |
| A L P Rabin | 292,500 | – | 17,352 | 99,430 | – | 409,282 | 361,528 |
| G H Sage | – | 31,500 | – | – | – | 31,500 | 10,000 |
| I P Tyler | 340,000 | – | 22,669 | 114,100 | – | 476,769 | 430,555 |
| Dr H C von Rohr | – | 51,908 | – | – | – | 51,908 | 28,410 |
| R J W Walvis | – | 37,000 | – | – | – | 37,000 | 30,000 |
| M W Welton | 470,000 | – | 26,925 | 158,110 | – | 655,035 | 582,109 |
| A J Wivell | 290,000 | – | 16,244 | 97,800 | – | 404,044 | 361,446 |
| Sir David Wright | – | 31,500 | – | – | – | 31,500 | 30,000 |
| P J L Zinkin | 317,500 | – | 15,668 | 105,950 | – | 439,118 | 399,402 |
| Former Directors (note vi) | – | – | 18,937 | – | 40,000 | 58,937 | 712,670 |
| Total | 2,002,500 | 389,908 | 133,974 | 673,190 | 40,000 | 3,239,572 | 3,477,330 |

Notes:

- Basic salary and fees were those paid in respect of the period of the year during which individuals were Directors.
- Christoph von Rohr receives a €30,000 per annum fee for his chairmanship of the supervisory board of Balfour Beatty Rail GmbH.
- The additional fee of £6,000 paid to Robert Walvis for his chairmanship of the RemCo was paid with effect from 1 February 2004.
- Benefits in kind are calculated in terms of UK taxable values. For the executive Directors they comprise: a fully expensed car, a fuel card, and private medical insurance for the Director and his immediate family.
- Other than as stated in Note (iv), no Director receives any expense allowance.
- As detailed in the previous Remuneration Report, a payment of £40,000 was made on 25 October 2004 to Malcolm Eckersall, a former Director, under the terms on which he left the Company on 31 October 2003. The Company also continued to provide Malcolm Eckersall with a fully expensed car, a fuel card, and private medical insurance until 31 October 2004, the estimated UK taxable value of which is shown in the table above.

Directors' interests

The interests of the Directors and their immediate families in the share capital of Balfour Beatty plc and its subsidiary undertakings during the year are set out below.

| Name of Director | Number of ordinary shares | |
|------------------|---------------------------|---------------------------|
| | At 1 January 2004 | At 31 December 2004 |
| J L Cohen | 24,195 | 79,286 |
| R Delbridge | 15,000 | 15,000 |
| Sir David John | 5,000 | 5,000 |
| A L P Rabin | 22,272 | 25,239 |
| G H Sage | – | 5,000 |
| I P Tyler | 62,623 | 63,981 |
| R J W Walvis | 10,000 | 10,000 |
| M W Welton | 137,880 | 138,660 |
| A J Wivell | 20,228 | 20,228 |
| P J L Zinkin | 26,380 | 51,049 |

Notes:

- Peter Zinkin was also interested at 1 January 2004 and 31 December 2004 in 325 cumulative convertible redeemable preference shares of 1p each of Balfour Beatty plc.
- As participants in the Performance Share Plan, which satisfies awards using shares held by the Balfour Beatty Employee Share Ownership Trust, all of the executive Directors are deemed to be interested in the entire shareholding of the Trust, which at 31 December 2004 amounted to 1.182m ordinary shares.
- All interests at the dates shown are beneficial and there were no changes between 31 December 2004 and 8 March 2005.

Directors' long-term incentives: the Performance Share Plan

| Name of Director | Date granted | Maximum number of shares subject to award | | | | | At 31 December 2004 | Exercisable from |
|------------------|---------------|---|-------------------------------|------------------------------|------------------------------|---------|---------------------------|------------------|
| | | At 1 January 2004 | Awarded during the year | Lapsed during the year | Vested during the year | | | |
| J L Cohen | 7 June 2001 | 115,384 | – | – | 115,384 | – | | |
| | 17 April 2002 | 105,226 | – | – | – | 105,226 | April 2005 | |
| | 16 April 2003 | 156,376 | – | – | – | 156,376 | April 2006 | |
| | 19 April 2004 | – | 109,439 | – | – | 109,439 | April 2007 | |
| A L P Rabin | 7 June 2001 | 80,267 | – | – | 80,267 | – | | |
| | 17 April 2002 | 71,553 | – | – | – | 71,553 | April 2005 | |
| | 16 April 2003 | 150,584 | – | – | – | 150,584 | April 2006 | |
| | 19 April 2004 | – | 107,519 | – | – | 107,519 | April 2007 | |
| I P Tyler | 7 June 2001 | 115,384 | – | – | 115,384 | – | | |
| | 17 April 2002 | 105,226 | – | – | – | 105,226 | April 2005 | |
| | 16 April 2003 | 179,543 | – | – | – | 179,543 | April 2006 | |
| | 19 April 2004 | – | 126,719 | – | – | 126,719 | April 2007 | |
| M W Welton | 7 June 2001 | 167,424 | – | – | 167,424 | – | | |
| | 17 April 2002 | 154,499 | – | – | – | 154,499 | April 2005 | |
| | 16 April 2003 | 240,356 | – | 240,356 | – | – | | |
| | 19 April 2004 | – | 174,719 | 174,719 | – | – | | |
| A J Wivell | 7 June 2001 | 71,867 | – | – | 71,867 | – | | |
| | 17 April 2002 | 65,307 | – | – | – | 65,307 | April 2005 | |
| | 16 April 2003 | 150,584 | – | – | – | 150,584 | April 2006 | |
| | 19 April 2004 | – | 107,519 | – | – | 107,519 | April 2007 | |
| P J L Zinkin | 7 June 2001 | 124,423 | – | – | 124,423 | – | | |
| | 17 April 2002 | 110,404 | – | – | – | 110,404 | April 2005 | |
| | 16 April 2003 | 167,960 | – | – | – | 167,960 | April 2006 | |
| | 19 April 2004 | – | 119,039 | – | – | 119,039 | April 2007 | |

Notes:

- (i) All awards are granted for nil consideration and are in respect of 50p ordinary shares of Balfour Beatty plc.
- (ii) For the awards made in April 2004, the performance period is the three years ending 31 December 2006. The maximum number of shares shown in the table above will vest only if earnings per share before exceptional items, goodwill amortisation and appropriations arising on the buy-back of preference shares ("EPS") grows by at least 70% over the performance period. If EPS growth is 25%, the Directors will be entitled to 30% of the maximum award of shares. If EPS growth is between 25% and 70%, the number of shares vesting will be pro rata to actual growth. No shares will vest if EPS growth is less than 25%, and there is no provision for retesting.
- (iii) For the awards made in April 2002 and April 2003, the performance periods are the three years ending 31 December 2004 and 31 December 2005 respectively. The maximum award of shares shown in the table above will vest only if EPS grows by at least 100% over the performance period. If EPS growth is 30%, the Directors will be entitled to 30% of the maximum award of shares. If EPS growth is between 30% and 100%, the number of shares vesting will be pro rata to actual growth. No shares will vest if EPS growth is less than 30%, and there is no provision for retesting.
- (iv) The performance period for the awards made in April 2002 was completed on 31 December 2004. The growth in EPS for this period was 65.96% and as a result, 65.96% of each participant's conditional award will vest on 17 April 2005.
- (v) The performance period for the awards made in June 2001 was completed on 31 December 2003. The growth in EPS for this period exceeded 100% and as a result, 100% of each participant's conditional award vested on 7 June 2004. The closing middle market price of ordinary shares on the vesting date was 250.25p.
- (vi) The awards made to Michael Welton in 2003 and 2004 lapsed on his retirement from the Company on 31 December 2004. However, since he had been employed by the Company for the entirety of the performance period for the 2002 award, the RemCo decided it was appropriate to exercise its discretion in his favour and allow him to retain this award on his retirement from the Company, exercisable at the same time and in the same proportion as the awards of other participants.
- (vii) The average middle market price of ordinary shares in the Company for the three dealing dates before the date of the 2001 award under the Plan, which was used for calculating the number of shares conditionally awarded, was 199.333p, for the 2002 award was 237.583p, for the 2003 award was 172.66p and for the 2004 award was 260.417p. The closing middle market price of ordinary shares on the date of the awards was 202.5p, 251p, 170.5p and 260p respectively.

Directors' share options

| Name of Director | Date granted | At 1 January 2004 | Granted during the year | Exercised during the year | Number of options | | Exercise price | Exercisable | | |
|-------------------------|-----------------|-------------------------|-------------------------------|---------------------------------|------------------------------|---------------------------|----------------|---------------|---------------|--|
| | | | | | Lapsed during the year | At 31 December 2004 | | from | to | |
| J L Cohen | | | | | | | | | | |
| Executive Share Options | 13 April 1995 | 15,340 | – | – | – | 15,340 | 311.9p | April 1998 | April 2005 | |
| | 9 November 1999 | 80,000 | – | 80,000 | – | – | 110.0p | November 2002 | November 2009 | |
| Savings-Related Options | 13 April 2000 | 100,000 | – | 100,000 | – | – | 79.0p | April 2003 | April 2010 | |
| | 19 July 2001 | 1,610 | – | 1,610 | – | – | 154.0p | October 2004 | March 2005 | |
| | 8 May 2002 | 743 | – | – | – | 743 | 184.0p | July 2005 | December 2005 | |
| | 5 May 2004 | – | 646 | – | – | 646 | 210.0p | July 2007 | December 2007 | |
| | | | | | | | | | | |
| A L P Rabin | | | | | | | | | | |
| Executive Share Options | 17 April 1996 | 10,227 | – | – | – | 10,227 | 344.2p | April 1999 | April 2006 | |
| Savings-Related Options | 6 October 1999 | 2,967 | – | 2,967 | – | – | 91.0p | December 2004 | May 2005 | |
| | 24 May 2000 | 3,286 | – | – | – | 3,286 | 76.0p | August 2005 | January 2006 | |
| | 19 July 2001 | 1,227 | – | – | – | 1,227 | 154.0p | October 2006 | March 2007 | |
| | 8 May 2002 | 575 | – | – | – | 575 | 184.0p | July 2007 | December 2007 | |
| | 7 May 2003 | 444 | – | – | – | 444 | 133.0p | July 2008 | December 2008 | |
| | 5 May 2004 | – | 903 | – | – | 903 | 210.0p | July 2009 | December 2009 | |
| I P Tyler | | | | | | | | | | |
| Savings-Related Options | 19 July 2001 | 1,358 | – | 1,358 | – | – | 154.0p | October 2004 | March 2005 | |
| | 8 May 2002 | 640 | – | – | – | 640 | 184.0p | July 2005 | December 2005 | |
| | 7 May 2003 | 511 | – | – | – | 511 | 133.0p | July 2006 | December 2006 | |
| M W Welton | | | | | | | | | | |
| Executive Share Options | 27 April 1994 | 15,340 | – | – | 15,340 | – | 438.1p | April 1997 | April 2004 | |
| | 13 April 1995 | 15,340 | – | – | – | 15,340 | 311.9p | April 1998 | April 2005 | |
| Savings-Related Options | 19 July 2001 | 780 | – | 780 | – | – | 154.0p | October 2004 | March 2005 | |
| | 8 May 2002 | 702 | – | – | 702 | – | 184.0p | July 2005 | December 2005 | |
| | 7 May 2003 | 653 | – | – | 653 | – | 133.0p | July 2006 | December 2006 | |
| | | | | | | | | | | |
| A J Wivell | | | | | | | | | | |
| Executive Share Options | 13 April 1995 | 15,340 | – | – | – | 15,340 | 311.9p | April 1998 | April 2005 | |
| P J L Zinkin | | | | | | | | | | |
| Savings-Related Options | 6 October 1999 | 1,260 | – | 1,260 | – | – | 91.0p | December 2004 | May 2005 | |
| | 24 May 2000 | 2,842 | – | – | – | 2,842 | 76.0p | August 2005 | January 2006 | |
| | 19 July 2001 | 2,454 | – | – | – | 2,454 | 154.0p | October 2006 | March 2007 | |
| | 8 May 2002 | 1,151 | – | – | – | 1,151 | 184.0p | July 2007 | December 2007 | |
| | 7 May 2003 | 839 | – | – | – | 839 | 133.0p | July 2008 | December 2008 | |
| | 5 May 2004 | – | 716 | – | – | 716 | 210.0p | July 2009 | December 2009 | |

Notes:

- (i) All options are granted for nil consideration on grant and are in respect of 50p ordinary shares of Balfour Beatty plc.
- (ii) All outstanding executive share options held by Directors have satisfied the performance conditions that were required to be met before exercise and are, therefore, exercisable at the discretion of the option holder.
- (iii) The closing market price of the Company's ordinary shares on 31 December 2004 was 315.25p. During the year the highest and lowest closing market prices were 315.25p and 212.75p.
- (iv) Michael Welton's savings-related share options granted in 2002 and 2003 lapsed immediately following his retirement from the Company on 31 December 2004. Executive share options granted to him in April 1994, lapsed unexercised in April 2004.
- (v) Details of options exercised and the value realisable on exercise are shown in the table on page 49.

| Name of Director | Date granted | Date exercised | Number of options exercised | Exercise price | Closing market price on date exercised | Value realisable on exercise* |
|-------------------------|-----------------|------------------|-----------------------------|----------------|--|-------------------------------|
| J L Cohen | | | | | | |
| Executive Share Options | 9 November 1999 | 14 May 2004 | 80,000 | 110.0p | 247.0p | £109,600 |
| | 13 April 2000 | 14 May 2004 | 100,000 | 79.0p | 247.0p | £168,000 |
| Savings-Related Options | 19 July 2001 | 17 December 2004 | 1,610 | 154.0p | 302.5p | £2,391 |
| A L P Rabin | | | | | | |
| Savings-Related Options | 6 October 1999 | 1 December 2004 | 2,967 | 91.0p | 302.0p | £6,260 |
| I P Tyler | | | | | | |
| Savings-Related Options | 19 July 2001 | 29 October 2004 | 1,358 | 154.0p | 271.25p | £1,592 |
| M W Welton | | | | | | |
| Savings-Related Options | 19 July 2001 | 15 October 2004 | 780 | 154.0p | 276.5p | £956 |
| P J L Zinkin | | | | | | |
| Savings-Related Options | 6 October 1999 | 1 December 2004 | 1,260 | 91.0p | 302.0p | £2,659 |

*The value realisable from shares acquired on exercise is the difference between the closing market price on the date exercised and the exercise price of the options, although the shares may have been retained, in which case they are included in the table on page 46, headed "Directors' interests".

Directors' pensions

Executive Directors participate in the Balfour Beatty Pension Fund. The scheme provides for a pension at a normal retirement age of 62 and each Director pays an annual contribution equal to 5% of pensionable salary. The pension for a Director who can complete 20 or more years' pensionable service at normal retirement age is targeted at two-thirds of final pensionable salary, subject to Inland Revenue limits. Directors have the option to pay additional voluntary contributions, but neither the contributions nor the resulting benefits are included in the tables below. The salaries of Jim Cohen, Anthony Rabin and Ian Tyler were subject to the Inland Revenue earnings cap for pension purposes and details of the Company's contributions to additional arrangements for them are noted underneath the table on page 50.

The table below sets out the accrued deferred pension which would be paid annually from the scheme at normal retirement age based on each executive Director's service to 31 December 2004 as well as the additional pension benefit secured in respect of service during the year.

| Name of Director | Age at 31 December 2004 years | Pensionable service at 31 December 2004 (Note i) years | Accrued deferred pension at 31 December 2003 £pa | Increase in accrued deferred pension during the year | | Accrued deferred pension at 31 December 2004 £pa | Transfer value corresponding to increase in excess of inflation at 31 December 2004 less Director's contributions (Note ii) £ |
|------------------|-------------------------------|--|--|--|-------------------------------------|--|---|
| | | | | Inflation £pa | Increase in excess of inflation £pa | | |
| J L Cohen | 62 | 11 | 32,386 | 907 | 3,668 | 36,961 | 80,149 |
| A L P Rabin | 49 | 2 | 4,472 | 125 | 3,104 | 7,701 | 27,375 |
| I P Tyler | 44 | 8 | 18,804 | 527 | 2,499 | 21,830 | 15,068 |
| M W Welton | 58 | 34 | 243,938 | 6,830 | 75,838 | 326,606 | 1,289,578 |
| A J Wivell | 59 | 31 | 162,276 | 4,544 | 10,796 | 177,616 | 195,817 |
| P J L Zinkin | 51 | 23 | 131,581 | 3,684 | 4,584 | 139,849 | 39,063 |

Notes:

- Michael Welton's pensionable service includes eight years of transferred-in service from previous employment.
- The transfer value of the increase in accrued deferred pension is the present value of the increase in excess of inflation in the deferred pension and associated benefits during the period, less the Director's contributions, calculated using the transfer basis in force at 31 December 2004 and on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11. For Michael Welton, the transfer value includes the value of his transferred-in pension benefits from a previous employer.

The table below sets out the transfer value at 31 December 2004 of each executive Director's accrued deferred pension at that date as well as the movement in that transfer value over the period. The transfer values represent the cash equivalent values that would have been payable from the scheme had the Directors left service on the dates shown, and reflect the age of the Director, his period of membership of the scheme and his pensionable salary.

| Name of Director | Age at 31 December 2004 years | Pensionable service at 31 December 2004 years | Transfer value at 31 December 2003 (Note i) £ | Contributions made by Director during the year £ | Increase in transfer value during the year less Director's contributions (Note ii) £ | Transfer value at 31 December 2004 (Note i) £ |
|-----------------------|-------------------------------|---|---|--|--|---|
| J L Cohen | 62 | 11 | 570,573 | 5,063 | 91,000 | 666,636 |
| A L P Rabin | 49 | 2 | 42,084 | 5,063 | 31,685 | 78,832 |
| I P Tyler | 44 | 8 | 137,405 | 5,063 | 31,023 | 173,491 |
| M W Welton (Note iii) | 58 | 34 | 3,741,383 | 23,352 | 2,076,989 | 5,841,724 |
| A J Wivell | 59 | 31 | 2,731,862 | 14,352 | 628,579 | 3,374,793 |
| P J L Zinkin | 51 | 23 | 1,387,446 | 15,727 | 214,792 | 1,617,965 |

Notes:

- (i) The transfer value is the present value of the accrued deferred pension and associated benefits at the relevant date, calculated using the transfer basis then in force and on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11.
- (ii) The figure is the difference between the transfer value of the accrued benefits at the start and end of the period, less the Director's contributions during the period.
- (iii) Michael Welton retired on 31 December 2004 and took immediate pension benefits. The transfer value at 31 December 2004 is the actuarial value of these benefits. The increase in transfer value is due to a combination of factors including an additional year of service, a salary increase from 1 July 2004, the effect of him taking early retirement, one year's ageing and changes in investment conditions. The benefit entitlements he accrued as a member of the Balfour Beatty Pension Fund were calculated with reference to his basic salary and in accordance with the Rules of this Fund. No augmentation to these benefits has been granted. As reported in Note (i) to the second table on page 49, Michael Welton had eight years of transferred-in service from a previous employer. On retirement, the Trustee was able to grant these transferred-in benefits from the Fund at their fair value, within Inland Revenue limits, and the transfer value shown at 31 December 2004 fully takes account of this.

