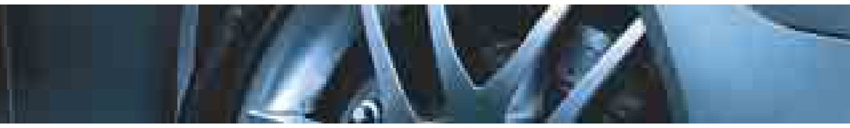
Pendragon | PLC

Annual Report 2006



CONTENTS

GROUP REVIEW

Financial summary

	2006	2005	2004	2003	2002
	IFRS	IFRS	IFRS	UK GAAP	UK GAAP
	£m	£m	£m	£m	£m
Revenue	**5,101.0**	3,284.5	3,168.2	1,841.6	1,875.5
Gross profit	**707.6**	467.7	450.1	265.5	258.6
Operating profit before other income	**139.3**	95.9	81.1	48.4	39.5
Profit before taxation	**96.4**	63.8	65.4	44.3	35.8
Net assets (as restated - note 7)	**306.0**	239.3	219.1	147.1	140.7
Net borrowings	**369.7**	177.0	246.8	96.7	114.0

Other financial information

Gross margin	**13.9 %**	14.2 %	14.2 %	14.4 %	13.8 %
Total operating margin (note 2)	**2.7 %**	3.0 %	2.8 %	2.8 %	2.3 %
After tax return on equity (note 3 and 7)	**24.8 %**	18.8 %	22.7 %	21.2 %	17.2 %
Basic earnings per share (note 4)	**10.7 p**	7.0 p	7.4 p	4.9 p	3.5 p
Adjusted earnings per share (note 5)	**7.5 p**	6.7 p	6.0 p	4.1 p	2.9 p
Dividends per share (note 6)	**3.45 p**	2.64 p	2.04 p	1.52 p	1.38 p
Dividend cover (times)	**3.1**	2.6	3.7	3.2	2.6
Interest cover (times)	**2.4**	2.6	2.9	4.5	3.7
Gearing (as restated - note 7)	**120.8 %**	70.1 %	112.0 %	65.8 %	81.0 %

Business development summary

Number of franchises	**390**	289	244	139	150

note 1 The amounts disclosed for 2003 and earlier periods are stated on the basis of UK GAAP. It is not practicable to restate amounts for periods prior to the date of transition to IFRS.

note 2 Total operating margin is calculated after adding back goodwill impairment / amortisation and exceptional items.

note 3 Return on equity is profit after tax as a percentage of average shareholders' funds.

note 4 Earnings per share has been restated for the impact of the 2003 bonus issue and the 2006 subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

note 5 Earnings per share adjusted to eliminate the effects of goodwill impairment / amortisation and exceptional items, see note 9 of the financial statements. It has been restated for the impact of the 2003 bonus issue and the 2006 subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

note 6 Dividends per share are based on the interim dividend paid and final dividend declared for the year. Dividends per share has been restated for the impact of the 2003 bonus issue and the 2006 subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

note 7 The above table has been adjusted to reflect the adjustments made to prior year net assets on adoption of UITF 38 - Accounting for ESOP Trusts and on the effects of the change in accounting policy as described in note 1(y) of the financial statements.

Pendragon, the leading car retailer in the UK, has delivered another solid financial performance in 2006. We increased revenues by 55% to £5.1 billion from £3.3 billion in 2005. Profits before tax and exceptionals were up by 15% to £68.1 million and earnings per share on this basis increased 12.3% to 7.5 pence. We made exceptional profits and gains on the sale of fixed assets in the year of £28.3 million. The gains on the sale of fixed assets were mainly in respect of property sales. Including these exceptionals, profits before tax were up by 51% to £96.4 million from £63.8 million in 2005 giving basic earnings per share of 10.7 pence.

Our achievements in 2006 have been considerable and have consolidated our position as the leading car retailer in the UK. We implemented a new divisional management structure which integrated the Reg Vardy business which was acquired early in the year. We have made significant inroads to the reduction of borrowings which we put in place for the Vardy acquisition. The roll out of our shared services business model is going well along with the implementation of our in house IT systems.

£m	**2006**	2005
Revenue	**5,101.0**	3,284.5
Underlying operating profit	**135.3**	98.8
Exceptional operating items and other income	**28.3**	4.5
Operating profit	**163.6**	103.3
Finance costs / share of joint venture	**(67.2)**	(39.5)
Profit before tax	**96.4**	63.8
Earnings per share – basic	**10.7 p**	7.0 p
Earnings per share – adjusted	**7.50 p**	6.68 p
Dividend per share	**3.45 p**	2.64 p

Dividend

The final dividend proposed is 2.0 pence per share, which together with the interim dividend of 1.45 pence gives a full year dividend of 3.45 pence per share, an increase of 30.7% over last year. We believe that this increase reflects the strong earnings potential and cash generating ability of the enlarged Group.

Strategy and shareholder value

Pendragon is the largest independent operator of franchised motor car dealerships in the UK, operating 390 franchises. We also operate motor car dealerships from nine locations in California and five in Germany. The UK is the principal market, which accounts for 95% of the Group's revenues. Pendragon sells a broad range of makes of motor cars and commercial vehicles, has a substantial presence in the UK vehicle leasing, wholesale parts and dealer management software markets.

Last year we successfully pursued our strategy of growing the business in partnership with a range of vehicle manufacturers and generating our income from three principal areas; new car sales, used car sales and aftersales service and parts. We have created economies of scale through the deployment of more of our own IT systems, by further utilisation of our shared services centre and reducing operational gearing through improved asset utilisation. Having diverse revenue streams, not simply focused on new car sales, we believe, reduces exposure to the normal retail economic cycles. One of the benefits that we highlighted at the time of the Vardy acquisition was that it gave us more exposure to the used car market which has continued to perform well and will be a major growth area for us.

Our strategy has delivered, and continues to deliver, outstanding results and in 2006 our after tax return on equity rose to 24.8% compared to 18.8% last year. We have also seen real growth rates in earnings and dividends. In 2006 adjusted earnings per share increased by 12.3% and dividends by 30.7%. Over the past five years our compound adjusted earnings per share growth rate has been 26.4% per annum and in the same period the compound dividend growth rate has been 22.1% per annum.

Stratstone Aston Martin Cardiff

Our markets

We operate in markets which offer excellent growth prospects. The UK vehicle retailing market is our principal one where changes to franchising rules have freed up the market for acquisitions and consolidation. Pendragon is the leading player in this consolidation. The total motor car parc in the UK now stands at around 30 million with annual sales of new and used motor cars of just under 10 million units. The new car market over the past four years has weakened by 5.25% and is expected, by industry analysts, to stabilise around the 2006 level for the next two years. The used car market by contrast has continued to perform well. The size of the market for aftersales has grown in line with the car parc in the UK and tends to be less affected by economic cycles as motor cars require regular maintenance and repair for both safety and performance reasons.

We own a large vehicle leasing and contract hire business in the UK. The market has been stable and importantly used car residual values have held up well enabling end of contract vehicles to be sold profitably.

The commercial van and truck market in the UK has enjoyed a period of growth in line with the UK economy and is around 0.4 million new units per annum. The key area in this market is aftersales service which remained strong in 2006.

We have gradually built a presence in the UK market for dealer management systems. The market for these systems is primarily linked to the number of franchised dealers and is served by a relatively small number of providers. We mainly sell into the UK market although we see other overseas markets such as North America and South Africa being additional markets for our products. We see this as a good growth area for our business.

Operational Review

Our group is structured operationally to reflect the range of business activities undertaken and has six distinct trading entities.

Stratstone Under our Stratstone brand we are the UK's leading luxury motor car retailer with 170 locations. Stratstone holds franchises to sell and service Aston Martin, BMW, Cadillac, Chrysler Jeep, Corvette, Dodge, Ferrari, Honda, Jaguar, Land Rover, Lotus, Maserati, Mercedes Benz, MINI, Saab and Volvo.

New vehicle registrations in this luxury sector declined by 1.2% in 2006 with marques represented by Stratstone down slightly more, by 2.8%. The used car market was stable year on year with no noticeable weakening of prices. Income from sales of finance and insurance products was up year on year. The aftersales market continued to perform well and despite increased cost pressures we managed to maintain gross margins in this area.

The split of activities within the Stratstone brand is detailed below showing the respective share of revenue, gross profit and the gross margins achieved.

	2006			2005		
	Revenue	Gross profit	Gross margin	Revenue	Gross profit	Gross margin
New	47 %	36 %	10.1 %	49 %	39 %	10.2 %
Used	36 %	20 %	7.3 %	35 %	18 %	6.8 %
Aftersales	10 %	45 %	58.1 %	10 %	44 %	57.6 %
Trade cars	7 %	(1)%	(1.2)%	6 %	(1)%	(2.9)%
Total	**100 %**	**100 %**	**13.3%**	**100 %**	**100 %**	**12.9 %**

The relative proportion of gross profit generated by activity in 2006 was in line with the previous year. Aftersales continued to contribute just under half of the total gross profits. Trade sales represents cars sent to auction which did not fit Stratstone's sales profile. In aftersales we have developed new products priced specifically for vehicles in the 4 to 6 year old market where we expect to grow our business, whereas historically our focus has been on the 0 to 3 year old car market.

We are including information relating to total units sold and gross profits per unit for the first time this year. We believe this information will give a better understanding of the dynamics of the business. Total units sold consists of both new and used cars. Gross profit per unit is the margin achieved on sales before overheads.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %	Total units sold '000	Gross profit per unit £
Existing	1,444.9	192.5	13.3 %	36.8	2.6 %	52.9	1,752
Acquired	463.3	61.0	13.2 %	13.4	2.9 %	18.5	1,912
Disposed	19.3	2.1	10.7 %	(0.7)	(3.8)%	0.9	1,448
Total 2006	**1,927.5**	**255.6**	**13.3%**	**49.5**	**2.6 %**	**72.3**	**1,796**
Total 2005	1,344.8	173.9	12.9 %	45.6	3.4 %	50.0	1,806

The revenue generated by existing businesses is marginally up on last year with much of the £100.1 million growth being achieved by the acquisitions and greenfield start ups completed in 2005.

Higher rents of £4.3 million, following the sale of some freehold properties to our property joint venture in 2005, and a loss of £3.5 million in respect of our start up Cadillac retail operation resulted in margins in the existing business reducing by 0.8%. We set up five greenfield sites during 2006 which normally take two years to establish themselves in their market place. In the year these greenfield sites made a loss of £0.3 million.

Evans Halshaw Ford Chorley

Evans Halshaw Vauxhall Chilwell

Profits per unit in the existing business were down year on year mainly due to the weakness in the new car market. Profits per unit and the operating margin in the acquired businesses were higher than the existing business due to a richer mix of franchises.

We have been actively branding our luxury car dealerships as Stratstone during the year and this task has now been largely completed. This means that moving into 2007 we can increase promotion of the brand and firmly establish it as the leading luxury car retail brand in the UK.

Evans Halshaw Under our Evans Halshaw brand we are the UK's leading volume motor car retailer with 183 locations. Evans Halshaw holds franchises to sell and service Chevrolet, Citroen, Fiat, Ford, Hyundai, Kia, Nissan, Peugeot, Renault, Suzuki and Vauxhall.

New car registrations have declined in the volume motor car sector by 3.8% in 2006. Evans Halshaw does not represent all the makes of volume cars sold in the UK and, for makes represented, national registrations fell by 5.1% year on year. In general the used car market was good and demand for nearly new used cars continued to be strong. The aftersales market was in line with the previous year although there has been some pressure on costs especially in terms of wage inflation and utility and fuel prices which led to small declines in margins.

	2006			2005		
	Revenue	Gross profit	Gross margin	Revenue	Gross profit	Gross margin
New	45 %	25 %	7.2 %	50 %	25 %	7.0 %
Used	27 %	34 %	16.6 %	27 %	28 %	13.9 %
Aftersales	11 %	41 %	49.0 %	13 %	47 %	49.9 %
National fleet	10 %	-	0.2 %	-	-	-
Trade cars	4 %	-	(1.7)%	5 %	(1)%	(1.6)%
Wholesale	3 %	-	0.7 %	5 %	1 %	1.5 %
Total	**100 %**	**100 %**	**13.2 %**	**100 %**	**100 %**	**13.9 %**

The mix of gross profits generated has changed year on year primarily due to an increase in used car profits where gross margins improved 2.7%. Aftersales continued to contribute a significant proportion of profits and margins held up well despite cost pressures during the year. These cost pressures were absorbed by increased labour sales and tight control of overhead expenses. Trade sales represents cars sent to auction which do not fit Evans Halshaw's sales profile. National fleet is sales to daily rental operators at very low margins which distorts the overall margin performance. The large proportion of profits from aftersales helps to mitigate the effect of economic cycles in that motor vehicles are serviced and repaired at least each year to ensure safety and performance standards are maintained.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %	Total units sold '000	Gross profit per unit £
Existing	1,385.3	189.0	13.6 %	25.5	1.8 %	125.9	648
Acquired	1,206.7	154.0	12.8 %	30.0	2.5 %	104.2	721
Disposed	32.5	3.0	9.1 %	(1.9)	(5.9)%	2.8	685
Total 2006	**2,624.5**	**346.0**	**13.2 %**	**53.6**	**2.0 %**	**232.9**	**694**
Total 2005	1,372.0	190.1	13.9 %	25.5	1.9 %	124.0	669

In the existing business we increased revenue by £50.0 million, mainly within our Ford and Vauxhall dealerships where we sold an extra 3,000 units. The additions we made to our dealership portfolio in 2005 have contributed a further £61.4 million of revenue which has in part offset the reduction in sales of £97.9 million from last year's disposals. Profits per unit in the existing business were down year on year mainly due to the weakness in the new car market. Profits per unit and operating margin in the acquired businesses were higher than the existing business due to a larger proportion of profits in these dealerships coming from higher margin used car sales.

We have a number of initiatives planned in 2007 to promote the Evans Halshaw brand and in January this year we used our first television advertising campaign in the North West. We envisage more television campaigns throughout the year.

Chatfields Under our Chatfields brand we sell and service commercial vans and trucks in the UK from 21 locations. Chatfields holds franchises to sell and service Iveco, DAF, LDV and MAN ERF.

The market for new truck sales in 2006 was down by 5.6% overall whereas the van market was up 1.3%. The market was distorted by regulatory changes last year relating to engine emissions standards which have led operators to delay purchases because of manufacturer price increases on these new cleaner engines.

