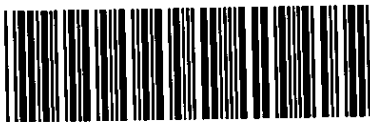


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MARSHALLS PLC

ANNUAL REPORT 2006

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COMPANIES HOUSE

Marshalls plc, proud sponsor of the
RHS Chelsea Flower Show 2007-2009

Scenic Blue Gold Medal Garden at RHS Chelsea 2006

Financial Highlights

- Revenue, including acquisitions, up 5.2 per cent
- EBITDA up 6.7 per cent to £67.6 million
- Operating profit up 7.5 per cent to £47.8 million
- Profit before tax up 9.7 per cent to £41.7 million
- EPS up 9.6 per cent to 20.34 pence per share
- Final dividend up 5.4 per cent to 8.85 pence per share



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Marshalls plc Annual Report 2006

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Corporate Objectives

Customers are at the centre of our business. We supply our customers with exclusive ranges of the highest quality landscape and walling products and provide outstanding levels of customer service in our chosen markets. We continually innovate in the design of our products and in our methods of manufacture. Our achievement of these objectives will ensure that we maintain and develop our market leading position.

Marshalls undertakes this challenging task with the objective of delivering superior rates of return to our shareholders and providing opportunities and reward for our employees.

Profile

Marshalls manufactures and supplies landscape, driveway and garden products from a range of materials including concrete, natural stone, iron, steel, wood, glass and polyurethane, for Domestic and Public Sector and Commercial use.

The home improvement and home building markets are the largest users of the Groups' products and we supply goods ranging from paving and walling to greenhouses and garages. Public Sector and Commercial customers use Marshalls' products to transform landscapes including retail, industrial, new build as well as repair and maintenance projects.

Marshalls' customers are the large builders' merchant groups, independent builders' merchants, garden centres, contractors and local authorities and Domestic consumers. Products are distributed from a national network of manufacturing and Service Centres either to customers' depots or, at their request, direct to site. The Domestic consumer business makes a range of services available to the consumer through its Drive & Garden Transformation Centres.

Bespoke signage panels, Temple Bar, London

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Chairman's Statement

Gaining Momentum

I am pleased to report a year of revenue and profit advance, as Marshalls builds momentum in pursuit of its strategic growth objectives

In keeping with our sustainable dividends policy, we are declaring a 5 per cent increase in dividends for the year and maintaining our record of continuous increases, broadly in line with medium term earnings growth

During the year we have made progress in implementing the various elements of our growth strategy

In our core Landscape Products operations we have continued to invest in the business. Examples of strategic investment include the acquisition of rights to develop new mineral reserves in North West England, the extension of the range of robotics in our manufacturing operations and further expansion in the machine laying of our products, thus making the block paving of large areas more economical. We have also worked to bring our overseas suppliers into the Ethical Trading Initiative, an innovation in the industry.

Haworth Moor Paving and Setts

The development of our Consumer strategy gained momentum with the sponsorship of the Royal Horticultural Society's Chelsea Flower Show, the acquisition of the garden design and installation company Scenic Blue and the opening of further Drive & Garden Transformation Centres.

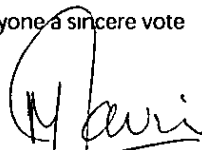
Our Public Sector and Commercial presence was reinforced by the acquisition of Urban Engineering, Tempakerb, Decathlon and, since the year end, Ollerton, thus reinforcing the unique proposition which Marshalls can offer by packaging both street furniture and surfacing. We are already seeing the benefits of this integration, for example, The Sage Gateshead.

All of these initiatives have been pursued together with an increased focus on our environmental and sustainability responsibilities. The Environmental Report on pages 26 to 29 contains a detailed report, but we are particularly proud of our employees at our Maltby site, who have achieved the Biodiversity Benchmark from the Wildlife Trust, the first UK manufacturing unit to be awarded the Benchmark.

Evening at The Sage Gateshead

The risk profile of the business also improved during the year as the result of the replacement of the defined benefit pension, with a defined contribution pension. Whilst this was a necessary step given the uncertainties of funding such schemes, Marshalls remains committed to the provision of pension benefits for its employees. All parties to this negotiation are to be congratulated on achieving a balanced and sensible outcome.

As ever, the programme of work I have described results from a positive interaction between our employees, our customers and suppliers. On behalf of the Board, I offer everyone a sincere vote of thanks.



Mike Davies

Chairman

9 March 2007

Operating and Financial Review

Marshalls is a market focussed UK Group combining inspirational design and innovative products and services to aid the transformation of Britain's patios, driveways and urban and commercial landscapes

Long Term Strategy and Business Objectives

Corporate Objectives

Marshalls corporate objectives are

- 1 Revenue growth of 7 per cent based on a compound annual growth rate ("CAGR") over a three year period,
- 2 Annual earnings per share growth of at least 3 per cent, and a target of 6 per cent, above the retail price index, on a CAGR basis, over a three year period,
- 3 Dividend policy where dividends will move in line with medium term earnings growth, and
- 4 Return on capital employed of 20 per cent per annum

Strategy

The strategy to achieve these objectives is

- 1 To deliver sustainable shareholder value by continuing to develop, innovate, improve and reduce cost in the core business

This is achieved by continually investing in market and brand development, developing long term customer relationships, continually innovating and introducing new products and services to meet the needs of consumers and installers that have been identified through extensive market research, investing in manufacturing technology to improve the quality of our products and to enable us to operate more effectively and reducing costs wherever possible. The business has high quality, timely management information and analysis and uses this to focus on areas for improvement

Festival Hall Walkway, London

- 2 To develop the landscape installations service offer to enhance and support the core hard landscape products business

This will allow consumers to view a full range of products in an aspirational and sympathetic setting, request a design and identify a quality installer for their project. Having already established a unique regional distribution and manufacturing network and having built an installer register, this will create the "pull through demand" by investing in sales and marketing directly to the consumer

- 3 To develop further the integrated product offering for the Public Sector and Commercial hard landscaping market

The Public Sector and Commercial hard landscaping market requires a range of co-ordinated products that deliver technical performance and the required appearance

- 4 To invest in selective acquisitions in existing and related product categories to support the initiatives above and to capitalise on the Marshalls brand and unique access to nationwide distribution channels

Operating and Financial Review (continued)

Review of the Operations

Markets

Overall market conditions were mixed in 2006. The Construction Products Association ("CPA") estimates that construction output has grown by only 0.9 per cent during 2006 although this is an improvement on the prior year which experienced a 0.9 per cent decline. The Public Sector and Commercial market was good with the CPA estimating that Other New Work, a proxy for demand, was up by 4.2 per cent in 2006. This contrasts with the Domestic market where the CPA estimates that Private Housing Repair, Maintenance and Improvement expenditure, a proxy for Domestic demand, was down 4.0 per cent, compared with a decrease of 3.0 per cent in 2005.

Trading Summary

Half of the revenue of the business continues to be from the consumer driven Domestic market and half from the Public Sector and Commercial market. This provides a balance to demand as the performance of the two markets can be counter cyclical.

Marshalls' revenue at £378.1 million (2005 £359.3 million) grew by 5.2 per cent, including acquisitions, compared with the prior year. Like for like revenue, excluding acquisitions, was 2.6 per cent ahead at £368.8 million (2005 £359.3 million).

In the Domestic market like for like revenue was flat with a robust installed market offset by the weaker DIY market. The Public Sector and Commercial market continued to perform well with like for like revenue up 5.0 per cent.

The results for the year ended 31 December 2006 represent a robust performance given the flat building materials market.

The Sage Gateshead

Strategic Key Performance Indicators ("KPIs")

Performance is monitored using a full suite of KPIs. The Directors have identified the six measures below as the strategic KPIs. The first two are measured on a CAGR basis over a three year period. In addition to the strategic KPIs there are KPIs for each area of the business. A number of these are included later in the individual sections of this review.

Target	
Revenue growth	7 per cent per annum
Earnings per share growth	RPI + 6 per cent per annum
Return on capital employed	20 per cent
Cash flow *	Detailed forecast
Customer service index **	95 per cent
Health & Safety reduction in reportable incidents	10 per cent per annum

* Cash performance targets have been established for the purpose of Directors Performance Share Awards, details of which are set out on page 44.

** The index combines measures of product availability, on time delivery performance and administrative and delivery accuracy.

The results achieved on each of these measures are set out in the appropriate sections below.

Marshalls plc Annual Report 2006

Domestic

Marshalls is a market leader in the domestic driveway and patio markets and has led the development of the consumer landscape products market over an extended period. The Group's Domestic strategy has not changed and products continue to be sold under the Marshalls and Stonemarket brands. Significant amounts of money are being invested annually to create "pull through" demand, improve the product mix and continually develop these brands. Drive & Garden Transformation Centres are designed to make a range of services available to the consumer from the opportunity to see how the product looks in a garden setting to assistance with design and the arrangement of installation. Three Centres are now operational and a fourth, at Enfield in North London, is due to open shortly.

The initial results from these Centres are encouraging and experience has shown that these Centres are welcomed by both installers and merchant stockists and footfall and direct order flow has been increasing steadily. The Group is also benefiting from improved sales and product mix in the areas where these Centres are based and the intention is to roll out further Drive & Garden Transformation Centres during 2007 and 2008. The total one-off investment in the consumer initiative start up costs in the year ended 31 December 2006 amounted to £20 million (2005 £10 million) and this has been disclosed separately in Note 4 of the Financial

Statements on page 64. Discussions are ongoing with a number of large, regional garden centre operators to build Drive & Garden Transformation Centres and Garden Design Studios and displays, which are a smaller version, on a number of their other sites.

Marshalls' consumer initiatives and research show that there are a significant number of consumers who want help with garden design, including planting, and the project management of the installation. On 30 November 2006 the Group acquired Scenic Blue, a design and installation franchising business which specialises in this area. Scenic Blue was a Gold Medal winner for its show garden at the Royal Horticultural Society's ("RHS") Chelsea Flower Show in 2006.

In order to improve brand recognition further, in December 2006, Marshalls announced the sponsorship of the RHS Chelsea Flower Show for a period of three years commencing in 2007. This provides the platform to launch a garden design and installation service nationally. The Group will also have a presence in 2007 at the RHS Hampton Court and Tatton Park Flower Shows. This sponsorship deal is a very important part of our strategy to improve further our brand awareness.

The Marshalls Register of approved installers, which are recommended to the consumer, comprises over 1,500 installation teams around the country whose work is constantly vetted. Installer order books, from the latest survey at the end of February 2007, were an encouraging 9.1 weeks (February 2006 8.4 weeks).

The Domestic landscape installations business is market focussed and future developments will continue to be driven by comprehensive market research. This research clearly demonstrates a demand for higher value products and a consumer willingness to pay for them. The benefits of providing an improved product mix for the consumer, installer and distributor is significant and hence much of our marketing investment will remain focussed on unlocking this opportunity.

Operating and Financial Review (continued)

Public Sector and Commercial

Marshalls is also a market leader for the supply of a wide range of natural stone, concrete and fabricated products to the Public Sector and Commercial market including paving, kerbs, edging, surface drainage and street furniture. The aim is to deliver products that are attractive to look at and are also practical to install. Marshalls have a portfolio of products that can be combined to create an attractive landscaped area and our technical expertise is an important part of our pre and post sales service.

An important part of Marshalls' strategy is the development of an integrated product offering for the Public Sector and Commercial market. In response to market demand, and working closely with architects, designers and contractors, the Group continues to offer solutions that combine natural stone and concrete paving, linear drainage, bollards, seating and attractively designed lighting. The strategy of formulating integrated solutions, together with the expansion of the range of products and services on offer, remains important for both organic growth and for increasing the flow of suitable acquisition opportunities. Investment continues to be made in new technology to improve productivity, such as robot handling and machine lay of concrete block paving, in order to take these products to the market. This investment continues to build competitive advantage and to make our workplace safer and reduce the environmental impact of our operations. Machine lay is four times faster than using manual labour and the finished installation is of a high quality. Marshalls has established the only machine lay training school in the country where installers are provided with training.

On 4 May 2006, the Group acquired Urban Engineering which specialises in the sale of a range of shelters and associated products, particularly to the Education Sector. In the second half of the year two other small businesses were acquired, being Tempakerb, a business that

manufactures temporary kerbs from recycled materials and Decathlon, which manufactures high capacity drainage systems which complement Marshalls' existing range of linear drainage products. On 5 February 2007, the Group also acquired Ollerton, a supplier of high quality and widely specified seating systems. A programme to introduce modern business systems and consolidate these businesses, to deliver synergies and provide a solid platform for future organic growth, is in progress.

The Group continues to seek opportunities to expand reserves and geographical coverage in natural stone. This growth will be achieved by both acquiring independent quarries, when these become available, and by investing capital to develop new stone reserves that are already owned or for which the Group is able to sign a royalty agreement to extract. During 2006 Marshalls acquired the rights to develop an aggregate reserve in North West England and, following capital investment of approximately £2 million, operations will commence fully during 2007. During the year the Group increased its total mineral reserves by 6.8 million tonnes comprising block stone for paving, walling stone and crushed aggregates. In January 2007 a further aggregate reserve was purchased.

Machine lay of concrete block paving

Manufacturing and Distribution

At the heart of Marshalls is a single logistics operation that supports the two main markets and this provides a fundamental competitive advantage and delivers industry leading product availability and delivery performance. The Marshalls operating strategy is to combine regional manufacturing and distribution sites ("Service Centres") with national manufacturing works. The same capital equipment produces products for both the Domestic market and the Public Sector and Commercial market. The national manufacturing sites produce the newly introduced and specialist products that have not reached the commercial volumes that justify regional manufacture. Marshalls geographical spread is unique in the industry and provides a competitive advantage.

Customer service is a high priority area. The KPIs cover product availability, accuracy and timeliness of deliveries as well as administrative accuracy. The Group's industry leading standards remained high in 2006 and the combined customer service measure was 97 per cent (2005 97 per cent).

The Group continues to invest to improve its productivity, to make the workplace safer and to reduce the environmental impact of its operations. Net capital investment in 2006 totalled £24.0 million (2005 £20.7 million). This compares to a depreciation charge of £19.5 million (2005 £18.7 million). The significant levels of capital expenditure in the last five years continue to generate improvements in productivity. Marshalls now has 49 robots installed and is developing new applications for them.

The Group also continues to focus on sustainability, including the elimination of waste and the better use of resources. There is a Group wide strategy of implementing and operating to independently audited and accredited systems for product quality, environmental management and health and safety. Emphasis on sustainability has also enabled the Group to add value to existing products. For instance, sales of sustainable urban drainage are increasing in response to demand from planners. This is a paving solution that allows water to percolate into the ground to sustain the water table rather than letting it run off into rivers.

The Group now sources significant quantities of natural stone from India and China. Marshalls is the only industry member from our sector of the Ethical Trading Initiative ("ETI"), an alliance of companies,

trade unions and non-profit organisations that aims to promote respect for the rights of workers worldwide. As a member of ETI, Marshalls has a programme in place to assess working conditions in suppliers' workplaces. These suppliers are regularly and independently audited on the ETI nine point base code, which covers working conditions in the supply chain, to ensure compliance with that code. During 2006 Marshalls Indian stone supplier has successfully demonstrated compliance with the ETI base code.

During the year Marshalls completed the closure, which commenced in 2005, of its Mansfield site which did not form part of the Service Centre and national manufacturing structure. In the second half of 2006 the Group also moved the manufacture of its internal paving business from a specialist unit, near Bristol, to a National Manufacturing Unit. These two initiatives have given rise to one-off works closure costs in the year of £1.1 million and will further reduce the fixed cost base going forward.

The Group has a number of surplus properties which are in the process of being sold. The timing of sales continues to be dependent on suitable planning permissions being obtained, but the Group's property portfolio is under constant review in order to identify opportunities to maximise its potential. It is estimated that between £15 million and £20 million may be realised from the surplus assets in the short to medium term.

Organisation

The Group's organisational structure incorporates specialist businesses such as those manufacturing Street Furniture products. The structure also enables the operationally independent businesses, such as Stonemarket and Paver Systems, to focus on the development of their own unique brand and position in the market place.

People

Marshalls has an experienced, flexible and well motivated workforce and is committed to developing its full potential. There is a wide range of internal and external training programmes with an emphasis towards "on the job" training. A detailed report on our employees and health and safety initiatives is included within the Corporate Social Responsibility Statement on pages 23 to 25. It is pleasing to report a further reduction of 13 per cent in incidents reportable to the Health & Safety Executive in 2006, following a reduction of 25 per cent in the previous year.

Operating and Financial Review (continued)

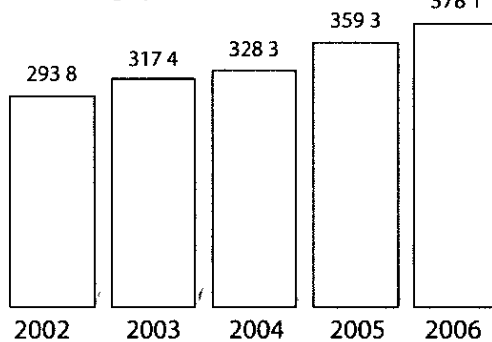
Research and Development

Marshalls' Management Innovation and Development team, staffed by high calibre engineers and technicians, are now increasing their emphasis towards the more recently acquired businesses where opportunities for efficiency improvements exist. They are continually striving to improve the flexibility and effectiveness of product manufacture and are at the forefront of technical research and development.

Innovation in all areas of the business over an extended period has been a key element of the Group's success and significant resources will continue to be invested in Research and Development in the future.

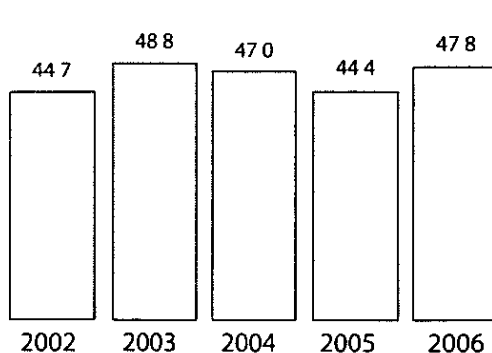
Financial History

Revenue (£'m)
Continuing operations

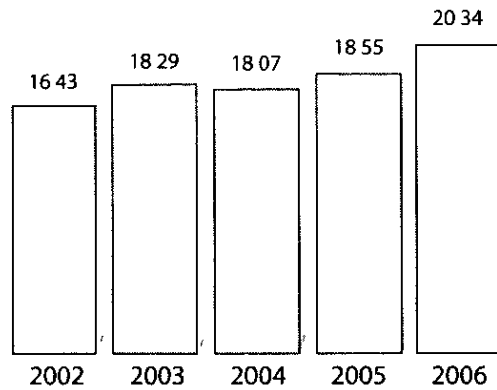


The CAGR for the five year period to the end of 2006 for revenue growth from continuing operations was 6.5 per cent.

Operating profit (£'m)
Continuing operations

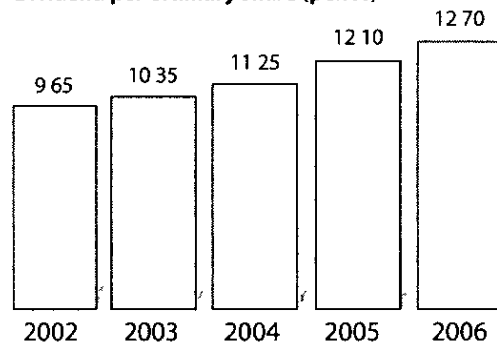


Basic earnings per share (pence)
Continuing operations



The CAGR for the five year period to the end of 2006 for earnings per share growth was 5.5 per cent.

Dividend per ordinary share (pence)



The above graph shows that dividends have, on a CAGR basis, grown by 7.1 per cent over the last five years. Dividends disclosed on an IFRS basis do not include the final 2006 declared dividend of 8.85 pence per share. This final dividend represents a 5.4 per cent increase over the comparative final dividend.

As at 31 December 2006 the Company's share price was 355 pence per share. When dividends are included this gives a total shareholder return (TSR) of 80.3 per cent over a five year performance period. A performance graph has been disclosed on page 45 where the Group's TSR is compared with the FTSE 250 Index.

Financial Review of 2006

Continuing operations

	2006 £'m	2005 £'m	Growth %
Revenue	378.1	359.3	5.2
Operating profit	47.8	44.4	7.5
Financing charges (net)	(6.1)	(6.4)	
Profit before tax	41.7	38.0	9.7
Tax	(12.6)	(11.6)	
Profit after tax	29.1	26.4	10.3

Revenue for the year ended 31 December 2006 increased by 5.2 per cent to £378.1 million (2005 £359.3 million). This growth was divided equally between organic growth and acquisition growth, both at 2.6 per cent. The growth strategy continues to include development through bolt-on acquisitions in addition to organic developments.

Underlying profit

	2006 £'m	2005 £'m	Growth %
Operating profit underlying	46.8	46.5	0.8
Consumer initiative start up costs	(2.0)	(1.0)	
Works closure costs	(1.1)	(3.0)	
Pension curtailment gain (net of expenses)	4.4	0.1	
Property	(0.3)	1.8	
Operating profit reported	47.8	44.4	7.5

Operating profit rose by 7.5 per cent to £47.8 million (2005 £44.4 million). EBITDA was £67.6 million (2005 £63.4 million), an improvement of 6.7 per cent.

The net effect of one-off items in the year was a net credit to operating profit of approximately £1.0 million (2005 £2.1 million net debit), giving an underlying operating profit of £46.8 million (2005 £46.5 million). The Group has expensed £2.0 million (2005 £1.0 million) of consumer initiative start up costs as the landscape installation strategy is a key element of future growth. Works closure costs in the year were approximately £1.1 million (2005 £3.0 million) as we reduced the fixed cost base of the business. During the year, following an extensive consultation process, the defined benefit section of the Pension Scheme was replaced with a defined contribution section. This reduces risk and the volatility of the accounting charge in the Consolidated Income Statement. As a consequence, there has been a one-off curtailment

gain, net of expenses, of £4.4 million (2005 £0.1 million gain). During the year there has been a small net loss on property transactions of £0.3 million (2005 £1.8 million profit).

After the net effect of the one-off items, detailed above, profit before tax increased by 9.7 per cent to £41.7 million (2005 £38.0 million).

Basic earnings per share from continuing operations increased by 9.6 per cent to 20.34 (2005 18.55) pence per share.

Underlying margin reconciliation

	Movement in Operating		
	Revenue £'m	profit £'m	Impact %
2005 underlying	359.3	46.5	12.9
Acquisitions	9.3	1.0	-
Cost increases recovered through			
sales prices	11.5	(0.4)	(0.5)
Organic	(2.0)	(0.3)	-
2006 underlying	378.1	46.8	12.4

Mistral Silver Grey, John Pond's Centre, Plymouth

Operating and Financial Review (continued)

The reported operating profit margin was 12.6 per cent, up 0.2 per cent compared with 2005. The underlying operating profit margin was 12.4 per cent. Acquisitions contributed additional sales of £9.3 million and operating profits of £1.0 million. The impact on operating margins has been negligible.

Cost increases were largely recovered through sales price increases, averaging between 3 and 4 per cent, with little effect on the absolute operating profit, although they did give rise to a dilution in the operating margin of 0.5 per cent. Cost increases incurred in the year were partly driven by higher energy costs either directly or indirectly as a component part of material or other input costs. Sales volumes overall were marginally lower than 2005 and production volumes and the levels of manufactured inventory were also lower. The production under recoveries that have consequently arisen, due to the level of operational gearing, have been recovered through productivity improvements and other cost reduction initiatives.