The salaries of Jim Cohen, Anthony Rabin and Ian Tyler were subject to the Inland Revenue earnings cap for pension purposes, and the Company has contributed to a Funded Unapproved Retirement Benefit Scheme ("FURBS") for each of them. In 2004, the Company's contribution to Jim Cohen's plan was £32,346, to Anthony Rabin's £50,531 and to Ian Tyler's £38,209. Benefits under these FURBS are additional to those set out in the tables above.

No past Director of the Company has received or become entitled to receive retirement benefits in excess of his entitlements on the date on which those benefits first became payable, or 31 March 1997 if later.

Remuneration report

Signed by order of the Board

C R O'N Pearson

Secretary
8 March 2005

To the members of Balfour Beatty plc

We have audited the financial statements of Balfour Beatty plc for the year ended 31 December 2004 which comprise the profit and loss account, the balance sheets, the cash flow statement, the statement of total recognised gains and losses, and the related notes 1 to 29. These financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the part of the Directors' remuneration report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

As described in the statement of Directors' responsibilities, the Company's Directors are responsible for the preparation of the financial statements in accordance with applicable United Kingdom law and accounting standards. They are also responsible for the preparation of the other information contained in the annual report including the Directors' remuneration report. Our responsibility is to audit the financial statements and the part of the Directors' remuneration report described as having been audited in accordance with relevant United Kingdom legal and regulatory requirements and auditing standards.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions with the Company and other members of the Group is not disclosed.

We review whether the corporate governance statement reflects the Company's compliance with the nine provisions of the July 2003 FRC Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the Directors' report and the other information contained in the Annual Report including the unaudited part of the Directors' remuneration report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Directors' remuneration report which is described as having been audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the Company and of the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Directors' remuneration report described as having been audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' remuneration report described as having been audited.

Opinion

In our opinion:

- the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December 2004 and of the profit of the Group for the year then ended; and
- the financial statements and the part of the Directors' remuneration report described as having been audited have been properly prepared in accordance with the Companies Act 1985.

Deloitte & Touche LLP

Chartered Accountants and Registered Auditors
London
8 March 2005

Group profit and loss account

For the year ended 31 December 2004

| | Notes | Before exceptional items 2004 £m | Exceptional items (Note 4) 2004 £m | Total 2004 £m | Before exceptional items 2003 £m | Exceptional items (Note 4) 2003 £m | Total 2003 as restated £m |
|--|--------|--|--|---------------------|--|--|------------------------------------|
| Turnover including share of joint ventures and associates | 2 | 4,171 | – | 4,171 | 3,678 | – | 3,678 |
| Share of turnover of joint ventures | 3 & 11 | (380) | – | (380) | (297) | – | (297) |
| Share of turnover of associates | 3 & 11 | (292) | – | (292) | (220) | – | (220) |
| Group turnover | | 3,499 | – | 3,499 | 3,161 | – | 3,161 |
| Continuing operations | | 3,432 | – | 3,432 | 3,058 | – | 3,058 |
| Acquisitions | 20 | 16 | – | 16 | – | – | – |
| Discontinued operations | 2 | 51 | – | 51 | 103 | – | 103 |
| Cost of sales | 3 | (3,161) | 7 | (3,154) | (2,850) | 3 | (2,847) |
| Gross profit | | 338 | 7 | 345 | 311 | 3 | 314 |
| Net operating expenses | 3 | (271) | – | (271) | (243) | – | (243) |
| Group operating profit | | 67 | 7 | 74 | 68 | 3 | 71 |
| Share of operating profit of joint ventures | 3 & 11 | 27 | – | 27 | 47 | – | 47 |
| Share of operating profit of associates | 3 & 11 | 44 | – | 44 | 29 | – | 29 |
| Operating profit including share of joint ventures and associates | | 138 | 7 | 145 | 144 | 3 | 147 |
| Operating profit before goodwill amortisation | | 173 | 7 | 180 | 161 | 3 | 164 |
| Goodwill amortisation and impairment | 9 & 11 | (35) | – | (35) | (17) | – | (17) |
| Continuing operations | | 121 | 7 | 128 | 128 | 3 | 131 |
| Acquisitions | 20 | 9 | – | 9 | – | – | – |
| Discontinued operations | 2 | 8 | – | 8 | 16 | – | 16 |
| Profit on sale of operations | | | 135 | 135 | | – | – |
| Provision for loss on sale of operations | | | 2 | 2 | | (10) | (10) |
| (Loss)/profit on sale of tangible fixed assets | | | (2) | (2) | | 12 | 12 |
| Profit on ordinary activities before interest | 3 | 138 | 142 | 280 | 144 | 5 | 149 |
| Net interest payable and similar charges: | | | | | | | |
| Group | 5 | – | – | – | (1) | – | (1) |
| Share of joint ventures' interest | 5 & 11 | (9) | – | (9) | (18) | – | (18) |
| Share of associates' interest | 5 & 11 | (14) | – | (14) | (12) | – | (12) |
| Profit on ordinary activities before taxation | | 115 | 142 | 257 | 113 | 5 | 118 |
| Profit on ordinary activities before goodwill amortisation and taxation | | 150 | 142 | 292 | 130 | 5 | 135 |
| Goodwill amortisation and impairment | 9 & 11 | (35) | – | (35) | (17) | – | (17) |
| Tax on profit on ordinary activities | 6 | (39) | (15) | (54) | (30) | 1 | (29) |
| Profit for the financial year | | 76 | 127 | 203 | 83 | 6 | 89 |
| Dividends: | | | | | | | |
| Preference | 7 | | | (13) | | | (15) |
| Ordinary | 7 | | | (28) | | | (25) |
| Premium paid on buy-back of preference shares | 19 | | | (6) | | | (5) |
| Transfer to reserves | | | | 156 | | | 44 |
| Adjusted earnings per ordinary share | 8 | | | 23.4p | | | 20.6p |
| Goodwill amortisation and impairment | | | | (8.3)p | | | (4.1)p |
| Exceptional items after attributable taxation | 4 | | | 30.2p | | | 1.4p |
| Premium paid on buy-back of preference shares | | | | (1.5)p | | | (1.0)p |
| Basic earnings per ordinary share | 8 | | | 43.8p | | | 16.9p |
| Diluted earnings per ordinary share | 8 | | | 43.4p | | | 16.7p |
| Dividends per ordinary share | 7 | | | 6.6p | | | 6.0p |

Balance sheets

At 31 December 2004

Balfour Beatty plc
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| | Notes | Group 2004 £m | Group 2003 as restated £m | Company 2004 £m | Company 2003 as restated £m |
|--|-------|---------------------|------------------------------------|-----------------------|--------------------------------------|
| Fixed assets | | | | | |
| Intangible assets – goodwill | 9 | 265 | 306 | – | – |
| Tangible assets – PFI/PPP constructed assets | 10 | 288 | – | – | – |
| – other | 10 | 149 | 158 | 1 | 1 |
| Investments | 11 | 42 | 36 | 534 | 775 |
| Investments in joint ventures: | | | | | |
| Share of gross assets | | 815 | 866 | – | – |
| Share of gross liabilities | | (715) | (777) | – | – |
| | 11 | 100 | 89 | – | – |
| Investments in associates | 11 | 81 | 47 | – | – |
| | | 925 | 636 | 535 | 776 |
| Current assets | | | | | |
| Stocks | 12 | 102 | 109 | 1 | 1 |
| Debtors – due within one year | 13 | 738 | 759 | 48 | 56 |
| – due after one year | 13 | 79 | 60 | 9 | 14 |
| Cash and deposits – PFI/PPP subsidiaries | 14 | 30 | – | – | – |
| – other | 14 | 388 | 202 | 259 | 37 |
| | | 1,337 | 1,130 | 317 | 108 |
| Creditors: amounts falling due within one year | | | | | |
| Borrowings – PFI/PPP non-recourse term loans | 14 | (13) | – | – | – |
| – other | 14 | (15) | (7) | (4) | (14) |
| Other creditors | 16 | (1,209) | (1,195) | (75) | (61) |
| Net current assets/(liabilities) | | 100 | (72) | 238 | 33 |
| Total assets less current liabilities | | 1,025 | 564 | 773 | 809 |
| Creditors: amounts falling due after more than one year | | | | | |
| Borrowings – PFI/PPP non-recourse term loans | 14 | (261) | (3) | – | – |
| – other | 14 | (62) | (68) | (62) | (66) |
| Other creditors | 16 | (110) | (95) | (25) | (35) |
| Provisions for liabilities and charges | 17 | (179) | (167) | (9) | (11) |
| | | 413 | 231 | 677 | 697 |
| Capital and reserves | | | | | |
| Called-up share capital | 18 | 213 | 212 | 213 | 212 |
| Share premium account | 19 | 150 | 328 | 150 | 328 |
| Revaluation reserves | 19 | 70 | 48 | – | – |
| Special reserve | 19 | 181 | – | 181 | – |
| Other reserves | 19 | 4 | 8 | 46 | 50 |
| Profit and loss account | 19 | (205) | (365) | 87 | 107 |
| Shareholders' funds | | 413 | 231 | 677 | 697 |
| Equity interests | | 277 | 81 | 541 | 547 |
| Non-equity interests | 18 | 136 | 150 | 136 | 150 |
| | | 413 | 231 | 677 | 697 |

On behalf of the Board

Sir David John Director
A L P Rabin Director
8 March 2005

Group cash flow statement

For the year ended 31 December 2004

| | Notes | 2004 £m | 2003 as restated £m |
|---|-------|------------|---------------------------|
| Net cash inflow from operating activities | 28(a) | 171 | 170 |
| Dividends from joint ventures and associates | 11(d) | 8 | 11 |
| Returns on investments and servicing of finance | | | |
| Interest received | | 18 | 9 |
| Interest paid | | (24) | (10) |
| Preference dividends paid | | (15) | (15) |
| Net cash outflow from returns on investments and servicing of finance | | (21) | (16) |
| UK corporation tax paid | | (25) | (19) |
| Foreign tax paid | | (16) | (6) |
| Taxation | | (41) | (25) |
| Capital expenditure and financial investment | | | |
| Capital expenditure | | (110) | (51) |
| Disposal of tangible fixed assets | | 13 | 24 |
| Investment in joint ventures and associates | | (11) | (6) |
| Other investments | | 51 | (6) |
| Net cash outflow from capital expenditure and financial investment | | (57) | (39) |
| Acquisitions and disposals | | | |
| Acquisitions of businesses | 28(d) | (56) | (21) |
| Disposals of businesses | 28(e) | 217 | – |
| Net cash inflow/(outflow) from acquisitions and disposals | | 161 | (21) |
| Ordinary dividends paid | | (25) | (22) |
| Cash inflow before use of liquid resources and financing | | 196 | 58 |
| Management of liquid resources | | | |
| Increase in term deposits | 28(b) | (206) | (32) |
| Net cash outflow from management of liquid resources | | (206) | (32) |
| Financing | | | |
| Ordinary shares issued | | 4 | 5 |
| Purchase of ordinary shares | | (2) | (1) |
| Buy-back of preference shares | | (20) | (16) |
| New loans | | 6 | 3 |
| Repayment of loans | | (12) | (11) |
| Capital element of finance lease payments | | (2) | (3) |
| Net cash outflow from financing | | (26) | (23) |
| (Decrease)/increase in cash in the period | 28(c) | (36) | 3 |

Group statement of total recognised gains and losses

For the year ended 31 December 2004

| | 2004 £m | 2003 as restated £m |
|--|------------|---------------------------|
| Profit for the financial year: | | |
| Group | | |
| Group operating profit | 74 | 71 |
| Profit on sale of operations | 135 | – |
| Provision for loss on sale of operations | 2 | (10) |
| (Loss)/profit on sale of tangible fixed assets | (2) | 12 |
| Net interest payable and similar charges | – | (1) |
| Tax on profit on ordinary activities | (36) | (14) |
| | 173 | 58 |
| Share of joint ventures (see Note 11(b)) | 10 | 19 |
| Share of associates (see Note 11(b)) | 20 | 12 |
| Exchange adjustments | (2) | (1) |
| Total recognised gains and losses for the year | 201 | 88 |

1 Principal accounting policies

A summary of the principal accounting policies, all of which have been applied consistently throughout the year and the preceding year, is set out below:

a) Basis of accounting

The accounts have been prepared under the historical cost convention, modified for the revaluation of certain land and buildings, and comply with all applicable accounting standards and the Companies Act 1985.

The Group has adopted UITF Abstract 38 "Accounting for ESOP trusts" and the amendments to UITF Abstract 17 "Employee share schemes" and comparative figures have been restated accordingly. Previously, investments in Balfour Beatty plc ordinary shares of 50p each acquired by the Group's discretionary trust, the Balfour Beatty Employee Share Ownership Trust, to satisfy awards under the Balfour Beatty Performance Share Plan, were recognised as a fixed asset investment, net of provisions. The cost of shares acquired was charged to the profit and loss account over the qualifying period. In accordance with UITF 38 and UITF 17, own shares held by the Group's discretionary trust are recorded as a deduction in arriving at shareholders' funds and the fair value of the shares at the date of award is charged to the profit and loss account over the qualifying period. In addition, purchases of shares, which were previously shown in the cash flow statement within capital expenditure and financial investment, are now disclosed within the financing section. This restatement has had no impact on operating profit in 2003. Shareholders' funds as at 31 December 2003 were increased by £1.3m. The Group has also adopted UITF Abstract 37 "Purchases and sales of own shares" and comparative figures have been restated accordingly, reducing basic earnings per ordinary share in 2003 by 1.0p. The difference between the carrying amount of preference shares bought back and the consideration paid has been reported as an appropriation of profit.

b) Basis of consolidation

The Group accounts include the accounts of the Company and its subsidiary undertakings, together with the Group's share of the results of joint ventures and associates drawn up to 31 December each year. The results of subsidiaries, joint ventures and associates acquired or sold in the year are consolidated from the respective date of acquisition or to the respective date of disposal. In accordance with FRS 10 "Goodwill and Intangible Assets", with effect from 1 January 1998, goodwill, being the excess of the fair value of consideration over the fair value of net assets acquired, arising on the acquisition of subsidiaries, joint ventures and associates is capitalised and amortised through the profit and loss account over the Directors' estimate of its economic useful life of up to 20 years. Goodwill arising before 1 January 1998 has been eliminated against reserves and is included in the profit and loss account at the time of the disposal of the business to which it relates.

The Group's share of the net assets of contracting joint arrangements is included under each relevant heading within the balance sheet.

c) Foreign currencies

Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction or, if hedged, at the forward contract rate. Monetary assets and liabilities denominated in foreign currencies are reported at the rates of exchange prevailing at the balance sheet date or, if appropriate, at the forward contract rate.

The results of overseas subsidiaries, joint ventures and associates are translated at average rates of exchange for the year and their assets and liabilities are translated at year end rates. Exchange differences on opening net assets less offsetting foreign currency loans and other hedging instruments to the extent that they hedge the Group's investments are reported in the statement of total recognised gains and losses. All other exchange differences are dealt with in the profit and loss account.

d) Financial derivatives

The Group uses derivative financial instruments to manage interest rate risk and to hedge exposures to fluctuations in foreign currencies. Receipts and payments on interest rate instruments are recognised on an accruals basis over the life of the instrument. Forward contracts used to hedge foreign currency investments are revalued to year end rates and any exchange differences are taken to reserves. The difference between the spot and forward rates on such contracts is recognised on an accruals basis as part of net interest payable. Gains and losses on financial instruments used to hedge foreign currency transactions are recognised on maturity of the underlying transaction in the profit and loss account or as adjustments to carrying amounts in the balance sheet. Gains and losses on financial instruments which are terminated because the underlying exposure ceases to exist are taken immediately to the profit and loss account.

e) Finance costs

Finance costs of debt are charged in the profit and loss account over the term of the instrument at a constant rate on the carrying amount. Finance costs that are directly attributable to the construction of tangible fixed assets and long-term finance assets in the course of construction are capitalised as part of the cost of those assets commencing at the start of construction and ceasing when the asset is complete and ready for use.

f) Turnover

Turnover represents amounts invoiced to outside customers, net of trade discounts, value added and similar sales-based taxes, except in respect of contracting activities where turnover represents the value of work carried out during the year including amounts not invoiced.

g) Profit recognition on contracting activities

Profit on individual contracts is taken only when their outcome can be foreseen with reasonable certainty, based on the lower of the percentage margin earned to date and that prudently forecast at completion, taking account of agreed claims. Full provision is made for all known or expected losses on individual contracts, taking a prudent view of future claims income, immediately such losses are foreseen. Profit for the year includes the benefit of claims settled on contracts completed in prior years.

Pre-contract costs are expensed as incurred until it is virtually certain that a contract will be awarded, from which time further pre-contract costs are recognised as an asset and charged as an expense over the period of the contract. Amounts recovered in respect of costs that have been written off are deferred and amortised over the life of the contract.

h) PFI/PPP concessions

Assets constructed by PFI/PPP concession companies are classified as fixed assets or as long-term finance assets of the concession company depending on the allocation of risks between the concession company and the public sector authority.