	2006			2005		
	Revenue	Gross profit	Gross margin	Revenue	Gross profit	Gross margin
New	67 %	27 %	5.6 %	69 %	30 %	5.9 %
Used	5 %	4 %	13.3 %	5 %	4 %	13.1 %
Aftersales	25 %	68 %	37.6 %	24 %	65 %	36.5 %
Trade vehicles	3 %	1 %	3.1 %	2 %	1 %	5.6 %
Total	**100 %**	**100 %**	**13.9 %**	**100 %**	**100 %**	**13.6 %**

Over two thirds of gross profits in this division are derived from the aftersales activity. This tends to be a higher proportion than in the motor car divisions because of the shorter service intervals required for commercial vehicles and the use of overnight servicing in many of the locations.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %	Total units sold '000	Gross profit per unit £
Total 2006	**200.4**	**27.8**	**13.9 %**	**6.1**	**3.1 %**	**5.5**	**1,550**
Total 2005	239.7	32.6	13.6 %	8.5	3.5 %	7.2	1,489

The year in the trucks division has been more difficult with truck sales down with its knock on effect on operating margins. In common with our other businesses inflationary cost pressures have been managed well. The 2005 figures included £1.6 million of operating profits and 937 unit sales contributed by our Mercedes-Benz franchise prior to its sale in July 2005.

Leasing We operate under three separate brands for vehicle leasing and contract hire. The brands are Pendragon Contracts, Bramall Contracts and Vardy Contract Motoring. Each offers a range of leasing and contract hire products mainly to the small corporate and fleet market and to local authorities. The market in which we operate is predominantly fleet sizes of up to 1,000 vehicles.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %	Fleet numbers 000's
Existing	33.9	8.5	25.1 %	7.1	21.1 %	11.1
Acquired	10.4	2.9	27.4 %	2.5	24.0 %	7.1
Total 2006	**44.3**	**11.4**	**25.7 %**	**9.6**	**22.8 %**	**18.2**
Total 2005	48.5	8.9	18.3 %	7.5	15.5 %	10.8

The existing vehicle fleet remained static during 2006 at eleven thousand units with an average lease period of 30 months. Profits are mainly generated through the sale of the vehicles at the end of the rental period. In 2006 we increased the profit per unit on disposal in the Bramall and Pendragon brands by £285 and £166 respectively. We acquired Vardy Contract Motoring as part of the Reg Vardy acquisition in February 2006. The performance of this business was much improved in the year with disposal profits per unit up considerably.

Quickco Parts


Chatfields Commercial Vehicles

Quickco The market for parts sales via the independent wholesaler has been significantly enhanced by changes to the franchising laws in the UK whereby franchised dealers need no longer source all their parts from the franchisor. Under our Quickco brand we are the leading independent genuine parts wholesale business in the UK. Quickco distributes both genuine manufacturer labelled parts and matching quality parts sourced from the original manufacturers. Currently 75% of revenues come from Ford related business and we are seeking to diversify by developing other profit streams. For example, we have been awarded franchises from seven other vehicle manufacturers to distribute their parts. Quickco has a national business with a fleet of 180 vans making 60,000 deliveries per month on a next day or same day basis.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %
Existing	74.0	18.9	25.6 %	4.9	6.7 %
Acquired	5.2	1.3	26.0 %	0.1	2.0 %
Total 2006	**79.2**	**20.2**	**25.6 %**	**5.0**	**6.4 %**
Total 2005	74.6	18.1	24.2 %	3.6	4.9 %

Revenues in 2006 for the existing business were in line with the previous year. The improvements in the operating profit have been achieved through a combination of better buying from its main suppliers and through a reduction in overheads. The overhead reductions were realised mainly by cutting out a number of inefficient delivery routes. Looking forward, we aim to expand our product lines and build on our new franchise relationships.

Pinewood Under our Pinewood brand we are the UK's third largest provider of software solutions to the retail motor industry. The principal product is Pinnacle which is a web enabled dealer management system designed with manufacturer interface and modules for vehicle sales and marketing, aftersales and bookkeeping and accounts generation. The market for technology solutions in the industry continues to grow especially for software packages which are simple to deploy and require minimal training. Under the CFC brand other products are sold which include fleet and workshop management solutions. Currently CFC has customers in over 20 countries.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %
Total 2006	**25.4**	**15.2**	**59.8 %**	**5.3**	**21.0 %**
Total 2005	22.2	11.3	51.0 %	2.9	13.0 %

At the end of 2006 we had over 7,000 Pinnacle user licences in place in over 400 dealerships in the UK. About 40% of the licences have been sold to third party dealers with the balance being used in Group. The Pinnacle product was launched three years ago and sales are now gathering momentum. We have recently secured our first overseas contract for Pinnacle in South Africa. We now have a development team of 40 which is actively working on existing and new products.

California The California business consists of nine locations in Southern California which operate franchises for Jaguar, Land Rover, Aston Martin and Saab.

	2006			2005		
	Revenue	Gross profit	Gross margin	Revenue	Gross profit	Gross margin
New	66 %	46 %	10.8 %	63 %	42 %	10.4 %
Used	15 %	7 %	7.5 %	17 %	9 %	8.3 %
Aftersales	14 %	47 %	51.5 %	15 %	49 %	51.3 %
Trade cars	5 %	-	0.4 %	5 %	-	(0.5)%
Total	**100 %**	**100 %**	**15.7 %**	**100 %**	**100 %**	**15.4 %**

The gross profit splits show a similar pattern to those in the UK for aftersales which contributes just under half of the gross profits. A significant difference is the lower proportion of used car gross profit due to a traditional emphasis on new car sales in this market.

£m	Revenue	Gross profit	Gross margin %	Underlying operating profit	Underlying operating margin %	Total units sold '000	Gross profit per unit £
Existing	201.8	32.2	16.0 %	7.8	3.9 %	6.2	2,513
Disposed	13.0	1.4	11.1 %	(1.3)	(9.7)%	0.4	890
Total 2006	**214.8**	**33.6**	**15.7 %**	**6.5**	**3.0 %**	**6.6**	**2,417**
Total 2005	217.6	33.6	15.4 %	7.0	3.2 %	7.4	2,123

Excluding the impact of the change in the dollar sterling exchange rate, revenues in the USA were marginally ahead of 2005. Sales of Range Rover Sport were very strong throughout the year which contrasted with sales of Jaguar which were poor. The same was true in aftersales where Land Rover had a good year whereas Jaguar was down year on year. Overall operating margins are similar to last year although they should improve going forward as, towards the end of the year, we sold our Lincoln Mercury dealership and closed our Saab operation in South Bay. Both businesses were loss making.

We were pleased to open our custom built Jaguar and Land Rover dealership in Mission Viejo in December and this year we are redeveloping our Land Rover site in Newport Beach to take Land Rover, Jaguar and Aston Martin franchises. We look forward to completing that development later this year.

Mission Viejo USA Jaguar

Germany Our German dealerships remain a relatively small part of the Group, contributing just 1% of revenues. In 2006 their performance improved at operating profit level by £1.5 million to a small loss of £0.3 million. We reduced the number of sites during the year which leaves five remaining around Frankfurt and Munich.

IT roll out and central services

Our scale allows us to invest in information technology solutions and to use a shared services business model. Over the last year we have implemented 83 new Pinnacle systems in our own dealership group and it is planned to have all our locations on the new operating platform by the end of 2007. Our shared service centre now has a team of 425 providing a range of services to around half of our Group including call centre and accounting. The financial benefits for the Group are accounted for in the divisions for which they perform the services.

Acquisitions and Disposals

We acquired the entire share capital of Reg Vardy plc in February 2006. We paid £504.2 million and acquired a business with 97 motor car franchises which enhanced our geographic coverage in the UK. Vardy held franchises which were complementary to those held by Pendragon and furthered our strategic growth plans. The process of integrating Vardy with Pendragon was prolonged due to an investigation by the Office of Fair Trading to determine whether there were any areas where competition was substantially reduced as a consequence of the takeover. As a result of the investigation we agreed to sell four dealerships out of our portfolio. The delay to the integration and consequent disruption of having to manage the Vardy businesses separately until November is now behind us. The Vardy and Pendragon businesses have been integrated as part of the overall restructure of the Group last year.

In March 2006 we purchased the business of Speeds Motor Group which consists of nine Volvo and three Chrysler/Jeep dealerships. The dealerships are predominantly located in the East Midlands. We also acquired five Peugeot and one Citroen dealership to add to our Evans Halshaw division.

Property

Our strategy is to ensure the maximum utilisation of property assets by maximising throughput; that surplus properties are disposed of so as to maximise proceeds, which may involve a change of use; and to utilise our property joint venture structure where appropriate in order to release cash to be invested in higher yielding business assets.

As planned we completed a major sale and leaseback transaction in December 2006 with our property joint venture. We sold 79 properties with a net book value of £191 million for a total consideration of £250 million. As a consequence of the interest we have retained in the properties through the joint venture structure, we are not able to recognise the entire disposal profits in the income statements in our accounts although all the cash has been received. The profit we are able to recognise on the transaction in our income statement is £17.7 million. The joint venture structure gives us operational flexibility mainly through being able to substitute properties.

In addition to the joint venture transaction we disposed of a further eleven properties which were operationally surplus to requirements. Included was the property at Solihull Business Park on which we made a profit of £10 million.

Cash flow

Our borrowings as at 31 December 2006 were £369.7 million compared to £177.0 million at the end of 2005. At the time of the Vardy acquisition, in early 2006, we said our target would be to reduce our borrowings to more normal levels by the end of 2007. We are well on course to achieve this target with reductions from a combination of good cash flow from operations and property and business disposals.

The cash flows of the business may be summarised as follows:

£m	2006	2005
Cash generated from operations	219.4	130.4
Net interest paid	(67.2)	(43.2)
Tax	(24.2)	(16.6)
Replacement capital expenditure	(43.8)	(45.2)
Free cash flow	**84.2**	**25.4**
Acquisitions	(570.2)	(60.8)
Disposals	312.9	119.7
Dividend	(17.4)	(15.6)
Other	(2.2)	1.1
(Increase) / reduction in net debt	**(192.7)**	**69.8**

Cash flow generated from operations was £219.4 million, which compares with £130.4 million generated in 2005. This is made up of two key components, operating profit and working capital movements. The operating profit element after adding back depreciation, intangible charges and property profits was £206.2 million, up £61.3 million on the £144.9 million in 2005. In respect of working capital we made a net reduction of £13.2 million which is after £23.1 million of final salary pension schemes funding. In 2005 we had a net increase in working capital of £14.5 million.

Net interest paid has increased year on year. This reflects the higher borrowings during the year following the acquisitions and increased interest rates in the second half.

Replacement capital expenditure was £43.8 million which includes plant and machinery, fixtures and fittings and motor vehicles (2005: £45.2 million). Expenditure on plant and machinery and fixtures and fittings was £11.5 million, up slightly on the £9.1 million in 2005. The balance of the expenditure of £32.3 million (2005: £36.1 million) is in respect of motor vehicles used either for our contract hire fleet or for service loan cars for our customers.

Acquisitions consist of businesses purchased during the year and property developments. In 2006 we have spent £540.9 million which includes the cost of acquiring Reg Vardy and its associated borrowings, our £15.1 million investment in the property joint venture plus the acquisition of 18 other dealerships. Dealership property developments totalled £28.3 million (2005: £19.2 million).

Business disposals raised £23.1 million in 2006 (2005: £16.2 million), which related to the sale of six dealerships. Property disposals raised £289.8 million (2005: £103.5 million). This includes the disposal of properties in December to our property joint venture company.

Financing costs

The total net interest charge for the year of £67.6 million includes bank interest, vehicle stocking charges and finance charges of £38.8 million, £25.5 million and £3.3 million respectively. Cover for bank interest was 2.9 times compared with 4.5 times in 2005.

Tax

The overall effective tax rate for the year was 30.0 per cent (2005: 32.4 per cent). The reduction in tax rate in 2006 was due to certain one off tax credits.

Treasury

Information regarding treasury policy and procedures together with details of financial risk management are set out in the notes to the financial statements.

Pension Funds

In 1999 we stopped accepting new members into our final salary schemes. During 2006 we took the difficult decision to cease future accruals in all the final salary schemes that were in operation due to the unpredictable nature of the cost of operating these arrangements. The final salary schemes' deficit before tax now stands at £65.1 million, a reduction of £25.2 million. All members of the final salary schemes are now either deferred or pensioner members.

In the 2005 financial statements the Group applied the corridor method to recognise actuarial gains and losses and spread them over the expected working lives of employees in the plans. We have changed this policy to recognise all actuarial gains and losses arising from defined benefit plans directly in equity each year. This change in accounting policy was due to the closure of the schemes to future accruals, and as employees no longer participate in the plan the service period over which the corridor movements are spread is nil. As a consequence the directors consider it is no longer appropriate to spread the gains and losses over the service period and the comparative balance sheet has been restated in line with the new policy.

Share capital

During the year a five for one share split was implemented, increasing the number of shares in issue to 656,027,350 including 18,750 shares issued during the year through the share option scheme. Comparative data in the report and accounts which is calculated based on the number of shares in issue, such as earnings per share and dividends per share, have been restated to reflect the share split.

Outlook

The outlook remains positive for the Group with Pendragon the clear leader in a highly fragmented market. The Vardy acquisition has given us greater scale and more of our businesses have adopted the Pinnacle IT platform and shared service model. The new divisional structure now in place has been designed to enable the Group to continue to expand and to optimise scale economies.

We have a positive view on the used car market and believe that the Group is well placed to expand its business in this market in 2007 and grow its like for like unit sales volumes. Profits from new car sales have become less important for the Group as we have expanded our used car revenues and continue to derive a significant proportion of profits from aftersales. As far as aftersales is concerned we see the market continuing to be stable and through some initiatives we have taken this year will see our revenues grow. Pinewood now has a strong foothold in the dealer management systems market in the UK and we expect to increase third party sales this year. We may see some reduction in profits in our leasing business in 2007 due to fewer cars being returned for disposal and we expect Quickco, our parts wholesale business, to have a good year in 2007.

We have put new operating structures in place during 2006 which are now settled and each division has its sights set firmly on achieving their objectives in 2007. We have set a number of objectives at Group level this year which include reducing the gearing as planned, implementing the Pinnacle system in all our dealerships and driving forward total shareholder returns. Our strategy has delivered superior returns for shareholders over the years and we look forward to continuing that into 2007.