The Group acquired a number of businesses in 2006 (Urban Engineering, Tempakerb, Decathlon and Scenic Blue) and the combined expenditure on

these and other capital expenditure amounted to £28.1 million. This continued investment in capital and acquisitions, to drive future growth, increased depreciation and amortisation by £0.9 million.

Operating Performance

Analysis of revenue growth by market

Market	2006 £'m	2005 £ m	Change %
Domestic	182.3	177.8	2.5
Public Sector and Commercial	195.8	181.5	7.9
Total (including acquisitions)	378.1	359.3	5.2
Overall percentage			
Domestic	48.2%	49.5%	
Public Sector and Commercial	51.8%	50.5%	

Like for like sales in the Domestic market were similar to last year with prices up 3 per cent and volumes down by a similar amount. Product sales of installed projects, which represent 80 per cent of Domestic sales, were 2 per cent ahead, however, sales through DIY channels were down.

Public Sector and Commercial like for like revenue showed an increase of 5.0 per cent in the year with natural stone products showing double digit growth.

The acquisitions made in the last few years have been progressively integrated into the expanded market offer and this will continue in 2007.

Financial KPIs

The key financial KPIs were set out on page 8. These financial KPIs were established in January 2006. The current performance against these targets, since that date, can be set out as follows:

- Revenue growth

Against a target of 7 per cent per annum, the Group has achieved a CAGR of 5.2 per cent since 1 January 2006.

- Earnings per share growth

Against a target of RPI + 6 per cent per annum on a CAGR basis (which for the period since 1 January 2006 equates to 10.4 per cent), the Group has achieved a CAGR of 9.6 per cent.

- Return on capital employed (ROCE) is defined as EBITA / Shareholders' Funds plus Net Debt

ROCE for 2006 was 20.0 per cent, which is equal to the long-term target of 20.0 per cent.

An additional financial KPI relates to cash flow targets, and the Group's cash generation performance is described on page 18.

Segmental Reporting

During the year, the Directors undertook a review of the Group's continuing operations and its associated business risks, and for the year ended 31 December 2006 consider that the continuing operations should be reported as a single business segment. The Directors consider that the continuing operations represent one product offering with similar risks and rewards and should be managed and reported as a single business segment in line with the Group's internal reporting framework.

Operating and Financial Review (continued)

Net Financial Expenses

Net financial expenses were £6.1 million (2005 £6.4 million) which is made up of external interest on borrowings (including debenture interest) of £4.8 million (2005 £4.9 million) and IAS 19 notional interest of £1.3 million (2005 £1.5 million). The IAS 19 notional interest comprises interest on obligations under the defined benefit Pension Scheme net of the expected return on scheme assets. The reduction in the IAS 19 notional interest charge reflects the reduction in the recognised liability for defined benefit obligations due, in part, to special contributions made in the year of £10.0 million. During the year dividends totalling £0.1 million were paid to the B shareholders in respect of the period ended 31 December 2006 and in accordance with IFRS these have been disclosed within net financial expenses. Interest cover remained healthy at 7.9 times (2005 6.9 times).

Taxation

The tax charge for 2006 was £12.6 million (2005 £11.7 million) which represented an effective rate of 30.3 per cent (2005 30.7 per cent). A deferred taxation asset of £12.6 million (2005 £19.6 million) has been established in relation to the net liability for defined benefit obligations of £41.9 million (2005 £65.3 million).

Dividends

The Group's dividend policy continues to be that dividends should move in line with medium term earnings growth.

An interim dividend of 4.30 pence (2005 4.10 pence) per share was paid on 8 December 2006. A final dividend of 8.85 pence (2005 8.40 pence) per share is now being recommended for payment on 6 July 2007 to shareholders on the register at the close of business on 8 June 2007. The ex-dividend date will be 6 June 2007. This gives a total of 13.15 pence (2005 12.50 pence) per share for the year which represents an increase of 5.2 per cent over 2005.

On an IFRS basis, which does not account for the final dividend until it is approved at the forthcoming

Annual General Meeting, the dividend for the year ended 31 December 2006 is 12.70 pence (2005 12.10 pence) per share which represents an increase of 5.0 per cent. On an IFRS basis dividends are covered 1.6 times (2005 1.5 times).

Balance Sheet

Net assets at 31 December 2006 were £184.5 million (2005 £166.3 million) which represented 129.0 pence (2005 116.3 pence) per share.

An evaluation of Marshalls' portfolio of commercial properties and mineral assets is being undertaken by CB Richard Ellis and Wardell Armstrong LLP respectively. The property portfolio is being valued on an existing use basis for the commercial and mineral portfolio and on a market value basis for surplus assets. These bases are in accordance with the valuation methods recommended by the Royal Institute of Chartered Surveyors. The valuation of the property portfolio as at 31 December 2006 is approximately £40 million above the net book value of the equivalent assets.

The liability for defined benefit pension obligations decreased from £65.3 million at 31 December 2005 to £41.9 million at 31 December 2006. Following the move to defined contribution for future service, special cash contributions of £10.0 million were made to the Pension Scheme in the second half of the year and, as a consequence of a change to the actuarial assumptions, there has been a one-off curtailment gain, net of expenses, of £4.4 million. There was also an increase in the AA corporate bond rate from 4.8 per cent to 5.1 per cent, an increase in investment returns and a strengthening of the mortality rate which together resulted in an actuarial gain of £7.3 million (net of deferred taxation) and this has been recorded in the Consolidated Statement of Recognised Income and Expenses.

The liability of £41.9 million is made up of £209.1 million in respect of the present value of funded obligations net of £167.2 million for the fair value of scheme assets. The deficit has been determined by the scheme Actuary using prudent assumptions in line with current market levels.

Analysis of Net Debt

Analysis of net debt	2006	2005
	£'m	£'m
Bank	32.3	23.4
11.375% Debenture Stock	20.0	20.0
B shares	2.1	2.8
Finance lease liabilities	0.2	0.5
Net debt	54.6	46.7
Net assets	184.5	166.3
Gearing	29.6%	28.1%

The above table shows an analysis of net debt at 31 December 2006. Net debt has increased from £46.7 million to £54.6 million during the year largely due to the cash outflow of £10.0 million in special cash contributions to the Pension Scheme in the second half of the year. Gearing at the year end of 29.6 per cent is similar to the previous year.

New bank facilities were agreed with the Group's principal bankers in September 2006 comprising a mixture of committed term loans and uncommitted short term facilities. Total bank borrowing facilities at 31 December 2006 amounted to £100 million (2005 £130 million) of which £67.7 million (2005 £106.6 million) remained unutilised. The Group's peak

Marshallite Rustic Walling and Heritage Coping, Yorkstone

seasonal working capital requirements run from 1 February until 31 July and an additional working capital facility of £15.0 million is available between these dates. Of the total bank facilities of £100 million, £30 million are in respect of committed three and five year loan facilities, £30 million are uncommitted facilities, with an option to convert into committed three and five year facilities, and the remaining £40 million is uncommitted and repayable on demand. The bank facilities are unsecured other than for inter-company cross guarantees between the Group's subsidiary undertakings.

The 11.375 per cent £20 million debenture stock is secured by a first floating charge on the assets of Marshall's Group plc and certain subsidiary undertakings and is repayable at par on 30 June 2014 or, at the Company's option, before then at a price related to the gross redemption yield of a specific category of Government Treasury Stock.

Operating and Financial Review (continued)

During the year 1,610,393 B shares were redeemed at 45 pence per share at a cost of £725,000. As a consequence of these redemptions an amount of £725,000 has been transferred to the capital redemption reserve from retained earnings. Holders of B shares have been able to make elections to have their B shares redeemed at 45 pence per share semi-annually on 30 June and 31 December since December 2004. The remaining B shares outstanding at 30 June 2007 will be redeemed.

Cash generation

The Group is cash generative. In the year ended 31 December 2006 the cash inflow from continuing operations, and before special pension contributions, was £64.0 million (2005: 59.1 million). This cash generation has been utilised as follows:

Analysis of cash utilisation	2006	2005
	£'m	£'m
Cash inflow from continuing operations	64.0	59.1
Interest and taxation	(15.2)	(16.2)
Operational cash generation (before special pension contributions)	48.8	42.9
Capital expenditure	(24.0)	(20.7)
Acquisitions	(4.1)	(8.7)
Sale of Clay business	-	65.0
Special pension contributions	(10.0)	-
Other financial items	0.4	1.4
Cash returned to shareholders	(19.0)	(18.3)
Movement in net debt	(7.9)	61.6
Cash returned to shareholders as a percentage of operational cash generation	39.3%	42.7%

Operational cash generation for the year ended 31 December 2006, before special cash contributions to the Pension Scheme, was £48.8 million, an increase of 14.0 per cent. This reflects interest and corporation tax payments in the year of £15.2 million (2005: £16.3 million) and includes a net cash outflow from working capital of £1.0 million (2005: £4.0 million outflow). This improvement in working capital has been achieved despite the impact of cost increases in inventory, with inventory being a significant contributor to the improvement. The reduction in inventory volumes and mix of inventory held was in line with budget.

Total expenditure in capital expenditure and acquisitions in the year was £28.1 million, with acquisitions comprising £4.1 million directly and £4 million by way of capital investment. Of the remaining £20 million of capital investment

approximately half was in the nature of replacement of existing assets and around £10 million was invested in business improvements and developments including robotics, new process technology and our direct to consumer initiatives.

Ordinary dividend payments in the year were £18.2 million (2005: £17.2 million). Over the past three years, in total, an amount of £128.7 million has been returned to shareholders. This includes £75.0 million by way of the Return of Value, to improve the Group's capital structure and balance sheet efficiency in 2004, and £53.7 million by way of regular dividend payments. The utilisation of cash over this three year period is best illustrated by the following summary:

Analysis of cash utilisation, 2004-2006

	£'m	
Operational cash generation	134.3	
Capital expenditure	(71.2)	
Acquisitions	(28.5)	
Sale of Clay business	65.0	
Cash returned to shareholders	(128.7)	
Special pension contributions	(10.0)	
Other financial items	(2.3)	
Movement in net debt	(41.4)	
	2003	2006
	£'m	£'m
Net debt	(13.2)	(54.6)
Capital employed	195.7	184.5
Gearing	6.8%	29.6%

The above summary provides a medium term three year analysis of the cash generation capacity of the Group and how cash generated has been invested to grow the business and also to show the cash returned to shareholders. Cash generated from operating activities was £134.3 million. The Group has invested £71.2 million back into the business to provide industry leading manufacturing and distribution facilities, new product manufacturing capability and to improve productivity. The medium term plan is to allocate £20 million for organic investment each year of which half will relate to the replacement of existing assets and half will be improvement and development expenditure.

The Group has also invested £28.5 million in acquisitions as part of the strategy of capitalising on Marshall's brand and unique access to nationwide distribution channels. The medium term plan is to

increase the flow of suitable acquisition candidates and to increase this allocation of capital to approximately £20 million per year directed towards bolt-on acquisitions. This will leave the Group with sufficient flexibility to make larger acquisitions if such opportunities should arise. This greater emphasis on investing in growth opportunities will deliver further shareholder value in the future. The Group's strategic plans, balance sheet, capital and funding arrangements are carefully structured to enable this to be achieved.

As explained earlier, the Group's cash generation performance against detailed cash flow targets is one of the main KPIs and in 2006 the targets that were set by the Board were achieved. At the time of the Return of Value of £75 million to shareholders in 2004 the Directors recognised that a year end gearing percentage of around 60 per cent represented an efficient balance sheet structure. The Board's objective in the medium term is to achieve and maintain an efficient balance sheet. Due to the Group's balance sheet strength and cash generating capacity gearing levels could comfortably be increased above the year end level of 29.6 per cent.

Financing and Risk Management

The Group's Risk Committee determines the policies and procedures that are put in place to mitigate exposure to risk. A formal rolling process exists to identify, assess and analyse risks and those of a more material nature are included in the Group Risk Register. The Group seeks to mitigate exposure to all forms of strategic and financial risk both external and internal. External risks include political and economic conditions, the effect of legislation or other regulatory actions, the actions of competitors, foreign exchange, raw material prices and pension funding. Internal risks include investment in new products, new business strategies and acquisitions.

Strategic Risks

Like all businesses in the UK the Group is susceptible to any economic downturn which could affect customer spending. Protracted weakness in the UK economy, together with a series of interest rate rises, could depress consumer spending and private sector construction activity. In addition, slow delivery of planned Government investment could depress

Operating and Financial Review (continued)

construction activity in the Public Sector and Commercial market. Long periods of adverse weather conditions could also have a short term impact on construction activity. Our aim is to ensure an excellent understanding of market conditions by constant communication with customers, installers and domestic consumers, together with significant investment in market research and active membership of the CPA.

Failure to compete with competitors on areas including price, product range, quality and service could have an adverse effect on the Group's financial results. All these areas are monitored on a constant basis and the Customer Service Index remains one of the Board's key strategic KPIs. The Group continues to invest in strategies that enhance the Marshalls brand. Any significant increases in oil and general utility prices could adversely affect the Group's performance. Diversity of operations reduces the risk on any single item on supplies and purchasing policies seek to take into account and mitigate such risks, where possible.

The defined benefit section of the Pension Scheme was closed to future service accrual on 1 July 2006 and the introduction of a new defined contribution

section to the Pension Scheme has allowed the Group to manage risk better and reduce volatility in the future. Nevertheless the Group continues to be subject to various financial risks in relation to the Pension Scheme, principally the volatility of the discount (AA corporate bond) rate, any downturn in the performance of equities and increases in the longevity of members.

Marshalls continues to make strategic business acquisitions that might have an impact on the performance and risk profile of the Group. These risks are mitigated by extensive due diligence and where practicable, by representations and indemnities from the vendors.

Financial Risks

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk and foreign currency risk. The Board reviews and agrees policies for managing each of these risks and these are summarised on Note 17 on pages 72 to 75 of the Financial Statements. These policies have remained unchanged since 2005. It is the Group's policy, and has been throughout the period under review, that no speculative trading in financial instruments shall be undertaken.

The Group manages its medium term bank debt to ensure continuity of funding and the policy is to arrange funding ahead of requirements and to maintain sufficient undrawn committed bank facilities.

The Group enters into forward foreign currency contract derivative transactions of relatively small value. The purpose of such transactions is to manage the currency risks arising from the Group's operations. An interest rate hedge has been entered into to manage the effect of the increased exposure to interest rate increases. The Group manages its insurance risk by continuous review and by maintaining a balance between capped self insurance and third party cover against major catastrophes.

Island Wharf, Hull

Group Outlook

Market intelligence shows that Public Sector and Commercial demand, which represents half of the Group's revenue, remains robust. The CPA forecasts that the Public Sector and Commercial market will grow by 4.9 per cent in 2007 and a further 5.1 per cent in 2008. From 2008 onwards, it is anticipated that building for the 2012 Olympics will start to deliver a benefit.

The Domestic market is more difficult to predict. The CPA is forecasting growth of 1.0 per cent in private housing repair, maintenance and improvement expenditure for 2007 and flat in 2008. Domestic installers' average order books from the latest survey at the end of February 2007 were an encouraging 9.1 weeks (2006: 8.4 weeks).

In 2007 the Group will continue the roll out phase of the consumer initiatives. The Royal Horticultural Society's Chelsea Flower Show sponsorship together with the national launch of the Marshalls design and installation service will further increase brand awareness and profile. A range of initiatives have also been developed to grow our Public Sector and Commercial business and the Group's management and workforce are committed to continue this growth strategy and deliver increased shareholder value.

Although the poor weather conditions in January and early February meant a flat start to 2007, the underlying indicators, including the installer order books and the Barbour ABI Building data, are encouraging and the outlook for the year is positive.

Directors Biographical Notes

Mike Davies (59) †* **Non-Executive Chairman**

Joined the Board in October 2004. He is currently the Senior Independent Non-Executive Director at Taylor Woodrow plc and a Non-Executive Director of Pendragon plc.

Graham Holden (47) **Chief Executive**

Joined the Company in 1986 and was appointed to the Board in 1992. He is a Chartered Accountant and was previously Finance Director and Chief Executive of the Landscape Products Division. He was appointed to his current position on 1 January 2004.

Ian Burrell (49) **Finance Director**

Joined the Company and the Board in June 2001. He is a Chartered Accountant and was previously Group Finance Director at Cornwell Parker plc.

David Sarti (41) **Chief Operating Officer**

Joined the Group in March 2001 and is currently Managing Director of Marshalls Landscape Products. He was appointed to the Board in November 2004.

Advisers

Stockbrokers

HSBC Investment Bank Plc
Bridgewell Group plc

Auditors

KPMG Audit Plc

Legal Advisers

Herbert Smith LLP
Eversheds LLP

Financial Advisers

N M Rothschild & Sons Limited

Bankers

Royal Bank of Scotland plc
Lloyds TSB Bank plc

Richard Scholes (61) **† **Senior Independent Non-Executive Director and Chairman of the Audit Committee**

He was appointed to the Board in July 2003. He is a Non-Executive Director and Chairman of the Audit Committees of Bodycote International plc, Chaucer Holdings PLC and Crest Nicholson PLC. He is also a Non-Executive Director of Keller Group PLC and is a Chartered Accountant.

Andrew Allner (53) **† **Independent Non-Executive Director and Chairman of the Remuneration Committee**

He was appointed to the Board in July 2003. He was the Group Finance Director of RHM plc and was previously Chief Executive Officer of Enodis Plc. He is a Chartered Accountant and a former partner of Price Waterhouse.

Bill Hesselby (67) **† **Independent Non-Executive Director**

He was appointed to the Board in March 2005. He is Chairman of Cogent Elliot Group, the independent advertising agency, and is a Board member of Welsh National Opera.

* Member of the Audit Committee

† Member of the Remuneration Committee

• Member of the Nomination Committee

Elizabeth Blease **Group Company Secretary**

Registrars

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PO Box 82, The Pavilions
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Shareholders' enquiries should be addressed to the Registrars at the above address (Tel 0870 702 0000)

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Registered in England and Wales No 5100353

Corporate Social Responsibility

Marshalls believe in conducting its business in a manner which achieves sustainable growth whilst incorporating and demonstrating a high degree of social responsibility. Marshalls regard Corporate Social Responsibility (CSR) as a journey, in the course of which it aims to align increasingly its business values, purpose and strategy with the social and economic needs of its stakeholders, whilst embedding responsible and ethical business policies and practices in everything it does.

The Board takes regular account of social, environmental and ethical matters in the business of the Group and believes in being responsible in the way that it conducts its operations. David Sarti is responsible for managing the key elements of the CSR policy together with a full time CSR manager.

Marshalls is pleased to be a constituent member of the FTSE4Good UK Index. During the year, the Group published its first Corporate Social Responsibility Report which was posted to shareholders in September 2006. Copies are available on the Company's web site at www.marshalls.co.uk.

The Market Place

The Group recognises the importance of building and maintaining positive relationships with its customers, suppliers and contractors.

There is a commitment to a process of continual improvement in meeting customers' requirements and expectations. This is highlighted in the established customer service improvement programme. This programme has, since its inception in 2003, resulted in significant and sustained improvement in customer order delivery, on time, in full and with increasingly error free product and administration.

The Group Purchasing Policy sets out the standards and ethics by which business is conducted. It ensures that there is no bias or conflict of interest and all suppliers will be treated fairly and without prejudice. The Group negotiates terms and conditions, including payment terms, with all its principal suppliers. Save in the case of a dispute, payments are made in accordance with such negotiated arrangements.

The Group values and derives considerable competitive advantage from active co-operation with its established suppliers in terms of innovation and product development.

Social and Ethical Responsibilities

The Group takes its Social and Ethical responsibilities very seriously and is the only member of the Ethical Trading Initiative (the ETI) in its sector.

As a member of the ETI it is committed to adopting the ETI Base Code on a progressive basis throughout its supply chains with specific focus on China and India. The Code is based on International Labour Organization conventions and as such is widely acknowledged as a model code of labour practice. It contains provisions based on the following principles: no-one should be forced to work, workers should be able to join and form trade unions, working conditions should be safe and healthy, child labour should not be used, working hours should not be excessive, wages should be enough to live on and provide some discretionary income, workers should be treated equally regardless of their sex, ethnic group, religion or political opinions, where possible, workers should be provided with regular employment, and workers should not be physically abused or disciplined.

As well as adopting the ETI Base Code, the Group has also committed to monitoring and independent verification of its supply chains, awareness-raising and training, driving year on-year improvements, assessing the impact of its core business activities on labour standards, reporting annually to the ETI on progress and participating in ETI projects.

Children from Churchfield Primary School, Cannock Works

Corporate Social Responsibility (continued)

In May 2006 an independent audit of the Group's sole supplier of Indian Natural Sandstone showed compliance to the ETI Base Code

The Environment

Marshalls is committed to assessing and managing the environmental impacts of all its operations. The Environmental Report is on pages 26 to 29

The Community

The Group is actively involved in programmes to promote good community relations and encourages each business to form and support mutually supportive relationships with their immediate communities which will add value to the local community

During the year, the Group made charitable donations of £25,657 (2005 £24,115). It is the Group's policy not to make political donations and no political donations were made in the year (2005 £Nil)

Alongside cash donations, the Group supports local community engagement by allowing employees to participate in local projects which add value to the local environment. The Group continues its policy to donate products to community groups and local charities to help transform the local environment for the people living in close proximity to its sites. Details of some of the community projects are included in the full Corporate Social Responsibility Report

Marshalls continues to be an active member of Business in the Community and has recently joined a Cares programme to progress further its connections with local communities, schools and other like minded responsible businesses. During 2006 Marshalls contributed to many locally organised initiatives including educational school visits, college tours, work experience schemes and many other local initiatives close to our operations

Employees

The Group's Statement of Values and Principles sets out the high standards to which all Marshalls' employees are encouraged and expected to adhere. The statement includes guidance on business practice, employee relations and equality of opportunity and is subject to regular review to

ensure that it continues to set stretching standards in terms of excellence, leadership, ownership, trust, honesty and integrity. There is also a published process through which employees can raise, in confidence, serious concerns about possible improprieties.

Marshalls believes that people are the key to the success of the business and recognises the importance of diversity in terms of the community, its employees and its customers. The Board is committed to promoting and maintaining a working environment where people are treated with respect and where individual talent is recognised and valued. The Group is committed to providing training designed to raise levels of awareness and sensitivity to matters of equality and dignity at work.

The Group's aim is to achieve this through the adoption of fair and merit-based employment policies and through adherence to relevant legislation as the minimum acceptable standard. Individuals with recognised disabilities are provided with equality of opportunity during their employment and wherever reasonably practicable, appropriate adjustments are made to ensure that they do not suffer disadvantage in the workplace.

Managers are charged with ensuring that employees for whom they have responsibility are properly inducted at business level and provided with the necessary support both to fulfil their roles effectively and to help them develop to their full potential. In this way, employees are encouraged to engage fully with the businesses in which they work and to identify closely with the Group's strategic aims and objectives.

Investment in personal development continues with initiatives in place designed to identify and nurture potential, ensure consistent management practices are applied and provide opportunities for succession into more senior roles. These comprise participation in regular internal coaching and mentoring programmes, undertaking internal development projects and assignments and active links with leading business schools, together with on-line access to the most up to date management thinking on leading business and development issues. The Group continues to encourage and support the development of its employees through programmes of NVQ accreditation and attainment of Investor in People status across many sites, to date in excess of 350 employees have attained NVQ accreditation with a similar number actively working towards them.