Where the concession company takes the greater share of the risks associated with the asset the asset is capitalised and depreciated over the life of the concession. Revenue is recognised as turnover as it is earned.

Where the public sector authority takes the greater share of the risks associated with the asset the asset is classified as a long-term finance asset. Revenues received are apportioned between capital repayments, relating to the provision of the asset, and operating revenue. The finance income element of the capital repayment is recognised as interest receivable using a rate of return specific to the asset. The operating revenue relating to the provision of services is recognised as turnover as it is earned.

i) Research and development

Research and development expenditure is written off in the year in which it is incurred.

j) Tangible fixed assets

Except for land and assets in the course of construction, the cost or valuation of tangible fixed assets is depreciated over their expected useful lives, on a straight line basis at rates of 2.5% for buildings and 4% to 33% for plant and equipment, or the life of the lease.

Assets held under finance leases are treated as tangible fixed assets; depreciation is provided accordingly, and the deemed capital element of future rentals is included within borrowings. Deemed interest, calculated on a reducing balance basis, is charged as interest payable over the period of the lease. The rental costs arising from operating leases are charged against operating profit as they arise.

k) Investments

Joint ventures and associates are included in the consolidated balance sheet at the Group's share of net tangible asset values, plus loans due from such undertakings and attributable goodwill arising since 1 January 1998, less amounts amortised and provided for. The excess of attributable net assets of joint ventures and associates over their cost is included in the Group's revaluation reserve. Other Group investments and the Company's investments are stated at cost plus loans, less amounts provided for.

l) Stocks

Stocks and unbilled contract work in progress are valued at the lower of cost and net realisable value. Cost, where appropriate, includes a proportion of manufacturing overheads. Applications for progress payments are deducted from cost, with any excess included in other creditors as advance progress applications.

m) Taxation

The tax charge is composed of current tax and deferred tax. Current tax is based on the profit for the year at the current rate.

Deferred taxation is provided using the liability method. Timing differences arising from provisions, post retirement benefits and capital allowances are fully recognised. Deferred tax assets are recognised to the extent it is believed they will be recovered against future taxable profits. Deferred tax assets and liabilities are not discounted.

Provision is not made for taxation which would be payable if the retained profits of overseas subsidiary undertakings, joint ventures and associates were remitted to the UK, or which would arise on any excess of the sale proceeds over the cost of land and buildings if they were to be sold at their revalued amounts.

n) Pensions

Contributions to defined benefit pension schemes are charged to the profit and loss account so as to spread the cost of providing pensions over employees' working lives with the Group. Variations in pension costs are allocated over the remaining service lives of employees as an adjustment to the regular pension cost. Differences between contributions paid and amounts charged in the profit and loss account are included as a prepayment or liability in the balance sheet. Contributions to defined contribution pension schemes are charged to the profit and loss account as they fall due.

2 Segment analysis*a) Total Group, including share of joint ventures and associates*

| | Turnover 2004 £m | Turnover 2003 £m | Operating profit before exceptional items 2004 £m | Operating profit before exceptional items 2003 £m | Capital employed 2004 £m | Capital employed 2003 as restated £m |
|---|------------------------|------------------------|---|---|-----------------------------------|--|
| Performance by activity | | | | | | |
| Building, building management and services | 1,586 | 1,093 | 32 | 28 | (154) | (153) |
| Civil and specialist engineering and services | 1,443 | 1,393 | 23 | 21 | (45) | (44) |
| Rail engineering and services | 803 | 873 | 43 | 41 | (57) | (51) |
| Investments and developments | 288 | 216 | 67 | 54 | 353 | 56 |
| | 4,120 | 3,575 | 165 | 144 | 97 | (192) |
| Discontinued operations | 51 | 103 | 8 | 17 | – | 21 |
| | 4,171 | 3,678 | 173 | 161 | 97 | (171) |
| Goodwill amortisation | | | (35) | (17) | | |
| Operating profit | | | 138 | 144 | | |
| Net interest payable | | | (23) | (31) | | |
| Profit before tax and exceptional items | | | 115 | 113 | | |
| Net cash | | | | | 67 | 124 |
| Goodwill (including share of joint ventures and associates) | | | | | 295 | 318 |
| Tax and dividends | | | | | (46) | (40) |
| | | | | | 413 | 231 |
| Performance by geographic origin | | | | | | |
| Europe | 3,591 | 3,127 | 204 | 170 | 70 | (221) |
| North America | 415 | 483 | (35) | (12) | 8 | 41 |
| Other | 165 | 68 | 4 | 3 | 19 | 9 |
| | 4,171 | 3,678 | 173 | 161 | 97 | (171) |

Andover Controls sold in July 2004 has been classified as discontinued. Goodwill amortisation arises in Building, building management and services £4.3m (2003: £1.2m), Civil and specialist engineering and services £5.0m (2003: £5.5m), Rail engineering and services £24.6m (2003: £9.0m), Investments and developments £0.3m (2003: nil) and Discontinued operations £0.7m (2003: £1.6m). In 2004, goodwill amortisation includes £15.9m impairment charge in respect of Balfour Beatty Rail Inc. In 2003, goodwill amortisation included £0.5m impairment charge in respect of Garanti Balfour Beatty. Goodwill arises in Building, building management and services £64m (2003: £62m), Civil and specialist engineering and services £95m (2003: £80m), Rail engineering and services £131m (2003: £152m), Investments and developments £5m (2003: £1m) and Discontinued operations nil (2003: £23m).

Goodwill amortisation arises in Europe £14.8m (2003: £12.3m), North America £19.4m (2003: £4.7m) and Other £0.7m (2003: £0.3m). Goodwill arises in Europe £240m (2003: £242m), North America £31m (2003: £72m) and Other £24m (2003: £4m).

b) Share of joint ventures and associates

| | Turnover 2004 £m | Turnover 2003 £m | Operating profit before exceptional items 2004 £m | Operating profit before exceptional items 2003 £m | Capital employed 2004 £m | Capital employed 2003 £m |
|---|------------------------|------------------------|---|---|-----------------------------------|-----------------------------------|
| Performance by activity | | | | | | |
| Building, building management and services | 118 | 122 | 3 | 6 | 4 | 3 |
| Civil and specialist engineering and services | 299 | 177 | 14 | 12 | 43 | 29 |
| Rail engineering and services | 3 | 2 | (1) | – | (1) | – |
| Investments and developments | 252 | 216 | 57 | 60 | 105 | 92 |
| | 672 | 517 | 73 | 78 | 151 | 124 |
| Goodwill amortisation | | | (2) | (2) | | |
| Operating profit | | | 71 | 76 | | |
| Net interest payable | | | (23) | (30) | | |
| Profit before tax and exceptional items | | | 48 | 46 | | |
| Goodwill | | | | | 30 | 12 |
| | | | | | 181 | 136 |
| Performance by geographic origin | | | | | | |
| Europe | 513 | 450 | 69 | 75 | 131 | 115 |
| Other | 159 | 67 | 4 | 3 | 20 | 9 |
| | 672 | 517 | 73 | 78 | 151 | 124 |

Goodwill amortisation arises in Building, building management and services £1.3m (2003: £1.2m), Civil and specialist engineering and services £0.6m (2003: £0.9m) and Rail engineering and services £0.1m (2003: £0.1m). Goodwill arises in Building, building management and services £6m (2003: £7m), Civil and specialist engineering and services £22m (2003: £2m), Rail engineering and services £2m (2003: £2m) and Investments and developments nil (2003: £1m).

Goodwill amortisation arises in Europe £1.3m (2003: £1.9m) and Other £0.7m (2003: £0.3m). Goodwill arises in Europe £6m (2003: £8m) and Other £24m (2003: £4m).

2 Segment analysis continued

c) Investments and developments performance

The Investments and developments segment includes the Group's PFI/PPP activities (Balfour Beatty Capital Projects) details of which are set out below:

| | Group turnover 2004 £m | Share of joint ventures' and associates' turnover 2004 £m | Total turnover 2004 £m | Group operating profit 2004 £m | Share of joint ventures' and associates' operating profit 2004 £m | Total operating profit 2004 £m | Group capital employed 2004 £m | Share of joint ventures' and associates' capital employed 2004 £m | Total capital employed 2004 £m |
|--|---------------------------|--|---------------------------|-----------------------------------|--|-----------------------------------|-----------------------------------|--|-----------------------------------|
| PFI/PPP joint ventures and associates (see Note 11b) | – | 206 | 206 | – | 42 | 42 | – | 87 | 87 |
| PFI/PPP subsidiaries (see (d) below) | 36 | – | 36 | 21 | – | 21 | 277 | – | 277 |
| PFI/PPP bidding costs and overheads | – | – | – | (10) | – | (10) | (10) | – | (10) |
| Loans from PFI/PPP joint ventures and associates | – | – | – | – | – | – | (25) | – | (25) |
| Balfour Beatty Capital Projects | 36 | 206 | 242 | 11 | 42 | 53 | 242 | 87 | 329 |
| Barking Power Ltd | – | 46 | 46 | – | 15 | 15 | – | 18 | 18 |
| Property development and other | – | – | – | (1) | – | (1) | 6 | – | 6 |
| | 36 | 252 | 288 | 10 | 57 | 67 | 248 | 105 | 353 |

| | Group turnover 2003 £m | Share of joint ventures' and associates' turnover 2003 £m | Total turnover 2003 £m | Group operating profit 2003 £m | Share of joint ventures' and associates' operating profit 2003 £m | Total operating profit 2003 £m | Group capital employed as restated 2003 £m | Share of joint ventures' and associates' capital employed 2003 £m | Total capital employed as restated 2003 £m |
|--|---------------------------|--|---------------------------|-----------------------------------|--|-----------------------------------|---|--|---|
| PFI/PPP joint ventures and associates (see Note 11b) | – | 174 | 174 | – | 54 | 54 | – | 81 | 81 |
| PFI/PPP subsidiaries (see (d) below) | – | – | – | – | – | – | 3 | – | 3 |
| PFI/PPP bidding costs and overheads | – | – | – | (5) | – | (5) | (18) | – | (18) |
| Loans from PFI/PPP joint ventures and associates | – | – | – | – | – | – | (25) | – | (25) |
| Balfour Beatty Capital Projects | – | 174 | 174 | (5) | 54 | 49 | (40) | 81 | 41 |
| Barking Power Ltd | – | 42 | 42 | – | 6 | 6 | – | 11 | 11 |
| Property development and other | – | – | – | (1) | – | (1) | 4 | – | 4 |
| | – | 216 | 216 | (6) | 60 | 54 | (36) | 92 | 56 |

d) PFI/PPP subsidiaries

The Group has a 100% interest in four PFI/PPP concessions through its shareholdings in Connect Roads Ltd, Connect M77/GSO Holdings Ltd and Connect Roads Underland Holdings Ltd. The performance of these PFI/PPP concessions (since becoming subsidiaries as appropriate) and their balance sheets are summarised below:

| | 2004 £m | 2003 £m |
|--|------------|------------|
| Profit and loss account | | |
| Turnover | 36 | – |
| Operating profit | 21 | – |
| Net interest payable | (12) | – |
| Profit on ordinary activities before taxation | 9 | – |
| Tax on profit on ordinary activities | (2) | – |
| Profit for the period | 7 | – |
| Cash flow | | |
| Operating profit | 21 | – |
| Depreciation | 9 | – |
| Working capital decrease/(increase) | 1 | (3) |
| Net cash inflow from operating activities | 31 | (3) |
| Returns on investments and servicing of finance | (20) | – |
| Taxation | (4) | – |
| Capital expenditure and financial investment | (2) | – |
| Dividends paid | (9) | – |
| Cash outflow before use of liquid resources and financing | (4) | (3) |
| Opening net borrowings/net borrowings at date of acquisition | (240) | – |
| Closing net borrowings | (244) | (3) |
| Balance sheet | | |
| Tangible fixed assets | 288 | – |
| Debtors | 25 | 3 |
| Creditors and provisions | (36) | – |
| Tax and dividends | (10) | – |
| Cash and deposits | 30 | – |
| Project finance non-recourse term loans | (274) | (3) |
| Net assets | 23 | – |

2 Segment analysis continued*e) Turnover by destination*

| | 2004 £m | 2003 £m |
|---|--------------|--------------|
| Total Group, including share of joint ventures and associates | | |
| United Kingdom | 3,261 | 2,749 |
| Rest of Europe | 263 | 268 |
| North America | 412 | 476 |
| Other | 235 | 185 |
| | 4,171 | 3,678 |

3 Profit before interest and exceptional items*a) Turnover, cost of sales and net operating expenses*

| | Continuing operations 2004 £m | Acquisitions 2004 £m | Discontinued operations 2004 £m | Total 2004 £m | Continuing operations 2003 £m | Discontinued operations 2003 £m | Total 2003 £m |
|---|--|----------------------------|--|---------------------|--|--|---------------------|
| Turnover including share of joint ventures and associates | 4,015 | 105 | 51 | 4,171 | 3,575 | 103 | 3,678 |
| Less: share of turnover of joint ventures | (291) | (89) | – | (380) | (297) | – | (297) |
| Less: share of turnover of associates | (292) | – | – | (292) | (220) | – | (220) |
| Group turnover | 3,432 | 16 | 51 | 3,499 | 3,058 | 103 | 3,161 |
| Cost of sales | (3,128) | (7) | (26) | (3,161) | (2,786) | (64) | (2,850) |
| Gross profit | 304 | 9 | 25 | 338 | 272 | 39 | 311 |
| Net operating expenses (including goodwill amortisation and impairment) | (252) | (2) | (17) | (271) | (220) | (23) | (243) |
| Group operating profit before exceptional items | 52 | 7 | 8 | 67 | 52 | 16 | 68 |
| Share of operating profit of joint ventures | 25 | 2 | – | 27 | 47 | – | 47 |
| Share of operating profit of associates | 44 | – | – | 44 | 29 | – | 29 |
| Operating profit before exceptional items | 121 | 9 | 8 | 138 | 128 | 16 | 144 |

b) Profit on ordinary activities before interest is stated after charging:

| | 2004 £m | 2003 £m |
|--|------------|------------|
| Depreciation | 50 | 43 |
| Goodwill amortisation – including share of joint ventures and associates £2m (2003: £2m) | 19 | 17 |
| Goodwill impairment | 16 | – |
| Hire charges for plant and equipment | 82 | 59 |
| Other operating lease rentals | 44 | 43 |
| Research and development expenditure | 8 | 10 |
| Auditors' remuneration, which for Balfour Beatty plc was £0.4m (2003: £0.4m) | 2 | 2 |

c) Analysis of fees paid to auditors

| | 2004 £m | 2003 £m |
|--|------------|------------|
| Services as auditors | 1.9 | 1.9 |
| Further assurance services – acquisition due diligence | 0.4 | 0.3 |
| – other assurance services | 0.5 | 0.3 |
| Tax services – compliance | 0.1 | – |
| – advisory | 0.1 | 0.3 |
| | 3.0 | 2.8 |

4 Exceptional items

| | 2004 £m | 2003 £m |
|--|------------|------------|
| a) Credited to/(charged against) operating profit | | |
| Compensation for loss of use of operating facility | – | 10 |
| Cancellation of Network Rail maintenance contracts | 7 | (7) |
| | 7 | 3 |
| b) Profit/(loss) on sale of operations | | |
| Profit on disposal of Andover Controls | 137 | – |
| Loss on disposal of Garanti Balfour Beatty | (2) | – |
| Loss on disposal of First Philippine Balfour Beatty Inc | (1) | – |
| Profit on sale of Hong Kong business | 1 | – |
| | 135 | – |
| c) Provision for loss on sale of operations | | |
| Losses arising from the disposal of the discontinued Cables businesses | – | (8) |
| Provision for loss on disposal of Garanti Balfour Beatty | 2 | (2) |
| | 2 | (10) |
| d) (Loss)/profit on sale of tangible fixed assets | | |
| Loss on sale of fixed assets | (2) | – |
| Profit on sale of operating facility | – | 12 |
| | (2) | 12 |
| | 142 | 5 |

- a) The exceptional item credited to Group operating profit in 2004 arises in respect of the resolution of certain matters previously provided for in 2003 in relation to the cancellation of three Network Rail maintenance contracts. Exceptional items charged against Group operating profit in 2003 also included compensation received in respect of business disruption, following the compulsory purchase of an operating facility. These exceptional items related to the Rail engineering and services segment and arose in Europe.
- b) In 2004 a profit of £137m (after charging goodwill previously written off to reserves of £37m) arose on the disposal of Andover Controls for a consideration of US\$403m.
In 2004, a loss of £2m (previously provided in 2003) arose on the disposal of the Group's 49.2% interest in Garanti Balfour Beatty Sanayi ve Ticaret AS for a consideration of US\$1; a loss of £1m (comprising goodwill previously written off to reserves) arose on the disposal of the Group's 40% interest in First Philippine Balfour Beatty Inc for a consideration of US\$3.5m; a profit of £1m arose on the transfer of the Group's construction contracts in progress in Hong Kong to the Gammon Skanska Group following the acquisition of a 50% interest in that business (see Note 20). These exceptional items arose in the Civil and specialist engineering and services segment.
- c) The provision for loss on sale of operations in 2003 comprised provision for environmental and employee retirement costs relating to the discontinued Cables businesses in North America sold in 1999 and provision for losses on the disposal in 2004 of the Group's 49.2% interest in Garanti Balfour Beatty in Turkey in the Civil and specialist engineering and services segment.
- d) In 2004, a net loss of £2m arose on the sale of fixed assets which comprises £2m profit on the sale of properties and plant in the UK and £4m loss on the disposal of specialist plant in the US marine civil engineering business. The net loss arose in the Building, building management and services segment £1m profit, Rail engineering and services £1m profit and Civil and specialist engineering and services £4m loss. The profit on sale of fixed assets in 2003 arose on the compulsory purchase of an operating facility. This profit related to the Rail engineering and services segment and arose in Europe.
- e) Exceptional items increased the Group's tax charge in 2004 by £15m (2003: £1m reduction).