Trevor Finn
Chief Executive
15 February 2007

Sir Nigel Rudd (60) Non-executive Chairman (N) (R)
Appointed non-executive chairman of Pendragon in October 1989. He is non-executive chairman of Alliance Boots plc, deputy chairman of Barclays PLC and an non-executive director of BAE Systems PLC. Sir Nigel chairs the company's Nomination Committee, and rejoined the Remuneration Committee from 1 January 2007.

William Rhodes (68) Non-executive Director † (N)
Joined Pendragon in October 1989. He is a director of a number of private companies. Mr. Rhodes chairs the boards of trustees of a number of the group's occupational pension schemes.

John Holt (67) Non-executive Director (A) (N) (R)
Joined Pendragon in November 1999. He was previously head of Coopers & Lybrand's (now PricewaterhouseCoopers) computer assurance practice in the North of England. Mr Holt is the senior non-executive director and chairman of the Audit Committee.

Mike Davies (59) Non-executive Director * (A) (N) (R)
Joined Pendragon in October 2004. He is the senior non-executive director of Taylor Woodrow plc and non-executive chairman of Marshalls plc. He also serves as a non-executive director on the boards of a number of private companies and has recently been appointed non-executive Chair of the Royal Mint. He is the chairman of the Remuneration Committee.

David Joyce (58) Non-executive Director (A) (N) (R)
Joined Pendragon on 1 March 2006. He is a civil engineer and chief operating officer of Vinci PLC (formerly Norwest Holst Group PLC).

Malcolm Le May (49) Non-executive Director (A) (N) (R)
Joined Pendragon on 1 March 2006. He is executive president of JER Partners Europe, an investment firm specialising in commercial property development in Europe and North America. Mr Le May is also a non-executive director of Royal & Sun Alliance Insurance Group Plc.

Trevor Finn (49) Chief Executive *
Joined the vehicle division of Williams PLC in 1982 and subsequently became divisional managing director. He was appointed chief executive of Pendragon prior to the demerger from Williams. He is also a non-executive director of Falcon Investment Trust PLC and of Automotive Skills Limited.

Martin Casha (46) Chief Operating Officer
Joined the vehicle division of Williams PLC in 1982 and subsequently became a group general manager. He was appointed operations director of Pendragon in September 1995 and chief operating officer in November 2001.

David Forsyth (50) Finance Director
Joined Pendragon in October 1997 from Lonrho PLC where, since 1986, he held a number of senior finance positions. He is a chartered accountant.

Hilary Sykes (46) Corporate Services Director *
Hilary Sykes is a solicitor and prior to joining Pendragon, advised the company as a corporate lawyer with Geldards LLP. She joined Pendragon in 1994 as company secretary and became a director in April 1999.

(A) Member of the Audit Committee
(N) Member of the Nomination Committee
(R) Member of the Remuneration Committee
† retires annually at the AGM, proposed for re-election
* retiring by rotation at the AGM, proposed for re-election

Secretary
Hilary Sykes

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Solicitors
CMS Cameron McKenna LLP
Geldards LLP

Auditors
KPMG Audit Plc

Bankers
Barclays Bank PLC
Lloyds TSB Bank plc
Royal Bank of Scotland plc

The directors present their annual report and the audited financial statements for the year ended 31 December 2006.

Results and dividends

The results of the group for the year are set out in the financial statements on pages 38 to 77. The directors recommend a final dividend for the year ended 31 December 2006 of 2.0 pence per ordinary share. Together with the interim dividend of 1.45 pence per share paid to shareholders on 3 October 2006, this brings the total dividend for the year to 3.45 pence per share. Subject to approval at the Annual General Meeting, the final dividend will be paid on 2 May 2007 to shareholders appearing on the register at the close of business on 10 April 2007. Total dividends paid in 2006 were £17.4 million, leaving retained profit for the year of £67.5 million. Movements in reserves are set out in note 20 to the financial statements.

Review of operations

A detailed review of the group's activities and future developments is presented in the Operational and Business Review on pages 2 to 13. In addition to the acquisition of Reg Vardy plc in February last year, the following businesses were acquired or disposed of during the year ended 31 December 2006.

Business	Location	Franchise	Date 2006	Status
Evans Halshaw	Edinburgh	Peugeot	February	Acquisition
Reg Vardy	Stourbridge	Volkswagen	March	Disposal
Reg Vardy	Stafford	Volkswagen	March	Disposal
Reg Vardy	Wolverhampton	Volkswagen	March	Disposal
Reg Vardy	Leicester	Volkswagen	March	Disposal
Reg Vardy	Redditch	Volkswagen	March	Disposal
Stratstone	Chesterfield	Volvo/Chrysler Jeep	March	Acquisition
Stratstone	Crewe	Volvo	March	Acquisition
Stratstone	Derby	Volvo/Chrysler Jeep	March	Acquisition
Stratstone	Mansfield	Volvo	March	Acquisition
Stratstone	Nottingham	Volvo	March	Acquisition
Stratstone	Nottingham West Bridgford	Volvo	March	Acquisition
Stratstone	Stoke on Trent	Volvo	March	Acquisition
Stratstone	Burton on Trent	Volvo	March	Acquisition
Stratstone	Stafford	Volvo	March	Acquisition
Evans Halshaw	Darlington	Peugeot/Citroen	September	Acquisition
Evans Halshaw	Huddersfield	Peugeot	December	Acquisition
Evans Halshaw	York	Peugeot	December	Acquisition
Evans Halshaw	Leeds	Peugeot	December	Acquisition
Stratstone	Luton	Land Rover	December	Disposal

Business review

Certain information required by the Companies Act 1985 to be included in the Directors' Report on business review is principally contained in the Operational and Business Review Report on pages 2 to 13. The Operational and Business Review principally covers the development and performance of the business and the external environment. Other disclosures required are contained within the Directors' Report, which includes the principal risks and uncertainties affecting the business and corporate social responsibility issues. The company has not disclosed certain specific non financial KPI's in the absence of relevant measures that have been measured consistently over the past two years. This will be addressed going forward.

Principal risks and uncertainties

We have set out below certain risk factors that we believe could cause our actual future Group results to differ materially from expected results. However, other factors could also adversely affect the Group results and so the factors set out below should not be considered to be a complete set of all potential risks and uncertainties. The risk factors outlined should be considered in connection with the statement on internal control and risk management in the Corporate Governance Report on pages 18 to 24. Health and safety is covered within the Corporate Social Responsibility Report on pages 25 to 26.

Business conditions and the general economy

The profitability of Pendragon's businesses could be adversely affected by a worsening of general economic conditions in the United Kingdom. Factors such as unemployment, the level and volatility of equity markets, interest rates, inflation, action taken by the UK government relating to the taxation of fuel for cars and the availability and cost of credit could significantly affect the market for the sale of new and used motor cars. In the case of new car sales during a period of economic downturn there is likely to be an oversupply of vehicles leading to reduced margins. Whilst a short term worsening in economic conditions in the United Kingdom should not significantly adversely impact profitability in our aftersales business, a sustained downturn over a number of years would be likely to lead to reduced profits in this area.

Franchise agreements

We operate franchised motor car dealerships. Franchises are awarded to us by the motor car manufacturers. Failure to continue to hold franchises could result in a significant reduction in the profits of the Group due to our inability then to source new car stock to sell, perform warranty repairs and display motor car manufacturer trade marks.

Vehicle manufacturer dependencies

We depend on the vehicle manufacturers' financial condition, marketing, vehicle design, production and distribution capabilities, reputation, management and industrial relations. Although we do not depend on any single vehicle manufacturer, a failure by a manufacturer in the areas noted could lead to significant losses especially in the case of the insolvency of a manufacturer. Vehicle manufacturers provide sales incentive, warranty and other programs that are intended to promote new vehicle sales. A withdrawal or reduction in these programs would have an adverse impact on our business.

Liquidity and financing

Liquidity and financing risks relate to our ability to pay for goods and services required by the Group to trade on a day to day basis. We have two main sources of financing facilities which are, from banks by way of committed borrowing facilities and from suppliers by way of trade credit. A withdrawal of financing facilities or a failure to renew them as they expire could lead to a significant reduction in the trading ability of the group.

Regulatory compliance risk

The Group is subject to regulatory compliance risk which can arise from a failure to comply fully with the laws, regulations or codes applicable, for example those set out by the Financial Services Authority. Non compliance can lead to fines, enforced suspension from sales of general insurance products or public reprimand.

Competition

We compete with other franchised vehicle dealerships, private buyers and sellers, internet based dealers, independent service and repair shops and manufacturers who have entered the retail market. We compete for the sale of new and used vehicles, the performance of warranty repairs, non warranty repairs, routine maintenance business and for the provision of spare parts. The principal competitive factors in service and parts sales are price, customer database, familiarity with a manufacturer's brands and models and the quality of customer service. We also compete with a range of financial institutions in arranging finance for vehicle purchases. Some of our competitors may have greater resources and lower overhead and sales costs.This could lead to our failure to be able to compete and result in a reduction in our profitability.

Reliance on certain members of management and staff

The Group is dependent on members of its senior management team and skilled personnel and the future financial well being of the Group could depend in part on our ability to attract and retain highly skilled management and personnel. The loss of the service of a number of such individuals could have a material adverse effect on the business. Additionally, if we fail to recruit and retain skilled staff it may not be possible to continue to grow the business.

Failure of information systems

Our businesses are dependent on the efficient and uninterrupted operation of our information technology and computer systems, which are vulnerable to damage or interruption from power loss, telecommunications failure, sabotage, vandalism or similar misconduct. Whilst we have put in place contingency and recovery plans in order to mitigate the impact of such failures it can never be certain that these plans could cover every eventuality or situation.

Reliance on the use of significant estimates

The company enters into leasing arrangements whereby it agrees to repurchase vehicles from their lessees or providers of lease finance at the end of the lease agreement which are typically two to four years in the future.The repurchase price is determined at the time the agreement is entered into based on the then estimate of a vehicle's future residual value. The actual value of the vehicles at the end of the lease contract and therefore the profits that the company can realise from their eventual sale could vary materially from these estimates due to changes in either the popularity or the reliability of the brand.

Directors The directors of the company are listed on page 14. Details of the terms of appointment and notice period of each of the current directors, together with their respective interests in the company's shares, appear in the Remuneration Report on pages 27 to 34. The Combined Code and the company's Articles of Association require directors to retire by rotation or, in the case of non-executive directors who have served more than nine years, annually. The notice to shareholders describes the business of the Annual General Meeting and includes details of the directors proposed for election or re-election. The directors in question are: Mr M T Davies, Mr T G Finn, Miss H C Sykes and Mr W W Rhodes each of whom, being eligible, will stand for re-election.

Substantial Shareholdings

At 8 January 2007 the directors had been advised of the following interests in the shares of the company:-

Shareholder	Shares	%
AXA Framlington Group Limited	49,158,115	7.49
Standard Life Investments	40,154,040	6.12
Lazard Asset Management LLC	38,881,190	5.93
Jupiter Asset Management Limited	34,651,410	5.28
The Bank of New York	33,791,378	5.15
JP Morgan Chase Bank/Nominees	30,155,346	4.60
Scottish Widows Investment Partnership	27,488,790	4.19
Barclays Global Investors (UK)	25,130,981	3.83
Legal & General Investment Management	24,015,191	3.66
Fidelity International Limited	23,271,695	3.55
Aviva Plc	19,619,210	2.99

Employee involvement

The company's approach to corporate social responsibility is set out on pages 25 to 26. No political donations were made (2005: £nil) and the company does not intend the company or any member of the group to make any such donations.

Payments to suppliers

The group's policy is to settle the terms of payment to its suppliers when agreeing the terms of the transaction and to abide by those terms, provided it is satisfied that the supplier has provided the goods or services in accordance with the agreed terms and conditions. The group has not adopted any specific code or standard on payment practice. The number of days' purchases outstanding for the payment by the group at 31 December 2006 was 66 days (2005: 82 days). The company had no trade creditors.

Repurchase of shares

Details of movements in the company's share capital are given in note 19 to the financial statements. At the Annual General Meeting on 28 April 2006 shareholders authorised the company to repurchase its own 25p ordinary shares† in the market. The company has not repurchased any of its own shares during the year. The authority is exercised only if the directors expect it to result in an increase in earnings per share.

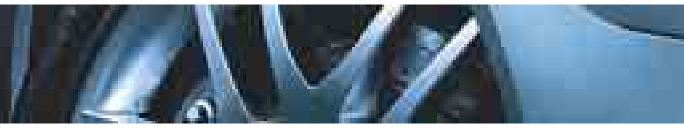
Auditors

KPMG Audit Plc has indicated its willingness to continue as independent auditor and a resolution concerning its reappointment will be proposed at the Annual General Meeting.

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 group's auditors are unaware; and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the group's auditors are aware of that information.

By order of the Board
H C Sykes
Secretary
15 February 2007

†Following an extraordinary general meeting of the company's shareholders held on the 22 December 2006, a sub-division of the company's ordinary shares was approved; the ordinary shares are now worth 5 pence each.



Compliance

Pendragon PLC is committed to maintaining high standards of corporate governance in line with the UK Listing Authority listing rules and its Board supports the principles of the Combined Code on Corporate Governance issued by the Financial Reporting Council ("the Code") which applies to financial years commencing on or after 1 November 2003. This statement, together with the Remuneration Report, on pages 27 to 34 below, explains how the company has applied the principles and complied with the provisions of the Code. The Board regularly reviews corporate governance matters, taking into account both guidance issued by bodies representing institutional shareholders and individual institutional shareholders' policies and feedback. Other than where expressly stated, the company has complied with the Code throughout the year.

Directors

The company and its group is managed through its board of directors. The Board is responsible for overall group strategy, acquisition and divestment policy, approval of major capital expenditure projects and consideration of significant financing matters. Through the company's divisional structure, the Board reviews the strategic direction of individual trading businesses, their annual budgets and their progress towards achievement of those budgets. The Board also takes charge of the company's standards in matters of corporate governance and policy matters affecting the company's stakeholders. The Board has overall responsibility for the group's system of internal control, including financial control and risk management and the group's records on matters of health and safety and environmental compliance. It is also responsible for approving appointments to the Board and of the company secretary and approving policies relating to directors' remuneration and severance. All matters of an operational nature and within the executive directors' capital expenditure authority are dealt with by the executive directors. Certain of the Board's duties are delegated to committees of the Board, whose responsibilities and composition are set out on pages 20 to 22 of this Report.