An increasing emphasis is being placed on internal communication to employees through the use of e-mail, intranet, newsletters, briefings and both formal and informal presentations.

Further development of information and consultation processes has continued during 2006, maintaining the improvement in communications through the increased involvement of, and engagement with, recognised trades unions and their elected employee representatives.

Employees are actively encouraged to donate funds to charity through payroll which accounted for approximately £23,000 in 2006 (2005 £23,000).

Health and Safety

Health and safety remains one of Marshalls' highest priorities and is considered fundamental to the success of the business. The Group is committed to a policy of continuous improvement of both its health and safety management system and its annual

health and safety performance. To complement the extensive management health and safety training programme, 2006 saw the introduction of one day refresher courses to ensure that the management population keep abreast of current legislation.

The Safety, Health and Incident Prevention Teams, which consist of employees and managers, continues to be the cornerstone of the safety management systems at site level and make a significant contribution to the improving annual safety performance. Manual handling continues to be the major health and safety risk and the Group's policy of eliminating manual handling activities wherever practicable remains unchanged.

Marshalls continues the implementation of BSI-accredited Integrated Management Systems throughout the Group. These systems incorporate accreditation to OHSAS (Occupational Health and Safety Management Systems Specification) 18001 and at the end of 2006 a total of 25 sites had secured the OHSAS 18001 accreditation, which represents 55.9 per cent of all employees. Accreditation of all the remaining locations is scheduled for 2007 and 2008.

In the course of 2006 the Group extended its Behavioural Safety Programme to 12 locations. This programme aims to identify and resolve unsafe acts in a positive non-judgemental manner. The programme will be progressively rolled out across the Group during 2007 and 2008.

The Group's accident performance is monitored by the Board on a monthly basis. The overall rate of workplace accidents within the Group continues to fall. The number of injury accidents reportable to the HSE under the Reporting of Injuries, Diseases and Dangerous Occurrence Regulations (RIDDOR) was 21.4 per 1,000 employees in 2006, compared with 24.6 per 1,000 employees in 2005, a reduction of 13 per cent. The target is to reduce this figure by a further 10 per cent in 2007.

Accidents and incidents		
(rate per 1,000 employees)	2006	2005
Major injury	2.9	2.7
Injury resulting in over 3 absence days from work	18.5	21.9
All RIDDORS	21.4	24.6
Average UK headcount	2,746	2,884

Environmental Report

Board Responsibility

David Sarti is the Director responsible for the Environmental Performance of the Group

Environmental Policy

The Group's Environmental Policy, which was reviewed in January 2007, states

"Marshalls is committed to achieving the highest standards of environmental performance, preventing pollution and minimising the impact of its operations. The Group's aim is that no lasting environmental damage occurs as a result of its activities and policies are being implemented to ensure that all its operations meet or exceed the requirements of legislation and applicable best practice

Marshalls regards compliance with relevant environmental laws and the adoption of responsible standards, where no legislation exists, as an integral part of its business strategy and is committed to considering the environmental impacts associated with its products throughout their life cycle

Marshalls has committed to monitor its environmental performance in line with the Construction Product Association requirements. Environmental aspects are identified at each site and corresponding objectives and targets set to reduce the significance of impacts in those areas. These will be reviewed on at least an annual basis to ensure continual improvement.

Marshalls accepts that its operations contribute to man made Climate Change as detailed by the Inter-governmental Panel on Climate Change. It also accepts that Climate Change will have an effect on its business operations and is working to minimise these effects.

Marshalls will continue to raise environmental awareness within the Group through the development and training of its employees and will communicate openly and consult with customers, suppliers and other stakeholders on relevant environmental matters

Marshalls strives to conserve natural habitats and create additional areas of wildlife value wherever possible. Work towards achieving Group registration to the Wildlife's Trust Biodiversity Benchmark is progressing, advancing with learning gained from the pilot site. The Group also recognises the need for sympathetic restoration and after use of quarry sites and considers the character of the local environment and the concerns of the community when planning such matters"

Environmental Management

During the year the Group continued the roll out of Integrated Management Systems ("IMS") at each of its manufacturing sites. The IMS combine ISO 9000 2000 for Quality Management, OHSAS 18001 for Health and Safety Management and ISO 14001 for Environmental Management.

In 2006 the Group asked BSI to Benchmark one of its precast concrete manufacturing units to BSI PAS 99. The site was awarded a "Gold" rating.

At the end of 2006 the Group had 38 manufacturing sites. Of these sites

25 had ISO 9000 2000 Quality Management Systems in place, representing 84.1 per cent of the Group's manufacturing output,

25 had Health and Safety Management Systems to OHSAS 18001 in place, representing 84.1 per cent of the Group's manufacturing output, and

19 had ISO 14001 for Environmental Management, representing 79.9 per cent of the Group's manufacturing output.

IMS therefore covers 79.9 per cent of the Group's manufacturing output. All the Group's accreditations are accredited through BSI.

A plan is in place to continue this roll out programme with the aim of completing the accreditation of the majority of the sites by the end of 2008. The roll out programme has been extended to include the businesses which were acquired during 2006. None of the new sites acquired held any robust Management Systems for the three disciplines.

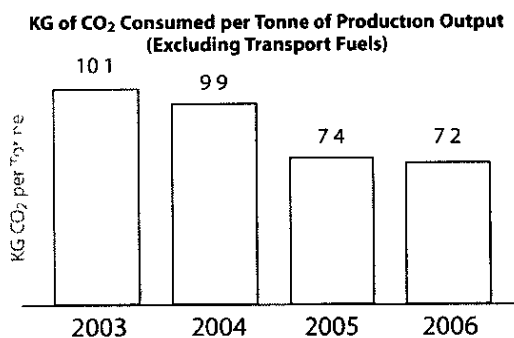
Environmental Impact

The Group continues to review the significant environmental impacts of its operations and utilises the CPA KPIs to measure the impacts year on year. The CPA KPIs are all based on a consistent "per tonne of production output" measure. Each KPI has been presented graphically showing four years of comparative data. The KPIs are as follows:

Energy

The KPI for energy consumption is "amount of energy consumed (kg CO₂) at manufacturer's sites per tonne of production output".

The bar chart below illustrates the Group performance for 2003 – 2006.



As part of the continuous improvement requirements of BS EN ISO 14001 targets are being set for the reduction of energy in the manufacturing process. Due to the requirements of different processes, each precast concrete manufacturing site has been given an individual target.

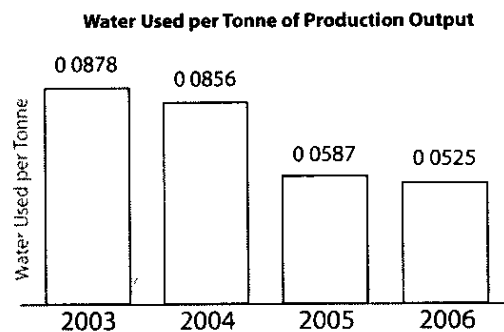
Marshalls is also setting a target for the reduction of Greenhouse Gases (GHG) emissions where the target unit will change from Kg CO₂ per tonne produced to Tonnes CO₂e. This reflects the increasing awareness within the business and wider community for the need for absolute emissions reductions. Marshalls target for 2007 is to reduce absolute emissions including transport by 2000 tonnes CO₂e (3.4 per cent reduction on 2006). Emissions will be calculated based on the GHG protocol, scope 1 and 2, on a continuing operations basis.

During 2006 the Group submitted data to the "Carbon Disclosure Project" which listed the Groups 2005 total CO₂ emissions as 62,966 tonnes from all operations, including transport.

Water Use

Significant progress continues to be made in the recycling and harvesting of water with a consequential reduction in the purchase of treated water. One of the Precast concrete production units is now, given average climatic conditions, self sufficient in production process water.

The CPA KPI for water usage is "volume of water used on site (including office use) from controlled waters (i.e. mains and extracted water) per tonne of production output".

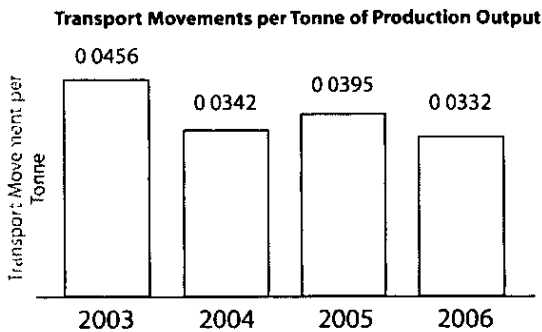


The Group monitors discharge water on a monthly basis at all sites producing precast concrete. Third party testing took place during the year and no concerns were raised by the relevant authorities.

Transport

The Group monitors deliveries made on its own vehicles and those made on vehicles of sub-contractors employed by the Group. Collections by Builders Merchants from the Group Service Centres using their own vehicles are not included in the Group figures. The CPA KPI is "number of transport movements (leaving site) made by a company or its contractor via road, rail, water or other method per tonne of production output".

Environmental Report (continued)



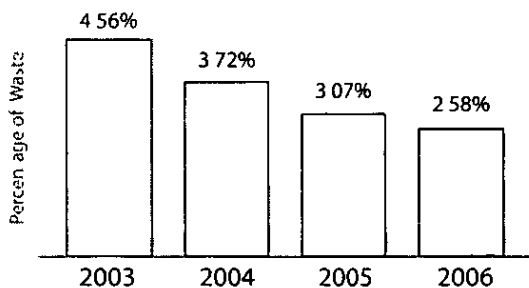
The overall transport efficiency remains high. Driver training has been extended by the appointment of a full time trainer. Initial training is concentrating on maximising fuel efficiency. During 2006 the Group transport operations were runners up in two Awards for sustainable operations.

Waste Reduction

A single waste contractor has been appointed to manage all waste activities with the aim of obtaining the maximum benefit for the recycling of waste streams from the Group. The partnership approach is leading to much better control of waste, overall reduction in waste quantities and a clear segregation of waste streams which cannot be recycled to ensure the correct disposal routes.

The CPA KPI for waste reduction is "amount of waste leaving site (tonnes) as a percentage of total production output".

Percentage of Waste Including Material for Recycling leaving Site as a Percentage of Total Production Output



The Group works hard to remove waste from its operations wherever possible. The CPA KPI does not differentiate between waste leaving site for landfill

and waste leaving site for recycling by third parties. Analysis shows that out of the total Group waste stream, recycling on site and recycling off site recovered 75.9 per cent of the Group's waste for other uses, with only 24.1 per cent going to landfill. This is a reduction in the percentage of recycling (2005 81.4 per cent) as the overall waste stream has reduced, limiting the potential for recycling.

Waste materials from other industries are being used where appropriate as aggregate replacement with some innovative products resulting from the incorporation of such materials. China clay waste, steel slag waste, slate waste and slag cements are typical of the products being utilised.

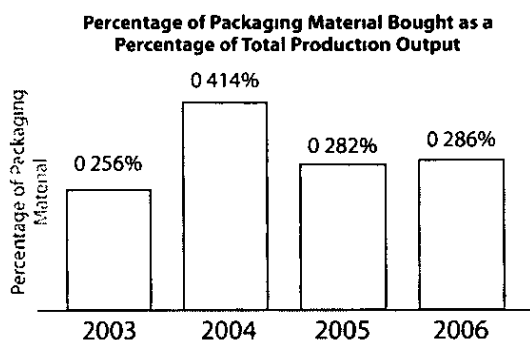
Packaging

The Group continues to explore every opportunity to reduce the amount of packaging used to ensure safe transport and handling of its products but also to ensure minimum damage and wastage of product between manufacturing site and point of use.

Suppliers of packaging products are monitored to ensure that either the supplies are obtained from sustainable sources, in the case of pallet timber, or wherever possible from recycled materials such as strapping.

The CPA KPI for packaging is "amount of packaging bought in (tonnes) to be used for the containment, protection, handling, delivery and presentation of goods as a percentage of production output".

There has been a very small increase in packaging requirements as end users of the Groups' products are demanding higher packaging standards. This is to provide firstly safe containment of the product during transportation and secondly good protection for the products during distribution and site storage.



Suppliers and Contractors

Suppliers and contractors are monitored closely and, in particular, on the environmental aspects of their operations. During the year, there has been ongoing liaison with key suppliers to ensure that their own operations cause minimal harm to the environment and to share best practice to ensure the Group benefits from the environmental experience of its suppliers. The Group is aiming to have all its key suppliers with ISO 14001 accreditation by the end of 2007.

Environmental Impact of Products

The Group maintains its policy of producing products intended for long life with low maintenance. These products produce a very low risk of pollution and in the majority of cases can be easily recycled at the end of their useful service, either as a primary product in the case of most block paving or, after crushing, as a secondary aggregate or other form of recycled material.

Sustainability

Marshalls continues to support the work being carried out by The British Precast Concrete Federation Sustainability Committee. During 2005 the Group published its own Sustainability Document. It is developing a Sustainability Policy based upon its IMS systems which provides a basis for decision making. Economic activity is considered, reinforced by the targets and objectives in the ISO 9000 accreditation. Environmental activities are considered by the targets and objectives in ISO 14001 and in addition social activities are supported by the OHSAS Health and Safety accreditation.

Land Management

During 2006 all of the Groups' major construction projects were contained within existing sites or were on brown field sites.

Environmental Awareness and Training

The Group continues to develop environmental awareness among its employees.

Wildlife Trust

During 2005 the Wildlife Trust helped in the establishment of a Biodiversity Benchmarking Project at the site in Maltby. This has proved successful, particularly, in raising staff awareness of the wide ranging biodiversity at the site. The Project has also drawn members of the local community into the site. The auditing of the operations of the site and its management of Biodiversity was completed at the end of 2006 and the Award of the Benchmark was confirmed in February 2007. Maltby is the first manufacturing site to be awarded the Benchmark. The site's efforts were recognised by the N Power Environmental Award in 2006.

Maltby Biodiversity Project

Directors' Report

The Directors have pleasure in submitting their Report and Financial Statements for the year ended 31 December 2006. The Consolidated Group Financial Statements have been prepared under International Financial Reporting Standards ("IFRSs"). The Parent Company Financial Statements have been prepared in accordance with UK Accounting Standards.

Principal Activities and Business Review

The principal activities of the Group are the manufacture and supply of landscape, driveway and garden products from a range of materials, including concrete, natural stone, iron, steel, wood, glass and polyurethane. Further details of the principal activities of the Group are set out in Note 33 on page 92.

The Chairman's Statement on pages 4 and 5 and the Operating and Financial Review on pages 7 to 21 contain a review of these activities.

Details of the Group's policy in relation to employees and information on charitable and political donations are disclosed on page 24.

Details of the Group's policies in relation to Corporate Governance are disclosed on pages 33 to 38.

Group Results

The Consolidated Income Statement for the year ended 31 December 2006 is shown on page 52.

Dividends

The Board is recommending a final dividend of 8.85 pence (2005 8.40 pence) per share which, together with the interim dividend of 4.30 pence (2005 4.10 pence) per share, make a combined dividend of 13.15 pence (2005 12.50 pence) per share. Payment of the final dividend, if approved at the Annual General Meeting, will be made on 6 July 2007 to shareholders registered at the close of business on 8 June 2007.

The dividend paid in the year to 31 December 2006 and disclosed in the Consolidated Income

Statement is 12.70 pence (2005 12.10 pence) per share being the previous year's final dividend of 8.40 pence (2005 8.00 pence) per share and the interim dividend of 4.30 pence (2005 4.10 pence) per share in respect of the year ended 31 December 2006 and paid on 6 December 2006. This follows the disclosure under IFRS.

Share Capital

Details of the share capital and allotments during the year are set out in Note 20 on pages 81 to 82. Details of outstanding awards under the Marshalls plc Long Term Incentive Plan are set out in Note 18 on pages 78 and 79.

Directors

Details of each of the Directors who served throughout the year, together with biographical details, are set out on page 22.

Graham Holden and Andrew Allner will retire by rotation at the Annual General Meeting. Both of these Directors, being eligible, offer themselves for re-election in accordance with the Company's Articles of Association.

Details of Directors' attendance at Board and Committee meetings and a statement on Board Evaluation is set out in the Corporate Governance Report on pages 33 to 38.

Directors' Interests

Full details of Directors' remuneration, interests in the share capital of the Company and of their share based payment awards are set out on pages 40 to 49 in the Directors' Remuneration Report.

Charitable and Political Donations

Details of the charitable donations made during the year are set out in the Corporate Social Responsibility Statement on pages 23 to 25.

Disposals and Acquisitions

On 4 May 2006, the Group acquired the assets of Urban Engineering which specialises in the sale of a range of shelters and associated products. Following the half year end the

Group also purchased the assets of Tempakerb, a business which manufactures temporary kerbs from recycled materials and Decathlon, which manufactures high capacity drainage systems

On 30 November 2006, the Group acquired the entire share capital of Scenic Blue (UK) Limited, a garden design and landscape installation franchising company

Since the year end the Group has acquired a small natural stone business and a supplier of high quality and widely specified seating systems.

Fixed Assets

The Group continues to invest in the business with net capital investments in the year of £24.0 million (2005 £20.7 million)

In the opinion of the Directors, the current existing use value in respect of commercial properties and mineral assets, combined with the current market value in respect of surplus assets, of the Group's interests in land and buildings exceeds the book value by approximately £40 million

Payment to Suppliers

The Group follows the CBI's prompt payment code and operates and abides by a clearly defined payment policy which has been agreed with all major suppliers. The Group's creditor payment period at 31 December 2006 was 51 days (2005 52 days)

Substantial Shareholdings

As at 9 March 2007, the Company had been notified of the following disclosable interests of 3 per cent or more in its voting rights

	%
Prudential plc	11.06
AXA S.A.	7.46
New Star Asset Management Limited	4.82
Liontrust Investment Services Limited	4.06
Credit Suisse Asset Management	3.36
Legal and General Investment Management Limited	3.36
Artemis Investment Management Limited	3.23

Statement of Directors' Responsibilities in respect of the Annual Report and the Financial Statements

The Directors are responsible for preparing the Annual Report and the Group and Parent Company Financial Statements in accordance with applicable law and regulations

Company law requires the Directors to prepare Group and Parent Company Financial Statements for each financial year. Under that law they are required to prepare the Group Financial Statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the Parent Company Financial Statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice)

The Group Financial Statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and the performance of the Group, the Companies Act 1985 provides in relation to such Financial Statements that references in the relevant part of that Act to Financial Statements giving a true and fair view are references to their achieving a fair presentation

The Parent Company Financial Statements are required by law to give a true and fair view of the state of affairs of the Parent Company

In preparing each of the Group and Parent Company Financial Statements, the Directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state for the Group Financial Statements, whether they have been prepared in accordance with IFRSs as adopted by the EU,

Directors' Report (continued)

- state for the Parent Company Financial Statements, whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Parent Company Financial Statements, and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its Financial Statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of Financial Statements may differ from legislation in other jurisdictions.

Disclosure of Information to Auditors

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's Auditors are unaware, and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the Company's Auditors are aware of that information.

Annual General Meeting

The Notice convening the Annual General Meeting to be held at Birkby Grange at 12 noon on Wednesday 16 May 2007, together with explanatory notes on the resolutions to be proposed, is contained in a circular to be sent to shareholders with this Annual Report.

Auditors

A resolution to re-appoint KPMG Audit Plc as Auditors to the Company and to authorise the Directors to determine their remuneration will be proposed at the Annual General Meeting.



By Order of the Board
Elizabeth Blease
Company Secretary
9 March 2007

Corporate Governance

Marshall's is committed to business integrity, high ethical values and professionalism in all its activities. As an essential part of this commitment, the Group supports the highest standards in corporate governance. It is committed to the principles of the Combined Code on Corporate Governance appended to the Listing Rules of the Financial Services Authority (the Code) and for which the Board is accountable to shareholders.

Statement of Compliance with the Code

Throughout the year ended 31 December 2006, the Company has complied with the Code in all material respects, with the following minor exception:

- For the whole year, the Board had not approved written Terms of Reference of the division of responsibilities between the Chairman and Chief Executive. During the year these were set out in writing and approved by the Board.

The paragraphs below, together with the Directors' Remuneration Report set out on pages 40 to 49 and the Report of the Audit Committee set out on page 39 describe how these principles are applied within the Company.

Directors

The Board, balance and independence

The Board is scheduled to meet nine times each year with additional meetings called if required.

There is a Schedule of Matters Reserved to the Board which was reviewed during the year. Medium and long-term strategy is frequently discussed and meetings are held with the Executive team, on a regular basis, to update the Board on business and strategic issues. In addition the Board is responsible for risk management and for the development of Group policies including areas such as health and safety, social, environmental and ethical issues.

The Board has formally delegated specific responsibilities to Board Committees, including

the Audit, Remuneration and Nomination Committees. The Board will also appoint Committees to approve specific processes as deemed necessary. For example, during the year, Board Committees were established to approve bank documentation, changes to the pension scheme, dividend payments and preliminary and interim announcements.

The Group's structure operates in such a way to ensure that all decisions are made by the most appropriate people in a timely manner that will not unnecessarily delay progress. The Directors and management teams of each Group business are responsible for those business entities. They are tasked with the delivery of targets approved by the Board and for the implementation of Group Strategy and Policy across their businesses.

The Board, at its meetings, reviews the financial results of the Group. A detailed business plan and annual budget is prepared for each operation in conjunction with local management. These are then compared in detail with the monthly management accounts. Executive Directors are required to comment on areas where performance departs from current expectations. Any significant variances are discussed at Board level and appropriate action taken.

These policies and procedures collectively enable the Board to make informed decisions on a range of key issues including those relating to strategy and risk management.

The Board comprises a Non-Executive Chairman, three Executive Directors and three independent Non-Executive Directors who are equally responsible for the proper stewardship and leadership of the Company. Taking into account the provisions of the Code, the Board has determined that each of the Non-Executive Directors is independent and free from any relationships which could compromise their independent judgement. The Board considers it is of sufficient size for the discharge of its duties and that the balance of skills and experience is appropriate for the requirements of the business. The biographical details of the Directors are on page 22.

Corporate Governance (continued)

The Board have appointed a Senior Independent Non-Executive Director who is available to shareholders if they have concerns which contact through the normal channels had failed to resolve or for which such contact is inappropriate

The attendance of the Directors at the Board and principal Board Committee meetings during the year are detailed in the table below

	Board (9 meetings)	Audit Committee (4 meetings)	Remuneration Committee (6 meetings)	Nomination Committee (1 meeting)
Mike Davies *	9	n/a	3	1
Andrew Allner	9	4	6	1
Ian Burrell	9	n/a	n/a	n/a
Graham Holden	9	n/a	n/a	n/a
Bill Husselby	9	4	6	1
David Sarti	9	n/a	n/a	n/a
Richard Scholes	9	4	6	1

Notes

* Following the report of the Financial Reporting Council on the Combined Code on Corporate Governance, in June 2006, Mike Davies was appointed a member of the Remuneration Committee on 30 August 2006 and has attended all Remuneration Committee meetings from that date

At least once a year the Chairman holds a meeting with the Non-Executive Directors without the Executive Directors being present. Led by the Senior Independent Non-Executive Director, the Non-Executives meet without the Chairman being present, at least annually, to appraise the Chairman's performance

Directors have the right to ensure that any concerns they raise about the running of the Company or a proposed action will be recorded in the Board minutes. Further, on resignation, if a Non Executive Director did have any such concerns, the Chairman would invite him to provide a written statement for circulation to the Board

The Company maintains an appropriate level of Directors' and Officers' Insurance in respect of legal action against the Directors.