5 Net interest payable and similar charges

| | 2004 £m | 2003 £m |
|---|------------|------------|
| Group | | |
| PFI/PPP non-recourse – other net interest payable | 13 | – |
| – interest on long-term finance assets | (1) | – |
| | 12 | – |
| Other net interest payable: | | |
| Bank loans and overdrafts | 2 | 2 |
| Finance leases | 1 | 1 |
| Other loans | 7 | 9 |
| PFI/PPP subordinated debt interest receivable | (9) | (2) |
| Other interest receivable and similar income | (13) | (9) |
| | – | 1 |
| Share of joint ventures | | |
| PFI/PPP concessions – other net interest payable | 27 | 36 |
| – interest on long-term finance assets | (18) | (18) |
| | | |
| Share of associates | | |
| PFI/PPP concessions – other net interest payable | 9 | 7 |
| Other associates – other net interest payable | 5 | 5 |
| | 23 | 31 |

6 Tax on profit on ordinary activities**a) Taxation charge**

| | 2004 £m | 2003 £m |
|---|------------|------------|
| UK current tax | | |
| Corporation tax for the period at 30% (2003: 30%) | 37 | 31 |
| Double tax relief | (2) | (2) |
| Adjustments in respect of previous periods | (8) | (4) |
| | 27 | 25 |
| UK advance corporation tax | | |
| Written back against current year UK tax | (11) | (8) |
| Adjustments in respect of other periods | (6) | (5) |
| | (17) | (13) |
| Foreign current tax | | |
| Foreign tax on profits of the period | 18 | 5 |
| Adjustments in respect of previous periods | (1) | 2 |
| | 17 | 7 |
| Total current tax | 27 | 19 |
| Deferred tax (see Note 17) | | |
| UK | 4 | (5) |
| Adjustments in respect of previous periods | 5 | – |
| Total deferred tax | 9 | (5) |
| Joint ventures and associates | | |
| Share of UK joint ventures' tax | 7 | 10 |
| Share of UK associates' tax | 10 | 5 |
| Share of foreign joint ventures' tax | 1 | – |
| Total joint ventures' and associates' tax | 18 | 15 |
| Taxation charge | 54 | 29 |

b) Factors that may affect future tax charges

The Group has benefited from overseas tax losses in 2004. These losses have resulted in reduced tax payments in recent years and the Group expects to continue to benefit in 2005. The unrecognised deferred tax asset in respect of losses that arose over a number of years in the USA and Germany is estimated to be £65m (2003: £100m).

In 2004, the Group has recognised £17m of surplus advance corporation tax, of which £8m is recoverable against future periods. The tax rate in future periods is expected to be higher following the recognition of this amount.

6 Tax on profit on ordinary activities continued*c) Taxation reconciliation*

| | 2004 £m | 2003 £m |
|---|------------|------------|
| Profit on ordinary activities before tax | 257 | 118 |
| Less: share of joint ventures' and associates' profit before tax | (48) | (46) |
| Group profit on ordinary activities before tax | 209 | 72 |
| Profit on ordinary activities before tax at standard UK corporation tax rate of 30% (2003: 30%) | 63 | 22 |
| Effects of: | | |
| Expenses not deductible for tax purposes including goodwill amortisation | 11 | 4 |
| Timing differences | | |
| – capital allowances for period in excess of depreciation | (1) | – |
| – other short-term timing differences | (3) | 5 |
| Utilisation of overseas tax losses | (35) | (1) |
| Losses not available for offset | 1 | 7 |
| Higher tax rates on overseas earnings | 1 | 3 |
| Disposal of investments and other assets not taxable | (2) | (6) |
| Goodwill written off on disposal of businesses | 7 | – |
| Goodwill previously written off to reserves | 11 | – |
| Advance corporation tax written back | (11) | (8) |
| Adjustments in respect of other periods | (15) | (7) |
| Current tax charge | 27 | 19 |

7 Dividends

| | Per share 2004 pence | Amount 2004 £m | Per share 2003 pence | Amount 2003 £m |
|-----------------------------|----------------------------|----------------------|----------------------------|----------------------|
| On preference shares | | | | |
| Paid | 4.8375 | 7 | 4.8375 | 7 |
| Payable | 4.8375 | 6 | 4.8375 | 8 |
| | 9.6750 | 13 | 9.6750 | 15 |
| On ordinary shares | | | | |
| Interim payable | 2.85 | 12 | 2.60 | 11 |
| Final proposed | 3.75 | 16 | 3.40 | 14 |
| | 6.60 | 28 | 6.00 | 25 |

8 Earnings per ordinary share

The calculation of earnings per ordinary share is based on the profit for the financial year, after charging preference dividends and appropriations arising on the buy-back of preference shares, divided by the weighted average number of ordinary shares in issue during the year of 419.4m (2003: 416.3m).

The calculation of diluted earnings per ordinary share is based on the profit for the financial year, after charging preference dividends and appropriations arising on the buy-back of preference shares, divided by the weighted average number of ordinary shares in issue adjusted for the potential conversion of share options by 4m (2003: 3m). As in 2003, no adjustment has been made in respect of the potential conversion of the cumulative convertible redeemable preference shares, the effect of which would have been antidilutive throughout the year.

Adjusted earnings per ordinary share before goodwill amortisation and impairment, exceptional items and appropriations arising on the buy-back of preference shares have been disclosed to give a clearer understanding of the Group's underlying trading performance.

9 Intangible assets – goodwill

| | Gross £m | Amortisation £m | Net £m |
|--|-------------|--------------------|-----------|
| At 1 January 2004 | 350 | (44) | 306 |
| Exchange adjustments | (4) | 1 | (3) |
| Businesses acquired (see Note 20) | 14 | – | 14 |
| – Businesses sold | (27) | 5 | (22) |
| – Other adjustments | 3 | – | 3 |
| Amortisation | – | (17) | (17) |
| Impairment | – | (16) | (16) |
| At 31 December 2004 | 336 | (71) | 265 |
| Goodwill arising on joint ventures and associates (see Note 11a) | | | 30 |
| Total goodwill | | | 295 |

10 Tangible fixed assets

a) Movements

| | Land and buildings £m | Plant and equipment £m | Assets in course of construction £m | PFI/PPP constructed assets £m | Group Total £m | Land and buildings £m | Plant and equipment £m | Company Total £m |
|------------------------------------|--------------------------|---------------------------|--|----------------------------------|-------------------|--------------------------|---------------------------|---------------------|
| Cost or valuation: | | | | | | | | |
| At 1 January 2004 | 46 | 343 | 3 | – | 392 | – | 2 | 2 |
| Exchange adjustments | – | (7) | – | – | (7) | – | – | – |
| Additions | 1 | 46 | 4 | 66 | 117 | – | – | – |
| Disposals | (3) | (32) | – | – | (35) | – | – | – |
| Businesses acquired | – | (2) | – | 231 | 229 | – | – | – |
| Businesses sold | (2) | (15) | – | – | (17) | – | – | – |
| Transfers | – | 2 | (2) | – | – | – | – | – |
| At 31 December 2004 | 42 | 335 | 5 | 297 | 679 | – | 2 | 2 |
| Depreciation: | | | | | | | | |
| At 1 January 2004 | 11 | 223 | – | – | 234 | – | 1 | 1 |
| Exchange adjustments | – | (5) | – | – | (5) | – | – | – |
| Charge for the year | 1 | 40 | – | 9 | 50 | – | – | – |
| Disposals | – | (24) | – | – | (24) | – | – | – |
| Businesses sold | (1) | (12) | – | – | (13) | – | – | – |
| At 31 December 2004 | 11 | 222 | – | 9 | 242 | – | 1 | 1 |
| Net book value at 31 December 2004 | 31 | 113 | 5 | 288 | 437 | – | 1 | 1 |
| Net book value at 31 December 2003 | 35 | 120 | 3 | – | 158 | – | 1 | 1 |

The net book value of fixed assets held under finance leases was £1m (2003: £2m) for the Group with related depreciation provided in the year of £1m (2003: £1m). The Company has no fixed assets held under finance leases.

PFI/PPP constructed assets, which arise in the concession companies Connect A30/A35 Ltd, Connect A50 Ltd and Connect M77/GSO plc, include £137m assets in course of construction. The cost of PFI/PPP constructed assets includes interest capitalised of £35m, of which £7m was capitalised in the year.

b) Analysis of net book value of land and buildings

| | Group 2004 £m | Group 2003 £m | Company 2004 £m | Company 2003 £m |
|--|---------------------|---------------------|-----------------------|-----------------------|
| Freehold | 25 | 29 | – | – |
| Long leasehold – over 50 years unexpired | 3 | 3 | – | – |
| Short leasehold | 3 | 3 | – | – |
| | 31 | 35 | – | – |

c) Valuations

On implementing the requirements of FRS 15 "Tangible Fixed Assets" the Group has not adopted a policy of revaluation. Certain land and buildings were revalued in 1991 and, in accordance with the transitional provisions of FRS 15, the carrying amount of these assets has been retained and has not been updated. In the Group, assets included at valuation, their original cost and depreciation based on cost are as follows:

| | At valuation 2004 £m | At valuation 2003 £m | Original cost 2004 £m | Original cost 2003 £m |
|--------------|-------------------------------|-------------------------------|--------------------------------|--------------------------------|
| Gross | 4 | 4 | 2 | 2 |
| Depreciation | (1) | (1) | (1) | (1) |
| Net | 3 | 3 | 1 | 1 |

The Company has no revalued assets.

11 Investments*a) Movements*

| | Joint ventures £m | Associates £m | Other £m | Group Total £m | Subsidiaries £m | Joint ventures and associates £m | Other £m | Company Total £m |
|--|----------------------|------------------|-------------|----------------------|--------------------|---|-------------|------------------------|
| Cost or valuation: | | | | | | | | |
| At 1 January 2004 – as originally reported | 38 | 44 | 42 | 124 | 1,103 | 8 | 4 | 1,115 |
| Prior year adjustment (see below) | – | – | (3) | (3) | – | – | (3) | (3) |
| At 1 January 2004 – as restated | 38 | 44 | 39 | 121 | 1,103 | 8 | 1 | 1,112 |
| Exchange adjustments | (2) | – | – | (2) | – | – | – | – |
| Profit and loss account | 8 | 16 | – | 24 | – | – | – | – |
| Additions | – | 9 | 6 | 15 | 12 | – | – | 12 |
| Businesses acquired | 13 | – | – | 13 | – | – | – | – |
| Disposals and transfers | (16) | 3 | – | (13) | (50) | (4) | – | (54) |
| At 31 December 2004 | 41 | 72 | 45 | 158 | 1,065 | 4 | 1 | 1,070 |
| Goodwill: | | | | | | | | |
| At 1 January 2004 | 12 | – | – | 12 | – | – | – | – |
| Amortisation | (2) | – | – | (2) | – | – | – | – |
| Businesses acquired | 21 | – | – | 21 | – | – | – | – |
| Disposals and transfers | (7) | 6 | – | (1) | – | – | – | – |
| At 31 December 2004 | 24 | 6 | – | 30 | – | – | – | – |
| Loans due from investments: | | | | | | | | |
| At 1 January 2004 | 40 | 30 | – | 70 | 433 | 32 | – | 465 |
| Movements | (5) | (2) | – | (7) | (107) | (8) | – | (115) |
| At 31 December 2004 | 35 | 28 | – | 63 | 326 | 24 | – | 350 |
| Provisions: | | | | | | | | |
| At 1 January 2004 – as originally reported | (1) | (27) | (6) | (34) | (166) | (2) | (4) | (172) |
| Prior year adjustment (see below) | – | – | 3 | 3 | – | – | 3 | 3 |
| At 1 January 2004 – as restated | (1) | (27) | (3) | (31) | (166) | (2) | (1) | (169) |
| Disposals and transfers | 1 | 2 | – | 3 | (31) | 2 | – | (29) |
| At 31 December 2004 | – | (25) | (3) | (28) | (197) | – | (1) | (198) |
| Loans due to investments: | | | | | | | | |
| At 1 January 2004 | – | – | – | – | (633) | – | – | (633) |
| Movements | – | – | – | – | (55) | – | – | (55) |
| At 31 December 2004 | – | – | – | – | (688) | – | – | (688) |
| Net book value at 31 December 2004 | 100 | 81 | 42 | 223 | 506 | 28 | – | 534 |
| Net book value at 31 December 2003 | 89 | 47 | 36 | 172 | 737 | 38 | – | 775 |

Principal subsidiaries, joint ventures and associates are shown in Note 29. The original cost of the Group's investments in joint ventures and associates was £73m (2003: £49m). The Group's share of borrowings of joint ventures and associates is shown in (b) below. The amount of these which was supported by the Group and the Company was nil (2003: nil). The borrowings of Barking Power Ltd and the PFI/PPP joint venture and associate companies are repayable over periods extending up to 2040. As disclosed in Note 24, the Company has committed to provide its share of further equity funding of joint ventures and associates in PFI/PPP projects. Further, in respect of a number of these investments the Company has committed not to dispose of its equity interest until the relevant construction has been accepted. As is customary in such projects, dividend payments and other distributions are restricted until certain banking covenants are met.

Other investments in the Group include £42m (2003: £36m) of bonds held by Delphian Insurance Company Ltd, the Group's captive insurance company, the market value of which is not significantly different to the book value. The prior year adjustment arises on the reclassification of the Balfour Beatty plc ordinary shares of 50p each held by the Group's discretionary trust to satisfy awards under the Balfour Beatty Performance Share Plan (see Note 1(a)).

11 Investments continued

b) Share of results and net assets of joint ventures and associates

| | Connect M1-A1 Ltd‡ 2004 £m | Metronet* 2004 £m | Other PFI/PPP investments 2004 £m | Total PFI/PPP investments 2004 £m | Barking Power Ltd 2004 £m | Gammon 2004 £m | Other 2004 £m | Total 2004 £m | Comprising | |
|---|----------------------------------|-------------------------|--|--|------------------------------------|----------------------|---------------------|---------------------|---------------------------------|--------------------------|
| | | | | | | | | | Joint ventures 2004 £m | Associates 2004 £m |
| Turnover | 23 | 137 | 46 | 206 | 46 | 90 | 330 | 672 | 380 | 292 |
| Operating profit | 17 | 18 | 7 | 42 | 15 | 2 | 12 | 71 | 27 | 44 |
| Interest | (13) | (8) | 3 | (18) | (5) | – | – | (23) | (9) | (14) |
| Profit before taxation | 4 | 10 | 10 | 24 | 10 | 2 | 12 | 48 | 18 | 30 |
| Taxation | (1) | (3) | (5) | (9) | (3) | (1) | (5) | (18) | (8) | (10) |
| Profit after taxation | 3 | 7 | 5 | 15 | 7 | 1 | 7 | 30 | 10 | 20 |
| Dividends | (2) | – | – | (2) | – | – | (6) | (8) | (4) | (4) |
| Retained profits | 1 | 7 | 5 | 13 | 7 | 1 | 1 | 22 | 6 | 16 |
| Fixed assets | 119 | 160 | 67 | 346 | 111 | 33 | 62 | 552 | 190 | 362 |
| Long-term finance assets | – | – | 184 | 184 | – | – | – | 184 | 184 | – |
| Assets in the course of construction | – | – | 171 | 171 | – | – | – | 171 | 171 | – |
| Cash and deposits | 11 | 162 | 33 | 206 | 14 | 48 | 20 | 288 | 100 | 188 |
| Other | 30 | 35 | 34 | 99 | 14 | 58 | 83 | 254 | 170 | 84 |
| Current assets | 41 | 197 | 422 | 660 | 28 | 106 | 103 | 897 | 625 | 272 |
| | 160 | 357 | 489 | 1,006 | 139 | 139 | 165 | 1,449 | 815 | 634 |
| Borrowings | – | – | (33) | (33) | (11) | (15) | – | (59) | (48) | (11) |
| Other creditors | (10) | (64) | (28) | (102) | (11) | (83) | (108) | (304) | (182) | (122) |
| Creditors – due within one year | (10) | (64) | (61) | (135) | (22) | (98) | (108) | (363) | (230) | (133) |
| Borrowings | (136) | (231) | (337) | (704) | (72) | (6) | (7) | (789) | (450) | (339) |
| Other creditors | – | (35) | (45) | (80) | (27) | (2) | (7) | (116) | (35) | (81) |
| Creditors – due after more than one year | (136) | (266) | (382) | (784) | (99) | (8) | (14) | (905) | (485) | (420) |
| | (146) | (330) | (443) | (919) | (121) | (106) | (122) | (1,268) | (715) | (553) |
| Net assets | 14 | 27 | 46 | 87 | 18 | 33 | 43 | 181 | 100 | 81 |

| | Connect M1-A1 Ltd‡ 2003 £m | Connect Roads Ltd 2003 £m | Metronet* 2003 £m | Other PFI/PPP investments 2003 £m | Total PFI/PPP investments 2003 £m | Barking Power Ltd 2003 £m | Other 2003 £m | Total 2003 £m | Comprising | |
|---|----------------------------------|------------------------------------|-------------------------|--|--|------------------------------------|---------------------|---------------------|---------------------------------|--------------------------|
| | | | | | | | | | Joint ventures 2003 £m | Associates 2003 £m |
| Turnover | 23 | 24 | 75 | 52 | 174 | 42 | 301 | 517 | 297 | 220 |
| Operating profit | 16 | 17 | 12 | 9 | 54 | 6 | 16 | 76 | 47 | 29 |
| Interest | (13) | (10) | (6) | 4 | (25) | (5) | – | (30) | (18) | (12) |
| Profit before taxation | 3 | 7 | 6 | 13 | 29 | 1 | 16 | 46 | 29 | 17 |
| Taxation | (1) | (2) | (2) | (5) | (10) | (1) | (4) | (15) | (10) | (5) |
| Profit after taxation | 2 | 5 | 4 | 8 | 19 | – | 12 | 31 | 19 | 12 |
| Dividends | (2) | (2) | – | (2) | (6) | – | (5) | (11) | (6) | (5) |
| Retained profits | – | 3 | 4 | 6 | 13 | – | 7 | 20 | 13 | 7 |
| Fixed assets | 124 | 109 | 94 | 121 | 448 | 116 | 61 | 625 | 328 | 297 |
| Long-term finance assets | – | – | – | 170 | 170 | – | – | 170 | 170 | – |
| Assets in the course of construction | – | – | – | 114 | 114 | – | – | 114 | 114 | – |
| Cash and deposits | 11 | 13 | 249 | 47 | 320 | 14 | 11 | 345 | 71 | 274 |
| Other | 29 | 8 | 17 | 91 | 145 | 13 | 74 | 232 | 183 | 49 |
| Current assets | 40 | 21 | 266 | 422 | 749 | 27 | 85 | 861 | 538 | 323 |
| | 164 | 130 | 360 | 543 | 1,197 | 143 | 146 | 1,486 | 866 | 620 |
| Borrowings | – | – | – | (2) | (2) | (10) | (3) | (15) | (6) | (9) |
| Other creditors | (8) | (11) | (46) | (42) | (107) | (12) | (84) | (203) | (109) | (94) |
| Creditors – due within one year | (8) | (11) | (46) | (44) | (109) | (22) | (87) | (218) | (115) | (103) |
| Borrowings | (143) | (88) | (250) | (432) | (913) | (82) | (10) | (1,005) | (626) | (379) |
| Other creditors | – | (14) | (53) | (27) | (94) | (28) | (5) | (127) | (36) | (91) |
| Creditors – due after more than one year | (143) | (102) | (303) | (459) | (1,007) | (110) | (15) | (1,132) | (662) | (470) |
| | (151) | (113) | (349) | (503) | (1,116) | (132) | (102) | (1,350) | (777) | (573) |
| Net assets | 13 | 17 | 11 | 40 | 81 | 11 | 44 | 136 | 89 | 47 |

‡ Connect M1-A1 Ltd changed its name from Yorkshire Link Ltd on 2 June 2004.