There is a clear separation of the functions of chairman and chief executive, recorded in a written statement reviewed annually by the Board and published on the Pendragon PLC website. This statement is also available for shareholders' inspection at the Annual General Meeting and at any time from the company secretary upon request.

The Board operates to a standing agenda which ensures that all matters reserved for its decision are dealt with in an appropriate manner, and all matters requiring regular or annual review receive adequate scrutiny and debate. Between meetings, information packs containing key performance data are circulated to directors. The chairman holds meetings with the non-executive directors without the executives present when he deems it appropriate. In addition to formal meetings of the Board, informal meetings to familiarise with particular operations or address strategic matters are held as dictated by the requirements of the company's business and any new developments. The attendance of directors at meetings of the Board and (where applicable) its committees during the year is set out in the table below. The informal meetings of the Board and meetings held in addition to the timetabled meetings are shown as "Ad hoc".

Board and committee attendance*

Director	Board	Ad hoc	Audit	Nomination	Remuneration	Total
Sir Nigel Rudd (N)	9/9	1/1	n/a	1/1	n/a	11/11
W W Rhodes (N)	9/9	1/1	1/1‡	1/1	3/3‡	15/15
N G Hannah (N)†	8/9	1/1	1/1‡	1/1	2/3‡	13/15
J H Holt (A, N, R)	9/9	1/1	4/4	1/1	4/4	19/19
M T Davies (A, N, R)	9/9	1/1	4/4	1/1	4/4	19/19
D A L Joyce (A, N, R)	7/7**	n/a**	3/3**	1/1**	1/1**	12/12
M J Le May (A, N, R)	7/7**	n/a**	3/3**	1/1**	1/1**	12/12
T G Finn	9/9	1/1	n/a	n/a	n/a	10/10
M S Casha	9/9	1/1	n/a	n/a	n/a	10/10
D R Forsyth	9/9	1/1	n/a	n/a	n/a	10/10
H C Sykes	9/9	1/1	n/a	n/a	n/a	10/10

(A) Audit Committee member (N) Nomination Committee member (R) Remuneration Committee member

***** Attendance is displayed showing the number of meetings attended out of the total directors were eligible to attend e.g. 19/19 means 19 out of the 19 meetings held were attended

† Mr N G Hannah retired from the Board on 31 December 2006.

‡ Mr N G Hannah and Mr W W Rhodes were members of the Remuneration Committee and Audit Committee until the 28 April 2006 (the date of Annual General Meeting); they were therefore eligible to attend those Committee meetings held between 1st January 2006 and 28 April 2006. There were 3 meetings of the Remuneration Committee and 1 meeting of the Audit Committee during this period.

** Mr D A L Joyce and Mr M J Le May were appointed to the Board 1st March 2006; they were therefore not eligible to attend meetings held between 1st January 2006 and 1st March 2006.

The names, brief biographical details and Committee appointments of each of the directors appear on page 14. The company has not identified any individual as deputy chairman. The senior non-executive director has met with the other non-executive directors, without the chairman present, to conduct the annual appraisal of the chairman's performance during the year. Directors have the opportunity at each meeting of the Board, and informally between meetings, to raise any concerns they may have regarding the way the company is being run or any proposed course of action. Any such concerns, if voiced at a meeting of the Board or any of its Committees, would be recorded in the minutes. No such concerns have been raised during the year.

The company supports the principles of the Code regarding Board balance and the ability of Board members to bring to bear an independent judgement on the matters put before them. In recognition of this principle, the appointments of Mr D A L Joyce and Mr M J Le May became effective on 1 March 2006. For 2006, the Board comprised four executive directors and six non-executive directors, of whom four are considered by the Code to be independent, and the chairman. Mr D A L Joyce and Mr M J Le May became members of the Audit, Nomination and Remuneration Committees. Following the Annual General Meeting in 2006, both Mr N G Hannah and Mr W W Rhodes stood down from the Audit Committee and the Remuneration Committee. Each of the Audit and Remuneration Committees were then composed entirely of non-executive directors treated by the Code as independent. In line with provision B2.1 of the Code, Sir Nigel Rudd re-joined the Remuneration Committee with effect from the 1 January 2007. Mr N G Hannah retired from the Board on 31 December 2006.

Independence

In the view of the Board, every non-executive director serving during the year has demonstrated the required degree of independence, both in character and judgement, taking into account all the relevant circumstances. The appointment of Mr M J Le May and Mr D A L Joyce as non-executive directors in March 2006 means that at least half the board, excluding the chairman, now comprises non-executive directors determined by the board to be independent. Due to the rebuttable presumption in the Code that a director who has served on the board for more than nine years is not independent, two of the directors, Mr W W Rhodes and Mr N G Hannah would not, due to their long service, be treated by the Code as independent, unless the company were able to rebut such presumption. The company continues to regard each of Mr W W Rhodes and Mr N G Hannah as independent, for the reasons set out below. The only matter relevant for consideration in relation to Mr W W Rhodes is the duration of his appointment as a director, which commenced in 1989. The Board considers that, notwithstanding his length of service, Mr Rhodes remains independent in character and judgement and continues to be committed to his role. Mr N G Hannah who served as a director throughout the year and had continuous service as a non-executive director for over nine years left office on 31 December 2006. In recent years he received a retainer for property related advice to group companies, negotiated on arms' length terms, which is subject to annual review. Mr Hannah is also non-executive chairman of one of the company's commercial property advisers, Innes England Limited. Property advisers to the company are selected through a rigorous tendering process and the allocation of work among the respective advisers is regularly reviewed. This transparent and objective process ensures that at all times the company's dealings with Innes England Limited are at arms' length. Details of the additional services provided to group companies by Mr Hannah and of his association with Innes England Limited appear on page 76. The amounts of payments are not regarded by either party as material and this relationship and the retainer arrangements are not regarded by the Board as having affected Mr N G Hannah's independence. Notwithstanding his length of service, the Board considers that Mr N G Hannah remained independent in character and judgement. Other than as set out above, there are no relationships or circumstances in relation to any director which are regarded by the company as having the potential to affect his exercising independent judgement.

Board composition and effectiveness

The Board reviews annually the composition of the Board and its Committees and the respective contributions of each director. The effectiveness of the Board and Committee structure is considered, together with the adequacy and appropriateness of the skill set of the Board, taking into account any new developments in the company's business or strategy, and the range of expertise, knowledge and experience represented. The latest of these reviews concluded that the Board and its Committees were operating effectively and that in particular, the clear demarcation of the respective responsibilities of the individual directors, the Committees and the Board contributed strongly to their effective operation. The Board also concluded that the skills and experience present are appropriate to the company's business activities and provide adequate oversight of the assessment and management of risk.

All directors seek election to the Board at the Annual General Meeting following their appointment. In accordance with the company's Articles of Association, all directors seek re-election by rotation at least once every three years.

For the year under review, the Board has evaluated the performance of each director. The non-executive directors, led by the senior non-executive director and assisted by the chief executive have reviewed the performance of the other executive directors, the non-executives have reviewed the performance of the chief executive, and the Board has reviewed the performance of the non-executive directors.

Each non-executive director's performance in furthering the company's objectives was assessed, together with his contribution in his areas of expertise, reflected in his Committee work, participation in Board discussion and, where applicable, familiarisation visits. Attendance at meetings was also considered.

The evaluation of the non-executive directors also addressed their capability, time commitment and, where applicable, effectiveness in the role of Committee chairman. The assessment of executive directors covered two aspects of performance: the director's individual contribution towards achievement of the company's goals; and the achievement of individual objectives appropriate to his or her role.

The performance review of the chairman was conducted by the non-executive directors led by the senior non-executive director. They considered the responsibilities of the role as set out in the Code, including capability, time commitment, effectiveness and shareholder communication.

The chairman's principal commitments outside the company as at February 2007 were as non-executive chairman of Alliance Boots plc, deputy chairman of Barclays PLC, non-executive director of BAE Systems PLC, and chairman of the Boardroom Issues Group of the Confederation of British Industry. The Board is satisfied that the chairman and each non-executive director is able to devote the amount of time required to attend to the company's affairs and his duties as a Board member.

Information and advice

The directors regularly receive financial and other information concerning the group's activities, plans and performance. Each director is entitled on request to receive from the company information to enable him to make informed judgements and adequately to discharge his duties and has access to the advice and services of the company secretary on all matters of Board procedures and corporate governance. The company secretary also provides advice and support to each of the Board's Committees and, in particular, to the chairman on all corporate governance matters. The directors' terms of appointment also permit them, at the company's expense, to take independent professional advice in connection with their duties.

In line with common practice, the company maintains insurance cover in respect of the liability of its directors and officers to third parties.

Professional development

The Board includes individuals from various backgrounds with many years' experience of senior positions either in listed companies or professional life. In carrying out their duties, the directors are expected to bring to bear an independent judgement on issues of strategy, performance, resource and standards of conduct. New Board members receive an induction tailored to their needs. An induction information pack, comprising constitutional documents, terms of reference and historical and accounting information is provided and operational site visits are undertaken to familiarise with the group's business. Where appropriate, both upon appointment and subsequently, formal training by external providers in matters such as the duties of directors, pension trusteeship and corporate governance is arranged. All directors are encouraged to maintain an awareness of new developments in the areas of the group's principal activities and attend appropriate briefings on individual aspects of the group's business or new developments. Where necessary, directors have access to professional training relating to their Board or committee functions. During the year, the chairmen of the Audit and Remuneration Committees have attended specialist briefings on issues relevant to their professional development and the business of their committees.

Board Committees

The Board delegates certain matters to committees of the Board, each of which operates under written terms of reference. These, together with the Committees' membership, can be found on the Pendragon PLC website.

Nomination Committee

The Committee is composed of the non-executive directors, meets at least once a year and its chairman is Sir Nigel Rudd. In 2006 it met once. The Committee is responsible for leading the process for appointments to the Board. The Committee and the Board operate to a protocol for the selection and appointment of executive and non-executive directors. This includes a six stage process, from the identification of the vacancy to the making of a recommendation to the Board for an appointment. Having identified a vacancy, the Committee assesses the current skills profile of the Board and produces a skills profile for the vacant position, with the aim of strengthening and enhancing the skills, knowledge base and experience of the Board. The need to advertise the vacancy or engage executive search advisers is considered. Interviews with short-listed candidates follow, conducted by an appropriately constituted panel of directors, comprising a majority of non-executive directors and excluding directors with any personal or business connection to the candidates. All Board members are given the opportunity to meet a recommended candidate before a nomination is put to the Board. The appointments of Mr M J Le May and Mr D A L Joyce were made in accordance with this selection and appointment protocol.

Remuneration Committee

The Chairman of the Remuneration Committee, Mr M T Davies, is an independent non-executive director. The Committee is composed of the non-executive directors and meets at least once a year. The retirements of Mr N G Hannah and Mr W W Rhodes following the Annual General Meeting held in April 2006, and the appointments of Mr D A L Joyce and Mr M J Le May, ensured that the Committee was comprised entirely of non-executive directors considered by the Code to be independent. In 2006 it met four times. The Committee has responsibility for determining the remuneration packages of the executive directors in the context of the policy adopted by the Board. It also liaises with the Nomination Committee to ensure the remuneration packages set for new executive directors are consistent with the company's overall remuneration policy. It sets the targets for any performance related pay schemes applicable to executive directors and determines the policy for and scope of pension agreements, termination packages and compensation commitments for the executive directors. It is also responsible for ensuring that due regard is given to best practice in matters of executive remuneration and that the company complies with all applicable regulations relating to executive remuneration. In 2006, the Remuneration Committee oversaw the introduction and implementation of a Long Term Incentive Plan ("LTIP"), the full details of which can be found on pages 27 to 30 of the Directors' Remuneration Report.

The Directors' Remuneration Report is considered by the Remuneration Committee, but adopted by the Board as a whole. That Report is set out on pages 27 to 34.

Audit Committee

The Committee is chaired by Mr J H Holt who is also the senior non-executive director. It is composed of the non-executive directors of the company (except the chairman). The retirements from the Committee of Mr N G Hannah and Mr W W Rhodes following the Annual General Meeting held in April 2006, and the appointments of Mr D A L Joyce and Mr M J Le May, ensured that the Committee was, and continues to be comprised entirely of non-executive directors considered by the Code to be independent.

Mr J H Holt is regarded by the Board as having recent and relevant financial experience, due to his lengthy career in accountancy, with PricewaterhouseCoopers, and as a result of his regular attendance at appropriate continuing professional development seminars. Meetings of the Audit Committee are held at least three times a year and are attended, by invitation, by the finance director, the head of the internal audit function and representatives of the company's external auditors, at the chairman's discretion. The Committee met four times in 2006.

Committee Activities

The meetings in February and August take place in advance of the preliminary and interim results announcements. At these meetings, the Committee considers the draft financial statements and the preliminary and interim results announcements. It also considers the report of the external auditors on the full-year audit, concentrating on issues of judgement and audit focus identified in the audit plan. Additional meetings, held in June and November, are concerned primarily with the review of the business risk management process, the outcomes from risk control visits, and the effectiveness of the visit plan for the current year, as well as the external audit plan for the year, the audit fee and other significant corporate governance issues, such as those with Financial Services Authority (FSA) implications. In particular, during 2006, systems of internal control and monitoring relating to FSA regulated products (particularly general insurance products) sold by the group were reviewed.

At each meeting attended by the external auditors, the members of the Committee have the opportunity for discussion with the auditors without the finance director or internal audit leader being present. This permits any issues to be reviewed with, and assurances to be sought from, the external auditors independent of executive management involvement. The chairman of the Committee also makes himself available for meetings with the leader of the company's internal audit function to allow issues concerning controls and, in particular, the working and resourcing of the internal audit function, to be reviewed. The Committee's terms of reference are published on the Pendragon PLC website and, in summary, include responsibility for: monitoring the integrity of the company's financial statements and any formal announcement relating to the company's financial performance; making recommendations to the Board in relation to the appointment and removal of the external auditors, reviewing the external auditors independence and objectivity and the effectiveness of the audit process, and developing and implementing the company's policy on the engagement of the external auditor to provide non-audit services. The Committee is also responsible for reviewing the company's internal financial controls and system of internal control and risk management, monitoring and reviewing the effectiveness of the company's internal audit department and ensuring adequate levels of staffing and ensuring that the company's systems of control as they relate to activities regulated by the Financial Services Authority are adequate and functioning properly and are adequately resourced.