Chairman and Chief Executive

The positions of Chairman and Chief Executive are held by separate individuals. The Chairman is primarily responsible for the leadership and effective working of the Board and ensuring that each Director, particularly the Non-Executive Directors, are able to make an effective contribution. He ensures that there is a constructive relationship between the Executive and the Non-Executive Directors. The Chief Executive has responsibility for all operational matters which include the implementation of the Group Strategy and policies approved by the Board. During the year the Board approved written Terms of Reference for the Chairman and Chief Executive.

The Chairman at the time of his appointment did meet, and continues to meet, the independence criteria set out in the Code.

Appointments to the Board

The Board has an established Nomination Committee to lead the process for Board appointments and to make recommendations to the Board. The Committee meets periodically and at least once each year. The members of the Nomination Committee are the Chairman, who chairs the meetings, and the three independent Non-Executive Directors.

The Terms of Reference of the Nomination Committee were reviewed during the year and are available on the Company's website at www.marshalls.co.uk. These Terms of Reference explain the role of the Committee and the authority delegated to it by the Board. These Terms of Reference state that the Chairman would not chair the Nomination Committee when it is dealing with his own re-appointment or the appointment of a successor to the Chairmanship.

On a regular basis the Nomination Committee undertakes an evaluation of the balance of skills, knowledge and experience of the Board. For a particular appointment it will use this evaluation to prepare a description of the role and capabilities required. This Committee would prepare the job specification, including an assessment of the time commitment expected, when it next appoints a Chairman. There have not been any Board appointments during the year.

The Nomination Committee leads the process for Board appointments and makes recommendations to the Board about filling vacancies on the Board, appointing additional persons to the Board and the re-election by shareholders of any Director under the retirement by rotation provisions in the Company's Articles of Association.

The Nomination Committee does review the plans in place for the orderly succession of Directors and senior managers.

Other significant commitments of the Chairman and the Non-Executive Directors were disclosed to the Board before appointment and the Board is notified of any subsequent changes. None of the Executive Directors hold a Non-Executive Directorship.

The letters of appointment of the Non-Executive Directors will continue to be available for inspection at the Company's registered office. These letters of appointment set out the expected time commitment and Non-Executive Directors undertake that they will have sufficient time to meet what is expected of them.

Information and Professional Development

All Directors are supplied in a timely manner, with all relevant documentation and financial information to assist them in the discharge of their duties. This includes information on the Company's operational and financial performance. At every meeting the Board receives a health and safety report.

To ensure that Directors continually update their knowledge and familiarity with the Company, each year a number of the Board meetings take place at operational sites around the Group. These visits enable the Directors to meet local management and to keep them up-to-date with the business. In addition, each of the Directors has on-line access to the Virtual Learning Resource Centre at Ashridge Business School, which provides Learning Guides covering a broad spectrum of management skills and competencies.

Corporate Governance (continued)

New appointments to the Board have experience and skills to bring to the Company. Training is offered to all new Directors. The Chairman, together with the Chief Executive and the Company Secretary, ensure that newly appointed Directors receive full, formal and tailored induction on joining the Board. Newly appointed Directors would be available to shareholders if a meeting were requested.

All Directors have access to the advice and services of the Company Secretary and are entitled to rely on the impartial and independent nature of that advice and those services. The Company Secretary is responsible for ensuring that Board procedures are complied with and, through the Chairman, advises the Board on Corporate Governance matters. Both the appointment and removal of the Company Secretary is a matter for the Board as a whole.

The Board has an approved procedure for all Directors to take independent professional advice at the Company's expense. All Board Committees are provided with sufficient resources to undertake their duties.

Performance evaluation

During the year, the Board conducted an evaluation of its own performance and that of its three principal Committees. A brief questionnaire covering the main areas of the evaluation was prepared by the Chairman and the Secretary and formed the basis of one-to-one discussions between each of the Directors and the Secretary. The evaluation questionnaire included questions about the effectiveness of the Executive and the Non-Executive Directors.

Feedback on the points raised was considered by the Board. The principal conclusions were that the Board should allocate more time to debating strategic issues, that the Board's monthly KPI pack should be further reduced to focus on key indicators, that the Board should spend more time understanding the Group's talent pool and succession planning issues and that the Remuneration Committee should refine its processes. The exercise was viewed positively by the Directors and it will be undertaken again during the course of the current financial year.

Following the evaluation in 2005 the Board set itself objectives for the year. Progress on these objectives was reviewed in 2006, new objectives for 2007 have been agreed and a Board timetable has been set to ensure that they are properly considered during the year.

As set out above there is an established process to evaluate the performance of the Chairman.

Re-election

The Company's Articles of Association require Directors to retire and seek re-election at the first Annual General Meeting of the Company following their appointment. The Articles of Association include a provision for one third of the Directors to retire and seek re-election at each Annual General Meeting, ensuring that no Director serves more than three years without retiring and being proposed for re-appointment.

Non-Executive Directors are appointed for specific terms subject to re-appointment and the Company's Articles of Association and subject to the Companies Act provisions relating to the removal of a Director. The Nomination Committee has ensured that performance evaluations for each Director who is retiring by rotation and being proposed for re-election have been undertaken. In the circular to shareholders, accompanying the resolution to re-appoint a Non-Executive Director, the Board will explain why it believes that the Non-Executive Directors should be re-appointed. The Chairman will confirm to shareholders when proposing re-appointment that, following a formal performance evaluation, the individual's performance continues to be effective and that they demonstrate commitment to the role.

Mike Davies and Bill Husselby are both serving their first three year term. Richard Scholes and Andrew Allner have each served one three year term, and following a review during the year, were re-appointed in July 2006 each for a second term of three years. Any Non-Executive Directors serving more than six years will be subject to a particularly rigorous review.

Directors' Remuneration

Details of the Directors' remuneration are set out in the Directors' Remuneration Report on pages 40 to 49. The report details the Company's compliance with the Code's requirements with regard to remuneration matters. The Terms of Reference of the Remuneration Committee were reviewed during the year and are available on the Company's website at www.marshalls.co.uk

Accountability and Audit

Financial Reporting

In presenting the Annual and Interim Financial Statements the Directors seek to present a balanced and understandable assessment of the Group's position and prospects. The Directors have adopted the going concern basis in preparing these Financial Statements.

The respective responsibilities of the Directors' and the Auditors in connection with the Financial Statements are explained in the Statement of Directors' Responsibilities and the Auditors' Report on pages 31 and 50 respectively.

Internal Control

The Board is responsible for the Group's system of internal controls and for reviewing its effectiveness. Throughout the year under review and up to the date of this report the Board has operated procedures to meet the requirements of the Code as set out in the 'Internal Control Guidance for Directors on the Combined Code' published in September 1999.

The Directors acknowledge their responsibility for the Group's system of internal control and for reviewing its effectiveness. Such a system 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.

There is an ongoing process for identifying, evaluating and managing the Group's significant

risks through a Risk Committee which reports directly to the Board.

The Risk Committee comprises the Executive Directors. The Risk Committee is responsible for identifying, evaluating and managing any material risks which might threaten the Group's business objectives. In undertaking this work, it receives regular risk reviews and an annual risk assessment report carried out by the head of each business unit. From this information, the Risk Committee has compiled a Register which identifies the Group's key risk areas, the probability of those risks occurring and the impact they would have. In addition, the Risk Register identifies the controls that exist to manage and, where possible, minimise or eliminate those risks. The Risk Register is used to direct action programmes to test the effectiveness, including independent audit assessment, of those controls. This process is regularly reviewed by the Audit Committee on behalf of the Board.

In addition to the major risk review process, the Group operates under an established internal control framework, the key features of which include clearly defined reporting lines and authorisation procedures and a comprehensive budget and monthly reporting system.

The Board has carried out an annual assessment of the Group's risk management and internal control system for the year to 31 December 2006 by considering reports from both the Audit Committee and the Risk Committee.

Audit Committee and Auditors

Information relating to the Audit Committee is set out in the Report of the Audit Committee on page 39. The report details the Company's compliance with the Code's requirements with regard to audit matters. The Terms of Reference of the Audit Committee are available on the Company's website at www.marshalls.co.uk

Corporate Governance (continued)

Going Concern

The Directors consider, after making appropriate enquires at the time of approving the Financial Statements, that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future, and accordingly, that it is appropriate to adopt the going concern basis in the preparation of the Financial Statements

Relations with Shareholders

Dialogue with Shareholders

The Board is accountable to shareholders for the Company's continued success. The Board accordingly places great emphasis on maintaining good communications with shareholders. The Chief Executive and Finance Director meet regularly with major shareholders to discuss the Group's performance, strategic issues and shareholder investment objectives. Reports of these meetings and any shareholder communications during the year, are reported to the Board

The regular announcements of significant events affecting the Group and the frequent updates on current trading emphasises the Board's commitment to keeping the Company's investors informed of developments affecting the Group. The Company does, periodically, arrange site visits for investors.

From time to time, and when appropriate, the Non-Executive Directors will attend meetings with major shareholders. The Board regularly receives copies of analysts' and brokers' briefings.

The Annual and Interim Reports, together with the Marshalls website, are the principal means of communication with all shareholders during the year

Constructive use of the Annual General Meeting

The Notice of Annual General Meeting is despatched to shareholders, together with explanatory notes or a circular on items of special business, at least 20

working days before the meeting. It is the Company's practice to propose separate resolutions on each substantially separate issue including a resolution relating to the Report and Accounts.

A presentation is made on the progress and performance of the business prior to the formal business of the meeting

The Chairmen of the Audit, Remuneration and Nomination Committee normally attend the Annual General Meeting and are available to answer questions. All Directors normally attend the meeting.

The Board welcomes questions from shareholders who have an opportunity to raise issues informally or formally before or at the Annual General Meeting.

For each resolution the proxy appointment forms provide shareholders with the option to direct their proxy vote either for or against the resolution or to withhold their vote. The Company will ensure that the proxy form and any announcement of the results of a vote will make it clear that a 'vote withheld' is not a vote in law and will not be counted in the calculation of the proportion of the votes for and against the resolution

All valid proxy appointments are properly recorded and counted. For each resolution, after the vote has been taken, information on the number of proxy votes for and against the resolution, and the number of shares in respect of which the vote was withheld, are given at the meeting and are made available on the Company's web site at www.marshalls.co.uk. The Company will continue this practice and will, in future, also include information on the number of shares in respect of which proxy appointments have been validly made

Report of the Audit Committee

The Board has an established Audit Committee. Each of its members is an independent Non-Executive Director. The Board is satisfied that this Committee includes members that have recent and relevant financial experience required by the Code. Richard Scholes, who is the Chairman, is a Chartered Accountant. Andrew Allner, who sits on the Committee, is also a Chartered Accountant and was, during the year, the Group Finance Director of RHM plc.

The main role and responsibilities of the Audit Committee are set out in written Terms of Reference which were reviewed during the year and are available on the Company's website at www.marshalls.co.uk

The Audit Committee has primary responsibility for making a recommendation on the appointment, reappointment and removal of the external auditor to the Board, to put to shareholders for their approval at the Annual General Meeting. It keeps under review the scope and results of the audit, its cost-effectiveness and the independence and objectivity of the auditor. Any work awarded to the external auditors with a value in excess of £25,000, or in aggregate a value exceeding £50,000 in any financial year, other than audit and tax compliance, requires the specific approval of the Audit Committee. Where the Committee perceives that the independence of the auditors could be compromised, the work will not be awarded to the external auditors. Details of amounts paid to the external auditors for audit and non-audit services in 2006 are analysed in Note 4 on page 64. The aggregate amount paid to other firms of accountants for non-audit services was £181,000 (2005 £225,000).

This Committee reviews the Interim and Annual Financial Statements before submission to the Board and reviews the effectiveness of the Group's internal control system.

The Audit Committee reviews the planned Internal Audit Programme. The results of all assignments have been reported to the Audit Committee during

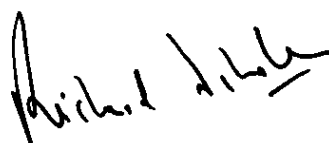
the year. These assignments form part of a much wider programme of independently audited aspects of the Group's operations.

The Audit Committee has, during the year, reviewed the arrangements by which employees, and other people working for the Company, may in confidence raise concerns about possible improprieties in matters of financial reporting or other matters. The Company does have a Serious Concerns Policy (Whistleblowing Policy) which is available to all employees. It is displayed on notice boards and on the Company's intranet. The policy sets out the procedure for employees to raise legitimate concerns about any wrong-doing without fear of criticism, discrimination or reprisal. If the concern cannot be dealt with by their immediate manager there is a process to refer it to the Group Human Resources Director or to the Group Company Secretary. The policy was reviewed during the year and the Audit Committee was satisfied that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.

The Audit Committee does monitor and review the effectiveness of internal control activities. During the year it did consider whether there was a need for an in-house internal audit function. It concluded, having reviewed the current process where firms of external accountants (other than the Company's auditors) carry out regular internal audit assignments of a financial and systems nature, that this was the most effective means of managing the internal audit function.

The Report of the Audit Committee has been approved by the Board and signed on its behalf by

Richard Scholes
Chairman of the Audit Committee
9 March 2007



Directors' Remuneration Report

The Report is divided into two sections, unaudited and audited information in accordance with Schedule 7A of the Companies Act 1985. The audited information commences on page 46.

The Remuneration Committee

During the year, the Remuneration Committee (the Committee) members were Andrew Allner, who chairs the Committee, Bill Hesselby and Richard Scholes all of whom are independent Non-Executive Directors. Mike Davies, independent Chairman, was appointed a member of the Committee with effect from 30 August 2006 following the announcement from the Financial Reporting Council in June 2006 that the Chairman of the Company may also sit on the Remuneration Committee if considered independent on appointment. Members of the Committee have no personal financial interest in the Company other than as shareholders and the fees paid to them as Non-Executive Directors. They are not involved in the day-to-day running of the Company.

The Chief Executive, although not a member of the Committee, on occasions, and for matters not related to himself, attends meetings and participates in discussions on salary and incentive packages.

Role of the Committee

The Committee is responsible for determining, on behalf of the Board, the framework of remuneration for the Executive Directors and reviewing the on-going appropriateness and relevance of the policy. The Committee approves the general recruitment terms, remuneration benefits, employment conditions, pension rights, compensation payments and service terms for the Executive Directors. It also approves the rules and associated guidelines for share based award schemes.

The Committee has no authority in relation to the remuneration of the Non-Executive Directors

whose fees are determined by the Board, after consultation with external advisers. The remuneration of the Chairman is determined by the Board.

In its deliberations the Committee gives full consideration to the principles of good governance and the code of best practice within the Combined Code on Corporate Governance (the Code). The Committee has its own Terms of Reference, which are approved by the Committee and the Board. These were reviewed during the year, to ensure compliance with the Code, and are displayed on the Company's web site. Andrew Allner is available to shareholders to discuss remuneration policy.

General Policy

The Committee and the Board recognise that in order to attract, retain and motivate talented Senior Executives it is necessary to operate a competitive pay and benefits structure. The Committee seeks to ensure that Executives are provided with appropriate incentives to encourage enhanced performance. It aims to reward Executives fairly and responsibly for their contribution to the Company's performance but to avoid paying more than necessary to achieve this objective.

It continues to be the Committee's policy to set the remuneration package at median for median performance, and upper quartile for exceptional performance. In setting all elements of remuneration the Committee is advised by independent consultants and uses data from external research into the salaries and benefits paid by companies in the FTSE 250. During the year, the Committee has taken advice from New Bridge Street Consultants LLP (New Bridge Street) on remuneration packages and long term incentive arrangements. The Committee has also taken advice from Mercer Human Resource Consulting (Mercers) on executive pension arrangements in connection with "A Day". In each case the advisers were appointed by the

Committee and they do not have any other connection with the Company save that a specialist team at Mercers have provided advice to the Company on employee communication in relation to the replacement of the Defined Benefit Section of the pension scheme with a Defined Contribution Section for future benefits

The Committee does receive and consider general information on pay and employment conditions around the Group. In reviewing Executive Directors' salaries, consideration is given to the levels of increase granted to other employees within the Group. Basic salaries are generally reviewed annually or when a change of responsibility occurs

Performance Related Pay

The policy of the Committee is to align Executive Directors' interests with those of shareholders and to give these Executives incentives to perform at the highest levels. To achieve this it seeks to link a significant proportion of the remuneration package to the financial performance of the Group

The performance related elements of the remuneration package are the annual bonus and the Marshalls plc 2005 Long Term Incentive Plan (the LTIP). The LTIP offers Executive Directors, and other senior executives, an opportunity to invest a proportion of their net after tax annual bonus in Investment Shares. Matching Share Awards are then

granted based on the grossed up value of these Investment Shares. The vesting of the Matching Share Awards is subject to the achievement of a three year performance target

As a matter of policy, the Executive Directors are encouraged to hold shares in Marshalls plc. The targets, which were set in 2004, are for the Chief Executive to hold shares equal in value to twice his basic salary and for the remaining Executive Directors to hold shares equal in value to their annual basic salary. Progress was made during the year towards these targets, as set out in the table below. The shareholding guidelines have been reviewed by the Committee as explained in the Proposed Amended LTIP section below

In 2006, each of the Executive Directors voluntarily invested the full amount of their 2005 annual bonus in the LTIP. This demonstration of commitment substantially increased their individual holdings. Each of the Executive Directors has indicated that it is again their intention to invest the maximum amount of their 2006 bonus, payable in March 2007, in the LTIP. The table below illustrates the progress that had been made towards the shareholding targets by the end of 2006 and the additional investment that is expected to be made in March 2007

	Number of shares held on 31 December 2005	Percentage of target	Number of shares held on 31 December 2006	Percentage of target	2006 net bonus invested in the LTIP £'000
Ian Burrell	26,716	46.1	42,982	82.0	81
Graham Holden	214,106	95.4	245,565	121.1	157
David Sarti	16,429	33.1	33,686	64.2	77

Notes

- (a) The share price on 31 December 2005 was 312 pence and on 31 December 2006 was 355 pence
- (b) The gross 2006 bonus payments are set out on page 46
- (c) The share price on 9 March 2007 was 339 pence

Directors' Remuneration Report (continued)

New Bridge Street Review

During the year the Committee undertook a review of executive remuneration. The Committee considered

- if the performance targets applying to awards made under the LTIP remain appropriate given the current prospects of the Company,
- the structure of the LTIP, which enables Matching Share Awards to be made based on annual bonus, and
- the relationship between the LTIP and the Company's share ownership guidelines

The key conclusions of the review were

- the structure of the LTIP should be amended to enable annual awards of Performance Shares to be made in tandem with Matching Share Awards,
- the performance targets applying to Matching Share Awards should be toughened to reflect better the potential earnings growth prospects of the Company,
- the performance targets applying to Performance Share awards should reflect the Company's dual focus on earnings growth and operating cash flow, and
- the share ownership guidelines should be strengthened so that half of any vested LTIP awards would be retained towards the satisfaction of the share ownership guidelines

Major shareholders and shareholder representatives were consulted about these proposed changes. Following this consultation it was agreed that, notwithstanding the separate Matching Share Award and Performance Share Award individual limits in the LTIP, an Executive may not receive Matching Share Awards and Performance Share Awards in any financial year over shares having a total market value (at grant) in excess of 250 per cent of his annual basic salary in that financial year. Shareholder approval will be

sought at the Annual General Meeting to amend the LTIP. Full details of the proposed changes are set out in the circular accompanying the Notice of Meeting.

Remuneration of Executive Directors Basic Salary

The Committee seeks to pay salaries which take account of individual performance and are similar to those paid in comparable companies in the FTSE Construction & Materials Sector and the FTSE 250 more generally. Each year the Executive Directors, along with all employees, receive a cost of living increase. Further increases will be awarded on merit, increased responsibility or to take account of changes in comparable companies. The Committee uses comparisons with caution to avoid increasing remuneration levels without a corresponding improvement in performance. Basic salary is reviewed at 31 December each year or when a change of responsibility occurs.

During the year the Committee reviewed the basic salary of each of the Executive Directors. Details of the basic salaries for 2006 and 2007 are set out on page 46. The 2007 increases were determined following advice from New Bridge Street and in consideration of the good relative performance of the Company during 2006. The increase for the Chief Executive, Graham Holden, is in line with median salaries for Chief Executives in comparable companies. The increases for Ian Burrell and David Sarti reflect additional responsibility and performance and move their basic salaries closer to the median for comparable companies.

Annual Performance Bonus

The principle behind the 2006 annual performance bonus was to align clearly shareholder interests with Executive Director remuneration and reward these Executives for creating shareholder value. During 2006 actual

profits were higher than budget, good progress has been made on implementation of Group Strategy and the annual dividend was increased by 5.2 per cent

Executive Directors have a maximum bonus opportunity of 100 per cent of salary. This was set having considered awards made in other FTSE 250 companies and to reflect the compulsory deferral of half of the bonus award under the LTIP.

The annual bonus for 2006 comprises 15 per cent for the achievement of a cash target and up to a maximum of 85 per cent for meeting a target for underlying profit set by reference to the previous year, budget and market expectations for the year. Underlying profit before tax reflects adjustments to the reported profits before tax in respect of one off items such as property profits, the pension curtailment gain and exceptional items. For the 2006 bonus, performance in line with budget would have attracted an award, based on the profit target, of 35 per cent with up to 85 per cent being awarded for exceptional performance above the budget.

Details of the bonus payments made to the Executive Directors are set out in the table on page 46. The cash target was met as a result of good control being exercised over working capital. The budget for underlying profit before tax was exceeded with good relative performance being achieved in mixed market conditions. Accordingly, a total annual bonus of 74 per cent of salary is payable to the Executive Directors.

The bonus scheme for 2007 is set on similar principles and the maximum annual bonus potential has not been increased. Under the rules of the LTIP half of any annual bonus award will, subject to a minimum threshold, be compulsorily invested until the share ownership guidelines have been achieved. Details of this Long Term Incentive Plan are set out below.

Marshalls plc 2005 Long Term Incentive Plan (the LTIP)

Shareholders approved the LTIP at the Annual General Meeting in May 2005. In the year under review Executive Directors, subject to a minimum threshold, were required to invest 50 per cent of their annual bonus in the LTIP. They chose to invest the full value of their net annual bonus into the LTIP on a voluntary basis. This will further improve the alignment between shareholders and management.

The annual bonus investment was used to purchase Investment Shares and Executive Directors receive a Matching Share Award that is limited to two times the number of Investment Shares, grossed up for tax and subject to the achievement of a three year earnings per share (EPS) performance target. The Matching Share Award vests dependent on an improvement in reported EPS measured using International Financial Reporting Standards, and subject to the discretion of the Committee with regard to one off items, of

RPI + 2 per cent per annum	50 per cent match
RPI + 3 per cent per annum	100 per cent match
RPI + 6 per cent per annum	200 per cent match

The Committee intends to grant Matching Share Awards shortly after the announcement of Preliminary Results on 9 March 2007. These awards will be based on the proposed new performance targets set out below.

Directors' Remuneration Report (continued)

Proposed Amended LTIP

Shareholder approval is being sought at the AGM to amend the LTIP. The proposed amended LTIP would operate with the features set out below.