* Metronet comprises Metronet Rail BCV Holdings Ltd and Metronet Rail SSL Holdings Ltd.

† Gammon comprises Gammon Asia Ltd, Gammon China Ltd and Gammon Construction Holdings Ltd.

11 Investments continued*c) PFI/PPP investments*

The Group's investment in PFI/PPP joint ventures and associates comprises:

| | Equity and loans 2004 £m | Retained profits 2004 £m | Total 2004 £m | Equity and loans 2003 £m | Retained profits 2003 £m | Total 2003 £m |
|--------------------------------|-----------------------------------|-----------------------------------|---------------------|-----------------------------------|-----------------------------------|---------------------|
| Connect M1-A1 Holdings Ltd | 11 | 3 | 14 | 11 | 2 | 13 |
| Connect Roads Ltd | – | – | – | 10 | 7 | 17 |
| Metronet Rail BCV Holdings Ltd | 8 | 5 | 13 | 4 | 1 | 5 |
| Metronet Rail SSL Holdings Ltd | 8 | 6 | 14 | 3 | 3 | 6 |
| Others | 31 | 15 | 46 | 31 | 9 | 40 |
| | 58 | 29 | 87 | 59 | 22 | 81 |

Connect Roads Ltd became a subsidiary on 16 January 2004.

d) Cash flow from/(to) joint ventures and associates

Net cash flow from/(to) joint ventures and associates comprises:

| | PFI/PPP 2004 £m | Other 2004 £m | Total 2004 £m | PFI/PPP 2003 £m | Other 2003 £m | Total 2003 £m |
|--|-----------------------|---------------------|---------------------|-----------------------|---------------------|---------------------|
| Dividends from joint ventures and associates | 2 | 6 | 8 | 6 | 5 | 11 |
| Returns on investments and servicing of finance | | | | | | |
| – subordinated debt interest received | 8 | – | 8 | 2 | – | 2 |
| Capital expenditure and financial investment | | | | | | |
| – investment in joint ventures and associates: | | | | | | |
| Equity | (9) | – | (9) | (7) | (1) | (8) |
| Subordinated debt | (2) | – | (2) | (3) | – | (3) |
| Subordinated debt repaid | – | – | – | 3 | – | 3 |
| Loans repaid | – | – | – | – | 2 | 2 |
| | (11) | – | (11) | (7) | 1 | (6) |
| Net cash flow from joint ventures and associates | (1) | 6 | 5 | 1 | 6 | 7 |

12 Stocks

| | Group 2004 £m | Group 2003 £m | Company 2004 £m | Company 2003 £m |
|---------------------------------------|---------------------|---------------------|-----------------------|-----------------------|
| Contract work in progress | 189 | 174 | – | – |
| Progress applications | (116) | (96) | – | – |
| Net contract balances | 73 | 78 | – | – |
| Development land and work in progress | 9 | 5 | 1 | 1 |
| Manufacturing work in progress | 3 | 2 | – | – |
| Raw materials and consumables | 14 | 19 | – | – |
| Finished goods and goods for resale | 3 | 5 | – | – |
| | 102 | 109 | 1 | 1 |

13 Debtors

| | Group 2004 £m | Group 2003 £m | Company 2004 £m | Company 2003 £m |
|--|---------------------|---------------------|-----------------------|-----------------------|
| <i>Amounts falling due within one year:</i> | | | | |
| Trade and other debtors | 404 | 411 | 14 | 8 |
| Due from subsidiary undertakings | – | – | 23 | 39 |
| Due from joint ventures and associates | 13 | 8 | 1 | 1 |
| Due from joint arrangements | 9 | 9 | – | – |
| Recoverable on contracts | 179 | 168 | – | – |
| Contract retentions | 75 | 86 | – | – |
| Pension prepayments | 1 | 4 | – | 2 |
| Other prepayments and accrued income | 31 | 37 | 1 | 1 |
| Deferred taxation (see Note 17) | 18 | 36 | 1 | 5 |
| Advance corporation tax recoverable | 8 | – | 8 | – |
| | 738 | 759 | 48 | 56 |
| <i>Amounts falling due after more than one year:</i> | | | | |
| Trade and other debtors | 23 | 17 | 9 | 12 |
| Contract retentions | 30 | 25 | – | – |
| Pension prepayments | 26 | 18 | – | 2 |
| | 79 | 60 | 9 | 14 |
| | 817 | 819 | 57 | 70 |

14 Borrowings

| | Group 2004 £m | Group 2003 £m | Company 2004 £m | Company 2003 £m |
|--|---------------------|---------------------|-----------------------|-----------------------|
| Unsecured borrowings: | | | | |
| US dollar fixed rate term loan 8.06% (2008) | 62 | 66 | 62 | 66 |
| Bank overdrafts | 12 | 4 | 4 | – |
| Other short-term loans | 1 | 1 | – | 14 |
| | 75 | 71 | 66 | 80 |
| Finance leases | 2 | 4 | – | – |
| | 77 | 75 | 66 | 80 |
| Cash and deposits | (119) | (147) | – | – |
| Term deposits | (269) | (55) | (259) | (37) |
| | (311) | (127) | (193) | 43 |
| UK PFI/PPP non-recourse project finance – sterling floating rate term loan (2008–2027) | 8 | 3 | – | – |
| – sterling floating rate term loan (2005–2011) | 25 | – | – | – |
| – sterling floating rate term loan (2005–2012) | 93 | – | – | – |
| – sterling fixed rate bond (2006–2034) | 148 | – | – | – |
| | 274 | 3 | – | – |
| UK PFI/PPP project finance – term deposits | (30) | – | – | – |
| | 244 | 3 | – | – |
| Net (cash)/borrowings | (67) | (124) | (193) | 43 |

Term deposits represent cash on deposit for periods in excess of 24 hours.

Borrowings are repayable in the following periods:

| | Group 2004 £m | Group 2003 £m | Company 2004 £m | Company 2003 £m |
|--|---------------------|---------------------|-----------------------|-----------------------|
| Amounts falling due after more than one year (excluding PFI/PPP non-recourse project finance): | | | | |
| Two to five years | 62 | 66 | 62 | 66 |
| One to two years | – | 2 | – | – |
| Amounts falling due within one year | 15 | 7 | 4 | 14 |
| | 77 | 75 | 66 | 80 |
| Borrowings comprise: | | | | |
| Bank borrowings | 13 | 5 | 4 | 14 |
| Other borrowings | 62 | 66 | 62 | 66 |
| Finance leases | 2 | 4 | – | – |
| | 77 | 75 | 66 | 80 |
| Amounts falling due after more than one year – PFI/PPP non-recourse project finance: | | | | |
| Over five years | 193 | 3 | – | – |
| Two to five years | 54 | – | – | – |
| One to two years | 14 | – | – | – |
| Amounts falling due within one year | 13 | – | – | – |
| | 274 | 3 | – | – |
| Borrowings comprise: | | | | |
| Bank borrowings | 126 | 3 | – | – |
| Other borrowings | 148 | – | – | – |
| | 274 | 3 | – | – |

In line with the policy set out in the Financial review on page 36 the interest rate obligations under the US dollar fixed rate term loan have been swapped into floating rate sterling obligations.

A significant part of the PFI/PPP non-recourse project finance floating rate term loans have been swapped into fixed rate debt by the use of interest rate swaps.

Unutilised committed borrowing facilities (excluding PFI/PPP non-recourse project finance facilities) expiring beyond 12 months amount to £210m (2003: £210m). Group borrowings repayable by instalments, any part of which is repayable after five years, are £274m (2003: £3m).

Cash, deposits and term deposits include the Group's share of amounts held by contracting joint arrangements of £88m (2003: £88m).

The PFI/PPP project finance debt obligations arise under non-recourse facilities in the concession companies Connect A30/A35 Ltd, Connect A50 Ltd, Connect M77/GSO plc and Connect Roads Sunderland Ltd. The borrowings are secured by fixed and floating charges over each concession company's right, title and interest in certain assets and/or revenues and over each concession company's shares held by their immediate parent companies, Connect Roads Ltd, Connect M77/GSO Holdings Ltd and Connect Roads Sunderland Holdings Ltd.

15 Financial instruments

A description of the Group's objectives, policies and strategies with regard to derivatives and other financial instruments can be found in the Financial review on page 35. As permitted by FRS 13, short-term debtors and creditors have been omitted from all disclosures other than the currency exposure profile shown in (c) below.

a) Interest rate risk profile

The interest rate risk profile for the financial liabilities and assets of the Group at 31 December 2004 was:

| | Fixed rate and floating rate total £m | Floating rate £m | Fixed rate £m | Weighted average interest rate % | Fixed rate Weighted average period for which rate is fixed years | Long-term creditors/debtors £m | Interest free Weighted average period until maturity years |
|--|--|---------------------|------------------|-------------------------------------|--|-----------------------------------|--|
| Liabilities | | | | | | | |
| Currency | | | | | | | |
| Sterling – excluding PFI/PPP non-recourse project finance | 5 | 5 | – | – | – | 76 | 9.2 |
| Sterling – PFI/PPP non-recourse project finance | 274 | 8 | 266 | 7.3 | 2.5 | – | – |
| US dollar | 72 | 70 | 2 | 9.1 | 0.5 | 30 | 1.5 |
| Other | – | – | – | – | – | 4 | 1.5 |
| Total borrowings and long-term creditors | 351 | 83 | 268 | 7.3 | 2.4 | 110 | 6.8 |
| Sterling cumulative convertible redeemable preference shares | 136 | – | 136 | 10.75 | 15.5 | – | – |
| Assets | | | | | | | |
| Currency | | | | | | | |
| Sterling – excluding PFI/PPP non-recourse project finance | 386 | 344 | 42 | 6.8 | 5.6 | 36 | 3.8 |
| Sterling – PFI/PPP non-recourse project finance | 30 | 30 | – | – | – | – | – |
| US dollar | 26 | 26 | – | – | – | 17 | 2.0 |
| Other | 18 | 18 | – | – | – | – | – |
| Cash and deposits, fixed asset investments and long-term monetary debtors | 460 | 418 | 42 | 6.8 | 5.6 | 53 | 3.2 |

The interest rate risk profile for the financial liabilities and assets of the Group at 31 December 2003 was:

| | Fixed rate and floating rate total £m | Floating rate £m | Fixed rate £m | Weighted average interest rate % | Fixed rate Weighted average period for which rate is fixed years | Long-term creditors/debtors £m | Interest free Weighted average period until maturity years |
|--|--|---------------------|------------------|-------------------------------------|--|-----------------------------------|--|
| Liabilities | | | | | | | |
| Currency | | | | | | | |
| Sterling | 8 | 7 | 1 | 6.0 | 0.8 | 61 | 7.8 |
| US dollar | 70 | 67 | 3 | 9.1 | 1.0 | 29 | 1.5 |
| Other | – | – | – | – | – | 5 | 1.6 |
| Total borrowings and long-term creditors | 78 | 74 | 4 | 8.7 | 1.0 | 95 | 5.5 |
| Sterling cumulative convertible redeemable preference shares | 150 | – | 150 | 10.75 | 16.5 | – | – |
| Assets | | | | | | | |
| Currency | | | | | | | |
| Sterling | 183 | 147 | 36 | 6.6 | 5.6 | 33 | 2.9 |
| US dollar | 28 | 28 | – | – | – | 7 | 1.9 |
| Other | 27 | 27 | – | – | – | 2 | 2.6 |
| Cash and deposits, fixed asset investments and long-term monetary debtors | 238 | 202 | 36 | 6.6 | 5.6 | 42 | 2.7 |

Floating rate liabilities include bank borrowings bearing interest rates fixed in advance for periods ranging from overnight to six months by reference to the relevant currency's inter-bank rate and fixed rate borrowings with other financial institutions that have been swapped into floating rate borrowings by means of interest rate swaps to match the maturity of the underlying borrowings. Floating rate assets include monies deposited on money markets for periods varying from overnight to three months.

b) Liquidity risk profile

The maturity profile of the Group's financial liabilities (excluding PFI/PPP non-recourse project finance) at 31 December was:

| | Preference shares 2004 £m | Borrowings 2004 £m | Long-term creditors 2004 £m | Preference shares 2003 £m | Borrowings 2003 £m | Long-term creditors 2003 £m |
|---|---------------------------------|--------------------------|-----------------------------------|---------------------------------|--------------------------|-----------------------------------|
| In one year or less, or on demand | – | 15 | – | – | 7 | – |
| In more than one year but not more than two years | – | – | 42 | – | 2 | 42 |
| In more than two years but not more than five years | – | 62 | 3 | – | 66 | 13 |
| In more than five years | 136 | – | 65 | 150 | – | 40 |
| | 136 | 77 | 110 | 150 | 75 | 95 |

The maturity profile of the Group's PFI/PPP non-recourse project finance financial liabilities at 31 December was:

| | Borrowings 2004 £m | Borrowings 2003 £m |
|---|--------------------------|--------------------------|
| In one year or less, or on demand | 13 | – |
| In more than one year but not more than two years | 14 | – |
| In more than two years but not more than five years | 54 | – |
| In more than five years | 193 | 3 |
| | 274 | 3 |

15 Financial instruments continued

The Group's undrawn committed borrowing facilities (excluding PFI/PPP non-recourse project finance facilities) in respect of which all conditions precedent were satisfied at 31 December were:

| | 2004 £m | 2003 £m |
|--|------------|------------|
| Expiring in one year or less | – | – |
| Expiring in more than one year but not more than two years | 210 | – |
| Expiring in more than two years | – | 210 |
| | 210 | 210 |

The Group's undrawn PFI/PPP non-recourse project finance committed borrowing facilities in respect of which all conditions precedent were satisfied at 31 December were:

| | 2004 £m | 2003 £m |
|--|------------|------------|
| Expiring in one year or less | – | – |
| Expiring in more than one year but not more than two years | – | – |
| Expiring in more than two years | 19 | 24 |
| | 19 | 24 |

c) Currency exposures profile

The Group's currency exposures, representing those monetary assets and monetary liabilities that are not denominated in the functional currency of the operating unit involved that give rise to exchange gains and losses recognised in the profit and loss account, at 31 December were:

| | Net foreign currency monetary assets/(liabilities) | | | | Net foreign currency monetary assets/(liabilities) | | | |
|----------------------------------|--|--------------------|---------------------|---------------------|--|--------------------|---------------------|---------------------|
| | US dollar 2004 £m | Euro 2004 £m | Other 2004 £m | Total 2004 £m | US dollar 2003 £m | Euro 2003 £m | Other 2003 £m | Total 2003 £m |
| Functional currency of operation | | | | | | | | |
| Sterling | – | 1 | 1 | 2 | – | (1) | – | (1) |
| Other | (3) | – | – | (3) | – | – | – | – |
| | (3) | 1 | 1 | (1) | – | (1) | – | (1) |

The figures shown in the above table take into account the effect of forward contracts and other derivatives used to hedge the operating units' foreign exchange transaction exposure.

d) Fair value of financial assets and liabilities

The table below compares by category the book value and fair value of the Group's primary and derivative financial instruments at 31 December:

| | Book value 2004 £m | Fair value 2004 £m | Book value 2003 £m | Fair value 2003 £m |
|--|--------------------------|--------------------------|--------------------------|--------------------------|
| Primary financial instruments | | | | |
| Short-term borrowings and current portion of long-term borrowings (excluding PFI/PPP project finance non-recourse) | (15) | (14) | (7) | (7) |
| PFI/PPP non-recourse project finance short-term borrowings and current portion of long-term borrowings | (13) | (30) | (3) | (2) |
| Long-term borrowings (excluding PFI/PPP non-recourse project finance) | (62) | (62) | (68) | (69) |
| PFI/PPP non-recourse project finance long-term borrowings | (261) | (246) | – | – |
| Cash and deposits (excluding PFI/PPP non-recourse project finance) | 388 | 388 | 202 | 202 |
| PFI/PPP project finance non-recourse cash and deposits | 30 | 30 | – | – |
| Other financial liabilities | (110) | (98) | (95) | (78) |
| Other financial assets | 95 | 94 | 78 | 76 |
| Sterling cumulative convertible redeemable preference shares | (136) | (207) | (150) | (224) |
| Derivative financial instruments | | | | |
| Forward foreign currency contracts | 1 | 1 | 4 | 4 |
| Interest rate swaps– excluding those related to PFI/PPP non-recourse project finance borrowings | – | (3) | – | (2) |
| Interest rate swaps related to PFI/PPP non-recourse project finance borrowings | – | (14) | – | 1 |

Market values have been used to determine the fair value of the Sterling cumulative convertible redeemable preference shares, interest rate swaps and certain other financial assets. The fair values of all other items have been determined by using yield curves and exchange rates prevailing at the balance sheet date and discounting expected future cash flows at interest rates prevailing at the balance sheet date.