The review of the arrangements for employees to raise, in confidence, concerns about possible improprieties in relation to financial reporting or other matters also falls within the Audit Committee's responsibilities. The Committee reviews at least once annually the company's whistleblowing policy and its procedures for the reporting and recording of suspected fraud and dishonest acts. These items also form part of the Committee's standing agenda. Throughout 2006, following the Committee's review, further improvements to the company's procedures were made, particularly in the areas of FSA compliance, Anti-Fraud, Theft and Corruption, whistleblowing and Anti-Money Laundering. The company's Anti-Fraud, Theft and Corruption Policy and Anti-Money Laundering Policy is available on the company's website.

During the year the Committee chairman has carried out an evaluation of the independence of the company's external auditor KPMG Audit Plc and reviewed the effectiveness of the external audit process. Matters addressed in the evaluation included an assessment of the quality of communication between the external auditor and the Audit Committee, the manner in which the relationship between the auditor and the company is managed and the ability of the auditor to challenge practices and procedures and to communicate appropriately with the company on any significant control weakness discovered in the course of their audit work. Also considered were the level of non-audit services provided by the external auditor and the potential this may have to impair the independence of the audit. The effectiveness of the internal audit function has also been formally assessed. The views of management and of the external auditor have been taken into account in the review of the internal audit function and the views of management have been taken into account in the review of the external auditor. Each review concluded that the functions were performing effectively.

The Committee has considered the policy in relation to the supply of non-audit services by the company's auditor during the year. The company's policy is not to exclude its auditor from undertaking non-audit work, but to permit the supply of such services in areas where, in the opinion of the Committee, it is appropriate to do so. The objective of the policy is to ensure that non-audit work is carried out in a way that affords full value for money, whilst obtaining a service that best serves the interests of the company. Contracts for non-audit work are not therefore awarded to the company's auditor where there is a perceived conflict of interest. Where appropriate, the provision of non-audit services is formally market tested through a tender process. The Committee has during the year reviewed the independence and objectivity of the external auditor, taking into consideration relevant professional and regulatory requirements with the aim of establishing that these are not impaired by the provision to the company of non-audit services.

During the year the company's auditor provided non-audit services as reporting accountants on the acquisition of Reg Vardy plc. Non audit fees for 2006 were higher than usual, mainly as a result of the significant work undertaken on permissible non-audit services including acting as reporting accountants to the company on the sale and leaseback of certain properties to the company's joint venture, PPH0 Limited. KPMG LLP also continued as advisers to, and actuary for, the company's various occupational pension schemes, details of which appear in the Remuneration Report on page 28, having been selected by competitive tender.

A full statement of the fees paid to KPMG Audit Plc and KPMG LLP for audit and non-audit services is provided in note 3 to the financial statements on page 51. The Committee has concluded that the provision of these services has not impaired audit independence.

System of internal control

The Board is ultimately responsible for maintaining a sound system of internal control and for reviewing its effectiveness. The Board has adopted a risk-based approach to establishing a sound system of internal control. The system of control has been in place throughout the year. High level risk assessment occurs at one meeting of the Board during the year in the context of the company's annual strategic review. Operational management is charged with responsibility for identifying and evaluating risks facing the group's businesses on a day-to-day basis. In establishing and maintaining the company's system of internal control, the Board has paid due regard to the Turnbull Guidance on risk management and internal controls.

The Board's process for satisfying itself of the effectiveness of the system of internal control relies on: assurance from executive management with regard to the design, communication and implementation of controls and provision of monitoring information; and assurance from the Audit Committee on the regular monitoring of the system and correction of any material control failures. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can provide only reasonable and not absolute assurance against material misstatement or loss. The Board has during the year reviewed all relevant risk areas and the system of internal controls and received reports on new risks and changes to the existing risks, based on the following broad areas:-

- financial
- physical
- transactional
- technological
- socio-economic
- political and regulatory
- reputational

Operational management is supported in its role by a multi-disciplinary team, known as the Risk Control Group. This group is formed from senior representatives of the central finance, internal audit, information technology, legal, insurance and human resources function and meets at least four times a year. During 2006, the Group met four times. It is attended by invitation by the chairman of the Audit Committee and representatives of the external auditor, at the discretion of the chairman. Its responsibilities include the regular review of risks, the identification of the need for corresponding controls and the monitoring of the design, communication and implementation of new controls and adaptation of existing controls to improve their effectiveness. The Risk Control Group has a reporting line direct to the main Board. The internal audit function reports on matters of financial control each month directly to the Board.

Major commercial, technological and financial risks are assessed at the Board's annual planning meeting, which reviews the company's principal areas of business and considers any adaptation to the company's business strategy required to meet specific commercial and other risks or threats. The conclusions are incorporated in the company's business strategy and formally adopted by the Board.

The Board has established a strong control framework within which the group operates. This contains the following elements:

Management structure

Pendragon is a large multi-franchise retailer of motor vehicles and ancillary services. During 2006, following the acquisition of Reg Vardy plc, the group has implemented a divisional structure. Today, the group consists of two principal operating divisions; Stratstone, which represents our luxury franchises and Evans Halshaw which represents our volume franchises and five support divisions (Information Technology, Parts Supply & Distribution, Finance & Insurance, Leasing and Marketing) each headed by a Divisional Managing Director. Each Divisional Managing Director participates in a bi-monthly operational review meeting, chaired by the Chief Operating Officer. Best practice meetings for each division, at which key operating controls and improvements to their implementation are discussed, are generally held monthly, chaired by the Divisional Managing Director for the division.

Communication

There is an embedded culture of openness of communication between management and the Board on matters relating to risk and control. Face-to-face and video-conferencing meetings of all operational teams occur regularly. Processes are reinforced at operational meetings and via the company's intranet and video communications.

Financial reporting

The group operates to comprehensive management reporting disciplines which involve the preparation of financial plans by all operating units. The plans are reviewed by executive management and are subsequently passed to the Board for approval. Monthly actual results are reported against the approved plans.

Investment appraisal

The group has a clearly defined framework for capital expenditure including appropriate authorisation levels, beyond which such expenditure requires the approval of the executive directors and, for larger capital projects, acquisitions and disposals, the Board. There is a prescribed format for capital expenditure applications which places heavy emphasis on the commercial strategic logic for the investment and demands a detailed financial presentation of the business case.

Functional reporting

The group has identified a number of key areas which are subject to periodic reporting to the Board. These areas are given particular emphasis through the operation of appropriately constituted teams which meet regularly, and report to the Board via a designated executive director. These include the following central functions: group finance, treasury, corporate tax, value added tax, health and safety, human resources, information systems, internal audit, insurance, legal, payroll, property, security and training.

Risk Control

The work of the risk control group is described on page 23. Its remit includes the identification and assessment of new risks facing the group's businesses, business continuity planning and the establishment of policies and procedures for risk control for implementation in the group's businesses. It has the power to co-opt representatives from the group's operating business to assist in the design of new controls and the improvement of existing ones. A twice-yearly review of the risk control group's work is included in the Board's agenda.

Processes, responsibilities and monitoring mechanisms and frequencies are defined and communicated to the directors and executives concerned and a regular pattern of meetings and reporting requirements established to ensure that the Board is sufficiently informed of risk management measures to enable them to review the effectiveness of the group's systems of internal control.

Going concern

The directors are satisfied that the group is in a sound financial position with adequate resources to continue in operation for the foreseeable future. In forming this view, the directors have reviewed budgets and other financial information. The financial statements of the group have therefore been prepared on the basis that the group is a going concern.

Shareholder relations

The Board as a whole takes responsibility for ensuring that the company is engaged in dialogue with shareholders which is constructive and fosters mutual understanding of the company's and shareholders' objectives. The Board's statement concerning the respective roles of chairman and chief executive also deals with the company's approach to shareholder communication and is available on the Pendragon PLC website. The chief executive, Mr T G Finn, is responsible for implementation of the strategy set by the Board. Among his duties is the conduct of communications with shareholders on the company's performance. He must ensure that major shareholders have the opportunity for regular dialogue with the company on issues of concern to them, and, in particular, that any changes in policy or strategy are effectively articulated to shareholders. In the main, shareholder communication is based around meetings with shareholders at key points in the financial reporting year. These are conducted by the chief executive and the finance director, rather than the non-executive chairman. In this respect the company's approach is not compliant with the Code. The directors believe this to be the most practical and efficient way of communicating on matters such as strategic direction, financial performance, underlying market conditions and operational issues. Issues raised by shareholders on these occasions are carefully noted and fed back to the Board, and, where appropriate, access to the chairman for further discussion is arranged. Each of the chairman and the senior non-executive director also holds himself available at all times for contact with shareholders. Unless specifically requested to participate in discussions or to provide information and explanations, each of them will, however, refer enquiries he receives to the chief executive. If the matter concerns the chairman's remuneration or performance or any other matter with which it is inappropriate for him to deal, it is referred to the senior non-executive director. During 2006, both private and institutional shareholders have undertaken tours of the company's Loxley House facility to view the technological advances now incorporated into the company's business model for its car retail operations. The Board is always willing, where practicable, to enter into dialogue with shareholders based on mutual understandings of their respective objectives and being mindful of the company's obligations under the listing rules. The respective chairmen of the Audit Committee, the Nomination Committee and the Remuneration Committee are available to answer shareholders' questions at the Annual General Meeting ("AGM").

Business at the Annual General Meeting

As well as dealing with formal business, the company takes the opportunity afforded at the AGM to provide up-to-date information about the company's trading position and to invite and answer questions from shareholders on its policies and business. At the AGM a separate resolution is being proposed for each substantive matter. The company's annual report and financial statements are despatched to shareholders, together with the Notice of Annual General Meeting, giving the requisite period of notice. The business being proposed at the AGM is summarised in the Notice of AGM, at page 87 of this report.

Philosophy

Our culture is about the way we behave as an organisation. As a large employer and provider of goods and services to many thousands of customers, Pendragon PLC and its group touch the lives of many. As the occupier of hundreds of business premises and a customer of a wide range of businesses the group benefits from and contributes to relationships with many suppliers and communities. Pendragon believes that long term success in business is greatly enhanced by valuing and developing relationships with key stakeholders. As a company, we operate within a framework of five core values, which recognise the broad needs and aspirations within each relationship. These values are the foundation of our culture and by ensuring that these values are known and understood, we can ensure that they can be applied by team members across all divisions and at all levels of the organisation.

Values

The company has adopted value statements which reflect the stakeholder groups. For each, Pendragon's vision is to be "the Number One Choice". Employees are encouraged to see themselves as part of a team, hence the expression "team member" is used for all those working within the group's businesses. Team members are introduced to the Pendragon vision and values on joining and through regular communication, which reinforces the company's philosophy and approach.

The Pendragon Vision

to be "the Number One Choice"

Our Customers

we provide a good value, personalised service to existing and potential customers

Our Manufacturers

we provide quality, brand focused representation, meeting mutual aspirations of customer retention and sales volume

Our Suppliers

we provide long term, profitable partnerships in return for quality service and competitive pricing

Our Team Members

we provide secure, satisfying employment, recognising the contribution of each individual to the success of our business

Our Shareholders

we provide the best earnings per share performance over a rolling 5 year view against defined sector competition

Involvement and development

The group recognises the importance of good communications and relations with its team members, as its ability to meet the needs of its customers in a profitable and competitive manner depends on the contribution of team members throughout the group. Team members are encouraged to develop their contribution to the business wherever they work. In many areas ongoing programmes, focused on quality and customer service, provide an opportunity for everyone to be involved in making improvements and in developing their own skills to that end. The company has been awarded Investors in People accreditation, first achieved in 1999, and renewed in 2006.The company's well-established practices in encouraging team member development and involvement provide substantial support for the renewal of this award.

Pension Trusteeship

Team member involvement also extends to the boards of trustees of the company's various occupational pension schemes, details of which appear on page 33 within the Remuneration Report. A total of seven employee representatives, who broadly reflect the businesses from which scheme beneficiaries originate, served either directly as trustees or as directors of the schemes' corporate trustees during the year.

Share schemes and incentives

Team members' financial participation is encouraged through the company's Sharesave scheme, which attracts membership from all levels within the group's business. A variety of bonus schemes provide team members with rewards linked to the growth and prosperity of the business. At 31 December 2006 a total of 2,760 team members (18%) participated in ownership of shares and/or schemes linked to the company's share performance.

Community

As a multi-site, predominantly retail operator, the group's community involvement is generated by its local businesses, which contribute to their local areas in a variety of ways. During the year dealerships have also responded to international humanitarian crises by holding fund-raising events. Closer to home, local schools, hospitals and medical charities as well as Comic Relief and the BBC's Children in Need Appeal have all been beneficiaries of charity events organised by team members. The company supports and encourages these activities and welcomes the opportunities they present for team-building within the businesses and relationship-building with the communities they serve.

Environment

Although not generally regarded as a high environmental impact sector, motor retailing and its associated aftersales service activities carries with it a range of responsibilities relating to protection of the environment. The company's policy is to promote and operate processes and procedures which, so far as is reasonably practicable, avoid or minimise the contamination of water, air or the ground; and to manage responsibly the by-products of our activities, such as noise, waste packaging and substances and vehicle movements. The company's statement of environment policy is available on the Pendragon PLC website.

Health and safety

The company recognises its responsibility to all team members and others working in or visiting its facilities to provide, so far as is reasonably practicable, an environment which is safe and without risk to their health. The company's policy is to identify all potential hazards and assess the risks presented by its activities and to provide systems and procedures which allow team members at all levels to take responsible decisions in their day to day work in relation to their own and others' health and safety. The company's health and safety policy is available on the Pendragon PLC website.

In matters of health and safety, the company promotes awareness of potential risks and hazards and implementation of corresponding preventative or remedial actions through its on-line health and safety systems, operations manuals and regular communication on topical issues. A clear hierarchy of responsibility is published to team members and reinforced through regular on-site monitoring. Team members are supported in discharging their responsibilities by specialist guidance from the company's health and safety function and a recently introduced on-line training tool.

Disabled People

The group recognises its responsibilities in employing and training people who are disabled, not all of whom are formally registered disabled persons in UK terms. If any team member becomes disabled it is standard practice, in all but the most extreme circumstances, to offer an alternative job or adapt the existing job and provide retraining where necessary.