Matching Share Awards

The EPS performance condition for future awards of Matching Shares is to be toughened and will be consistent with the EPS growth range set for awards of Performance Shares below. Since the EPS condition applies to the entire award, there will be a 50 per cent match for EPS growth of RPI + 9 per cent with a 200 per cent match taking place at, or above, EPS growth of RPI + 21 per cent over the three year performance period.

Details of the Matching Share Award for March 2007 are set out in the LTIP section below.

Performance Share Awards

Executive Directors will be eligible to receive conditional awards of up to 100 per cent of basic salary each year. The vesting of an award would be equally dependent on an improvement in reported EPS measured using International Financial Reporting Standards and subject to the discretion of the Committee with regard to one off items and operating cash flow growth with both targets measured over a three year performance period.

An Executive Director may not receive Matching Share Awards and Performance Share Awards in any financial year over shares having a total market value (at grant) in excess of 250 per cent of his annual basic salary in that financial year.

Choice of Performance Conditions

The performance measures are considered the most appropriate measures of long term performance at Marshalls plc and the targets have been calibrated to reflect the current prospects of the business. Earnings growth represents the main internal benchmark of the business' performance and cash flow represents an effective measure of the quality of the Company's investment proposition.

Stronger Share Ownership Guidelines

To provide greater relevance to the share ownership guidelines, the following changes are also being made: (i) the principle of reinvesting at least half of annual bonus will apply until the guidelines are met, and (ii) at least half of the after tax value of shares must be retained from vested Matching Share and Performance Share Awards until the guidelines are met. This latter change replaces the informal two year retention period that applied to LTIP awards made during the year.

Performance Share Award conditions

Three year earnings per share growth

Below RPI + 9 per cent

RPI + 9 per cent

RPI + 21 per cent

Straight line vesting occurs between points

Proportion of total award vesting

No vesting

12.5 per cent

50 per cent

Three year operating cash flow growth

Below RPI + 9 per cent

RPI + 9 per cent

RPI + 21 per cent

Straight line vesting occurs between points

Proportion of total award vesting

No vesting

12.5 per cent

50 per cent

Performance Share Award Grants

If shareholders approve these proposed amendments, the Committee intends to grant Performance Share Awards to Executive Directors and Senior Executives

shortly after the AGM. In the first year, the award to the Chief Executive will be 100 per cent of basic salary and awards to the Executive Directors will be 75 per cent of basic salary

Five Year Total Shareholder Return

This graph shows the Group's total shareholder return (TSR) performance compared to the FTSE 250 Index for the period from 1 January 2002 to 31 December 2006. TSR is defined as share price growth plus reinvested dividends. This provides a basis for comparison as a relevant equity index in which Marshalls plc is a constituent member. Marshalls has a TSR for the five year period of 80.3 per cent compared to a TSR provided by the FTSE 250 Index of 91.9 per cent. In the opinion of the Directors the FTSE 250 Index is considered the most appropriate index against which the TSR of the Group should be measured because it represents a wider index of alternative investments for shareholders. However, the Committee does not consider TSR an appropriate measure comparator for incentive purposes as sector factors can significantly affect relative performance.

Directors' Remuneration Report (continued)

Audited Information Directors' Remuneration

	Salary/ fees	Performance related bonus	Benefits	Total remuneration (excluding pensions)	
	£'000	£'000	£'000	2006 £'000	2005 £'000
Chairman					
Mike Davies	125	-	-	125	125
Executive Directors					
Ian Burrell	186	138	16	340	292
Graham Holden	360	267	14	641	548
David Sarti	175	130	18	323	252
Non-Executive Directors					
Andrew Allner	42	-	-	42	40
Bill Husselby	32	-	-	32	25
Richard Scholes	42	-	-	42	40
	<u>962</u>	<u>535</u>	<u>48</u>	<u>1,545</u>	<u>1,322</u>

Notes to Directors' Remuneration

- The salaries fees performance related bonuses and benefits all relate to the year ended 31 December 2006
- The highest paid Director in the year was Graham Holden
- Benefits are the provision of a fully expensed company car and medical insurance
- In September 2006, following a change of responsibility, David Sarti's basic salary was increased from £170,000 to £186,000
- The fees for the Non-Executive Directors were reviewed in July 2006. The basic fixed annual fee was increased from £30,000 to £33,000 with an additional fee of £10,000 for the Chairmanship of a Board Committee. During the year the Chairman received a fixed fee of £125,000 and this was increased to £145,000 with effect from 1 January 2007
- With effect from 1 January 2007 the salaries of the Executive Directors are as follows: Graham Holden £380,000, Ian Burrell £210,000 and David Sarti £210,000
- The total amount paid to Directors during the year was £1,545,000 (2005: £1,322,000)

Service Contracts

Each of the Executive Directors has a service contract with the Company which is terminable by the Company on not more than twelve months' notice and by the Director on six months' notice. If a contract is to be terminated, the Committee will determine such mitigation as it considers fair and reasonable in each circumstance and the compensation that may be paid. It will take into account the best practice provisions of the Code and it will take legal advice on the Company's liability to pay compensation and the appropriate amount. The Committee does, periodically, consider what compensation commitments the Executive Directors' contracts would entail in the event of early termination.

There are no contractual arrangements that would guarantee a pension with limited or no abatement on severance or early retirement.

The Company's practice is to appoint the Non-Executive Directors, including the Chairman, under letters of appointment. Their appointment is usually for a term of three years. Andrew Allner and Richard Scholes completed their first three year term during 2006 and, following a review, they have both been reappointed for a second three year term.

During the year, as part of the Non-Executive Directors' performance appraisal of the Chairman, it was recognised that his term of office would expire in October 2007. Following the appraisal a recommendation was made to the Board by the Nomination Committee that he be appointed for a second three year term. This offer has been made to and accepted by the Chairman.

Details of the appointment dates, notice periods and terms of appointment are set out below

	Appointment date	Notice period
Ian Burrell	June 2001	1 year
Graham Holden	August 1992	1 year
David Sartı	November 2004	1 year

	Appointment date	Term of appointment
Mike Davies	October 2004	3 years
Andrew Allner	July 2003 renewed July 2006	3 years
Bill Husseyby	March 2005	3 years
Richard Scholes	July 2003 renewed July 2006	3 years

Pension Benefits

The Marshalls plc Pension Scheme (the Scheme) has two sections the Defined Benefit section which was closed to new members in 2000 and closed to future service accrual in 2006 and a Defined Contribution section.

On 6 April 2006 the Government introduced some significant changes to the legislation affecting pension schemes. The Company, and the Trustees, considered the impact of these changes for all of the members. A number of changes have been made to the Trust Deed to allow members to take advantage of the additional flexibility afforded by these changes at no additional cost to the Company.

The Committee considered the impact of these changes on the Company's pension arrangements for the Executive Directors. Following advice from Mercers it introduced the option for Executive Directors to take a salary supplement in place of the Company's contribution to the Scheme. The salary supplement would be set at a level which incurs no additional cost for the Company. Other Scheme benefits, such as life assurance, would remain unchanged.

On 1 July 2006 the Group replaced its Defined Benefit section of the Scheme with a Defined Contribution section of the Scheme for all active members, including Graham Holden. From this date Graham Holden, in common with all other former Defined Benefit section members, contributes 6 per cent of his salary to the Defined Contribution section. In line with the other Executive Directors the Company makes a contribution of 30 per cent of his salary on his behalf.

Ian Burrell and David Sartı are members of the Defined Contribution section of the Scheme. The Company makes a contribution of 30 per cent of their basic salary and they are required to make a minimum contribution of 4 and 3 per cent respectively of their basic salary. They are eligible for a lump sum payment and dependants pension benefits on death in service.

The Company made pension contributions of £54,000 in respect of Graham Holden for the 6 months from 1 July 2006. Company contributions of £55,800, (2005 £54,232) were paid for the full year in respect of Ian Burrell and £52,600, (2005 £46,485) in respect of David Sartı.

As a former member of the Defined Benefit section of the Scheme, Graham Holden is entitled to a deferred pension. In addition the Scheme provides for a pension for dependents and, in the event of death within the first five years following the date of retirement, a lump sum payment equal to the balance of the pension entitlement for that five year period.

Directors' Remuneration Report (continued)

	Age at 31 December 2006	Years of service	Accrued entitlement 31 December 2006 (see Note a) £'000	Increase in accrued entitlement earned during the year (see Note b) £'000	Transfer value of pension increase earned in year (see Note c) £'000
Graham Holden	47	20	142	3	17

Notes to Pension Entitlements

- (a) The pension entitlement shown is that which was preserved in the Scheme when the member ceased to be an active member of the Defined Benefit section on 1 July 2006
- (b) The increase in accrued entitlement during the year is net of any increase for revaluation in deferment
- (c) The transfer value has been calculated in accordance with Actuarial Guidance Note GN11 less Directors' contributions

Details of accrued pension valued on a transfer basis as required under the Directors' Remuneration Report Regulations 2002 are as follows

	Transfer value as at 31 December 2006 £'000	Transfer value as at 31 December 2005 £'000	Increase in transfer value less member contribution over the year (see Note a) £'000
Graham Holden	1,659	1,429	217

Notes to Pension Entitlements

- (a) The increase in the transfer value less Directors' contributions is the increase in the transfer value of the accrued benefits during the year after deducting the Director's personal contribution to the Scheme

Directors' Interests, Share Options and Long Term Incentive Plan Awards

Directors' Interests

The beneficial interests of the Directors and their immediate families in the shares of the Company, according to the Register of Directors' Interests required to be kept pursuant to section 325 of the Companies Act 1985, are set out below

	1 January 2006			Total	31 December 2006			Total
	Ordinary Shares	Marshall's Share Purchase Plan Shares	LTIP Investment Shares		Ordinary Shares	Marshall's Share Purchase Plan Shares	LTIP Investment Shares	
Andrew Allner	5,000	-	-	5,000	8,333	-	-	8,333
Ian Burrell	26,716	-	-	26,716	26,716	35	16,231	42,982
Mike Davies	30,000	-	-	30,000	30,000	-	-	30,000
Graham Holden	214,106	-	-	214,106	214,106	35	31,424	245,565
Bill Hesselby	5,000	-	-	5,000	10,000	-	-	10,000
David Sarti	16,429	-	-	16,429	19,739	35	13,912	33,686
Richard Scholes	-	-	-	-	3,000	-	-	3,000

Notes to Directors' Interests

- (a) There were no changes to the above mentioned interests between 1 January 2007 and 9 March 2007 save that each of the Executive Directors acquired 71 shares in the Marshall's Share Purchase Plan (the Plan) between January and March 2007. The Plan is an HM Revenue & Customs approved Employee Share Incentive Plan which was approved by shareholders in 2006. All employees with more than 6 months service are eligible to participate in the Plan which entitles them to purchase shares in Marshall's with pre-tax salary.
- (b) The Non-Executive Directors are not eligible to participate in the Plan or the LTIP.
- (c) None of the Directors held any share options during the year.

Long Term Incentive Plan

	Matching Share Awards 1 January 2006	Matching Share Awards granted during the year shares	Date of grant	Market price of shares on date of grant pence	Market value on date of grant £	Market value on 31 December 2006 £	Vesting period
Ian Burrell	-	55,018	31 March 2006	345	189,812	195,314	3 years
Graham Holden	-	106,521	31 March 2006	345	367,497	378,150	3 years
David Sarti	-	47,158	31 March 2006	345	162,695	167,411	3 years

Notes to the Long Term Incentive Plan

- (a) The share price on 31 December 2006 was 355 pence
- (b) The Matching Share Awards are subject to an EPS performance target as set out above
- (c) The Black-Scholes fair value of the Matching Share Awards at 31 March 2006 was 290 pence
- (d) During March 2007 the Executive Directors will invest 100 per cent of their net 2006 Annual Bonus in Investment Shares. Graham Holden will invest £157,388, Ian Burrell will invest £81,317 and David Sarti will invest £76,653. Matching Share Awards will be granted based on the number of Investment Shares purchased.

There are no other disclosable transactions by the Group under IAS 24 - "Related Party Disclosures". There have been no other disclosable transactions by the Company and its subsidiaries with Directors of Group companies and with substantial shareholders since the publication of the last Annual Report.

The Directors' Remuneration Report was approved by the Board and signed on its behalf by



Andrew Allner
Chairman of the Remuneration Committee
9 March 2007

Independent Auditors' Report to the Members of Marshalls plc

We have audited the Group and Parent Company Financial Statements (the "Financial Statements") of Marshalls plc for the year ended 31 December 2006 which comprise the Consolidated Income Statement, the Consolidated and Parent Company Balance Sheets, the Consolidated Cash Flow Statement, the Consolidated Statement of Recognised Income and Expense, the Parent Company Reconciliation of Movement in Shareholders' Funds and the related Notes. These Financial Statements have been prepared under the accounting policies set out therein. We have also audited the information in 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

The Directors' responsibilities for preparing the Annual Report and the Group Financial Statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU, and for preparing the Parent Company Financial Statements and the Directors' Remuneration Report in accordance with applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice), are set out in the Statement of Directors' Responsibilities on page 31.

Our responsibility is to audit the Financial Statements and the part of the Directors' Remuneration Report to be

audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

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 to be audited have been properly prepared in accordance with the Companies Act 1985 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the Financial Statements. The information given in the Directors' Report includes that specific information presented in the Operating and Financial Review that is cross referred from the Business Review Section of the Directors' Report.

In addition we report to you if, in our opinion, 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 other transactions is not disclosed.

We review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2003 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 other information contained in the Annual Report and consider whether it is consistent with the audited Financial Statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Financial Statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) 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 to be audited. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the Financial Statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, 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 to be 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 to be audited.

Opinion

In our opinion:

- the Group Financial Statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the Group's affairs as at 31 December 2006 and of its profit for the year then ended,
- the Group Financial Statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation,
- the Parent Company Financial Statements give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of the Parent Company's affairs as at 31 December 2006,
- the Parent Company Financial Statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the Directors' Report is consistent with the Financial Statements.

KPMG Audit Plc
KPMG Audit Plc
Chartered Accountants
Registered Auditor
1 The Embankment
Neville Street
Leeds LS1 4DW

9 March 2007

Consolidated Income Statement

for the year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Revenue	2	378,100	359,310
Net operating costs	4	(330,339)	(314,885)
Operating profit	2	47,761	44,425
Financial expenses	6	(14,904)	(14,421)
Financial income	6	8,846	8,014
Profit before tax	2	41,703	38,018
Income tax expense	7	(12,623)	(11,661)
Profit after tax but before post tax gain on sale of discontinued operation		29,080	26,357
Post tax gain on sale of discontinued operation	3	-	31,517
Profit for the financial period attributable to equity shareholders of the parent	20	29,080	57,874
Earnings per share (total operations including post tax gain on sale in 2005)			
Basic	9	20 34p	40 73p
Diluted	9	20 32p	40 71p
Earnings per share (continuing operations):			
Basic	9	20 34p	18 55p
Diluted	9	20 32p	18 54p
Dividend:			
Pence per share	8	12 70p	12 10p
Dividends declared	8	18,158	17,169

The notes on pages 55 to 87 form part of these Consolidated Financial Statements

Consolidated Balance Sheet

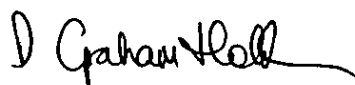
at 31 December 2006

	Notes	2006 £'000	2005 £'000
Assets			
Non-current assets			
Property, plant and equipment	10	202,941	198,030
Intangible assets	11	52,667	46,461
Deferred taxation assets	19	15,018	19,690
		<u>270,626</u>	<u>264,181</u>
Current assets			
Inventories	12	68,256	67,759
Trade and other receivables	13	34,290	36,598
Cash and cash equivalents	14	22	5,210
		<u>102,568</u>	<u>109,567</u>
Total assets		<u>373,194</u>	<u>373,748</u>
Liabilities			
Current liabilities			
Bank overdraft	14	999	-
Trade and other payables	15	65,547	64,570
Interest bearing loans and borrowings	16	3,565	348
		<u>70,111</u>	<u>64,918</u>
Non-current liabilities			
Trade and other payables	15	-	475
Interest bearing loans and borrowings	16	50,064	51,550
Employee benefits	18	41,945	65,264
Deferred taxation liabilities	19	26,532	25,201
		<u>118,541</u>	<u>142,490</u>
Total liabilities		<u>188,652</u>	<u>207,408</u>
Net assets		<u>184,542</u>	<u>166,340</u>
Equity			
Capital and reserves attributable to equity shareholders of the parent			
Share capital	20	35,777	35,772
Share premium account	20	2,732	2,694
Own shares	20	(453)	(102)
Capital redemption reserve	20	73,298	72,573
Consolidation reserve	20	(213,067)	(213,067)
Hedging reserve	20	(6)	(2)
Retained earnings	20	286,261	268,472
Equity shareholders' funds		<u>184,542</u>	<u>166,340</u>

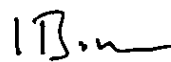
Approved at a Directors' meeting on 9 March 2007

On behalf of the Board

DG Holden
Chief Executive



ID Burrell
Finance Director



The notes on pages 55 to 87 form part of these Consolidated Financial Statements

Consolidated Cash Flow Statement

for the year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Net cash flow from operating activities (after special pension scheme contributions of £10,000,000 (2005 £nil))	21(i)	38,846	42,750
Net cash flow from investing activities	21(ii)	(28,033)	35,668
Net cash flow from financing activities	21(iii)	(17,000)	(56,539)
Net (decrease)/increase in cash and cash equivalents		(6,187)	21,879
Cash and cash equivalents at 1 January		5,210	(16,669)
Cash and cash equivalents at 31 December	14	(977)	5,210

The above includes the operating, investing and financing cash flows of the discontinued operation disclosed in Note 3
The relevant cash flows of the discontinued operation are included in Note 21

Reconciliation of Net Cash Flow to Movement in Net Debt

	Notes	2006 £'000	2005 £'000
Net (decrease)/increase in cash and cash equivalents		(6,187)	21,879
Cash (inflow)/outflow from (increase)/decrease in debt and lease financing		(1,731)	39,910
Finance leases acquired on acquisition of subsidiary undertakings		-	(238)
Movement in net debt in the period		(7,918)	61,551
Net debt at 1 January		(46,688)	(108,239)
Net debt at 31 December	22	(54,606)	(46,688)

Consolidated Statement of Recognised Income and Expenses

	2006 £'000	2005 £'000
Cash flow hedges Effective portion of changes in fair value (net of deferred taxation)	(4)	4
Actuarial gains/(losses) (net of deferred taxation)	7,342	(8,563)
Net expense recognised directly in equity	7,338	(8,559)
Profit for the financial period attributable to equity shareholders of the parent	29,080	57,874
Total recognised income and expenses for the period (for equity shareholders of the parent)	36,418	49,315

Notes to the Consolidated Financial Statements

1 Accounting policies

Significant accounting policies

Marshalls plc (the "Company") is a company domiciled in the United Kingdom. The Consolidated Financial Statements of the Company for the year ended 31 December 2006 comprise the Company and its subsidiaries (together referred to as the "Group").

The Consolidated Financial Statements were authorised for issue by the Directors on 9 March 2007.

The following paragraphs summarise the significant accounting policies of the Group, which have been applied consistently in dealing with items which are considered material in relation to the Group's Consolidated Financial Statements.

(a) Statement of compliance

The Group Consolidated Financial Statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs). The Parent Company has elected to prepare its Financial Statements in accordance with UK GAAP, these are presented on pages 88 to 94.

(b) Basis of preparation

The Consolidated Financial Statements have been prepared on the basis of the requirements of IFRSs in issue and adopted by the EU and effective (or available for early adoption) at 31 December 2006.

The IFRS accounting policies have been applied consistently to all periods presented in these Consolidated Financial Statements. The accounting policies have been applied consistently throughout the Group for the purposes of these Consolidated Financial Statements and are set out on the Company's website (www.marshalls.co.uk).

The Consolidated Financial Statements are presented in sterling, rounded to the nearest thousand.

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of IFRSs that have a significant effect on the Consolidated Financial Statements and estimates with a significant risk of material adjustment in the next year are discussed in Note 28.

(c) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The Financial Statements of subsidiaries are included in the Consolidated Financial Statements from the date that control commences until the date that control ceases.

Notes to the Consolidated Financial Statements (continued)

1 Accounting policies (continued)

(c) Basis of consolidation (continued)

(ii) Transactions eliminated on consolidation

Intragroup balances and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the Consolidated Financial Statements

(d) Foreign currency transactions

Transactions in foreign currencies are translated to sterling at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to sterling at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the Consolidated Income Statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to sterling at foreign exchange rates ruling at the dates the fair value was determined.

(e) Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operational, financing and investment activities. In accordance with its treasury policy, the Group does not hold or issue derivative financial instruments for speculative purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are recognised at fair value and transaction costs are recognised in the Consolidated Income Statement when incurred. The gain or loss on re-measurement to fair value is recognised immediately in the Consolidated Income Statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged (see accounting policy f).

(f) Hedging

(i) Cash flow hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecasted transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. When the forecasted transaction subsequently results in the recognition of a non-financial asset or non-financial liability, the associated cumulative gain or loss is removed from equity and included in the initial cost or other carrying amount of the non-financial asset. For cash flow hedges, other than those covered by the preceding policy statement, the associated cumulative gain or loss is removed from equity and recognised in the Consolidated Income Statement in the same period or periods during which the hedged forecast transaction affects the income or expense. The ineffective part of any gain or loss is recognised immediately in the Consolidated Income Statement.

When a hedging instrument expires or is sold, terminated or exercised or the entity revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, it no longer meets the criteria for hedge accounting. The cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in equity is recognised immediately in the Consolidated Income Statement and cash flow hedge accounting is discontinued prospectively.

(ii) Economic hedges

Where a derivative financial instrument is used to hedge the foreign exchange exposure of a recognised monetary asset or liability, no hedge accounting is applied and any gain or loss on the hedging instrument is recognised in the Consolidated Income Statement.

1 Accounting policies (continued)

(g) Property, plant and equipment

(i) Owned assets

Items of property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses (see accounting policy I). The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of directly attributable production overheads.

Certain items of property, plant and equipment that had been revalued to fair value on or prior to 1 January 2004, the date of transition to IFRSs, are measured on the basis of deemed cost, being the revalued amount at the date of that revaluation.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

(ii) Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Property, plant and equipment acquired by way of finance lease are stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation (see below) and impairment losses (see accounting policy I).

(iii) Subsequent costs

The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied within the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the Consolidated Income Statement as an expense as incurred.

(iv) Depreciation

Depreciation is charged to the Consolidated Income Statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Depreciation on leased assets is charged over the shorter of the lease term and their useful economic life. Land is not depreciated. The rates are as follows:

Freehold and long leasehold buildings	-	2.5% to 5% per annum
Short leasehold property	-	over the period of the lease
Fixed plant and equipment	-	5% to 25% per annum
Mobile plant and vehicles	-	14% to 30% per annum

The residual values, useful economic lives and depreciation methods are reassessed annually. Assets under construction are not depreciated until they are ready for use.

Costs associated with the development of new stone reserves are capitalised. Depreciation commences when commercial extraction commences and is based on the rate of extraction.

Provisions for the cost of quarry restoration are recorded once a present legal or constructive obligation exists, it is probable that an outflow of economic benefits will be required to settle the obligation and the financial cost of restoration work can be reliably measured.