e) Hedges

Gains and losses on instruments used for transaction hedging are not recognised in the profit and loss account until the maturity of the underlying transaction, or an adjustment is made to the carrying amount in the balance sheet. Unrecognised gains and losses at 31 December were:

| | Gains 2004 £m | Losses 2004 £m | Net 2004 £m | Gains 2003 £m | Losses 2003 £m | Net 2003 £m |
|---|---------------------|----------------------|-------------------|---------------------|----------------------|-------------------|
| Unrecognised gains and losses on hedges at 1 January | 2 | (3) | (1) | 1 | (1) | – |
| Gains and losses arising in previous years recognised in the year | 1 | (1) | – | 1 | (1) | – |
| Gains and losses arising in previous years not recognised in the year | 1 | (2) | (1) | – | – | – |
| Gains and losses arising in the year not recognised in the year | – | (16) | (16) | 2 | (3) | (1) |
| Unrecognised gains and losses on hedges at 31 December | 1 | (18) | (17) | 2 | (3) | (1) |
| Of which: | | | | | | |
| Gains and losses expected to be recognised in the next year | 1 | (1) | – | 1 | (1) | – |
| Gains and losses expected to be recognised thereafter | – | (17) | (17) | 1 | (2) | (1) |

16 Other creditors

| | Group 2004 £m | Group 2003 as restated £m | Company 2004 £m | Company 2003 as restated £m |
|--|---------------------|------------------------------------|-----------------------|--------------------------------------|
| <i>Amounts falling due within one year:</i> | | | | |
| Trade and other creditors | 376 | 424 | 5 | 4 |
| Advance progress applications | 275 | 234 | – | – |
| Due to subsidiary undertakings | – | – | 6 | 2 |
| Due to joint arrangements | 2 | 5 | – | – |
| Corporate taxation | 38 | 43 | 8 | 6 |
| VAT, payroll taxes and social security | 60 | 66 | 9 | 7 |
| Dividends on ordinary shares | 28 | 25 | 28 | 25 |
| Dividends on preference shares | 6 | 8 | 6 | 8 |
| Accruals and deferred income | 417 | 388 | 6 | 8 |
| Due on acquisitions | 7 | 2 | 7 | 1 |
| | 1,209 | 1,195 | 75 | 61 |
| <i>Amounts falling due after more than one year:</i> | | | | |
| Trade and other creditors | 59 | 60 | – | – |
| Due to joint ventures and associates | 25 | 25 | 25 | 25 |
| Accruals and deferred income | 26 | – | – | – |
| Due on acquisitions | – | 10 | – | 10 |
| | 110 | 95 | 25 | 35 |

17 Provisions for liabilities and charges*a) Group*

| | Deferred taxation £m | Retirement and other employee provisions £m | Contract provisions £m | Other provisions £m | Total £m |
|--|----------------------------|---|------------------------------|---------------------------|-------------|
| At 1 January 2004 | – | 76 | 40 | 51 | 167 |
| Exchange adjustments | – | – | (1) | – | (1) |
| Profit and loss account – before exceptional items | 7 | 2 | 24 | 11 | 44 |
| – exceptional items | 2 | (4) | – | 2 | – |
| Utilised | – | (3) | (11) | (11) | (25) |
| Businesses acquired (see Note 20) | 9 | 2 | – | 2 | 13 |
| Businesses sold | – | – | (1) | – | (1) |
| Transfer to debtors | (18) | – | – | – | (18) |
| At 31 December 2004 | – | 73 | 51 | 55 | 179 |

Retirement and other employee provisions comprise obligations to current and former employees including pension obligations of Mansell plc, overseas pension and other post-retirement benefits. Contract provisions include warranty, fault and rectification provisions. Other provisions principally comprise environmental, lease, legal claims and costs and other onerous commitments. The majority of provisions, other than retirement and other employee provisions, are expected to be utilised within five years. Provision is made for the Directors' best estimate of known legal claims and legal actions in progress.

The provision for UK deferred taxation is based on a corporation tax rate of 30%. The recognised amount of deferred taxation, included in debtors, comprises:

| | UK 2004 £m | Foreign 2004 £m | UK 2003 £m | Foreign 2003 £m |
|---|------------------|-----------------------|------------------|-----------------------|
| Excess of depreciation over taxation allowances | (3) | – | (7) | – |
| Other, including short-term timing differences | (15) | – | (29) | – |
| | (18) | – | (36) | – |
| | | (18) | | (36) |

b) Company

| | Deferred taxation £m | Other provisions £m | Total £m |
|-------------------------|----------------------------|---------------------------|-------------|
| At 1 January 2004 | – | 11 | 11 |
| Profit and loss account | 4 | (1) | 3 |
| Utilised | – | (1) | (1) |
| Transfer to debtors | (4) | – | (4) |
| At 31 December 2004 | – | 9 | 9 |

Other provisions principally comprise lease and other onerous commitments, the majority of which are expected to be utilised within five years.

18 Share capital

| | Authorised 2004 £m | Authorised 2003 £m | Issued and fully paid 2004 £m | Issued and fully paid 2003 £m |
|---|--------------------------|--------------------------|--|--|
| Ordinary shares of 50p each – authorised 696m (2003: 696m) issued 424m (2003: 420m) | 348 | 348 | 212 | 210 |
| Cumulative convertible redeemable preference shares of 1p each – authorised 177m (2003: 177m) issued 136m (2003: 150m) | 2 | 2 | 1 | 2 |
| | 350 | 350 | 213 | 212 |

The preference shares are convertible at the option of the holder on the first day of the next calendar month following receipt of the conversion notice into new Balfour Beatty plc ordinary shares effectively on the basis of 21.05263 ordinary shares for every 100 preference shares based on the current conversion price of 475p per ordinary share, which is subject to adjustment in certain circumstances. Holders are entitled to a preferential dividend equivalent to a gross payment of 10.75p per preference share per annum, payable half yearly. Any preference shares still outstanding are redeemable on 1 July 2020 at £1 each, together with any arrears of accruals of dividend, unless the holder exercises any option granted by the Company to extend the redemption date. The maximum redemption value of all of the issued and outstanding preference shares, excluding any arrears or accruals of dividend, was £136m at 31 December 2004 and this amount has been disclosed on the balance sheet as the total of non-equity shareholders' funds. The Company is entitled to convert all outstanding preference shares into ordinary shares if there are fewer than 44,281,239 preference shares in issue or if the average of the closing mid-market price for a Balfour Beatty plc ordinary share during a 30 day period exceeds 200% of the conversion price. The preference shares carry no voting rights at a general meeting of the Company, except where the dividend is six months or more in arrears, or where the business of the meeting includes a resolution which directly affects the rights and privileges attached to the preference shares or a resolution for the winding-up of the Company. On a winding-up of the Company, holders are entitled to receive the sum of £1 per preference share, together with any arrears or accruals of dividend, in priority to any payment on any other class of shares.

Details of share capital issued and repurchased by the Company during the year are set out in the Directors' report on page 40.

At 31 December share options outstanding were as follows:

| Year of issue | Subscription prices | Normally exercisable in periods to | Number of ordinary shares 2004 | Number of ordinary shares 2003 |
|------------------------|---------------------|------------------------------------|--------------------------------|--------------------------------|
| Savings-related | | | | |
| 1998 | 120.0p | January 2004 | – | 151,970 |
| 1999 | 91.0p | May 2005 | 115,000 | 1,018,557 |
| 2000 | 76.0p | January 2006 | 1,188,937 | 1,445,458 |
| 2001 | 154.0p | March 2007 | 852,334 | 1,640,330 |
| 2002 | 184.0p | December 2007 | 1,432,521 | 1,722,455 |
| 2003 | 133.0p | December 2008 | 1,593,566 | 1,927,211 |
| 2004 | 210.0p | December 2009 | 1,911,059 | – |
| Executive | | | | |
| 1994 | 438.1p | April 2004 | – | 718,936 |
| 1995 | 311.9p | April 2005 | 1,165,850 | 1,165,850 |
| 1996 | 288.5p | February 2006 | 153,404 | 153,404 |
| 1996 | 344.2p | April 2006 | 459,181 | 459,181 |
| 1997 | 231.0p | May 2007 | 265,000 | 350,000 |
| 1998 | 181.0p | May 2008 | 167,500 | 245,500 |
| 1999 | 110.0p | November 2009 | 255,818 | 765,818 |
| 2000 | 79.0p | April 2010 | 304,366 | 728,683 |
| 2001 | 200.0p | June 2011 | 675,150 | 1,375,000 |
| 2002 | 238.0p | April 2012 | 1,466,000 | 1,496,000 |
| 2003 | 146.0p | January 2013 | 100,000 | 100,000 |
| 2003 | 173.0p | April 2013 | 1,762,500 | 1,795,000 |
| 2004 | 261.0p | April 2014 | 1,835,000 | – |
| 2004 | 268.0p | September 2014 | 55,970 | – |

On 19 April 2004, options were granted over 1,835,000 ordinary shares under the Balfour Beatty executive share option scheme at 261p per share, and these are normally exercisable in the period from April 2007 to April 2014. On 6 September 2004, options were granted over 55,970 ordinary shares under the Balfour Beatty executive share option scheme at 268p per share, and these are normally exercisable in the period from September 2007 to September 2014. On 5 May 2004, options were granted over 1,983,018 ordinary shares under the Balfour Beatty savings-related share option scheme, at 210p per share, and these are normally exercisable in the periods from July 2007 to December 2007 and from July 2009 to December 2009 depending upon the length of savings contract chosen by the participant.

19 Reserves*a) Group*

| | Share premium account £m | Revaluations | | | Other £m | Profit and loss account £m |
|---|-----------------------------|-----------------------------|--|-----------------------|-------------|-------------------------------|
| | | Tangible fixed assets £m | Investments in joint ventures and associates £m | Special reserve £m | | |
| At 1 January 2004 – as previously reported | 328 | 2 | 46 | – | 4 | (362) |
| Prior year adjustment (see Note 1a) | – | – | – | – | 4 | (3) |
| At 1 January 2004 – as restated | 328 | 2 | 46 | – | 8 | (365) |
| Retained profit for the year | – | – | 24 | – | – | 132 |
| Exchange adjustments | – | – | (1) | – | – | (1) |
| Goodwill – on business sold | – | – | – | – | – | 38 |
| Issue of ordinary shares | 3 | – | – | – | – | – |
| Buy-back of preference shares – carrying value | – | – | – | – | – | (14) |
| Cancellation of share premium account and capital redemption reserve fund | (181) | – | – | 185 | (4) | – |
| Transfers | – | – | (1) | (4) | – | 5 |
| At 31 December 2004 | 150 | 2 | 68 | 181 | 4 | (205) |

At 31 December 2004, cumulative goodwill, net of merger relief of £39m (2003: £39m), eliminated against the profit and loss account amounted to £41m (2003: £79m), net of negative goodwill of £8m (2003: £8m).

b) Company

| | Share premium account £m | Special reserve £m | Other £m | Profit and loss account £m |
|---|-----------------------------|-----------------------|-------------|-------------------------------|
| At 1 January 2004 – as previously reported | 328 | – | 46 | 110 |
| Prior year adjustment (see Note 1a) | – | – | 4 | (3) |
| At 1 January 2004 – as restated | 328 | – | 50 | 107 |
| Retained profit/(loss) for the year | – | – | – | (10) |
| Exchange adjustments | – | – | – | – |
| Issue of ordinary shares | 3 | – | – | – |
| Buy-back of preference shares – carrying value | – | – | – | (14) |
| Cancellation of share premium account and capital redemption reserve fund | (181) | 185 | (4) | – |
| Transfers | – | (4) | – | 4 |
| At 31 December 2004 | 150 | 181 | 46 | 87 |

By special resolution on 13 May 2004, confirmed by the Court on 16 June 2004, the share premium account was reduced by £181m and the £4m capital redemption reserve fund was cancelled, effective on 25 June 2004. A special reserve of £185m was created which becomes distributable to the extent of future increases in share capital and share premium account.

The profit and loss account of Balfour Beatty plc is wholly distributable.

Under Section 230(3) of the Companies Act 1985, no profit and loss account is presented for Balfour Beatty plc. The profit for the financial year dealt with in the accounts of the parent company was £37m (2003: £45m).

The profit and loss account in the Group and the Company is stated net of investments in Balfour Beatty plc ordinary shares of 50p each acquired by the Group's employee discretionary trust, the Balfour Beatty Employee Share Ownership Trust, to satisfy awards under the Balfour Beatty Performance Share Plan. In 2004, 0.8m (2003: 0.5m) shares were purchased at a cost of £2.0m (2003: £1.0m). The market value of the 1.2m (2003: 1.8m) shares held by the Trust at 31 December 2004 was £3.7m (2003: £4.0m). The cost of the awards under the scheme is charged to the profit and loss account over the performance period. Following confirmation of the performance criteria the appropriate number of shares will be unconditionally transferred to participants. In 2004, 1,438,624 shares were transferred to participants (2003: 78,000). The trustees have waived the rights to dividends on shares held by the Trust. Other reserves in the Group and the Company include £4m relating to unvested Performance Share Plan awards.

c) Reconciliation of movements in shareholders' funds

| | 2004 £m | 2003 as restated £m |
|---|------------|---------------------------|
| Profit for the financial year | 203 | 89 |
| Dividends | (41) | (40) |
| Premium paid on buy-back of preference shares | (6) | (5) |
| | 156 | 44 |
| Other recognised gains and losses (net) | (2) | (1) |
| Goodwill – on businesses sold | 38 | – |
| Issue of ordinary shares | 4 | 5 |
| Buy-back of preference shares – carrying value | (14) | (11) |
| Movements relating to Balfour Beatty Employee Share Ownership Trust | – | 2 |
| | 182 | 39 |
| Opening shareholders' funds – as previously reported | 230 | 193 |
| Prior year adjustment | 1 | (1) |
| Closing shareholders' funds – as restated | 413 | 231 |

20 Acquisitions

a) On 16 January 2004 and 23 January 2004 the Group acquired from Atkins its 32.2% interests in Connect Roads Ltd and Connect M77/GSO Holdings Ltd respectively for a total consideration of £13.3m cash. As a result, the Group's interests in the companies increased to 100% and they have been accounted for as subsidiaries from these dates. The fair value of the net assets acquired, consideration paid and goodwill arising were:

| | Fair value of assets acquired £m |
|---|-------------------------------------|
| Tangible fixed assets | 231 |
| Debtors | 14 |
| Investments | 59 |
| Creditors and provisions | (31) |
| Tax | (11) |
| Cash and deposits | 41 |
| Project finance non-recourse term loans | (278) |
| | 25 |
| Investment in joint ventures | (17) |
| | 8 |
| Consideration and costs | 13 |
| Goodwill | 5 |

The incremental operating profit, before goodwill amortisation, attributable to the 32.2% interests acquired, of £6m in the period since acquisition, is included in the Investments and developments segment.

b) On 6 August 2004 the Group acquired from the Skanska Group its 50% shareholdings in each of Gammon China Ltd, Gammon Asia Ltd and Gammon Construction Holdings Ltd (the "Gammon Skanska Group") for a total consideration of HK\$475m (£33m) in cash and costs of £1m. The Group's share of the book value of net assets acquired was £27m. Provisional fair value adjustments amounting to £14m have been made to harmonise accounting policies for income and profit recognition on long-term contracts and the cost of pension obligations. Provisional goodwill arising amounted to £21m. The Group has recorded its share of operating profit, before goodwill amortisation, of £2m for the period since acquisition, which is included in the Civil and specialist engineering and services segment.

c) On 1 January 2004 the Group acquired the business and assets of the railway division of ABB Gebaudetechnik AG based in Germany for a consideration of €3.3m. On 8 October 2004 the Group acquired the business and assets of HLM Design, a US design and engineering business, for a consideration of US\$5.5m. On 14 October 2004 the Group acquired Bombardier Transportation's UK Solid State Interlocking signalling resources for a consideration of £2.1m.

The provisional fair value of the net assets acquired, consideration paid and provisional goodwill arising on these transactions were:

| | Fair value of assets acquired £m |
|--------------------------------|-------------------------------------|
| Tangible fixed assets | 1 |
| Debtors | 6 |
| Creditors and provisions | (8) |
| | (1) |
| Consideration and costs – cash | 8 |
| Goodwill | 9 |

The businesses recorded an operating profit of £1m, before goodwill amortisation, in the periods since acquisition. The results of the former ABB and Bombardier businesses are included in the Rail engineering and services segment and the results of HLM Design are included in the Building, building management and services segment.

d) In 2004, £4m deferred consideration was paid in respect of acquisitions completed in prior years.

Goodwill arising on businesses acquired in 2003 has been increased by £3m. This reflects amendments to the provisional fair value of the net assets of Mansell plc of £4m, offset by a reduction in the consideration payable in respect of Marta Metroplex of £1m.

The Group has used acquisition accounting to account for these transactions.

21 Employees

| | 2004 £m | 2003 £m |
|---|------------|------------|
| Group employee costs during the year amounted to: | | |
| Wages and salaries | 828 | 802 |
| Social security costs | 80 | 79 |
| Other pension costs (see Note 23) | 35 | 28 |
| | 943 | 909 |

| | 2004 | 2003 |
|---|--------|--------|
| The average number of Group employees was as follows: | | |
| Building, building management and services | 11,098 | 9,300 |
| Civil and specialist engineering and services | 9,985 | 10,214 |
| Rail engineering and services | 6,582 | 7,532 |
| Investments and developments | 118 | 105 |
| Discontinued operations | 342 | 677 |
| | 28,125 | 27,828 |

At 31 December 2004, the total number of Group employees was 27,030 (2003: 28,848).

22 Directors' emoluments

| | 2004 £m | 2003 £m |
|--|------------|------------|
| The remuneration of Directors of Balfour Beatty plc was: | | |
| Non-executive Directors' fees and benefits | 0.390 | 0.354 |
| Executive Directors' emoluments | | |
| – salary and benefits | 2.136 | 2.238 |
| – performance related bonus | 0.673 | 0.581 |
| – compensation for loss of office | 0.040 | 0.304 |
| Value of awards vested under the Performance Share Plan | 1.689 | – |
| Gain on exercise of share options | 0.291 | 0.909 |
| Money purchase pension contributions | 0.121 | 0.139 |
| | 5.340 | 4.525 |

Further details of Directors' emoluments, pension benefits and interests are set out in the Remuneration report on pages 44 to 50.