Equal Opportunities

The quality of the company's relationships with its stakeholders will, in large measure, determine its success. Critical to those relationships is its ability to attract, motivate and retain the best team members. The company's policy is to ensure that team members achieve their full potential within the business and that all employment decisions, from the advertisement of a vacancy through to the offer of development opportunities and further advancement, are taken without reference to any form of discriminatory criteria. The company's equal opportunities policy is available on the Pendragon PLC website. Vacancies are first advertised internally on the Pendragon intranet to maximise the opportunity for career progression within the group. The company's bonus and incentive programmes are carefully researched and designed to ensure they are tailored to match reward to performance and recognise outstanding contributions to the group's business.

Remuneration Committee

The remuneration policy is determined by the Board and is described below. During 2006, the composition of the Remuneration Committee changed, with Mr M J Le May and Mr D A L Joyce joining the Committee following their appointment to the Board on the 1 March 2006, and Mr N G Hannah and Mr W W Rhodes retiring from the Committee immediately following the 2006 Annual General Meeting. At the 31 December 2006, the Remuneration Committee of the Board was composed of the non-executive directors Mr M T Davies (Chairman), Mr J H Holt, Mr M J Le May and Mr D A L Joyce (the "Committee"). In February 2007, Sir Nigel Rudd rejoined the Committee as a member.

The Committee recommends to the Board the specific remuneration packages for executive directors. All of its recommendations made to the Board during the year were accepted. The Committee meets as often as necessary to discharge its duties, which during 2006 was four times. Details of members' attendance are set out in the Corporate Governance report on page 18.

Advisers

New Bridge Street Consultants LLP, who are independent remuneration consultants continue to provide specialist advice to the Committee. They provided no other type of services to the Pendragon group. During 2006, Sir Nigel Rudd and Mr T G Finn, provided internal advice to the Committee but not in respect of their own pay. The secretary to the Committee is Hilary Sykes.

Remuneration Policy

A summary of the Committee's conclusions and policies implemented during the year were:

- Annual bonuses will be linked with corporate performance targets, and capped at 100% of salary for exceptional performance;
- Introduction of a new Long Term Incentive Plan following approval by shareholders at the 2006 AGM, with a matching element of share based incentives;
- A cost-neutral alternative of a salary supplement in lieu of continued membership of the company pension scheme was offered to executive directors.

The Committee reviewed its remuneration policy at its February 2007 meeting and concluded that it remains appropriate and supports the corporate strategy.

The Company's policy on non-executive directors' remuneration is reviewed annually by the Board. Remuneration for non-executive directors is confined to basic salary without a performance related element. Non-executive directors may elect to receive all or part of their remuneration in the form of benefits in kind, typically the provision of a motor vehicle for their use. The Company did not remunerate the Chairmanship of Board committees during 2006. For 2007, the Chairmen of the Board committees will be remunerated commensurate with the extra time commitment and responsibility involved. During 2007, the Renumeration Committee will review the fees payable to the Chairmen to ensure that these are consistant with the size of the Company and the time commitment required.

Total remuneration

The Company's policy in respect of executive director's remuneration recognises the need to attract and retain directors with levels of remuneration that are arrived at responsibly and reflect their individual contribution and value to the Company.

The remuneration policy places great emphasis on ensuring that the executive directors' incentive arrangements have the potential to provide a greater reward than base salary. Combined with an approach that requires all incentive arrangements to be linked directly to business specific measures, this ensures that rewards will be based on the continued creation of shareholder value.

Further, in order to promote retention and sustained corporate performance, an equal emphasis will normally be placed on short-term and long-term rewards.

Importance of share ownership

The company recognises the importance and value of having executive directors who are significant shareholders in the company.

To promote this goal for the next generation of executive directors, during 2005, the company adopted share ownership guidelines. These guidelines encourage executive directors to hold shares worth 100% of salary (200% of salary for the chief executive) within three years of being appointed to the Board.

The following table shows the directors' interest in shares (not subject to audit):

	31 December 2006 Shares	31 December 2005 Shares
Sir Nigel Rudd	9,400,000*	9,150,000
T G Finn	14,711,905	14,515,635
M S Casha	4,466,010	4,119,185
W W Rhodes	3,283,360	3,283,810
D R Forsyth	1,582,400	1,506,510
H C Sykes	1,637,500	1,066,635
N G Hannah	990,865	990,865
J H Holt	125,000	125,000
M T Davies	100,000	100,000
D A L Joyce	25,000	25,000†
M J Le May	19,000	19,000†

†At date of appointment to board, 1 March 2006.

*Other than the acquisition of 100,000 shares by Sir Nigel Rudd on 15 February 2007 (not reflected above), there were no changes to the directors' interests shown above between 31 December 2006 and the date of this report. The table above displays interests in shares following the share split on the 22 December 2006.

Base salary

Base salaries are reviewed annually and are set by reference to the individual's skill, experience and contribution. The 2006 salaries were provisionally set on this basis and then New Bridge Street Consultants were then asked to review them against the market. The Committee was reassured by this exercise and is satisfied that the variable pay opportunity outweighs the salary positioning. 2007 salaries are to be reviewed by the Remuneration Committee in early 2007, again with appropriate benchmarking and with reference to individual's skill, experience and contribution.

Benefits

Life assurance, private health cover, professional subscriptions, contribution to home telephone costs and the provision of two cars, one of which is fully expensed, are provided to the executive directors.

Pensions

During the course of 2006, and in response to the A-Day pension reforms, the Committee offered the executive directors the choice of withdrawing from the Pendragon Pension Plan in respect of future pension accrual and instead receive a payment in lieu of pension contribution. By 31 December 2006 all of the executive directors had decided to leave the Pendragon Pension Plan.

In calculating the level of the payment in lieu of pension contribution the Committee was mindful to ensure that the net effect would be broadly cost neutral for the company, with the payment based on the expected cost of funding the current defined benefit pension promise. This has translated to a payment of circa 26% of salary for executive directors who opt for this choice. The payment will not be consolidated into base salary for the purposes of future annual bonus payments and long term incentive awards, but will be maintained as a percentage of base salary.

Annual bonus

For 2006, the Committee concluded that the executive directors' annual bonus potential will be based on corporate financial measures. The executive directors can earn up to 100% of salary in any one year on a sliding scale with 50% being awarded for achieving expected results and a further 50% for outstanding performance. Bonus awards at the highest available percentage of salary are made only upon achievement of outstanding performance. Bonuses are not pensionable. For 2006, the corporate financial measures used in determining bonus were adjusted profit before tax (weighted at 40%), gearing (weighted at 30%) and a measure of the success of the integration of Reg Vardy plc (weighted at 30%). For 2007, the corporate financial measures used in determining bonus will be adjusted profit before tax (weighted at 40%), gearing (weighted at 30%) and a personal performance objective specific to each executive director (weighted at 30%).

Equity incentives

At the Annual General Meeting, shareholders approved the adoption of a new Long Term Incentive Plan ("LTIP"). The key features are:

- each year, commencing with bonuses paid in 2006, an executive director may choose to re-invest his annual bonus in purchasing Pendragon shares or buy shares from his own personal resources of an amount up to 100% of salary (referred to as "Investment Shares"), which will then be matched with an award over shares with the same pre-tax value as the monies used to buy the shares;

- matching share awards will vest on the third anniversary of their grant date (a) provided the executive is still employed by Pendragon; (b) to the extent that a performance condition has been satisfied; and (c) to the extent that the associated shares purchased by the executive have been retained for the three years;

- the performance condition or conditions will be tailored to the long-term performance of the company and, for the 2006 and 2007 awards, adjusted earnings per share ("EPS") growth targets will be used:

EPS growth per annum	Vesting percentage
less than RPI + 4%	0%
RPI + 4%	30%
RPI + 10% or more	100%
between RPI + 4% and RPI + 10%	straight-line vesting between 30% and 100%

- the Company has chosen adjusted EPS on the performance measure because:-
  - the Company has relatively few direct competitors and therefore choosing a total shareholder return peer group would be problematic
  - EPS is the most common internal performance measure used in the market by companies of a similar size to Pendragon
  - the EPS performance condition is considered to be very stretching

- additionally, under the LTIP, the executive may be granted performance share awards worth up to 100% of base salary per annum;

- the vesting of performance share awards will occur on the third anniversary of the grant date, provided that the executive is still employed by the company and the same performance conditions as described above have been satisfied; and

- the adjusted EPS growth targets for 2006 are underpinned by a requirement that the company's total shareholder return ("TSR") outperforms the FTSE 350 total return index over the performance period, with TSR calculations being averaged over a three monthly period prior to both the beginning and end of the performance period.

On the 9 May 2006 the executive directors each invested their total post tax bonus for 2005 in Pendragon shares, in each case at a purchase price of £1.24 per share. The number of shares acquired is as follows, and forms part of the total shares held by each director as detailed in the table at page 28 above.

	Number of Investment Shares Acquired
T G Finn	196,270
M S Casha	96,825
D R Forsyth	75,890
H C Sykes	51,390

Also on the 9 May 2006, matching and performance share awards were granted to the executive directors, as below†. Future vesting of both matching and performance share awards is subject to the satisfaction of the performance conditions explained above.

	Matching Shares Awarded	Performance Shares Awarded
T G Finn	329,100	359,020
M S Casha	162,355	199,455
D R Forsyth	127,250	139,620
H C Sykes	86,000	99,725

Share Options

Executive directors have historically participated in the Pendragon 1999 Approved Executive Share Option Scheme, which is an HM Revenue and Customs approved scheme, and the Pendragon 1999 Unapproved Executive Share Option Scheme (the “Executive Schemes”), each of which was approved at the company’s 1999 Annual General Meeting. Options become exercisable between three and ten years after grant subject to fulfilment of the performance conditions set out in the notes to the table on page 29 of this Report. No variation has been made during the financial year in the terms and conditions of the share options or the Executive Schemes. Going forward, grants will only be made under the Executive Schemes in exceptional circumstances.

Changes from previous year

The LTIP has now replaced the grant of executive share options to the executive directors. The executive directors will continue to be eligible to participate in the company's all-employee sharesave scheme.

Directors’ share options (audited information)†

	At 01.01.06	Number of options lapsed during year	Number of options exercised during year	Number of options granted during year	At 31.12.06	Exercise price (pence)	Exercise period
T G Finn							
1999 4th Grant**	3,750,000	-	3,750,000	-		23.44	24.03.06 to 23.03.13
	*202,360	-	-	-	*202,360	9.08	01.07.07 to 31.12.07
M S Casha		-					
1999 4th Grant **	1,875,000	-	1,875,000	-		23.44	24.03.06 to 23.03.13
	*27,355				*27,355	60.4	01.07.10 to 31.12.10
D R Forsyth							
1999 4th Grant**	875,000	-	875,000			23.44	24.03.06 to 23.03.13
	*27,355				*27,355	60.4	01.07.10 to 31.12.10
H C Sykes							
1999 4th Grant**	625,000	-	625,000	-		23.44	24.03.06 to 23.03.13
		-		-	-	23.44	01.07.05 to 31.12.05
	*161,855	-	-	-	*161,855	9.08	01.07.07 to 31.12.07
	*14,450	-	-	-	*14,450	24.56	01.07.10 to 31.12.10
	*21,880				*21,880	60.4	01.07.10 to 31.12.10
Total	7,580,255	-	7,125,000	-	455,255		

†Displays post-share split position. There have been no changes in director's share options outstanding or exercised since the 31 December 2006.

* Sharesave options granted under the Pendragon 1998 Sharesave Scheme that have no performance conditions.

** Discretionary share options granted under the Executive Schemes the exercise of which is conditional on the Company's adjusted earnings per share over the three consecutive financial years beginning with the financial year in which the option is granted exceeding by at least 3 per cent per annum compound the increase in the Retail Prices Index over the same period.

When determining the extent to which the EPS performance targets have been met under the Executive Schemes, the Remuneration Committee will seek guidance from external advisors on the effect of the move to Internal Financial Reporting Standards and will endeavour to ensure consistency of measurement over the relevant performance period.

Details of share options exercised during the year are shown below	Number exercised	Exercise date	Price at exercise date* (£)	Exercise price (£)	Exercise period
T G Finn	3,750,000	09.05.06	1.247	0.2344	24.03.06 to 23.03.13
M S Casha	1,875,000	09.05.06	1.247	0.2344	24.03.06 to 23.03.13
D R Forsyth	875,000	09.05.06	1.247	0.2344	24.03.06 to 23.03.13
H C Sykes	625,000	09.05.06	1.247	0.2344	24.03.06 to 23.03.13

*Daily Official List closing price on the exercise date.

The aggregate gain made by the directors on share options exercised during 2006 was £7,214,775. The aggregate gain made by the directors on share options exercised during 2005 was £7,080.

Share price information and performance (not subject to audit)

There are no other share option or long term incentive schemes for which the directors are eligible. The middle market price of Pendragon PLC ordinary sales at 31 December 2006 was £1.00 and the range during the year was £0.94 to £1.31. Pursuant to a special resolution passed on the 22 December 2006, a share split was approved such that the trading price of the company's ordinary shares on the London Stock Exchange was approximately one-fifth of the price of an ordinary share prior to the split. Following the share split, shareholders will also own five times as many shares.

Directors' service contracts

All four of the executive directors have service contracts that commenced on 20 December 1999 and do not have an expiry date but can be terminated on giving one year's notice. The appointment to the Board of any further executive directors would be expected to be on similar terms.

Each of the executive directors' contracts includes protection for the director in the event of a termination arising from a change of control. Compensation of one year's salary and benefits, together with the value of the maximum annual bonus is payable if the director or the acquirer serves notice of termination within six months of a change of control. Bearing in mind the consolidation being witnessed in the motor retailing sector at present, the company continues to believe that these provisions are appropriate. These provisions will be reviewed annually and it is not necessarily the case that any executive director appointed to the Board in the future would be afforded this protection. Copies of the individual contracts of appointment are available for inspection by shareholders at the Annual General Meeting.