Notes to the Consolidated Financial Statements (continued)

1 Accounting policies (continued)

(h) Intangible assets

(i) Goodwill

All business combinations are accounted for by applying the purchase method. Goodwill represents consideration given by the acquirer in anticipation of future economic benefits from assets that are not capable of being individually identified and separately recognised. In respect of business acquisitions that have occurred since 1 January 2004, goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets acquired.

In respect of acquisitions prior to this date, goodwill is included on the basis of its deemed cost, which represents the amount recorded under the Group's previous accounting framework. The classification and accounting treatment of business combinations that occurred prior to 1 January 2004 have been reconsidered in preparing the Group's opening IFRS balance sheet at 1 January 2004 and no adjustments have been made.

Goodwill is subsequently stated at cost less any accumulated impairment losses. Goodwill is allocated to cash generating units and is no longer amortised but is tested annually for impairment (see accounting policy i).

Negative goodwill arising on an acquisition is recognised directly in the Consolidated Income Statement.

In respect of acquisitions where there is a deferred consideration element, an accrual is created if it is probable that an outflow of economic benefits will be required to settle the obligation and this can be measured reliably.

(ii) Research and development

Expenditure on research activities, undertaken with the prospect of gaining new scientific or technical knowledge and understanding, is recognised in the Consolidated Income Statement as an expense as incurred.

Expenditure on development activities, whereby research findings are applied to a plan or design for the production of new or substantially improved products and processes, is capitalised if the product or process meets the recognition criteria for development expenditure as set out in IAS 38 – "Intangible Assets". The expenditure capitalised includes all directly attributable costs, from the date which the intangible asset meets the recognition criteria, necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Other development expenditure is recognised in the Consolidated Income Statement as an expense as incurred. Capitalised development expenditure is stated at cost less accumulated amortisation (see below) and impairment losses (see accounting policy i).

(iii) Other intangible assets

Other intangible assets that are acquired by the Group are stated at cost less accumulated amortisation (see below) and impairment losses (see accounting policy i).

Expenditure on internally generated goodwill and brands is recognised in the Consolidated Income Statement as an expense as incurred.

(iv) Subsequent expenditure

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

(v) Amortisation

Amortisation is charged to the Consolidated Income Statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Goodwill is systematically tested for impairment at each balance sheet date. Other intangible assets are amortised from the date they are available for use. The rates applied are as follows:

Customer and supplier relationships	-	5 to 20 years
Patents, trademarks and know-how	-	2 to 20 years
Development costs	-	10 to 20 years

1 Accounting policies (continued)

(i) Trade and other receivables

Trade and other receivables are stated at their cost less impairment losses (see accounting policy l)

(j) Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs to completion and of selling expenses.

The cost of inventories is based on the first-in, first-out principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity which were incurred in bringing the inventories to their present location and condition.

(k) Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the Consolidated Cash Flow Statement.

(l) Impairment

(i) Impairment review

The carrying amounts of the Group's assets, other than inventories (see accounting policy j) and deferred tax assets (see accounting policy w), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

For goodwill, assets that have an indefinite useful life and intangible assets that are not yet available for use, the recoverable amount is estimated at each balance sheet date.

An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount. Impairment losses are recognised in the Consolidated Income Statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then, to reduce the carrying amount of the other assets in the unit on a pro rata basis. A cash-generating unit is the group of assets identified on acquisition that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

The recoverable amount of assets or cash-generating units is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

(ii) Reversals of impairments

An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Notes to the Consolidated Financial Statements (continued)

1 Accounting policies (continued)

(m) Share capital

(i) Share capital

Share capital is classified as equity if it is non-redeemable and any dividends are discretionary, or is redeemable but only at the Company's option. Dividends on share capital classified as equity are recognised as distributions within equity. Non-equity share capital is classified as a liability if it is redeemable on a specific date or at the option of the shareholders or if dividend payments are not discretionary. Dividends thereon are recognised in the Consolidated Income Statement as a financial expense.

(ii) Dividends

Dividends on non-equity shares are recognised as a liability and accounted for on an accrual basis. Equity dividends are recognised as a liability in the period in which they are declared (appropriately authorised and no longer at the discretion of the Company).

(n) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the Consolidated Income Statement over the period of the borrowings on an effective interest basis.

(o) Pension schemes

(i) Defined benefit schemes

The net obligation in respect of the Group's defined benefit Pension Scheme is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods, that benefit is discounted to determine its present value, and the fair value of any scheme assets is deducted. The discount rate is the yield at the balance sheet date on AA credit rated corporate bonds that have maturity dates approximating to the terms of the Group's obligations. The calculation is performed by a qualified Actuary using the projected unit credit method.

Actuarial gains and losses that arise in calculating the Group's obligation in respect of a plan are recognised immediately within the Consolidated Statement of Recognised Income and Expenses as allowed by the amendment to IAS 19 - "Employee Benefits".

(ii) Defined contribution schemes

Obligations for contributions to defined contribution schemes are recognised as an expense in the Income Statement as incurred.

(p) Share-based payment transactions

The Group enters into equity-settled share-based payment transactions with its employees. In particular, annual awards are made to Directors under a Long Term Incentive Plan.

The long term incentive plan allows Group employees to acquire shares of the ultimate parent company, these awards are granted by the ultimate parent. The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using an option valuation model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest.

Current tax relief is available based on the market value of shares issued. Consequently, a deferred tax asset is recognised at grant date based on the number of shares expected to be issued proportioned in line with the vesting period.

1 Accounting policies (continued)

(q) Own shares held by employee benefit trust

Transactions of the group-sponsored employee benefit trust are included in the Group Financial Statements. In particular, the trust's purchases of shares in the Company are debited directly to equity.

(r) Provisions

A provision is recognised in the Consolidated Balance Sheet when the Group has a present legal or constructive obligation as a result of a past event, it can be measured reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for.

(s) Trade and other payable

Trade and other payables are stated at cost.

(t) Revenue

Revenue from the sale of goods is recognised in the Consolidated Income Statement when all the following conditions have been satisfied:

- the entity has transferred to the buyer the significant risks and rewards of ownership of the goods,
- the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold,
- the amount of revenue can be measured reliably,
- it is probable that the economic benefits associated with the transaction will flow to the entity, and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably.

Revenue from services rendered is recognised in the Consolidated Income Statement in proportion to the stage of completion of the transaction at the balance sheet date. The stage of completion is assessed by reference to surveys of work performed.

No revenue is recognised if there are significant uncertainties regarding recovery of the consideration due or the possible return of goods or continuing management involvement with the goods.

(u) Expenses

(i) Operating lease payments

Payments made under operating leases are recognised in the Consolidated Income Statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the Consolidated Income Statement over the life of the lease.

(ii) Finance lease payments

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

(iii) Financial expenses

Net financial expenses comprise interest on obligations under the defined benefit pension scheme, the expected return on scheme assets under the defined benefit pension scheme, interest payable on borrowings calculated using the effective interest rate method, dividends on non-equity shares, interest receivable on funds invested, dividend income, foreign exchange gains and losses, and gains and losses on hedging instruments that are recognised in the Consolidated Income Statement (see accounting policy f).

Notes to the Consolidated Financial Statements (continued)

1 Accounting policies (continued)

(v) Financial guarantees

When Group companies enter into financial guarantee contracts to guarantee the indebtedness of other companies within the Group, the Group considers these to be insurance arrangements and accounts for them as such. In this respect the Group treats the guarantee contract as a contingent liability until such time as it becomes probable that the Group will be required to make a payment under the guarantee.

(w) Income tax

Income tax on the profit or loss for the year comprises current and deferred taxation. Income tax is recognised in the Consolidated Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

Deferred taxation is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of goodwill, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, other than in a business combination, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred taxation provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates that are expected to apply when the temporary difference reverses, based on rates that have been enacted or substantively enacted at the balance sheet date.

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

Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

(x) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

(y) Discontinued operations

A discontinued operation is a component of the Group's business that represents a separate major line of business or a geographical area of operations that either have been disposed of or are classified as held for sale.

Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier.

2 Segmental analysis

	Revenue		Operating profit	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Continuing operations	<u>378,100</u>	<u>359,310</u>	<u>47,761</u>	<u>44,425</u>
Financial income and expenses (net)			<u>(6,058)</u>	<u>(6,407)</u>
Profit on ordinary activities before taxation			<u>41,703</u>	<u>38,018</u>

The Directors have undertaken a review of the Group's continuing operations and its associated business risks and consider that the continuing operations should be reported as a single business segment. The Directors consider that the continuing operations represent one product offering with similar risks and rewards and should be managed and reported as a single business segment in line with the Group's internal reporting framework.

	2006 £'000	2005 £'000
Geographical destination of revenue		
United Kingdom	<u>374,627</u>	<u>356,051</u>
Rest of the world	<u>3,473</u>	<u>3,259</u>
	<u>378,100</u>	<u>359,310</u>

All revenue originates in the United Kingdom from continuing operations and there is no material inter-segmental turnover.

3 Discontinued operations

On 4 January 2005 Marshalls Clay Products Limited was sold to Hanson PLC for a cash consideration of £65.0 million (including the repayment of all intergroup indebtedness) and a post-tax gain of £31.5 million was realised. The results of this former business have been disclosed under discontinued operations in the Consolidated Income Statement. The cash flow disclosures in respect of these discontinued operations are shown in Note 21. There was no tax arising in the prior year in respect of the gain on sale of discontinued operations.

Notes to the Consolidated Financial Statements (continued)

4 Net operating costs – continuing operations

	2006 £'000	2005 £'000
Raw materials and consumables	116,213	110,350
Changes in inventories of finished goods and work in progress	(250)	(6,480)
Personnel costs (Note 5)	85,618	85,764
Depreciation - owned	19,222	18,449
- leased	308	267
Own work capitalised	(2,317)	(2,382)
Other operating expenses	112,472	107,045
Amortisation of intangible assets (Note 11)	357	259
Consumer initiative start up costs	2,006	1,002
Works closure costs	1,135	3,008
Restructuring costs	691	391
Operating costs	<u>335,455</u>	<u>317,673</u>
Curtailment gains (net of expenses)	(4,367)	(141)
Other operating income	(1,033)	(1,412)
Net loss/(profit) on asset and property disposals	284	(1,235)
Net operating costs	<u>330,339</u>	<u>314,885</u>
Net operating costs include		
Auditors' remuneration (in respect of the audit of the Group Financial Statements)	116	114
Other fees paid to the auditors and their associates	35	7
Leasing costs	6,039	5,971
Hire of plant and machinery	<u>2,843</u>	<u>2,932</u>

In respect of the year under review, KPMG Audit Plc carried out additional work in relation to corporate taxation and other corporate compliance procedures which amounted in aggregate to £35,000 (2005 £7,000)

5 Personnel costs

	2006 £'000	2005 £'000
Personnel costs (including Directors)		
Wages and salaries	74,740	74,565
Social security costs	7,598	7,429
Share based expenses (Note 18)	250	-
Contributions to defined contribution pension scheme	1,353	708
Current service cost for defined benefit pension scheme	1,677	3,062
	<u>85,618</u>	<u>85,764</u>

Details of Directors' remuneration, share options, long term incentive plans and Directors' pension entitlements are disclosed in the Directors' Remuneration Report on pages 40 to 49

The average number of persons employed by the Group during the year was -

	2006 Number	2005 Number
Continuing operations	<u>2,746</u>	<u>2,884</u>

6 Financial expenses and income

	2006 £'000	2005 £'000
(a) Financial expenses		
Interest expense on bank loans, overdrafts and loan notes	2,406	2,487
Interest on obligations under the defined benefit pension scheme	10,107	9,505
Debenture interest expense	2,275	2,275
B share dividend expense	92	132
Finance lease interest expense	24	22
	<u>14,904</u>	<u>14,421</u>
(b) Financial income		
Expected return on scheme assets under the defined benefit pension scheme	8,802	7,953
Interest receivable and similar income	44	61
	<u>8,846</u>	<u>8,014</u>

7 Income tax expense

	2006 £'000	2005 £'000		
Current tax expense				
Current year	11,004	12,165		
Adjustments for prior years	(947)	(274)		
	<u>10,057</u>	<u>11,891</u>		
Deferred taxation expense				
Origination and reversal of temporary differences				
Current year	2,235	371		
Adjustments for prior years	331	(601)		
	<u>2,566</u>	<u>(230)</u>		
Total tax expense in the Consolidated Income Statement	<u>12,623</u>	<u>11,661</u>		
Reconciliation of effective tax rate				
	2006 %	2006 £'000	2005 %	2005 £'000
Profit before tax	100.0	41,703	100.0	38,018
Tax using domestic corporation tax rate	30.0	12,511	30.0	11,405
Disallowed amortisation of fixed assets	0.3	107	0.2	77
Net items not taxable	1.5	621	2.8	1,054
Adjustments for prior years	(1.5)	(616)	(2.3)	(875)
	<u>30.3</u>	<u>12,623</u>	<u>30.7</u>	<u>11,661</u>

The net amount of deferred taxation debited to the Consolidated Statement of Recognised Income and Expenses in the year was £3,146,000 (2005 £3,677,000 credit) (Note 19)

Notes to the Consolidated Financial Statements (continued)

8 Dividends

Ordinary dividends equity shares

	2006		2005	
	per share	£'000	per share	£'000
2005 Final paid 7 July 2006	8.40p	12,010	8.00p	11,353
2006 Interim paid 8 December 2006	4.30p	6,148	4.10p	5,816
	<u>12.70p</u>	<u>18,158</u>	<u>12.10p</u>	<u>17,169</u>

9 Earnings per share

Basic earnings per share on total operations of 20.34 (2005 40.73) pence per share is calculated by dividing the profit attributable to ordinary shareholders from total operations of £29,080,000 (2005 £57,874,000) by the weighted average number of shares in issue during the year of 142,949,818 (2005 142,106,234)

Basic earnings per share on continuing operations of 20.34 (2005 18.55) pence per share is calculated by dividing the profit attributable to ordinary shareholders from continuing operations of £29,080,000 (2005 £26,357,000) by the weighted average number of shares in issue during the year of 142,949,818 (2005 142,106,234)

Basic earnings per share for discontinued operations of nil (2005 22.18) pence per share is calculated by dividing the profit attributable to ordinary shareholders from discontinued operations of £nil (2005 £31,517,000) (see Note 3) by the weighted average number of shares in issue during the year of 142,949,818 (2005 142,106,234)

Profit attributable to ordinary shareholders

	2006	2005
	£'000	£'000
Profit attributable to ordinary shareholders		
- Continuing operations	29,080	26,357
- Discontinued operations	-	31,517
Total	<u>29,080</u>	<u>57,874</u>

Weighted average number of ordinary shares

	Note	2006	2005
Issued ordinary shares at 1 January	20	143,087,712	141,913,313
Effect of shares issued in the year		14,536	192,921
Effect of shares transferred into employee benefit trust		(152,430)	-
Weighted average number of ordinary shares at 31 December		<u>142,949,818</u>	<u>142,106,234</u>

Diluted earnings per share on total operations of 20.32 (2005 40.71) pence per share is calculated by dividing the profit attributable to ordinary shares, and potentially dilutive ordinary shares, from total operations of £29,080,000 (2005 £57,874,000) by the weighted average number of shares in issue during the year of 142,949,818 (2005 142,106,234) plus dilutive shares of 152,430 (2005 44,303) which totals 143,102,248 (2005 142,150,537)

9 Earnings per share (continued)

Diluted earnings per share on continuing operations of 20.32 (2005 18.54) pence per share is calculated by dividing the profit attributable to ordinary shares, and potentially dilutive ordinary shares, from continuing operations of £29,080,000 (2005 £26,357,000) by the weighted average number of shares in issue during the year of 142,949,818 (2005 142,106,234) plus dilutive shares of 152,430 (2005 44,303) which totals 143,102,248 (2005 142,150,537)

Diluted earnings per share for discontinued operations of nil (2005 22.17) pence per share is calculated by dividing the profit attributable to ordinary shares, and potentially dilutive ordinary shares, from discontinued operations of £nil (2005 £31,517,000) by the weighted average number of shares in issue during the year of 142,949,818 (2005 142,106,234) plus dilutive shares of 152,430 (2005 44,303) which totals 143,102,248 (2005 142,150,537)

Weighted average number of ordinary shares (diluted)

	2006	2005
Weighted average number of ordinary shares at 31 December	142,949,818	142,106,234
Effect of share options in issue	-	44,303
Effect of shares transferred into employee benefit trust	152,430	-
Weighted average number of ordinary shares at 31 December	143,102,248	142,150,537

10 Property, plant and equipment

Cost	Land and buildings	Plant, machinery and vehicles	Total
	£'000	£'000	£'000
At 1 January 2005	91,584	225,371	316,955
Acquisitions through business combinations (Note 23)	954	1,858	2,812
Other acquisitions	5,778	18,045	23,823
Disposals	(358)	(6,231)	(6,589)
At 31 December 2005	97,958	239,043	337,001
At 1 January 2006	97,958	239,043	337,001
Reclassification	(45)	45	-
Acquisitions through business combinations (Note 23)	184	324	508
Other acquisitions	5,570	18,994	24,564
Disposals	(126)	(3,360)	(3,486)
At 31 December 2006	103,541	255,046	358,587

Notes to the Consolidated Financial Statements (continued)

10 Property, plant and equipment (continued)

	Land and buildings	Plant, machinery and vehicles	Total
	£'000	£'000	£'000
Depreciation and impairment losses			
At 1 January 2005	18,990	106,565	125,555
Depreciation charge for the year	2,699	16,017	18,716
Disposals	(59)	(5,241)	(5,300)
At 31 December 2005	21,630	117,341	138,971
At 1 January 2006	21,630	117,341	138,971
Depreciation charge for the year	2,964	16,566	19,530
Disposals	(62)	(2,793)	(2,855)
At 31 December 2006	24,532	131,114	155,646
Net Book Value			
At 1 January 2005	72,594	118,806	191,400
At 1 January 2006	76,328	121,702	198,030
At 31 December 2006	79,009	123,932	202,941

The carrying amount of tangible fixed assets includes £883,000 (2005 £1,113,000) in respect of assets held under finance leases

Group cost of land and buildings and plant and machinery includes £211,000 (2005 £1,591,000) and £5,518,000 (2005 £4,504,000) respectively for assets in the course of construction

Capital commitments

	2006 £'000	2005 £'000
Capital expenditure that has been contracted for but for which no provision has been made in the Consolidated Financial Statements	2,368	4,196

11 Intangible assets

	Goodwill	Customer relation- ships	Supplier relation- ships	Patents, trademarks and know- how	Development costs	Total
Cost	£'000	£'000	£'000	£'000	£'000	£'000
At 1 January 2005	36,643	-	2,400	1,585	159	40,787
Acquisitions through business combinations (Note 23)	4,028	1,960	-	-	-	5,988
At 31 December 2005	40,671	1,960	2,400	1,585	159	46,775
At 1 January 2006	40,671	1,960	2,400	1,585	159	46,775
Acquisitions through business combinations (Note 23)	5,593	250	-	720	-	6,563
At 31 December 2006	46,264	2,210	2,400	2,305	159	53,338
Amortisation and impairment losses						
At 1 January 2005	-	-	37	13	5	55
Amortisation for the year	-	30	189	32	8	259
At 31 December 2005	-	30	226	45	13	314
At 1 January 2006	-	30	226	45	13	314
Amortisation for the year	-	123	134	92	8	357
At 31 December 2006	-	153	360	137	21	671
Carrying amounts						
At 1 January 2005	36,643	-	2,363	1,572	154	40,732
At 1 January 2006	40,671	1,930	2,174	1,540	146	46,461
At 31 December 2006	46,264	2,057	2,040	2,168	138	52,667

The carrying amount of goodwill is allocated across multiple cash generating units and the amount allocated to each unit is not significant in comparison with the total carrying amount of goodwill

The recoverable amount of each cash generating unit has been assessed based on value in use which is derived from individual forecasts using appropriate growth rates

Amortisation charge

The amortisation charge is recognised in the following line item in the Consolidated Income Statement

	2006	2005
	£'000	£'000
Net operating costs (Note 4)	357	259

Notes to the Consolidated Financial Statements (continued)

12 Inventories

	2006 £'000	2005 £'000
Raw materials and consumables	10,599	10,716
Finished goods and goods for resale	57,657	57,043
	<u>68,256</u>	<u>67,759</u>

13 Trade and other receivables

	2006 £'000	2005 £'000
Trade receivables	29,276	33,378
Other receivables	881	127
Prepayments and accrued income	4,133	3,093
	<u>34,290</u>	<u>36,598</u>

No debtors were due after more than one year

14 Cash and cash equivalents

	2006 £'000	2005 £'000
Bank balances	-	5,189
Cash in hand	22	21
	<u>22</u>	<u>5,210</u>
Bank overdraft	(999)	-
	<u>(977)</u>	<u>5,210</u>
Cash and cash equivalents in the Consolidated Cash Flow Statement		

15 Trade and other payables

	2006 £'000	2005 £'000
Current liabilities		
Trade payables	28,810	28,637
Corporation tax	8,185	8,937
Taxation and social security	6,899	6,362
Other payables	5,235	4,474
Accruals	16,418	16,160
	<u>65,547</u>	<u>64,570</u>
Non current liabilities		
Other payables	-	475
	<u>-</u>	<u>475</u>

16 Loans

	2006 £'000	2005 £'000
Current liabilities		
Bank loans	1,327	-
B shares	2,096	-
Finance lease liabilities	142	348
	<u>3,565</u>	<u>348</u>
Non current liabilities		
Bank loans	30,000	28,569
11 375% debenture stock 1992/2014	20,000	20,000
B shares	-	2,821
Finance lease liabilities	64	160
	<u>50,064</u>	<u>51,550</u>

Debenture stock

The 11 375 per cent debenture stock 1992/2014 which is secured by a first floating charge on the assets of the Marshalls Group plc and certain subsidiary undertakings is repayable at par on 30 June 2014, or at the Company's option, between 1 January 1992 and 30 June 2014, at a price related to the gross redemption yield of the 12 per cent Exchequer Stock 2013/2017

Rights attaching to the B shares

(a) Income

Holders of B shares are entitled to a non-cumulative preferential dividend at a rate equal to the lower of

- i) 10 per cent per annum, and
- ii) 75 per cent of LIBOR for six months deposits, as determined at 11 00 am on the first business day of each calculation period

These dividends are paid semi-annually in arrears on 30 June and 31 December

(b) Capital

On a return of capital on a winding up (except on a redemption in accordance with the terms of issue) each holder of B shares is entitled to the sum of 45 pence in respect of each B share, together with a sum equal to the relevant proportion of the preferential dividend which would have been payable if the winding up had taken effect on the last day of the then calculation period

Holders of B shares are able to make elections to have their B shares redeemed at 45 pence per B share semi-annually on 30 June and 31 December

At any time after the anniversary of the Scheme Effective Date or, if earlier, when the number of B shares remaining in issue becomes less than 25 per cent of the total number of B shares issued, the Company may elect to redeem all of the B shares still in issue at their 45 pence nominal value

(c) Attendance and voting at general meetings

The holders of the B shares shall not be entitled, in their capacity as holders of such shares, to receive notice of any general meeting of the Company or to attend, speak or vote at any such general meeting

Bank loans

The bank loans are secured by inter-group guarantees with certain subsidiary undertakings

Notes to the Consolidated Financial Statements (continued)

16 Loans (continued)

Finance lease liabilities

	Minimum lease 2006 £'000	Interest 2006 £'000	Principal 2006 £'000	Minimum lease 2005 £'000	Interest 2005 £'000	Principal 2005 £'000
Less than one year	160	18	142	375	27	348
Between one and five years	92	28	64	185	25	160
	<u>252</u>	<u>46</u>	<u>206</u>	<u>560</u>	<u>52</u>	<u>508</u>

17 Financial instruments

The Group holds and uses financial instruments to finance its operations and to manage its interest rate, liquidity and currency risks. The Group primarily finances its operations using share capital, retained profits and borrowings. The Group has, or had, in issue the following non-equity funding instruments:

- Debenture stock at 11.375 per cent as detailed in Note 16
- B shares as detailed in Note 16

As directed by the Board the Group does not engage in speculative activities using derivative financial instruments. Group cash reserves are held centrally to take advantage of the most rewarding short term investment opportunities. Forward foreign currency contracts are used in the management of currency risk.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk and exchange rate risk. The Board reviews and agrees the policies for managing each of these risks and they have remained unchanged since 2005.