23 Pensions

a) The Group, through trustees, operates a number of pension schemes the majority of which are of the defined benefit type and are funded. Contributions are determined in accordance with independent actuarial advice. Details of the last actuarial valuations and reviews and the assumptions used by the actuaries are set out below. The Group continues to account for the cost of pensions in accordance with the requirements of SSAP 24 "Accounting for pension costs".

The last formal valuation of the Balfour Beatty Pension Fund was carried out by the actuaries at 31 March 2004 using the projected unit method and disclosed an excess of assets over past service liabilities of 1.7%. The assets and liabilities of the defined contribution section are included within reported results of the Balfour Beatty Pension Fund. The excess of cumulative amounts paid to this scheme over pension costs charged in the accounts of £10m (2003: £4m) is included within debtors.

Certain Group employees are members of the Balfour Beatty Shared Cost section of the Railways Pension Scheme ("Railways Pension Scheme"). The last formal valuation of this defined benefit scheme was carried out by independent actuaries at 31 December 2001 using the projected unit method and disclosed a surplus of assets over past service liabilities of 4.2% of which, being a shared cost scheme, the Group obtains an economic benefit of circa 60%. This proportion has been based on the apportionment of the surplus which has already been agreed together with the relevant provisions of the Trust Deed and Rules and Trustee guidelines regarding future surplus apportionments. A prepayment of £17m (2003: £18m) is included within debtors.

Mansell plc operates two funded defined benefit schemes, the Mansell plc Pension Scheme and the Hall & Tawse Retirement Benefit Plan ("Mansell schemes"), and two funded defined contribution schemes. The most recent actuarial valuation of the Mansell plc Pension Scheme, which was closed to new members from 31 December 2001, was carried out by independent actuaries at 31 July 2002 using the projected unit method. The valuation showed that the market value of the scheme's assets represented 65.4% of the benefits that had accrued to members on an ongoing funding basis. The most recent actuarial valuation of the Hall & Tawse Retirement Benefit Plan, which was closed to new members from 1 July 1998, was carried out by independent actuaries at 31 March 2002 using the projected unit method. The valuation showed that the market value of the scheme's assets represented 96.7% of the benefits that had accrued to members on an ongoing funding basis.

The Group's actuaries have reviewed the funding valuations of the Balfour Beatty Pension Fund, the Railways Pension Scheme and the Mansell schemes at 31 December 2004. The results of these reviews along with the assumptions used by the actuaries are set out below together with comparatives at 31 December 2003.

| | At the last formal actuarial funding valuation | | | | At 31 December 2004 valuation review | | | At 31 December 2003 valuation review | | |
|---|--|--------------------------------------|----------------------|--------------------------------|--------------------------------------|---------------------------|-------------------|--------------------------------------|---------------------------|-------------------|
| | Balfour Beatty Pension Fund 31/3/2004 % | Railways Pension Scheme 31/12/2001 % | Mansell schemes | | Balfour Beatty Pension Fund % | Railways Pension Scheme % | Mansell schemes % | Balfour Beatty Pension Fund % | Railways Pension Scheme % | Mansell schemes % |
| | | | H&T Plan 31/3/2002 % | Mansell plc Scheme 31/7/2002 % | | | | | | |
| Principal actuarial valuation assumptions: | | | | | | | | | | |
| Inflation assumption | 2.7 | 2.5 | 2.5 | 2.5 | 2.8 | 2.8 | 2.8 | 2.7 | 2.7 | 2.7 |
| Rate of increase in salaries | 4.2 | 4.0 | 4.0 | 4.0 | 4.3 | 4.3 | 4.3 | 4.2 | 4.2 | 4.2 |
| Rate of increase in pensions in payment (or such other fixed rate as is guaranteed) | 2.7 | 2.5 | 2.5 | 2.5 | 2.8 | 2.8 | 2.8 | 2.7 | 2.7 | 2.7 |
| Return on existing investments: | | | | | | | | | | |
| – actives and deferred members | n/a | 5.6 | 6.0 | 6.2 | n/a | n/a | n/a | 7.1 | 7.1 | 7.1 |
| – pre-retirement | 8.1 | n/a | n/a | n/a | 7.8 | 7.8 | 7.8 | n/a | n/a | n/a |
| – post-retirement | 5.6 | n/a | n/a | n/a | 5.5 | 5.5 | 5.5 | n/a | n/a | n/a |
| – pensioners, widows and dependants | 5.1 | 5.6 | 6.0 | 5.2 | 5.0 | 5.0 | 5.0 | 5.0 | 5.0 | 5.0 |
| Number of members: | | | | | | | | | | |
| Active members | 7,954 | 2,329 | 310 | 716 | 7,706 | 655 | 676 | 8,461 | 1,565 | 787 |
| Deferred pensioners | 11,540 | 1,647 | 1,103 | 435 | 12,020 | 1,664 | 1,609 | 11,137 | 1,665 | 1,596 |
| Pensioners, widows and dependants | 16,989 | 695 | 922 | 117 | 16,442 | 1,008 | 1,149 | 16,378 | 873 | 1,098 |
| Total | 36,483 | 4,671 | 2,335 | 1,268 | 36,168 | 3,327 | 3,434 | 35,976 | 4,103 | 3,481 |
| | £m | £m | £m | £m | £m | £m | £m | £m | £m | £m |
| Scheme surplus/(deficit) | | | | | | | | | | |
| Market value of assets | 1,398 | 295 | 87 | 28 | 1,480 | 185 | 133 | 1,385 | 238 | 118 |
| Present value of scheme liabilities | (1,374) | (283) | (90) | (43) | (1,479) | (174) | (169) | (1,331) | (222) | (156) |
| Surplus/(deficit) in scheme | 24 | 12 | (3) | (15) | 1 | 11 | (36) | 54 | 16 | (38) |
| Funding level | 101.7% | 104.2% | 96.7% | 65.4% | 100.1% | 106.1% | 78.9% | 104.0% | 107.2% | 75.6% |
| | | | | | £m | £m | £m | £m | £m | £m |
| Amounts included within Debtors (Note 13) and Provisions (Note 17) arising under SSAP24 and FRS 7: | | | | | | | | | | |
| Pension prepayments | | | | | 10 | 17 | – | 4 | 18 | – |
| Provisions | | | | | – | – | (37) | – | – | (38) |

23 Pensions continued

| | Contributions paid | | Amounts charged to P&L | |
|--|--------------------|------------|------------------------|------------|
| | 2004 £m | 2003 £m | 2004 £m | 2003 £m |
| Group contributions paid and amounts charged to profit and loss account: | | | | |
| Balfour Beatty Pension Fund | 30 | 16 | 24 | 18 |
| Railways Pension Scheme | 2 | 1 | 3 | 5 |
| Mansell schemes | 8 | – | 5 | – |
| Other defined benefit schemes | 1 | 2 | 1 | 2 |
| Other defined contribution schemes | 2 | 3 | 2 | 3 |
| | 43 | 22 | 35 | 28 |

The Group's other defined contribution schemes cover mainly overseas employees, principally in North America.

b) The Group continues to account for pensions in accordance with the requirements of SSAP 24 "Accounting for pension costs". The following supplementary analysis is given in accordance with the requirements of FRS 17 "Retirement benefits".

The latest actuarial funding valuations of the Group's principal defined benefit schemes, the Balfour Beatty Pension Fund, the Railways Pension Scheme and the Mansell schemes, have been updated by the actuaries to 31 December 2004 on the basis prescribed by FRS 17. In particular, scheme liabilities have been discounted using the rate of return on a high quality corporate bond rather than the expected rate of return on the assets in the scheme used in the funding valuations.

The principal assumptions used by the actuaries were:

| | At 31 December 2004 | | | At 31 December 2003 | | | At 31 December 2002 | |
|---|-------------------------------|---------------------------|-------------------|-------------------------------|---------------------------|-------------------|-------------------------------|---------------------------|
| | Balfour Beatty Pension Fund % | Railways Pension Scheme % | Mansell schemes % | Balfour Beatty Pension Fund % | Railways Pension Scheme % | Mansell schemes % | Balfour Beatty Pension Fund % | Railways Pension Scheme % |
| Inflation assumption | 2.80 | 2.80 | 2.80 | 2.70 | 2.70 | 2.70 | 2.20 | 2.20 |
| Rate of increase in salaries | 4.30 | 4.30 | 4.30 | 4.20 | 4.20 | 4.20 | 3.70 | 3.70 |
| Rate of increase in pensions in payment (or other such other fixed rate as is guaranteed) | 2.80 | 2.80 | 2.80 | 2.70 | 2.70 | 2.70 | 2.20 | 2.20 |
| Discount rate | 5.30 | 5.30 | 5.30 | 5.40 | 5.40 | 5.40 | 5.60 | 5.60 |

The fair value of the assets held by the schemes, the expected rate of return on those assets and the present value of the scheme liabilities were:

| | Balfour Beatty Pension Fund | | Railways Pension Scheme | | Mansell schemes | | Other funded schemes | |
|---|---|------------------------------|---|------------------------------|---|------------------------------|---|------------------------------|
| | Long-term expected rate of return at 31 December 2004 % | Value at 31 December 2004 £m | Long-term expected rate of return at 31 December 2004 % | Value at 31 December 2004 £m | Long-term expected rate of return at 31 December 2004 % | Value at 31 December 2004 £m | Long-term expected rate of return at 31 December 2004 % | Value at 31 December 2004 £m |
| Equities | 8.30 | 586 | 8.30 | 116 | 8.30 | 85 | – | – |
| Gilts | 4.55 | 572 | – | – | 4.60 | 28 | – | – |
| Other bonds | 4.99 | 295 | 4.80 | 44 | 5.30 | 19 | 4.90 | 12 |
| Property | – | – | 6.60 | 16 | – | – | – | – |
| Cash and other net current assets | 3.80 | 27 | 3.80 | 9 | 3.80 | 1 | – | – |
| Total market value of assets/rate of return | 6.11 | 1,480 | 7.11 | 185 | 7.06 | 133 | 4.90 | 12 |
| Present value of scheme liabilities | | (1,638) | | (199) | | (190) | | (12) |
| Surplus/(deficit) in scheme | | (158) | | (14) | | (57) | | – |
| Related deferred tax asset | | 47 | | 4 | | 17 | | – |
| Net pension assets/(liabilities) | | (111) | | (10) | | (40) | | – |

| | Balfour Beatty Pension Fund | | Railways Pension Scheme | | Mansell schemes | | Other funded schemes | |
|---|---|------------------------------|---|------------------------------|---|------------------------------|---|------------------------------|
| | Long-term expected rate of return at 31 December 2003 % | Value at 31 December 2003 £m | Long-term expected rate of return at 31 December 2003 % | Value at 31 December 2003 £m | Long-term expected rate of return at 31 December 2003 % | Value at 31 December 2003 £m | Long-term expected rate of return at 31 December 2003 % | Value at 31 December 2003 £m |
| Equities | 8.50 | 548 | 8.50 | 197 | 8.50 | 79 | – | – |
| Gilts | 4.78 | 505 | – | – | – | – | – | – |
| Other bonds | 4.91 | 309 | 5.00 | 23 | 5.00 | 38 | 5.20 | 12 |
| Property | 8.50 | 3 | 7.00 | 18 | – | – | – | – |
| Cash and other net current assets | 3.70 | 20 | – | – | 3.70 | 1 | – | – |
| Total market value of assets/rate of return | 6.27 | 1,385 | 8.10 | 238 | 7.34 | 118 | 5.20 | 12 |
| Present value of scheme liabilities | | (1,523) | | (264) | | (178) | | (12) |
| Surplus/(deficit) in scheme | | (138) | | (26) | | (60) | | – |
| Related deferred tax asset | | 41 | | 8 | | 18 | | – |
| Net pension assets/(liabilities) | | (97) | | (18) | | (42) | | – |

23 Pensions continued

| | Balfour Beatty Pension Fund | | Railways Pension Scheme | | Other funded schemes | |
|---|---|------------------------------|---|------------------------------|---|------------------------------|
| | Long-term expected rate of return at 31 December 2002 % | Value at 31 December 2002 £m | Long-term expected rate of return at 31 December 2002 % | Value at 31 December 2002 £m | Long-term expected rate of return at 31 December 2002 % | Value at 31 December 2002 £m |
| Equities | 8.30 | 482 | 8.30 | 204 | 8.00 | 4 |
| Gilts | 4.39 | 492 | – | – | – | – |
| Other bonds | 4.63 | 256 | 4.90 | 12 | 5.31 | 12 |
| Property | 8.30 | 14 | 8.50 | 18 | – | – |
| Cash and other net current assets | 3.70 | 24 | – | – | – | 1 |
| Total market value of assets/ <i>rate of return</i> | 5.96 | 1,268 | 8.10 | 234 | 5.57 | 17 |
| Present value of scheme liabilities | | (1,350) | | (254) | | (22) |
| Surplus/(deficit) in scheme | | (82) | | (20) | | (5) |
| Related deferred tax asset | | 25 | | 6 | | 1 |
| Net pension assets/(liabilities) | | (57) | | (14) | | (4) |

The analysis of the movement in the surplus/(deficit) in the schemes is as follows:

| | Balfour Beatty Pension Fund £m | Railways Pension Scheme £m | Mansell schemes £m | Other funded schemes £m |
|--------------------------|--------------------------------|----------------------------|--------------------|-------------------------|
| At 1 January 2004 | (138) | (26) | (60) | – |
| Current service cost | (42) | (4) | (3) | – |
| Settlement gain | – | 8 | – | – |
| Contributions | 30 | 2 | 8 | – |
| Other finance income | 5 | 2 | – | – |
| Actuarial gains/(losses) | (13) | 4 | (2) | – |
| At 31 December 2004 | (158) | (14) | (57) | – |

The actuarial gain/(loss) in 2004 comprises:

| | | | | | |
|---|----------------------------------|--------|--------|--------|---|
| Actual return less expected return on pension scheme assets | amount | £40m | £10m | £2m | – |
| | percentage of scheme assets | 2.8% | 5.5% | 1.9% | – |
| Experience gains and losses arising on scheme liabilities | amount | £(59)m | £(2)m | £2m | – |
| | percentage of scheme liabilities | (3.6)% | (0.8)% | 0.9% | – |
| Changes in assumptions underlying the present value of scheme liabilities | amount | £6m | £(4)m | £(6)m | – |
| | percentage of scheme liabilities | 0.4% | (2.1)% | (3.3)% | – |
| Total actuarial gain/(loss) | amount | £(13)m | £4m | £(2)m | – |
| | percentage of scheme liabilities | (0.8)% | 2.1% | (1.0)% | – |

The actuarial gain/(loss) in 2003 comprised:

| | | | | | |
|---|----------------------------------|---------|--------|---|---|
| Actual return less expected return on pension scheme assets | amount | £84m | £14m | – | – |
| | percentage of scheme assets | 6.1% | 6.1% | – | – |
| Experience gains and losses arising on scheme liabilities | amount | £17m | £(1)m | – | – |
| | percentage of scheme liabilities | 1.1% | (0.4)% | – | – |
| Changes in assumptions underlying the present value of scheme liabilities | amount | £(139)m | £(21)m | – | – |
| | percentage of scheme liabilities | (9.1)% | (8.3)% | – | – |
| Total actuarial gain/(loss) | amount | £(38)m | £(8)m | – | – |
| | percentage of scheme liabilities | (2.5)% | (3.0)% | – | – |

23 Pensions continued

The Railways Pension Scheme is a shared cost scheme. Accordingly the surplus/(deficit) shown above assumes that the Group will obtain economic benefit from, or be required to finance, only a proportion of the surplus or deficit in the Balfour Beatty section of the scheme. This proportion has been based on the apportionment of the surplus/(deficit) which has already been agreed together with the relevant provisions of the Trust Deed and Rules and Trustee guidelines regarding future surplus apportionments and deficit financing.

Contributions paid in 2004 for the principal schemes were £30m (2003: £16m) for the Balfour Beatty Pension Fund, £2m (2003: £1m) for the Railways Pension Scheme and £8m (2003: £nil) for the Mansell Schemes.

In addition the Group has unfunded post retirement benefit obligations in Europe and North America amounting to £18m (2003: £17m), the majority of which arrangements are closed to new entrants.

If the Group had accounted for pensions in accordance with the requirements of FRS 17 the following amounts, excluding the effect of the share of joint ventures' and associates' schemes, would have been recognised in the profit and loss account and statement of recognised gains and losses:

| | | 2004 £m | 2003 £m |
|---|--|------------|------------|
| Profit and loss account | | | |
| Charge to operating profit | current service cost | (49) | (39) |
| Exceptional item | settlement gain | 8 | 5 |
| Credit to net interest payable and similar charges | expected return on pension scheme assets | 103 | 84 |
| | interest on pension scheme liabilities | (98) | (82) |
| Charge to profit on ordinary activities before taxation | | (36) | (32) |
| Statement of total recognised gains and losses | actuarial gain/(loss) | (10) | (47) |

Pension costs charged to profit and loss account in respect of defined contribution schemes were £2m (2003: £3m).

If the Group had accounted for pensions in accordance with the requirements of FRS 17 net assets would have been restated as follows:

| | 2004 £m | 2003 as restated £m |
|---|------------|---------------------------|
| Net assets per financial statements – as restated | 413 | 231 |
| SSAP 24 pension provisions/(prepayments) | 27 | 30 |
| FRS 17 pension assets/(liabilities) | | |
| Group schemes – funded | (161) | (157) |
| Group schemes – unfunded | (18) | (17) |
| Share of joint ventures' and associates' schemes | (17) | (28) |
| Net assets as adjusted | 244 | 59 |
| Net assets excluding pension assets | 440 | 261 |
| Net pension (liabilities)/assets | (196) | (202) |
| | 244 | 59 |

24 Commitments

Capital expenditure authorised and contracted for which has not been provided for in the accounts amounted to £15m (2003: £11m) in the Group and nil (2003: nil) in the Company.