Non-executive directors

Each non-executive director has a fixed two year contract, renewable upon expiry at the company's discretion. Copies of the individual contracts of appointment are available for inspection by shareholders at the Annual General Meeting. When making a decision on reappointment, the Board reviews the non-executive director's attendance and performance at meetings and the composition and skills of the Board as a whole. Individual details of contracts are:

Name	Commencement	Expiry
Sir Nigel Rudd	01.01.06	31.12.07
W W Rhodes	01.01.06	31.12.07
N G Hannah†	01.01.05	31.12.06
J H Holt	01.01.06	31.12.07
M T Davies	01.01.07	31.12.08
D A L Joyce	01.03.06	27.04.07
M J Le May	01.03.06	27.04.07

†Retired on 31 December 2006

Consistent with the policy for executive directors, the contracts include a provision that the non-executive director will be entitled to a year's total fees and benefits if the contract is terminated by either party following a change of control. Copies of the individual contracts of appointment are available for inspection by shareholder at the Annual General Meeting.

Directors' additional services (not subject to audit)

In addition to services as a non-executive director, Mr N G Hannah provides commercial property advice to the group under a retainer agreement. In 2006 he earned fees of £30,000 (2005: £30,000) under this agreement. As non-executive chairman of commercial property surveyors Innes England Limited he is interested in contracts for the provision of their services to the company which, during 2006, had an aggregate value of £35,000 (2005: £89,000).

Fees from external directorships

Mr T G Finn earns fees of £10,000 per annum as a non-executive director of Falcon Investment Trust Limited, which he retains. No other executive directors holds paid office with any company outside the company's group.

Directors' remuneration for the year to 31 December 2006 (audited information)

	Salary/Fees	Bonus	Benefits	Payment in lieu of Pension Contribution	Total emoluments	Total emoluments exc. pensions 2006	Total emoluments exc. pensions 2005
	£000	£000	£000	£000	£000	£000	£000
Executive directors							
T G Finn	441	189	45	86	761	675	868
M S Casha	238	105	24	48	415	367	433
D R Forsyth	171	74	27	23	295	272	347
H C Sykes	121	53	16	14	204	190	231
Non-executive directors							
Sir Nigel Rudd	89	-	36	-	125	125	75
N G Hannah	35	-	-	-	35	35	35
W W Rhodes	25	-	10	-	35	35	35
J H Holt	35	-	-	-	35	35	35
M T Davies	35	-	-	-	35	35	35
D A L Joyce	29*	-	-	-	29	29*	nil
M J Le May	29*	-	-	-	29	29*	nil
Total	1,248	421	158	171	1,998	1,827	2,094

*Mr D A L Joyce and Mr M J Le May were appointed on 1 March 2006 and accordingly these figures represent fees for a 10 month period only.

Pension contributions

In addition to the amounts included in the table on the previous page, company pension contributions paid in 2006 were £1,078,254 (2005: £227,088). The charge for 2006 includes a one off cost of £992,449 in respect of an increase in past service accruals following the removal of the statutory earnings cap and the cessation of the defined benefit pension plan.

Directors' pension entitlements (audited information)

Pensions

The assets of the Pendragon Pension Plan, established for the benefit of the group's eligible employees, are held by trustees separately from those of the group. The Plan operates through a trustee company of which Mr W W Rhodes is the chairman. The management of the Plan's assets is delegated to specialist independent investment managers and there is no direct investment in Pendragon PLC. During 2006, the executive directors withdrew from the Plan. They remain entitled to a deferred pension, calculated up to the date of leaving the Plan. The non-executive directors are not eligible to participate in the Pendragon Pension Plan.

£000	T G Finn	M S Casha	D R Forsyth	H C Sykes
Total annual accrued pension entitlement at 31.12.05 (p.a)	287	116	34	19
Total annual accrued pension entitlement at 31.12.06 (p.a)	379	131	67	42
Increase in accrued pension during the year excluding inflation (p.a)	79	10	31	22
Increase in accrued pension during the year including inflation (p.a)	92	15	33	23
Transfer value of increase excluding inflation	1,505	167	305	185
Transfer value of accrued benefit at 31.12.05	4,872	1,476	263	130
Transfer value of accrued benefit at 31.12.06	7,216	2,111	651	355
Increase in transfer value over the year	2,344	635	388	225

The pension benefits shown are those which would be paid annually on retirement, based on service up until the date the Director withdrew from the Plan. The benefits allow for any retained benefits which the directors may have relating to previous employment.

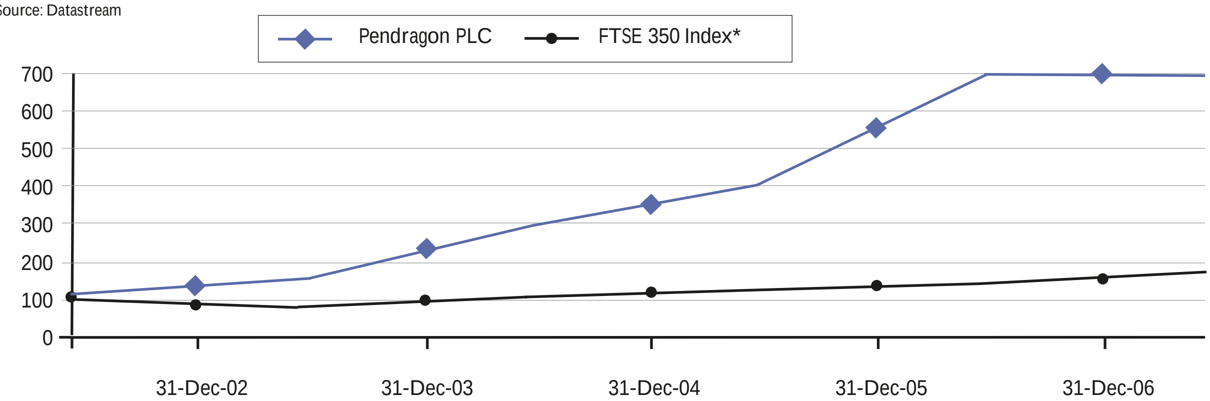
The transfer values have been calculated in accordance with actuarial advice and exclude directors' contributions. All the above pension benefits exclude any additional pension purchased by additional voluntary contributions.

Total shareholder return (not subject to audit)

The graph below shows the growth in total shareholder return on the Company's shares in comparison to the FTSE 350 Index (excluding investment companies). For the purposes of the graph, total shareholder return has been calculated as the percentage change during the relevant period in the market price of the shares, assuming that any dividends paid are reinvested. The relevant period is the five years ending 31 December 2006. A more detailed description of the total shareholder return calculation is set out in the Notes.

Total shareholder return

Source: Datastream



This graph shows the value, by 31 December 2006, of £100 invested in Pendragon PLC on 31 December 2002 compared with the value of £100 invested in the FTSE 350 Index*. The other points plotted are the values at intervening financial year-ends.

* excluding investment trusts

1. This report is required, pursuant to the Regulations, to contain this graph as a visual interpretation of the share price performance against a comparator stock market index.

2. Total Shareholder Return ("TSR") is calculated over the period of five years ended on 31 December 2006 and reflects the theoretical growth in the value of a shareholding over that period, assuming dividends are reinvested in shares in the company. The price at which the dividends are reinvested is assumed to be the amount equal to the closing price of the shares on the ex-dividend date plus the gross amount of annual dividend. The calculation ignores tax and reinvestment charges. For each company in the index the TSR statistics are normalised to a common start point, which gives the equivalent to investing the same amount of money in each company at that time. The percentage growth in TSR is measured over the chosen period. To obtain the TSR growth of the relevant index over the chosen period, the weighted average TSR growth for all the companies in the index is calculated. In this case, it is the FTSE 350 Index (excluding investment companies) as explained in Note 3. The weighting is by reference to the market capitalisation of each company in the index in proportion to the total market capitalisation of all the companies in the index at the end of the chosen measurement period.

3. The FTSE 350 Index has been selected because the company clearly falls within the criterion reported on by that index, namely, market capitalisation not less than circa £340 million.

Whilst reporting on remuneration issues, I am pleased to advise that below Board level, 24% of the company's costs of employing its team members related to team incentives, reflecting the performance culture that exists throughout the company. In addition as at 31 December 2006, 18% of the company's team members were participants in one or more of its share based incentive plans.

Approved on behalf of the Board
Mike Davies
Chairman of the Remuneration Committee

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 judgments and estimates that are reasonable and prudent;
- for the group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent company financial statements, state 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.

We have audited the group and parent company financial statements (the "financial statements") of Pendragon PLC for the year ended 31 December 2006 which comprise the Group Income Statement, the Group and Parent Company Balance Sheets, the Group Cash Flow Statement, the Statement of Recognised Income and Expense 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 auditor's 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 35.

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.

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
Birmingham
Chartered Accountants
Registered Auditors
15 February 2007

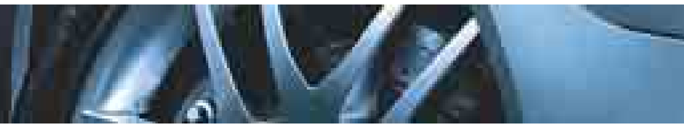
CONSOLIDATED INCOME STATEMENT
YEAR ENDED 31 DECEMBER 2006

	Notes	Existing £m	Acquisition £m	**2006 Total £m**	2005 £m
Revenue		3,415.9	1,685.1	**5,101.0**	3,284.5
Cost of sales		(2,928.4)	(1,465.0)	**(4,393.4)**	(2,816.8)
Gross profit		487.5	220.1	**707.6**	467.7
Operating expenses	3	(390.3)	(178.0)	**(568.3)**	(371.8)
Operating profit before other income		97.2	42.1	**139.3**	95.9
Operating profit before other income, analysed as:					
Before exceptional items		89.2	46.1	**135.3**	98.8
Goodwill impairment	3	(0.9)	-	**(0.9)**	(1.1)
Closure and integration costs	3	-	(4.0)	**(4.0)**	(1.8)
Abortive acquisition costs	3	(1.0)	-	**(1.0)**	-
Gain on curtailment of defined benefit pension schemes	3	9.9	-	**9.9**	-
Operating profit before other income		97.2	42.1	**139.3**	95.9
Other income - gains on the sale of businesses and property	3			**24.3**	7.4
Operating profit				**163.6**	103.3
Finance costs	6			**(85.3)**	(54.9)
Finance income	7			**17.7**	15.3
Net finance costs				**(67.6)**	(39.6)
Share of profit before tax from joint venture	12			**0.5**	0.1
Share of income tax expense from joint venture	12			**(0.1)**	-
Share of post tax profit from joint venture				**0.4**	0.1
Profit before taxation				**96.4**	63.8
Income tax expense	8			**(28.9)**	(20.7)
Profit for the year attributable to equity shareholders				**67.5**	43.1
Basic earnings per ordinary share	9			**10.7p**	7.0p
Diluted earnings per ordinary share	9			**10.6p**	6.8p

The notes on pages 42 to 77 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

AT 31 DECEMBER 2006



	Notes	2006 £m	restated * 2005 £m
Non-current assets			
Property, plant and equipment	11	**420.4**	394.0
Goodwill	10	**433.8**	166.3
Other intangible assets	10	**1.4**	1.2
Derivative financial instruments	17	**-**	6.5
Investment in joint venture	12	**3.0**	1.4
Total non-current assets		**858.6**	569.4
Current assets			
Inventories	13	**850.2**	641.8
Trade and other receivables	14	**260.9**	161.6
Cash and cash equivalents	24	**19.7**	82.1
Non-current assets classified as held for sale	30	**38.4**	18.9
Total current assets		**1,169.2**	904.4
Total assets		**2,027.8**	1,473.8
Current liabilities			
Bank overdrafts	24	**-**	(4.7)
Interest bearing loans and borrowings	16	**(10.4)**	(4.9)
Trade and other payables	15	**(1,171.8)**	(855.5)
Deferred income	29	**(0.9)**	-
Current tax payable		**(19.5)**	(19.1)
Provisions	18	**(4.3)**	(0.7)
Total current liabilities		**(1,206.9)**	(884.9)
Non-current liabilities			
Interest bearing loans and borrowings	16	**(371.0)**	(256.0)
Derivative financial instruments	17	**(8.0)**	-
Deferred income	29	**(21.1)**	-
Deferred tax liabilities	8	**(42.0)**	(2.0)
Retirement benefit obligations	27	**(65.2)**	(90.4)
Provisions	18	**(7.6)**	(1.2)
Total non-current liabilities		**(514.9)**	(349.6)
Total liabilities		**(1,721.8)**	(1,234.5)
Net assets		**306.0**	239.3
Capital and reserves			
Called up share capital	19	**32.8**	32.8
Share premium account	20	**56.8**	56.8
Capital redemption reserve	20	**2.5**	2.5
Other reserves	20	**12.6**	12.6
Translation reserve	20	**(0.3)**	(0.1)
Retained earnings	20	**201.6**	134.7
Total equity		**306.0**	239.3

Approved by the Board of Directors on 15 February 2007 and signed on its behalf by:

T G Finn
Chief Executive

D R Forsyth
Finance Director

* See change in accounting policy - see note 1r.
The notes on pages 42 to 77 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT
YEAR ENDED 31 DECEMBER 2006

	Notes	2006 £m	2005 £m
Cash flows from operating activities			
Profit after taxation		**67.5**	43.1
Adjustment for income from joint venture		**(0.4)**	(0.1)
Adjustment for taxation		**28.9**	20.7
Adjustment for interest		**67.6**	39.6
Operating profit		**163.6**	103.3
Depreciation and amortisation		**65.1**	47.5
Share based payments		**0.9**	0.4
Profit on sale of businesses and property		**(24.3)**	(7.4)
Goodwill impairment		**0.9**	1.1
Changes in inventories		**74.9**	(8.4)
Changes in trade and other receivables		**(31.8)**	(28.4)
Changes in trade and other payables		**(9.6)**	29.5
Changes in retirement benefit obligations		**(23.1)**	(6.9)
Changes in provisions		**2.8**	(0.3)
Cash generated from operations		**219.4**	130.4
Taxation paid		**(24.2)**	(16.6)
Interest received		**0.8**	1.3
Interest paid		**(68.0)**	(44.5)
Net cash from operating activities		**128.0**	70.6
Cash flows from investing activities			
Business acquisitions	22	**(466.0)**	(35.1)
Proceeds from sale of businesses	23	**23.1**	16.2
Purchase of investment in joint venture		**(15.1)**	(6.5)
Purchase of property, plant and equipment		**(171.2)**	(154.4)
Proceeds from sale of property, plant and equipment		**388.9**	193.5
Receipts from sales of investments		**1.7**	0.3
Net cash (used in) / from investing activities		**(238.6)**	14.0
Cash flows from financing activities			
Payment of capital element of finance lease rentals		**(5.6)**	(1.0)
Repayment of unsecured bank loans		**(413.3)**	(73.2)
Repayment of loan notes		**(12.5)**	(32.7)
Proceeds from issue of unsecured loans		**502.8**	-
Dividends paid to shareholders		**(17.4)**	(15.6)
Net cash inflow / (outflow) from financing activities		**54.0**	(122.5)
Effects of exchange rate changes on cash held		**(1.1)**	1.0
Net decrease in cash and cash equivalents		**(57.7)**	(36.9)
Cash and cash equivalents at 31 December 2005		**77.4**	114.3
Cash and cash equivalents at 31 December 2006	24	**19.7**	77.4

The notes on pages 42 to 77 form part of these financial statements.