Interest rate risk

The Group's policy is to review regularly the terms of its available short term borrowing facilities and to assess individually and manage each long term borrowing commitment accordingly. An interest rate swap, denominated in sterling, has been entered into to achieve an appropriate mix of fixed and floating rate exposure within the Group's policy. This has the effect of fixing a 6 per cent cap and a 4.5 per cent floor in respect of a three year amortising profile of borrowings commencing at £75,000,000 on 2 August 2004. The fair value of the swap is adjusted against the hedging reserve at the balance sheet date.

Liquidity risk

Cash resources are largely and normally generated through operations. As explained in Note 3, cash proceeds of £65.0 million (including the repayment of all intergroup indebtedness) were received on 4 January 2005 on the disposal of the former Clay Products business. Short term flexibility is achieved by overdraft facilities.

17 Financial instruments (continued)

Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount. The Group does not require collateral in respect of financial assets.

Investments are allowed only in liquid securities and only with counterparties that have a credit rating equal to or better than the Group. Transactions involving derivative financial instruments are with counterparties with whom the Group has a signed netting agreement as well as sound credit ratings. Given their high credit ratings, management does not expect any counterparty to fail to meet its obligations.

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet.

Foreign currency risk

The Group is exposed to foreign currency risk on sales and purchases that are denominated in a currency other than sterling. The currencies giving rise to this risk are primarily Euros and US Dollars.

The Group's policy is to cover all significant foreign currency commitments in respect of trade receivables and trade payables by using forward foreign currency contracts. Most of the forward exchange contracts have maturities of less than one year after the balance sheet date. Where necessary, the forward exchange contracts are rolled over at maturity.

The Group classifies its forward exchange contracts which hedge forecasted transactions as cash flow hedges and states them at fair value. The fair value of forward exchange contracts is £795,000 (2005: £740,000) and is adjusted against the hedging reserve on an ongoing basis.

Sensitivity analysis

In managing interest rate and currency risks the Group aims to reduce the impact of short term fluctuations on the Group's earnings. Over the longer term, however, permanent changes in foreign exchange and interest rates would have an impact on consolidated earnings.

Notes to the Consolidated Financial Statements (continued)

17 Financial instruments (continued)

Effective interest rates and maturity of liabilities

At 31 December 2006 36.6 per cent (2005 42.8 per cent) of the Group's borrowings were on a fixed rate. The interest rate profile of the financial liabilities were:

31 December 2006	Fixed or variable rate	Effective interest rate %	Total £'000	6 months or less £'000	6-12 months £'000	1-2 years £'000	2-5 years £'000	More than 5 years £'000
Cash and cash equivalents (Note 14)	Variable	5.65	977	977	-	-	-	-
Bank loans	Variable	5.58	31,327	-	1,327	-	30,000	-
11.375% debenture stock 1992/2014	Fixed	11.375	20,000	-	-	-	-	20,000
B shares	Variable	3.53	2,096	2,096	-	-	-	-
Finance lease liabilities	Variable	10.0	206	72	70	54	10	-
			54,606	3,145	1,397	54	30,010	20,000
31 December 2005	Fixed or variable rate	Effective interest rate %	Total £'000	6 months or less £'000	6-12 months £'000	1-2 years £'000	2-5 years £'000	More than 5 years £'000
Cash and cash equivalents	Variable	5.25	(5,210)	(5,210)	-	-	-	-
Bank loans	Variable	5.25	28,569	-	-	-	28,569	-
11.375% debenture stock 1992/2014	Fixed	11.375	20,000	-	-	-	-	20,000
B shares	Variable	3.57	2,821	-	-	2,821	-	-
Finance lease liabilities	Variable	10.2	508	176	172	114	46	-
			46,688	(5,034)	172	2,935	28,615	20,000

Borrowing facilities

The total bank borrowing facilities at 31 December 2006 amounted to £100 million (2005 £130 million) of which £67.7 million (2005 £106.6 million) remained unutilised. The undrawn facilities available at 31 December 2006, in respect of which all conditions precedent had been met, were as follows:

	2006 £'000	2005 £'000
Committed		
- Expiring in more than two years but not more than five years	-	-
- Expiring in one year or less	-	61,431
Uncommitted		
- Expiring in one year or less (with option to convert to committed)	28,673	-
- Expiring in one year or less	39,023	45,210
	67,696	106,641

17 Financial instruments (continued)

Fair values of financial assets and financial liabilities

A comparison by category of the book values and fair values of the financial assets and liabilities of the Group at 31 December 2006 are shown below -

	2006		2005	
	Book amount £'000	Fair Value £'000	Book amount £'000	Fair value £'000
Trade and other receivables	34,290	34,290	36,598	36,598
Cash and cash equivalents	22	22	5,210	5,210
Bank overdrafts	(999)	(999)	-	-
Bank loans	(31,327)	(31,327)	(28,569)	(28,569)
11 375 per cent debenture stock 1992/2014	(20,000)	(28,942)	(20,000)	(29,936)
B shares	(2,096)	(2,096)	(2,821)	(2,821)
Finance lease liabilities	(206)	(206)	(508)	(508)
Trade and other payables	(65,547)	(65,547)	(65,045)	(65,045)
Other assets/(liabilities) - net	270,405	270,405	241,475	241,475
	<u>184,542</u>	<u>175,600</u>	<u>166,340</u>	<u>156,404</u>

Estimation of fair values

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the table

(a) Derivatives

Forward exchange contracts are either marked to market using listed market prices or by discounting the contractual forward price and deducting the current spot rate. For interest rate swaps broker quotes are used.

(b) Interest-bearing loans and borrowings

Fair value is calculated based on discounted expected future principal and interest cash flows.

(c) B shares

The fair value is based on market prices.

(d) Finance lease liabilities

The fair value is estimated as the present value of future cash flows, discounted at market interest rates for homogeneous lease agreements. The estimated fair values reflect changes in interest rates.

(e) Trade and other receivables/payables

For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value. All other receivables/payables are discounted to determine the fair value.

Notes to the Consolidated Financial Statements (continued)

18 Employee benefits

The Group operates the Marshalls plc Pension Scheme (the "Scheme") which has both a defined benefit and a defined contribution section. The assets of the Scheme are held in separately managed funds which are independent of the Group's finances. After extensive consultation with the employees affected and their representatives, the Group introduced a new defined contribution section to the Scheme to replace the existing defined benefit section which closed to future service accrual on 1 July 2006. Following this change the Company has made special cash contributions amounting to £10.0 million to the Scheme.

	2006 £'000	2005 £'000	2004 £'000	2003 £'000	2002 £'000
Present value of funded obligations	(209,152)	(212,245)	(176,703)	(159,740)	(142,270)
Fair value of Scheme assets	167,207	146,981	125,848	113,965	96,338
Recognised liability for defined benefit obligations (see below)	(41,945)	(65,264)	(50,855)	(45,775)	(45,932)
Experience adjustments on Scheme liabilities	4,988	(28,123)	(7,137)	(7,851)	(5,365)
Experience adjustments on Scheme assets	5,501	15,881	6,146	13,282	(22,825)

Movements in the net liability for defined benefit obligations recognised in the balance sheet

	2006 £'000	2005 £'000
Net liability for the defined benefit obligations at 1 January	(65,264)	(50,855)
Contributions received	10,960	1,695
Gain/(expense) recognised in the Consolidated Income Statement	1,870	(3,862)
Actuarial gains/(losses)	10,489	(12,242)
Net liability for the defined benefit obligations at 31 December	(41,945)	(65,264)

Gain/(expense) recognised in the Consolidated Income Statement

	2006 £'000	2005 £'000
Current service costs	(1,677)	(3,062)
Interest on obligations	(10,107)	(9,505)
Expected return on Scheme assets	8,802	7,953
Curtailment gains continuing operations	4,852	141
Curtailment gains discontinued operations	-	611
	1,870	(3,862)

18 Employee benefits (continued)

The expense is recognised in the following line items in the Consolidated Income Statement

	2006 £'000	2005 £'000
Net operating costs	3,175	(2,921)
Interest on obligations (financial expenses)	(10,107)	(9,505)
Attributable to discontinued operation	-	611
	<u>(6,932)</u>	<u>(11,815)</u>
Expected return on Scheme assets (financial income)	8,802	7,953
	<u>1,870</u>	<u>(3,862)</u>

Actuarial gains and losses on the defined benefit scheme are recognised in the period in which they occur in the Consolidated Statement of Recognised Income and Expenses

Liabilities for defined benefit obligations

Principal actuarial assumptions at the balance sheet date (expressed as weighted averages)

	2006	2005
Discount rate (AA corporate bond rate)	5.1%	4.8%
Expected return on Scheme assets	6.4%	6.4%
Future salary increases	N/A	3.6%
Future pension increases	3.1%	2.75%
Future expected lifetime of pensioner at age 65 (years)		
Male	18.6	17.0
Female	21.6	19.9

Changes in the present value of the defined benefit obligation are as follows

	2006 £'000	2005 £'000
Benefit obligation at 1 January	212,245	176,703
Current service cost	1,677	3,062
Interest cost	10,107	9,505
Scheme participants' contributions	935	1,978
NI rebates	312	750
Curtailement gain	(4,852)	(752)
Actuarial (gain)/loss	(4,988)	28,123
Benefits paid	(6,284)	(7,124)
Benefit obligation at 31 December	<u>209,152</u>	<u>212,245</u>

Notes to the Consolidated Financial Statements (continued)

18 Employee benefits (continued)

Changes in the fair value of Scheme assets are as follows

	2006 £'000	2005 £'000
Fair value of Scheme assets at 1 January	146,981	125,848
Expected return on Scheme assets	8,802	7,953
Actuarial gain	5,501	15,881
Employer contributions	10,960	1,695
Scheme participants' contributions	935	1,978
NI rebates	312	750
Benefits paid	(6,284)	(7,124)
Fair value of Scheme assets at 31 December	167,207	146,981

The fair value of Scheme assets at the balance sheet date is analysed as follows

	2006 £'000	2005 £'000
Equity	114,306	104,968
Debt	43,672	38,954
Other	9,229	3,059
	167,207	146,981

Share-based payments

Share based payment awards have been made during the year in accordance with the rules of the Marshalls plc 2005 Long Term Incentive Plan (the LTIP). Under the LTIP rules Executive Directors are required to invest a minimum of 50 per cent of their annual bonus in the LTIP. Other eligible employees are entitled to invest a stated percentage of their annual bonus into the LTIP on a voluntary basis. The annual bonus investment is used to purchase Investment Shares and eligible employees receive a Matching Share award, subject to defined limits, and subject to the achievement of a three year earnings per share performance target.

The Matching Share award is dependent on an improvement in reported EPS measured using International Financial Reporting Standards, and is subject to the discretion of the Remuneration Committee with regard to one off items, of

RPI + 2 per cent per annum	50 per cent match
RPI + 3 per cent per annum	100 per cent match
RPI + 6 per cent per annum	200 per cent match

The terms and conditions of the grants are as follows. All options are settled by physical delivery of shares. There is no exercise price in relation to any of these grants and no entitlement to dividends during the vesting period. There are no market conditions associated with these instruments.

	Number of instruments	Date of grant	Vesting period
Equity settled awards granted to Directors of Marshalls plc	208,697	31 March 2006	3 years
Equity settled awards granted to employees of Marshalls Group plc	50,101	31 March 2006	3 years
	258,798		

18 Employee benefits (continued)

The fair value of services received in return for Matching Shares granted are measured by reference to the fair value at the date of grant. The estimate of the fair value of the services received is measured based on a Black-Scholes valuation model.

31 March 2006 grant

Fair value at measurement date (pence per share)	290
Share price on date of grant (pence per share)	329
Expected volatility used in the modelling under the Black-Scholes valuation model	14.0%
Dividend yield	4.2%
Risk-free interest rate (based on national government bonds)	4.75%

The expected volatility is wholly based on the historic volatility (since the Scheme of Arrangement in July 2004) adjusted for any expected changes to future volatility due to publicly available information.

The total expenses recognised for the period arising from share based payments are as follows:

	2006	2005
	£'000	£'000
Equity settled share based expenses	250	-

Further details in relation to the Directors are set out in the Directors' Remuneration Report on pages 40 to 49.

Savings-related share option scheme

Details of the options outstanding at 31 December 2006 are:

Number of options outstanding		Number of ordinary shares		Exercise price	Normally exercisable between
31 December 2006	31 December 2005	31 December 2006	31 December 2005		
-	10	-	19,363	230 Op	1 Dec 2005 – 31 May 2006

In accordance with the transitional arrangements under IFRS, no awards made under the Savings-Related Share Option Scheme have been included in the calculation of the Consolidated Income Statement charge under IFRS 2 as this scheme was established before 7 November 2002.

Employee profit sharing scheme

At 31 December 2006 the scheme held 42,584 (2005 42,584) ordinary shares in the Company.

Notes to the Consolidated Financial Statements (continued)

19 Deferred taxation

Recognised deferred taxation assets and liabilities

	Assets		Liabilities	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Property, plant and equipment	-	-	(21,272)	(19,683)
Intangible assets	-	-	(1,921)	(1,737)
Inventories	-	-	(900)	(685)
Employee benefits	12,584	19,579	-	-
Special pension contributions	2,047	-	-	-
Equity settled share based expenses	75	-	-	-
Other items	312	111	(2,439)	(3,096)
Tax assets/(liabilities)	15,018	19,690	(26,532)	(25,201)

The deferred taxation asset of £12,584,000 (2005 £19,579,000) in relation to employee benefits is in respect of the net liability for the defined benefit obligations of £41,945,000 (2005 £65,264,000) (Note 18) calculated at 30%

Included within this movement is a recognition of a deferred taxation asset with a corresponding credit to deferred taxation expense in the Consolidated Income Statement in respect of the special pension contributions. Current tax relief is obtained on total pension contributions of this magnitude over a four year period with relief in the current year based on 110 per cent of prior year contributions plus 25 per cent of the remaining total contributions

Movement in temporary differences during the year

	1 January 2006 £'000	Recognised in income £'000	Recognised on acquisition/ disposal of subsidiary undertaking £'000	Recognised in equity £'000	31 December 2006 £'000
Property, plant and equipment	(19,683)	(1,589)	-	-	(21,272)
Intangible assets	(1,737)	107	(291)	-	(1,921)
Inventories	(685)	(215)	-	-	(900)
Employee benefits	19,579	(3,848)	-	(3,147)	12,584
Special pension contributions	-	2,047	-	-	2,047
Equity settled share based expenses	-	75	-	-	75
Other items	(2,985)	857	-	1	(2,127)
	(5,511)	(2,566)	(291)	(3,146)	(11,514)

20 Capital and reserves

	Share Capital	Share Premium Account	Own Shares	Capital Redemption Reserve	Consolidation Reserve	Hedging Reserve	Retained Earnings
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
At 1 January 2005	35,478	287	(655)	71,237	(213,067)	(6)	238,219
Shares issued	294	2,407	-	-	-	-	-
Shares in LTIP	-	-	553	-	-	-	(553)
Redemption of B shares	-	-	-	1,336	-	-	(1,336)
Profit for the financial period attributable to equity shareholders of the parent	-	-	-	-	-	-	57,874
Dividends to shareholders	-	-	-	-	-	-	(17,169)
Actuarial loss on defined benefit pension scheme	-	-	-	-	-	-	(12,242)
Increase in fair value of hedging derivatives	-	-	-	-	-	6	-
Deferred taxation arising	-	-	-	-	-	(2)	3,679
Total movements in the year	294	2,407	553	1,336	-	4	30,253
At 31 December 2005	35,772	2,694	(102)	72,573	(213,067)	(2)	268,472
At 1 January 2006	35,772	2,694	(102)	72,573	(213,067)	(2)	268,472
Purchase of own shares	-	-	(351)	-	-	-	-
Share based expenses	-	-	-	-	-	-	250
Shares issued	5	38	-	-	-	-	-
Redemption of B shares	-	-	-	725	-	-	(725)
Profit for the financial period attributable to equity shareholders of the parent	-	-	-	-	-	-	29,080
Dividends to shareholders	-	-	-	-	-	-	(18,158)
Actuarial gain on defined benefit pension scheme	-	-	-	-	-	-	10,489
Decrease in fair value of hedging derivatives	-	-	-	-	-	(5)	-
Deferred taxation arising	-	-	-	-	-	1	(3,147)
Total movements in the year	5	38	(351)	725	-	(4)	17,789
At 31 December 2006	35,777	2,732	(453)	73,298	(213,067)	(6)	286,261

Notes to the Consolidated Financial Statements (continued)

20 Capital and reserves (continued)

Share capital

	Authorised		Issued	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
At 1 January	75,000	75,000	35,772	35,478
Shares issued	-	-	5	294
At 31 December	75,000	75,000	35,777	35,772
Number of ordinary shares	300,000,000	300,000,000	143,106,254	143,087,712

Share premium account

During the year ended 31 December 2006, 18,542 ordinary shares were issued under the Savings-Related Share Option Scheme at an exercise price of 230 pence per share. An amount of £38,000 has been credited to the share premium account in relation to the issue of these shares.

Capital redemption reserve

On 30 June 2006 917,180 B shares were redeemed at 45 pence per share and an amount of £413,000 was paid to shareholders. As at 31 December 2006 further applications had been received, in accordance with the Articles of Association, in respect of 693,213 B shares and amounts totalling £312,000 were paid to shareholders on 5 January 2007. As a consequence of these redemptions, an amount of £725,000 has been transferred to the capital redemption reserve from retained earnings.

Consolidation reserve

On 8 July 2004 Marshalls plc was introduced as the new holding company of the Group by way of a Court approved Scheme of Arrangement under Section 425 of the Companies Act 1985. The restructuring was accounted for as a capital reorganisation and accounting principles were applied as if the Company had always been the holding company of the Group. The difference between the aggregate nominal value of the new shares issued by the Company and the called up share capital, capital redemption reserve and share premium account of Marshalls Group plc (the previous holding company) was transferred to a consolidation reserve.

Dividends

After the balance sheet date the following dividends were proposed by the Directors. The dividends have not been provided and there were no income tax consequences.

	2006 £'000	2005 £'000
8.85 pence (2005 8.40 pence) per ordinary share	12,665	12,019

21 Notes to the cash flow statement

	Continuing operations	2006 Discont- inued operations	Group	Continuing operations	2005 Discont- inued operations	Group
	£'000	£'000	£'000	£'000	£'000	£'000
21(i) Cash flows from operating activities						
Profit before tax	41,703	-	41,703	38,018	-	38,018
Adjustments for						
Depreciation	19,530	-	19,530	18,716	-	18,716
Amortisation	357	-	357	259	-	259
Loss/(gain) on sale of property, plant & equipment	66	-	66	(1,545)	-	(1,545)
Equity settled share based expenses	250	-	250	-	-	-
Financial income and expenses (net)	6,058	-	6,058	6,407	-	6,407
Operating cash flow before changes in working capital, provisions and special pension scheme contributions	67,964	-	67,964	61,855	-	61,855
Decrease/(increase) in trade and other receivables	2,323	-	2,323	(533)	-	(533)
(Increase) in inventories	(53)	-	(53)	(6,805)	-	(6,805)
(Decrease)/increase in trade and other payables	(3,197)	-	(3,197)	3,336	-	3,336
(Decrease)/increase in employee benefits	(2,968)	-	(2,968)	1,225	-	1,225
Special pension scheme contributions	(10,000)	-	(10,000)	-	-	-
Cash generated from the operations	54,069	-	54,069	59,078	-	59,078
Financial expenses paid	(4,265)	-	(4,265)	(4,969)	-	(4,969)
Non equity dividends paid	(149)	-	(149)	(75)	-	(75)
Income tax paid	(10,809)	-	(10,809)	(11,284)	-	(11,284)
Net cash flow from operating activities (after special pension scheme contributions)	38,846	-	38,846	42,750	-	42,750
21(ii) Cash flows from investing activities						
Proceeds from sale of property, plant and equipment	565	-	565	3,172	-	3,172
Financial income received	44	-	44	61	-	61
Disposal of subsidiary, net of cash disposed of	-	-	-	-	65,000	65,000
Acquisition of subsidiaries	(4,157)	-	(4,157)	(9,406)	-	(9,406)
Bank balance acquired with subsidiaries	79	-	79	664	-	664
Acquisition of property, plant & equipment	(24,564)	-	(24,564)	(23,823)	-	(23,823)
Net cash flow from investing activities	(28,033)	-	(28,033)	(29,332)	65,000	35,668
21(iii) Cash flows from financing activities						
Proceeds from issue of share capital	43	-	43	2,701	-	2,701
Payments to acquire own shares	(453)	-	(453)	-	-	-
(Decrease) in other debt and finance leases	(302)	-	(302)	(293)	-	(293)
Redemption of B shares	(848)	-	(848)	(1,102)	-	(1,102)
Increase in /(repayment of) borrowings	2,758	-	2,758	(38,281)	-	(38,281)
Payment of transaction costs	(40)	-	(40)	(118)	(2,277)	(2,395)
Equity dividends paid	(18,158)	-	(18,158)	(17,169)	-	(17,169)
Net cash flow from financing activities	(17,000)	-	(17,000)	(54,262)	(2,277)	(56,539)

Notes to the Consolidated Financial Statements (continued)

22 Analysis of net debt

	1 January 2006	Cash flow	Other non cash changes	31 December 2006
	£'000	£'000	£'000	£'000
Cash at bank and in hand	5,210	(5,188)	-	22
Overdrafts	-	(999)	-	(999)
	<u>5,210</u>	<u>(6,187)</u>	<u>-</u>	<u>(977)</u>
Debt due within one year	-	(1,327)	(2,096)	(3,423)
Debt due after one year	(51,390)	(583)	1,973	(50,000)
Finance leases	(508)	302	-	(206)
	<u>(46,688)</u>	<u>(7,795)</u>	<u>(123)</u>	<u>(54,606)</u>

23 Acquisitions of subsidiaries

Year ended 31 December 2006

On 4 May 2006 the Group acquired Urban Engineering, a business which specialises in a range of shelters and associated products, particularly to the Education Sector

On 30 November 2006 the Group acquired Scenic Blue (UK) Limited, a specialist garden design and landscape installation franchising company

The following disclosures are given in aggregate for all acquisitions in the year

	Recognised values £'000	Fair value adjustments £'000	Carrying amount £'000
Property, plant and equipment (Note 10)	556	(48)	508
Intangible assets (Note 11)	-	970	970
Inventories	378	66	444
Trade and other receivables	422	(407)	15
Cash and cash equivalents (net of bank overdrafts)	79	-	79
Trade and other payables	(1,107)	14	(1,093)
Deferred taxation (Note 19)	-	(291)	(291)
Net identified assets and liabilities	<u>328</u>	<u>304</u>	<u>632</u>
Goodwill on acquisition			<u>5,204</u>
Satisfied by			
Cash consideration			3,648
Deferred consideration			1,788
Professional fees paid			134
Professional fees accrued			266
			<u>5,836</u>

23 Acquisitions of subsidiaries (continued)

Year ended 31 December 2006 (continued)

Fair value adjustments reflect the recognition of intangible assets ("Customer Relationships" and "Know-how"), the recognition of liabilities on an accruals basis, deferred taxation liabilities in respect of intangible assets and the application of the Group's accounting policies. The results of these businesses have been included in the Consolidated Group Financial Statements using the acquisition method of accounting, from the date of purchase. The post acquisition results are not considered to be material and no separate disclosure has been provided in these Consolidated Financial Statements. In addition, the revenue and profit that would have been generated had these acquisitions been at the beginning of the period have not been disclosed. These are not considered material.