The Company has committed to provide its share of further equity funding and subordinated debt of joint ventures and associates in PFI/PPP projects amounting to £73m (2003: £100m), of which £73m (2003: £98m) is projected to be drawn down.

Annual operating lease commitments comprise:

| | Land and buildings 2004 £m | Other 2004 £m | Land and buildings 2003 £m | Other 2003 £m |
|--|-------------------------------------|---------------------|-------------------------------------|---------------------|
| Group | | | | |
| Leases terminating: | | | | |
| Within one year | 3 | 4 | 4 | 5 |
| Between one and five years | 9 | 16 | 10 | 19 |
| In five years or more | 10 | 2 | 10 | 1 |
| | 22 | 22 | 24 | 25 |
| Company – leases terminating in five years or more | 3 | – | 5 | – |

25 Contingent liabilities and assets*a) Contingent liabilities:*

Contingent liabilities, which are not expected to give rise to any material loss, include:

| | Group 2004 £m | Group 2003 £m | Company 2004 £m | Company 2003 £m |
|---|---------------------|---------------------|-----------------------|-----------------------|
| Guarantees of subsidiary undertakings and other support | – | – | 2 | 3 |

The Company and certain subsidiary undertakings have, in the normal course of business, given guarantees and entered into counter-indemnities in respect of bonds relating to the Group's own contracts and given guarantees in respect of the Group's share of certain contractual obligations of joint ventures and associates. The Company has given limited indemnities up to a maximum of £11m to Halliburton Company and Brown & Root Ltd in respect of the performance of Devonport Management Ltd on certain construction contracts and a further limited guarantee in respect of operational contracts undertaken for the Ministry of Defence. The Company has guaranteed the property lease commitments of a former subsidiary undertaking currently amounting to £2m per annum terminating in 2005.

Prior to 1999 the Group owned large cable manufacturing businesses, predominantly in Europe and North America. These businesses have subsequently been sold through a number of sale and purchase agreements. In common with many such agreements, the Group gave certain indemnities in respect of environmental and other matters which extend until 2007. The Group maintains provisions against all identified issues based on current available information and carries some insurance cover against further liabilities that may arise.

As stated in Note 17, provision is made for the Directors' best estimate of known legal claims and legal actions in progress. The Group takes legal advice as to the likelihood of success of claims and actions and no provision is made where the Directors consider, based on that advice, that the action is unlikely to succeed or a sufficiently reliable estimate of the potential obligation cannot be made.

b) Contingent assets:

In November 2002, TXU Europe, whose subsidiaries are respectively a shareholder and customer of Barking Power Ltd, in which the Group holds a 25.5% interest, entered administration. As a result, the long-term electricity supply contract with a TXU subsidiary was terminated, triggering an entitlement to a payment for damages, for which Barking Power Ltd lodged a substantial claim. In December 2004, Barking Power Ltd reached an agreement in principle with the administrators on the value of its claim at £179m, subject to the approval of the TXU Europe subsidiary's company voluntary arrangement by its creditors. In January 2005, those creditors approved the company voluntary arrangement. Barking Power Ltd expects to recognise the initial dividend from the settlement by the end of March 2005 once the period for submission of claims has expired, the company voluntary arrangement has been implemented and the quantum and timing of the first dividend has been settled by the administrators.

26 Post balance sheet events

On 17 February 2005, the Group acquired JCM Group in the USA for a consideration of approximately US\$10m.

27 Related party transactions

The Group recharged the Balfour Beatty Pension Fund with the costs of administration and advisers' fees borne by the Group amounting to £2.9m in 2004 (2003: £3.3m).

The Group provided services to, and received management fees from, certain joint ventures, associates and joint arrangements amounting to £266m (2003: £246m). These transactions occurred in the normal course of business at market rates and terms. In addition, the Group procured equipment and labour on behalf of certain joint ventures and joint arrangements which were recharged at cost with no mark-up. Amounts due from and to joint ventures and associates are set out in Notes 13 and 16.

28 Notes to the cash flow statement*a) Net cash inflow from operating activities*

| | 2004 £m | 2003 as restated £m |
|---|------------|---------------------------|
| Group operating profit before exceptional items | 67 | 68 |
| Depreciation | 50 | 43 |
| Goodwill amortisation | 33 | 15 |
| Profit on sale of tangible fixed assets | (1) | (3) |
| Charge relating to Performance Share Plan | 2 | 3 |
| Exceptional items – cash (expenditure)/receipts | (6) | 5 |
| Working capital decrease: | | |
| Stocks | 3 | (6) |
| Debtors | (15) | 70 |
| Other creditors and provisions | 38 | (25) |
| | 26 | 39 |
| Net cash inflow from operating activities | 171 | 170 |

28 Notes to the cash flow statement continued

b) Analysis of movement in net cash

| | Cash and deposits and overdrafts £m | Term deposits £m | Borrowings (including finance leases) £m | Total 2004 £m | Total 2003 £m |
|--|--|---------------------|---|------------------|------------------|
| At 1 January 2004 | 143 | 55 | (74) | 124 | 67 |
| Cash flow | (36) | 206 | 8 | 178 | 46 |
| Acquisitions of businesses – net (borrowings)/term deposits at date of acquisition | – | 39 | (278) | (239) | 5 |
| Exchange adjustments | – | (1) | 5 | 4 | 6 |
| At 31 December 2004 | 107 | 299 | (339) | 67 | 124 |

c) Reconciliation of cash flow to movement in net cash

| | 2004 £m | 2003 £m |
|--|------------|------------|
| (Decrease)/increase in cash in the period | (36) | 3 |
| Cash outflow from decrease in borrowings | 8 | 11 |
| Cash outflow from increase in term deposits | 206 | 32 |
| Change in net cash resulting from cash flows | 178 | 46 |
| Acquisitions of businesses – net (borrowings)/term deposits at date of acquisition | (239) | 5 |
| Exchange adjustments | 4 | 6 |
| Movement in net cash | (57) | 57 |

d) Acquisitions of businesses

| | 2004 £m | 2003 £m |
|--|------------|------------|
| Net assets acquired: | | |
| Intangible assets – goodwill | 17 | 54 |
| Tangible fixed assets | 229 | 24 |
| Investments in joint ventures | 34 | – |
| Stocks | – | 4 |
| Debtors (including deferred tax) | 81 | 115 |
| Creditors and provisions (including current tax) | (54) | (174) |
| Term deposits | 39 | 5 |
| PFI/PPP non-recourse term loans | (278) | – |
| | 68 | 28 |
| Due on acquisitions | 5 | (7) |
| | 73 | 21 |
| Satisfied by: | | |
| Cash consideration | 58 | 36 |
| Cash, deposits and overdrafts acquired | (2) | (15) |
| Cash outflow | 56 | 21 |
| Interest in joint ventures transferred | 17 | – |
| | 73 | 21 |

Companies acquired during the year (see Note 20) generated a net cash inflow from operating activities of £37m in periods since acquisition to 31 December 2004.

e) Disposals of businesses

| | 2004 £m | 2003 £m |
|---|------------|------------|
| Net assets disposed of: | | |
| Intangible assets – goodwill (including £38m goodwill previously written off to reserves) | 60 | – |
| Tangible fixed assets | 4 | – |
| Investments | 3 | – |
| Stocks | 2 | – |
| Debtors | 29 | – |
| Creditors and provisions | (18) | – |
| | 80 | – |
| Profit on sale | 137 | – |
| | 217 | – |
| Satisfied by: | | |
| Cash consideration | 221 | – |
| Cash, deposits and overdrafts sold | (4) | – |
| Cash inflow | 217 | – |

Disposals in 2004 comprise Andover Controls, the Group's Hong Kong business and the Group's investments in Garanti Balfour Beatty Insaat Sanayi ve Ticaret AS and First Philippine Balfour Beatty Inc.

29 Principal subsidiaries, joint ventures and associates continued

d) PFI/PPP concessions

| Concession | Project | Total debt and equity funding | Shareholding | Date of financial close | Construction completion | Duration years | Equity and subordinated debt | |
|--|--------------------------------------|-------------------------------|--------------|-------------------------|-------------------------|----------------|------------------------------|---------------------------------|
| | | | | | | | Invested to 31 December 2004 | Committed post 31 December 2004 |
| Infrastructure – Transport | | | | | | | | |
| Connect M1-A1 | M1-A1 30km DBFO road | £290m | 50% | 1996 | 1999 | 30 | £14.4m | – |
| Connect A30/A35 | A30/A35 102km DBFO road | £127m | 100% | 1996 | 2000 | 30 | £19.5m | – |
| Connect A50 | A50 57km DBFO road | £42m | 100% | 1996 | 1999 | 30 | £6.7m | – |
| Connect M77 | M77/GSO 25km DBFO road | £167m | 100% | 2003 | – | 32 | £0.3m | £14.9m |
| Connect Sunderland Street Lighting | Street lighting | £27m | 100% | 2003 | – | 25 | – | £2.7m |
| Metronet BCV | London Underground | £1,783m | 20% | 2003 | – | 30 | £8.3m | £26.7m |
| Metronet SSL | London Underground | £2,108m | 20% | 2003 | – | 30 | £7.6m | £27.4m |
| Infrastructure – Other | | | | | | | | |
| Powerlink/PADCo | London Underground power system | £184m | 10/25% | 1998 | – | 30 | £4.3m | £1.8m |
| Aberdeen Environmental Services | Wastewater treatment plant | £92m | 45% | 2000 | 2002 | 30 | £3.4m | – |
| Accommodation | | | | | | | | |
| Consort Healthcare: Edinburgh Royal Infirmary | Teaching hospital and medical school | £220m | 42.5% | 1998 | 2003 | 30 | £8.4m | – |
| Consort Healthcare: North Durham Hospital | District general hospital | £90m | 50% | 1998 | 2001 | 30 | £6.7m | – |
| Consort Healthcare: Blackburn Hospital | District general hospital | £116m | 50% | 2003 | – | 38 | – | £6.0m |
| University College London Hospital | Teaching hospital | £282m | 33.3% | 2000 | – | 40 | £8.4m | £1.0m |
| Transform Schools Stoke | Grouped schools project | £74m | 50% | 2000 | – | 25 | – | £4.6m |
| Transform Schools Rotherham | Grouped schools project | £113m | 50% | 2003 | – | 31 | – | £5.5m |
| Total | | £5,715m | | | | | £88.0m | £90.6m |

| | 2004 £m | 2003 as restated £m | 2002 as restated £m | 2001 as restated £m | 2000 as restated £m |
|---|--------------|---------------------------|---------------------------|---------------------------|---------------------------|
| Profits | | | | | |
| Turnover (including share of joint ventures and associates) | 4,171 | 3,678 | 3,441 | 3,071 | 2,603 |
| Operating profit – before goodwill amortisation and exceptional items | 173 | 161 | 149 | 136 | 110 |
| Goodwill amortisation and impairment | (35) | (17) | (21) | (12) | (3) |
| Exceptional items | 142 | 5 | (9) | 13 | 11 |
| Profit on ordinary activities before interest | 280 | 149 | 119 | 137 | 118 |
| Net interest payable | (23) | (31) | (31) | (34) | (28) |
| Profit before tax | 257 | 118 | 88 | 103 | 90 |
| Capital employed | | | | | |
| Shareholders' funds | 413 | 231 | 192 | 185 | 154 |
| Minority interests | – | – | – | – | 1 |
| Net cash | (67) | (124) | (67) | (63) | (104) |
| | 346 | 107 | 125 | 122 | 51 |
| Statistics | | | | | |
| Adjusted earnings per ordinary share* | 23.4p | 20.6p | 16.1p | 14.1p | 10.2p |
| Basic earnings/(loss) per ordinary share | 43.8p | 16.9p | 8.5p | 13.8p | 11.0p |
| Diluted earnings/(loss) per ordinary share | 43.4p | 16.7p | 8.4p | 13.6p | 11.0p |
| Dividends per ordinary share | 6.6p | 6.0p | 5.4p | 5.0p | 4.5p |
| Operating profit before goodwill amortisation and exceptional items: turnover | 4.2% | 4.4% | 4.3% | 4.4% | 4.2% |

*Adjusted earnings per ordinary share before goodwill amortisation, exceptional items and appropriations arising on the buy-back of preference shares have been disclosed to give a clearer understanding of the Group's underlying trading performance.

Shareholder information

Financial calendar

| | | 2005 |
|------------|--|------|
| 27 April | Ex-dividend date for final 2004 ordinary dividend | |
| 29 April | Final 2004 ordinary dividend record date | |
| 12 May | Annual General Meeting | |
| 25 May | Ex-dividend date for July 2005 preference dividend | |
| 27 May | July 2005 preference dividend record date | |
| 10 June | Final date for receipt of DRIP mandate forms (see below) | |
| 1 July | Preference dividend payable | |
| 1 July* | Final 2004 ordinary dividend payable | |
| 17 August* | Announcement of 2005 half-year results | |
| | | 2006 |
| 1 January | Preference dividend payable | |
| 3 January* | Interim 2005 ordinary dividend payable | |

*Provisional dates

Registrar and transfer office

All administrative enquiries relating to shareholdings should, in the first instance, be directed to the Company's Registrars and clearly state the shareholder's registered name and address and, if available, the full shareholder reference number. Please write to:

The Balfour Beatty plc Registrar
Computershare Investor Services PLC
PO Box 82
The Pavilions
Bridgwater Road
Bristol BS99 7NH
Telephone 0870 702 0122
or by e-mail to: web.queries@computershare.co.uk

They can help you to:

- check your shareholding;
- register a change of address or name;
- obtain a replacement dividend cheque or tax voucher;
- record the death of a shareholder;
- amalgamate multiple accounts;
- resolve any other question about your shareholding.

Dividend mandates

If you wish dividends to be paid directly into your bank or building society account, you should contact the Registrars for a dividend mandate form.

Dividends paid in this way will be paid through the Bankers Automated Clearing System (BACS).

Information about Balfour Beatty's Dividend Reinvestment Plan ("DRIP") can also be obtained from the Registrars.

Subject to shareholder approval, the final dividend for 2004 will be paid on 1 July 2005. If you have already elected to join the DRIP, then you need take no further action. If you wish to join the DRIP, then you should complete a mandate form and return it to the Registrars by no later than 10 June 2005 in order to participate in the DRIP for this dividend. If you do not have a DRIP mandate form, please contact the Registrars.

Shareholder information on the Internet and electronic communications

The Balfour Beatty website at <http://www.balfourbeatty.com/> offers shareholders and prospective investors a wealth of information about the Company, its people and businesses and its policies on corporate governance and corporate responsibility. It should be regarded as your first point of reference for information on any of these matters.

Computershare Investor Services have introduced a facility enabling Balfour Beatty shareholders to access details of their shareholding over the internet subject to complying with an identity check. You can access this service via the shareholder information section of the Balfour Beatty website at <http://www.balfourbeatty.com/>. You can also obtain information on recent trends in Balfour Beatty's share price.

Balfour Beatty actively encourages all shareholders to register now for our electronic communications service through the eShareholder™ campaign being run by ComputersharePepper. When you register for electronic communications, we will dedicate a tree on your behalf in a UK area selected for reforestation. This service enables you to save paper, contribute to a better environment and reduce harmful carbon dioxide emissions which impact climate change.

In order to receive shareholder communications such as notices of shareholder meetings and the annual report and accounts electronically rather than by post, you should register your details via the shareholder information section of the Balfour Beatty website.

Unsolicited mail

Balfour Beatty is obliged by law to make its share register available on request to other organisations who may then use it as a mailing list. This may result in you receiving unsolicited mail. If you wish to limit the receipt of unsolicited mail, you may do so by writing to the Mailing Preference Service, an independent organisation whose services are free to you. Once your name and address have been added to its records, it will advise the companies and other bodies that support the service that you no longer wish to receive unsolicited mail.

If you would like more details, please write to:

Mailing Preference Service
Freepost 29 LON20771
London W1E 0ZT

Gifting shares to your family or to charity

To transfer shares to another member of your family as a gift, please ask the Registrars for a Balfour Beatty gift transfer form. If you only have a small number of shares whose value makes it uneconomic to sell them, you may wish to consider donating them to the share donation charity ShareGift (registered charity no. 1052686). The relevant share transfer form may be obtained from the Registrars; further information about the scheme is available from the ShareGift Internet site www.ShareGift.org.

Share dealing services

The Company has established an execution-only postal share dealing service, through Cazenove & Co. Ltd, for private investors who wish to buy or sell Balfour Beatty plc's shares. Further details can be obtained from:

The Balfour Beatty Share Dealing Service
Cazenove & Co. Ltd
20 Moorgate
London EC2R 6DA
Telephone: 020 7155 5155

Alternatively, Hoare Govett Limited also offers a low-cost share dealing service. Further details can be obtained from:

Hoare Govett Limited (LCSD)
250 Bishopsgate
London EC2M 4AA
Telephone: 020 7678 8300

Both Cazenove & Co. Ltd and Hoare Govett Limited are authorised and regulated by the Financial Services Authority.

Share price

The Balfour Beatty share price can be found at the Balfour Beatty website at www.balfourbeatty.com and in the appropriate sections of national newspapers under the classification "Construction and Building Materials". It is also available on Ceefax and Teletext and a number of personal finance websites on the Internet. Historic share prices are available from the library at Hoare Govett. Telephone: 020 7678 1718.

The London Stock Exchange Daily Official List (SEDOL) codes are:

Ordinary shares: 0096162
Preference shares: 0097820

The London Stock Exchange "ticker" codes are:

Ordinary shares: BBY
Preference shares: BBYB

Capital gains tax

For capital gains tax purposes the market value on 31 March 1982 of Balfour Beatty plc's ordinary shares of 50p each was 307.3p per share. This has been adjusted for the 1-for-5 rights issue in June 1992 and the 2-for-11 rights issue in September 1996.

Enquiries

Enquiries relating to Balfour Beatty's results, business and financial position should be made in writing to the Corporate Communications Department at the Company's Registered Office address or by e-mail to info@balfourbeatty.com.



Balfour Beatty

Balfour Beatty plc

130 Wilton Road
London SW1V 1LQ

Telephone: 44 (0) 20 7216 6800

Facsimile: 44 (0) 20 7216 6950

www.balfourbeatty.com

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