Goodwill arising on the above acquisitions represents integration synergies which include both the ability to sell new product lines through the existing Marshalls network and the opportunity to market our existing products through additional distribution channels.

Analysis of movements in goodwill

	£'000
Acquisitions in the year (see above)	5,204
Adjustments to the carrying amounts in relation to acquisitions made in the prior year	389
	<hr/>
Additions to goodwill (Note 11)	5,593

The adjustments to the carrying amounts in relation to acquisitions made in the prior year relate to a re-assessment of deferred consideration and additional professional fees.

Analysis of net cash outflow

	£'000
Acquisitions in the year (see above)	3,782
Adjustments to the carrying amounts in relation to acquisitions made in the prior year (including payment of professional fees previously accrued)	375
	<hr/>
Net cash outflow (Note 21)	4,157

Notes to the Consolidated Financial Statements (continued)

23 Acquisitions of subsidiaries (continued)

Year ended 31 December 2005

On 2 September 2005 the Group acquired the entire issued share capital of Paver Systems (Carlisle) Limited which is based in Lanarkshire, Scotland. The company is a manufacturer of concrete block paving.

	Recognised values £'000	Fair value adjustments £'000	Carrying amount £'000
Property, plant and equipment (Note 10)	2,812	-	2,812
Intangible assets (Note 11)	-	1,960	1,960
Inventories	453	-	453
Trade and other receivables	973	-	973
Cash and cash equivalents	664	-	664
Trade and other payables	(942)	-	(942)
Finance leases	(238)	-	(238)
Corporation tax	(223)	-	(223)
Deferred taxation	(276)	(588)	(864)
Net identifiable assets and liabilities	<u>3,223</u>	<u>1,372</u>	<u>4,595</u>
Goodwill on acquisition			<u>4,696</u>
Satisfied by			
Cash consideration			8,716
Deferred consideration			375
Professional fees paid			187
Professional fees accrued			13
			<u>9,291</u>

Other than the recognition of "Customer Relationships" as an intangible asset (and the associated deferred taxation) no material fair value adjustments were required in respect of the assets acquired. The results of the business have been included in the Consolidated Group Financial Statements using the acquisition method of accounting, from the date of purchase. The post acquisition results are not considered to be material and no separate disclosure has been provided in these Consolidated Financial Statements. In addition, the revenue and profit that would have been generated had the acquisition of Paver Systems been at the beginning of the period have not been disclosed. These are not considered material. With effect from 31 December 2005 the trade and net assets of the business have been transferred to the Group's main operating subsidiary, Marshalls Mono Limited.

Goodwill arising on the above acquisition represents the value of synergies and the assembled workforce acquired.

Analysis of movements in goodwill

	£,000
Acquisition of Paver Systems (see above)	4,696
Adjustments to the carrying amounts in relation to acquisitions made in the prior year	(668)
Additions to goodwill (Note 11)	<u>4,028</u>

The adjustments to the carrying amounts in relation to acquisitions made in the prior year relate mainly to a re-assessment of the fair value adjustments arising in respect of deferred taxation and a re-assessment of deferred consideration.

24 Operating leases

	2006	2005
	£'000	£'000
At 31 December 2006 the Group had commitments under non-cancellable operating leases in respect of property, plant and machinery as follows.		
Expiring		
within one year	499	643
between two and five years	15,469	16,115
More than five years	18,769	17,282
	<u>34,737</u>	<u>34,040</u>

Certain leased properties have been sublet by the Group. In each case the sublease expires in 2009. Sublease payments of £75,000 (2005: £75,000) are expected to be received during the following financial year. An amount of £75,000 (2005: £75,000) was recognised as income in the Consolidated Income Statement within net operating costs in respect of subleases.

25 Contingencies

Royal Bank of Scotland plc has issued, on behalf of Marshalls plc, irrevocable letters of credit totalling £2,100,000 in respect of the Group's employers liability insurance cover with Mitsui Sumitomo Insurance (London Management) Limited. These sums relate to the Group's cap on self insurance in relation to the periods ending 31 October 2005, 31 October 2006 and 31 October 2007.

26 Related parties

Identity of related parties

The Group has a related party relationship with its subsidiaries and with its Directors and Executive Officers.

Transactions with key management personnel

Directors of the Company and their immediate relatives control 0.26 per cent (2005: 0.21 per cent) of the voting shares of the Company.

In addition to their salaries, the Group also provides non-cash benefits to Directors and Executive Officers, and contributes to a defined contribution Pension Scheme on their behalf. Further details are disclosed in the Directors' Remuneration Report on pages 40 to 49.

27 Post Balance Sheet Events

There are no significant adjusting or disclosable post balance sheet events.

28 Accounting estimates and judgements

Management discussed with the Audit Committee the development, selection and disclosure of the Group's critical accounting policies and estimates and the application of these policies and estimates. The accounting policies are set out in Note 1 on pages 55 to 62. In relation to the Group's intangible assets (Note 11) impairment tests have been undertaken using commercial judgement and a number of assumptions and estimates to support their carrying amounts. Note 17 contains information about the assumptions and their risk factors relating to interest rate and foreign currency exposures. Note 18 contains information about the principal actuarial assumptions used in the determination of the net liability for defined benefit pension obligations.

Company Balance Sheet

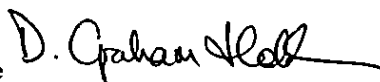
at 31 December 2006

	Notes	2006 £'000	2005 £'000
Fixed assets			
Investments	33	<u>288,388</u>	<u>288,340</u>
Current assets			
Debtors	34	<u>3,722</u>	<u>1,030</u>
Cash at bank and in hand		<u>635</u>	<u>600</u>
		<u>4,357</u>	<u>1,630</u>
Creditors Amounts falling due within one year	35	<u>(2,494)</u>	<u>(80,478)</u>
Net current assets / (liabilities)		<u>1,863</u>	<u>(78,848)</u>
Total assets less current liabilities		<u>290,251</u>	<u>209,492</u>
Creditors Amounts falling due after more than one year	36	<u>-</u>	<u>(2,821)</u>
Net assets		<u>290,251</u>	<u>206,671</u>
Capital and reserves			
Called up share capital	38	<u>35,777</u>	<u>35,772</u>
Share premium account	39	<u>2,732</u>	<u>2,694</u>
Own shares	39	<u>(453)</u>	<u>(102)</u>
Capital redemption reserve	39	<u>73,298</u>	<u>72,573</u>
Other reserve	39	<u>48</u>	<u>-</u>
Profit and loss account	39	<u>178,849</u>	<u>95,734</u>
Equity shareholders' funds		<u>290,251</u>	<u>206,671</u>

Approved at a Directors' meeting on 9 March 2007

On behalf of the Board

DG Holden
Chief Executive



I D Burrell
Finance Director



The notes on pages 89 to 94 form part of these Company Financial Statements

Company Reconciliation of Movements in Shareholders' Funds

for the year ended 31 December 2006

	2006 £'000	2005 £'000
Profit for the financial year	101,796	17,465
Equity dividends	(18,158)	(17,169)
Retained profit for the financial year	83,638	296
New share capital issued	43	2,701
Purchase of own shares	(351)	-
Share based expenses	250	-
Net additions to shareholders' funds	83,580	2,997
Shareholders' funds at beginning of year	206,671	203,674
Shareholders' funds at end of year	290,251	206,671

The notes on pages 89 to 94 form part of these Company Financial Statements

Notes to the Company Financial Statements

29 Accounting policies

The following paragraphs summarise the main accounting policies of the Company, which have been applied consistently in dealing with items which are considered material in relation to the Company's Financial Statements

The corresponding amounts in these Company Financial Statements are restated in accordance with the new policies

(a) Basis of preparation

The Company Financial Statements are prepared under the historical cost convention and in accordance with applicable accounting standards. There is no material difference between historical cost profits and those reported in the profit and loss account.

Under section 230(4) of the Companies Act 1985 the Company is exempt from the requirement to present its own profit and loss account.

Under FRS 1 the Company is exempt from the requirement to prepare a cash flow statement on the grounds that the consolidated cash flows for all Group companies are included within the Consolidated Financial Statements.

As these Parent Company Financial Statements are presented together with the Consolidated Financial Statements, the Company has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the Group (or investees of the Group qualifying as related parties). The Consolidated Financial Statements of Marshalls plc within which this Company is included are set out on pages 52 to 87.

(b) Investments

Fixed asset investments are stated at cost less provision for impairment where appropriate. The Directors consider annually whether a provision against the value of investments on an individual basis is required. Such provisions are charged in the profit and loss account in the year.

Notes to the Company Financial Statements (continued)

(c) Pension costs

Defined benefit scheme

The Company participated in a group pension scheme providing benefits based on final pensionable pay. The assets of the Scheme are held separately from those of the Company. The Company is unable to identify its share of the underlying assets and liabilities of the Scheme on a consistent and reasonable basis and therefore, as required by FRS 17 - "Retirement benefits", accounts for the Scheme as if it were a defined contribution scheme. As a result, the amount charged to the profit and loss account represents the contributions payable to the Scheme in respect of the accounting period.

Defined contribution scheme

Contributions to the Group's defined contribution Pension Scheme are determined as a percentage of employees' earnings and are charged to the profit and loss account as incurred.

(d) Share-based payment transactions

The Company enters into equity-settled share-based payment transactions with its employees. In particular, annual awards are made to Directors under a long term incentive plan.

The long term incentive plan allows Company employees to acquire shares of the ultimate parent company. These awards are granted by the ultimate parent. The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using an option valuation model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest. Shares granted to subsidiary company employees for their services to that subsidiary are recognised as an increase in the investment with a corresponding entry in equity.

(e) Own shares held by employee benefit trust

Transactions of the Group-sponsored employee benefit trust are included in the Group Financial Statements. In particular, the trust's purchases of shares in the Company are debited directly to equity.

(f) Cash and liquid resources

Cash comprises cash in hand and deposits repayable on demand, less overdrafts repayable on demand.

Liquid resources are current asset investments which are disposable without curtailing or disrupting the business and are either readily convertible into known amounts of cash, at or close to their carrying values, or traded in an active market. Liquid resources comprise term deposits of less than one year.

(g) Leased assets

Elements of plant and machinery are subject to finance leases giving rights approximating to ownership. Such assets are treated as though they had been purchased outright and are included in tangible fixed assets at a value equal to the present value of the minimum lease payments to be made during the term of the lease. The total amount of the future obligations outstanding is included in creditors.

The amount included in tangible fixed assets is written off over the shorter of the useful life of the asset or the term of the lease.

The rental cost of all operating leases is charged to the profit and loss account on a straight line basis over the lives of the leases.

(h) Current tax

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

29 Accounting policies (continued)

(i) Deferred taxation

Full provision is made for deferred taxation resulting from timing differences, other than those specifically excluded by FRS19 - "Deferred Taxation", between profits computed for taxation purposes and profits stated in the Financial Statements to the extent that there is an obligation to pay more tax in the future as a result of those timing differences. Deferred taxation assets are recognised to the extent that they are expected to be recoverable. Deferred taxation assets and liabilities are not discounted.

(j) Financial guarantees

Where the Company enters into financial guarantee contracts to guarantee the indebtedness of other companies within the Group, the Company considers these to be insurance arrangements, and accounts for them as such. In this respect, the Company treats the guarantee contract as a contingent liability until such time as it becomes probable that the Company will be required to make a payment under the guarantee.

30 Operating costs

The audit fee for the Company was £20,000 (2005 £20,000). This is in respect of the audit of the Financial Statements.

31 Employees

The Directors are employed by the Company.

Details of Directors' remuneration, share options, long term incentive plans and Directors' pension entitlements are disclosed in the Directors' Remuneration Report on pages 40 to 49.

32 Ordinary dividends equity shares

	2006		2005	
	per share	£'000	per share	£'000
2005 Final paid 7 July 2006	8.40p	12,010	8.00p	11,353
2006 Interim paid 8 December 2006	4.30p	6,148	4.10p	5,816
	<u>12.70p</u>	<u>18,158</u>	<u>12.10p</u>	<u>17,169</u>

33 Investments

At 1 January 2006	£'000
Additions	288,340
	<u>48</u>
At 31 December 2006	<u>288,388</u>

Investments comprise shares in the subsidiary undertaking, Marshalls Group plc.

The increase in the year of £48,000 represents the fair value of LTIP awards granted to employees of Marshalls Group plc.

Notes to the Company Financial Statements (continued)

33 Investments (continued)

The principal wholly owned subsidiary undertakings of Marshalls plc at 31 December 2006 are set out below. All the companies operate within the United Kingdom and are registered in England and Wales.

Subsidiaries	Principal activities
Marshalls Group plc	Intermediate holding company
Marshalls Mono Limited *	Landscape products manufacturer and supplier and quarry owner supplying a wide variety of paving, street furniture and natural stone products
Scenic Blue (UK) Limited *	Specialist garden design and landscape installations franchising company

* held by subsidiary undertaking

34 Debtors

	2006	2005
	£'000	£'000
Amounts owed by subsidiary undertakings	2,449	-
Corporation tax	1,273	1,030
	<u>3,722</u>	<u>1,030</u>

No debtors were due after more than one year

35 Creditors Amounts falling due within one year

	2006	2005
	£'000	£'000
Other creditors	398	433
Amounts owed to subsidiary undertakings	-	80,045
B shares	2,096	-
	<u>2,494</u>	<u>80,478</u>

36 Creditors Amounts falling due after more than one year

	2006	2005
	£'000	£'000
B shares	-	<u>2,821</u>

During the year 1,610,393 B shares were redeemed at 45 pence per share. Further details are disclosed in Note 20 on page 82.

37 Deferred taxation

There is no deferred taxation in the Company.

38 Share capital

As at 31 December 2006, the authorised, issued and fully paid up share capital was as follows -

	2006 Number	2006 Nominal Value £'000	Authorised	
			2005 Number	2005 Nominal Value £'000
Ordinary Shares	<u>300,000,000</u>	<u>75,000</u>	<u>300,000,000</u>	<u>75,000</u>
			Issued and paid up	
	2006 Number	2006 Nominal Value £'000	2005 Number	2005 Nominal Value £'000
Ordinary Shares	<u>143,106,254</u>	<u>35,777</u>	<u>143,087,712</u>	<u>35,772</u>

Disclosures regarding share based payments are given in note 18 on page 78

39 Share capital and reserves

	Ordinary share capital £'000	Share premium account £'000	Own shares £'000	Capital redemption reserve £'000	Equity reserve £'000	Profit and loss account £'000
At 1 January 2006	35,772	2,694	(102)	72,573	-	95,734
Purchase of own shares	-	-	(351)	-	-	-
Equity settled share based expenses	-	-	-	-	48	202
Shares issued	5	38	-	-	-	-
Redemption of B shares	-	-	-	725	-	(725)
Profit for the financial year	-	-	-	-	-	83,638
At 31 December 2006	<u>35,777</u>	<u>2,732</u>	<u>(453)</u>	<u>73,298</u>	<u>48</u>	<u>178,849</u>

40 Capital and leasing commitments

The Company had no capital or leasing commitments at 31 December 2006 or 31 December 2005

41 Contingent liabilities

Royal Bank of Scotland plc has issued, on behalf of Marshalls plc, irrevocable letters of credit totalling £2,100,000 in respect of the Group's employers liability insurance cover with Mitsui Sumitomo Insurance (London Management) Limited. These sums relate to the Group's cap on self insurance in relation to the periods ending 31 October 2005, 31 October 2006 and 31 October 2007.

42 Pension scheme

The Company is a member of the Marshalls plc Pension Scheme (the "Scheme") which has both a defined benefit and a defined contribution section. The assets of the Scheme are held in separately managed funds which are independent of the Group's finances. As set out in Note 18 the Group introduced a new defined contribution section to the Scheme to replace the existing defined benefit section which closed to future service accrual on 1 July 2006.

Notes to the Company Financial Statements (continued)

42 Pension scheme (continued)

Full details of the Scheme are provided in Note 18. The Company is unable to identify its share of the Scheme assets and liabilities on a consistent and reasonable basis. Accordingly, as permitted by FRS 17 - "Retirement benefits", the Scheme has been accounted for in these Company Financial Statements as if the Scheme was a defined contribution scheme.

The latest funding valuation of the Scheme was carried out as at 6 April 2006 and was updated for FRS 17 purposes to 31 December 2006 by a qualified independent Actuary. Certain employees are members of the company defined contribution scheme which invests funds in which the contributions for each individual member are separately identifiable and the benefits calculated accordingly.

The Group deficit on an FRS17 basis at 31 December 2006 was £41,196,000 (2005 £65,264,000)

Shareholder Information

Shareholder analysis at 31 December 2006

<i>Size of Shareholding</i>	<i>Number of Shareholders</i>	<i>%</i>	<i>Number of Ordinary Shares</i>	<i>%</i>
1 to 500	2,181	37.6	339,603	0.2
501 to 1,000	772	13.3	592,845	0.4
1,001 to 2,500	1,155	19.9	1,927,565	1.4
2,501 to 5,000	773	13.3	2,729,547	1.9
5,001 to 10,000	384	6.6	2,753,146	1.9
10,001 to 25,000	190	3.3	2,940,829	2.1
25,001 to 100,000	176	3.0	8,932,167	6.2
100,001 to 250,000	67	1.2	10,636,496	7.4
250,001 to 500,000	41	0.7	15,246,417	10.7
500,001 and above	61	1.1	97,007,639	67.8
	<u>5,800</u>	<u>100.0</u>	<u>143,106,254</u>	<u>100.0</u>

Base cost of Marshalls plc shares following the Scheme of Arrangement

For the purposes of UK taxation of chargeable gains, the base cost of Marshalls plc ordinary shares and B Shares can be calculated by apportioning the base cost of the shares of the former Marshalls plc shares between the Marshalls plc ordinary shares and the B Shares by reference to the market value of the Marshalls plc ordinary shares on the first day of dealings on 8 July 2004 which was 273 125p (the "quarter up value") and the nominal value of the B Shares which is 45 pence

Financial calendar

Preliminary Announcement of results for the year ended

31 December 2006	Announced	9 March 2007
Annual General Meeting		16 May 2007
Final dividend for the year ended 31 December 2006	Payable	6 July 2007
Interim results for the year ending 31 December 2007	Announcement	7 September 2007
Interim dividend for the year ending 31 December 2007	Payable	7 December 2007
Results for the year ending 31 December 2007	Announcement	Early March 2008

Registrars and general

All administrative enquiries relating to shareholdings should, in the first instance, be directed to Computershare Investor Services PLC, PO Box 82, The Pavilions, Bridgwater Road, Bristol BS99 7NH, telephone 0870 702 0000, fax 0870 703 6116, and clearly state the registered shareholder's name and address

Amalgamation of shareholdings

If you are receiving more than one copy of our Annual Report, this may be because you have several accounts on our Share Register. If you would like these accounts amalgamated, this can be done without charge if you write to the Registrar enclosing your Share Certificates

Dividend mandate

Any shareholder wishing dividends to be paid directly into a bank or building society should contact the Registrar for a dividend mandate form. Dividends paid in this way will be paid through the Bankers Automated Clearing System (BACS)

Website

The Group has an internet website which gives information on the Group, its products and provides details of significant Group announcements. The address is www.marshalls.co.uk

Financial History – Consolidated Group

	Year to December 2002 £'000	Year to December 2003 £'000	Year to December 2004 £'000	Year to December 2005 £'000	Year to December 2006 £'000
Consolidated Income Statement					
Revenue	293,834	317,351	328,343	359,310	378,100
Net operating costs	(249,106)	(268,546)	(281,370)	(314,885)	(330,339)
Operating profit	44,728	48,805	46,973	44,425	47,761
Financial income and expenses (net)	(3,653)	(4,613)	(6,718)	(6,407)	(6,058)
Profit before tax	41,075	44,192	40,255	38,018	41,703
Income tax expense	(13,616)	(13,626)	(12,230)	(11,661)	(12,623)
Profit after tax but before post tax gain on sale and post tax profit of discontinued operations	27,459	30,566	28,025	26,357	29,080
Post tax gain on sale and post tax profit of discontinued operations	7,247	2,091	3,278	31,517	-
Profit for the financial period	34,706	32,657	31,303	57,874	29,080
Financial Information					
EBITA	44,728	48,805	47,028	44,684	48,118
EBITDA	58,376	64,407	64,033	63,400	67,648
Earnings per share (pence)					
Basic (continuing operations)	16 43	18 29	18 07	18 55	20 34
Basic (total operations)	20 77	19 54	20 18	40 73	20 34
Dividends per share (pence)	9 65	10 35	11 25	12 10	12 70
Dividend cover (times)	1 70	1 77	1 61	1 53	1 60
Year end share price (pence)	216 0	251 0	297 0	312 0	355 0
Tax rate (%)	33 1	30 8	30 4	30 7	30 3
Consolidated Balance Sheet					
	2002 £'000	2003 £'000	2004 £'000	2005 £'000	2006 £'000
Non-current assets	210,002	230,375	232,132	264,181	270,626
Current assets	101,282	98,040	131,913	109,567	102,568
Total assets	311,284	328,415	364,045	373,748	373,194
Current liabilities	(57,096)	(57,612)	(81,114)	(64,918)	(70,111)
Non-current liabilities	(73,994)	(75,082)	(151,438)	(142,490)	(118,541)
Net assets	180,194	195,721	131,493	166,340	184,542
Net borrowings	(18,117)	(13,243)	(108,239)	(46,688)	(54,606)
Gearing ratio	(10 1%)	(6 8%)	(82 3%)	(28 1%)	(29 6%)

In respect of the above information and graphs on page 12 which disclose a five year performance record for certain information the additional disclosures for 2002 and 2003 have been prepared on the basis of the historic UK GAAP figures adjusted for the following

- exclusion of the activities of the Clay Products business, which was disposed of on 4 January 2005,
- elimination of goodwill amortisation previously charged under UK GAAP,
- inclusion of accounting entries in relation to employee benefits in accordance with previously disclosed information required under UK GAAP by FRS 17, and
- adjustment to the timing of dividend provisions

In relation to the limited graphical disclosures for 2002 and 2003 these are the only adjustments that have been made to past disclosures made under UK GAAP. In terms of the transitional adjustments required for conversion to IFRS, these are the only material adjustments considered by the Directors to be necessary to produce a five year record that discloses the results of continuing operations on a consistent, like for like basis