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSE YEAR ENDED 31 DECEMBER 2006

	2006 £m	restated * 2005 £m
Foreign currency translation differences for foreign operations	**(0.2)**	0.2
Defined benefit plan actuarial gains and losses	**18.1**	(17.1)
Income tax on income and expense recognised directly in equity	**(5.4)**	5.1
Income and expense recognised directly in equity	**12.5**	(11.8)
Profit for period	**67.5**	43.1
Total recognised income and expense for the period attributable to equity holders of the company	**80.0**	31.3
Impact of change in accounting policy on retained earnings at 1 January	**(13.3)**	-

* see change in accounting policy - see note 1r

The notes on pages 42 to 77 form part of these financial statements

1 Accounting policies

Pendragon PLC is a company domiciled in the United Kingdom. The consolidated financial statements of the group for the year ended 31 December 2006 comprise the company and its subsidiaries and the group's interest in jointly controlled entities.

(a) Statement of compliance The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted for use by the EU, including International Accounting Standards Interpretations adopted by the International Accounting Standards Board and with those parts of the Companies Act 1985 applicable to companies reporting under IFRS.

The company has elected to prepare its parent company financial statements in accordance with UK GAAP, these are presented on pages 78 to 85.

(b) Basis of Preparation The financial statements are presented in millions of UK pounds, rounded to the nearest £0.1million. They have been prepared under the historical cost convention except for certain financial instruments which are stated at their fair value. In addition non current assets held for sale are stated at the lower of carrying amount and fair value less costs to sell.

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting year. Although these estimates are based on management's best knowledge of the amount, events or actions, actual results ultimately may differ from those 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 IFRS that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 31.

(c) Basis of consolidation The consolidated financial statements include the financial statements of Pendragon PLC, all its subsidiary undertakings and the group's share of its joint venture under the equity accounting method. Consistent accounting policies have been applied in the preparation of all such financial statements including those of the joint venture with the exception of that for employee benefits in respect of pension obligations, the details of which are given in subsection r below.

(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.

(ii) Joint ventures
Joint ventures are those entities over whose activities the group has joint control, established by contractual agreement. The consolidated financial statements include the group's proportionate share of the entities net assets and profit after tax, on an equity accounted basis, from the date joint control commences until the date that joint control ceases.

(iii) Transactions eliminated on consolidation
Intragroup balances and any unrealised gains or losses or income and expenses arising from intragroup transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with joint ventures are eliminated to the extent of the group's interest in the entity.

(d) Accounting for business combinations and disposals The results of companies and businesses acquired or disposed of during the year are included from the effective date of acquisition or up to the effective date of disposal using the acquisition method of accounting. The purchase consideration is allocated to assets and liabilities on the basis of fair value at the date of acquisition.

(e) Revenue Revenue from the sale of goods is recognised in the income statement, net of discounts, when the significant risks and rewards of ownership have been transferred to the buyer. In general this occurs when vehicles or parts have been supplied or when service has been completed.

1 Accounting policies (continued)

Where vehicles are supplied to a leasing company for contract hire purposes and the group undertakes to repurchase the vehicle at a predetermined date and value the significant risks and rewards of ownership are deemed not to have transferred outside the group and consequently no sale is recognised. As a result the accounting for the arrangement reflects the group's retention of the asset to generate future rentals and, in accordance with IAS 17 'Leases', with the group being considered to be an operating lessor for all arrangements in place. The initial amounts received in consideration from the leasing company are held as deferred income allocated between the present value of the repurchase commitment and a residual amount of deferred revenue, both amounts being held within trade and other payables. A finance charge is accrued against the present value of the repurchase commitment and recorded as a finance expense in the income statement. The remaining deferred revenue, which effectively represents rentals received in advance, is taken to the income statement on a straight line basis over the related lease term. No additional disclosures are made under IAS 17 as there are no future rentals receivable. These vehicles are held as plant and equipment at their cost to the group and are depreciated to their residual values over the terms of the leases.

(f) Intangible assets and goodwill
(i) Goodwill represents the excess of the cost of acquisition over the fair value of the identifiable net assets of the acquired subsidiary undertakings at the effective date of acquisition and is included in the balance sheet under the heading of intangible assets. The goodwill is allocated to cash generating units and an impairment test is performed annually. Goodwill is then held in the balance sheet at cost less any accumulated impairment losses.

If the cost on acquisition is less than the fair value of the net assets acquired the difference is recognised directly in the consolidated income statement.

Adjustments are applied to bring the accounting policies of the acquired businesses into alignment with those of the group. The costs associated with reorganising or restructuring are charged to the post acquisition income statement. For those acquisitions made prior to 1 January 2004, goodwill is recorded on the basis of its deemed cost which represented its carrying value as at 1 January 2004 under UK GAAP.

(ii) Intangible assets, other than goodwill are stated at cost less accumulated amortisation and any impairment losses. This category of asset includes computer software, which is amortised by equal instalments over four years and the fair value of the benefit of forward sales orders assumed on acquisition, which is amortised by reference to when those orders are delivered.

(iii) 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.

Intangible assets arising on an acquisition are recognised separately from goodwill if the fair value of the asset can be identified separately and measured reliably. Amortisation is calculated on a straight line basis over the estimated useful life of the intangible asset. Amortisation methods and useful lives are reviewed annually and adjusted if appropriate.

(g) Property, plant and equipment Freehold land is not depreciated. Depreciation is provided to write off the cost less the estimated residual value of other assets by equal instalments over their estimated useful economic lives. On transition to IFRS as at 1 January 2004, all land and buildings were restated to fair value as permitted by IFRS1, which is then treated as the deemed cost. All other assets are initially measured and recorded at cost.

Depreciation rates are as follows:
Freehold buildings – 2% per annum
Leasehold properties – 2% per annum or over the period of the lease if less than 50 years
Fixtures, fittings and office equipment – 10–20% per annum
Plant and machinery – 10–33% per annum
Motor vehicles – 20–25% per annum
Motor vehicles held for contract hire depreciated to their residual value over the period of their lease.

The residual value of all assets, if significant, is reassessed annually.

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 possible that the future economic benefits embodied with the item will flow to the group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense as incurred.

(h) Non-current assets held for sale Non-current assets that are expected to be recovered primarily through sale rather than through continuing use are classified as held for sale. Immediately before classification as held for sale, the assets are remeasured in accordance with the group's accounting policies. Thereafter the assets are measured at the lower of their carrying amount and fair value less costs to sell. Impairment losses on remeasurement are recognised in the income statement. Gains are not recognised in excess of any cumualtive impairment loss. Non-current assets classified as held for sale are available for immediate sale and a resultant disposal is highly probable within one year.

1 Accounting policies (continued)

(i) Impairment The carrying amounts of the group's assets, other than inventories (see accounting policy j) and deferred tax assets (see accounting policy n), 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 (see accounting policy b).

For goodwill 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 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.

The recoverable amount of assets 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 inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

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.

(j) Inventories
(i) Consignment vehicles are regarded as being effectively under the control of the group and are included within inventories on the balance sheet as the group has the significant risks and rewards of ownership even though legal title has not yet passed. The corresponding liability is included in trade and other payables.

(ii) Motor vehicles (including consignment and demonstrator vehicles) and parts inventories are stated at the lower of cost and fair value less costs to sell. Parts inventories are based on an average purchase cost principle and are written down to fair value by providing for obsolescence on a time in stock based formula approach.

(k) Trade and other receivables Trade and other receivables are recognised initially at fair value and are stated at amortised cost using the effective interest method, less any impairment losses.

(l) Trade and other payables Trade and other payables are recognised initially at fair value and are stated at amortised cost using the effective interest method, less any impairment losses.

(m) Cash and Cash Equivalents For the purposes of the cash flow statement, cash and cash equivalents comprise deposits with banks and financial institutions, bank and cash balances, and liquid investments, net of bank overdrafts. 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 statement of cash flows. In the balance sheet, bank overdrafts are included in current borrowings.

1 Accounting policies (continued)

(n) Income tax Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is 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 tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

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

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

(o) Foreign currencies
(i) Foreign currency transactions Transactions in foreign currencies are translated 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. 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.

(ii) Financial statements of foreign operations The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to sterling at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to sterling at rates approximating to the foreign exchange rates ruling at the dates of the transactions.

(iii) Net investment in foreign operations Exchange differences arising from the translation of the net investment in foreign operations, and of related hedges are taken to translation reserve. They are released into the income statement upon disposal.

In respect of all foreign operations, any differences that have arisen after 1 January 2004, the date of transition to IFRS, are presented as a separate component of equity.

(p) Financial instruments The group holds derivative financial instruments to hedge currency and interest risks arising from its activities. Derivative financial instruments are recognised at fair value. Any gain or loss on remeasurement is recognised in the income statement. However, the treatment of gains or losses arising from derivatives which qualify for hedge accounting depends on the nature of the hedged item itself. The fair value of derivatives is the estimated amount receivable or payable to terminate the contract determined by reference to the market prices prevailing at the balance sheet date.

Hedging
(i) Fair value hedges
In the current year where a derivative financial instrument hedges the changes in fair value of recognised assets or liabilities, any gain or loss is recognised within finance costs or finance income, as appropriate, in the income statement. The hedged item is also stated, separately from the derivative, at fair value in respect of the risk being hedged with any gain or loss also recognised within finance costs or finance income, as appropriate, in the income statement. This will result in variations in the balance sheet values of the gross debt and the offsetting derivatives as the market value fluctuates.

(ii) Hedges of net investments in overseas operations
A gain or loss in respect of an effective hedge of a net investment in an overseas operation is recognised directly in equity. Any ineffective portion of the hedge is recognised in the income statement.

Non-derivative financial instruments
Non-derivative financial instruments comprise investments in equity and debt securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

1 Accounting policies (continued)

Non-derivative financial instruments are recognised initially at fair value.

A financial instrument is recognised if the group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the group's contractual rights to the cash flows from the financial asset expire. Financial liabilities are derecognised if the group's obligations specified in the contract expire or are discharged and cancelled.

(q) 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 income statement over the period of the borrowings on an effective interest basis.

(r) Employee benefits – Pension obligations The group operates a number of defined benefit and defined contribution plans, the assets of which are held in independent trustee administered funds. Pension accounting costs for defined benefit plans are assessed by determining the pension obligation using the projected unit credit method after including a credit for the expected return on plan assets. Under this method, in accordance with the advice of qualified actuaries, the amounts charged in respect of employee benefits reflect the cost of benefits accruing in the year and the cost of financing historical accrued benefits.

The present value of pension obligations is measured by reference to market yields on high quality corporate bonds which have terms to maturity approximating to the terms of the related pension liability. Plan assets are measured at fair value. The group’s total contributions relating to the defined contribution plans are charged to the income statement in the year to which they relate.

Change in accounting policy

The group recognises all actuarial gains and losses arising from defined benefit plans directly in equity. In its financial statements for periods beginning before 1 January 2006 the group applied the corridor method to recognise in the income statement actuarial gains and losses over the expected working lives of employees in the plans. This change in accounting policy was due to the closure of the schemes to future accrual, employees no longer participate in the plan and the service period over which the corridor movements are spread is nil. As a consequence of this the directors consider it is no longer appropriate to spread the gains and losses over the service period and the directors consider that full recognition of the actuarial gains and losses in the 'Statement of Recognised Income and Expense' gives more reliable and relevant information. The directors consider this to be more reliable and relevant as the revised policy will therefore reflect the full pension obligation on the balance sheet.

The change in accounting policy was recognised retrospectively in accordance with the transitional provisions of the amendment, and comparatives have been restated. The change in accounting policy had the following impact on these financial statements:

Income Statement for the year ended 31 December

	2006	2005
	£m	£m
Decrease in net administration expense	8.6	-
Increase in income tax expense	(2.6)	-
Increase in profit for the year attributable to equity shareholders	6.0	-
Increase in earnings per share (pence)	1.0p	-

The above amount arises primarily due to the curtailment of the defined benefit scheme which has been deemed exceptional in nature.

Consolidated Statement of Recognised Income and Expense	2006	2005
	£m	£m
Increase / (decrease) in net income recognised directly in equity	12.7	(12.0)
Increase / (decrease) in total recognised income and expense for the year	12.7	(12.0)

Balance Sheet	2006	2005
	£m	£m
Cumulative increase in retirement benefit obligations	(0.9)	(19.0)
Cumulative increase in deferred tax asset	0.3	5.7
Cumulative decrease in retained earnings	(0.6)	(13.3)

The adjustment to retained earnings at 1 January 2005 was a decrease of £1.3 million.

1 Accounting policies (continued)

(s) Employee benefits – Share based payments The group operates a number of employee share option schemes. The fair value at the date at which the share options are granted is recognised in the income statement on a straight line basis over the vesting period, taking into account the number of options that are expected to vest. The fair value of the options granted is measured using an option pricing model, taking into account the terms and conditions upon which the options were granted. The number of options that are expected to become exercisable is reviewed at each balance sheet date and if necessary estimates are revised. In accordance with the transitional provisions of IFRS2, no income statement expenses are recorded in respect of grants of share options made prior to 7 November 2002.

(t) Leases Leases are classified as finance leases wherever the lease transfers substantially all the risks and rewards of ownership to the group. All other leases are treated as operating leases.

Assets held under finance leases are recorded at inception at the lower of the fair value of the asset and the present value of the minimum payments required to be made under the lease. The corresponding liability is recorded as a finance lease obligation. The finance charge element of rentals paid under these leases is expensed so as to give a constant rate of finance charge on the remainder of the obligation. Finance charges are expensed in the income statement and the capitalised leased asset is depreciated over the shorter of the lease term and the asset's useful economic life.

Rentals paid under operating leases are charged directly to the income statement on a straight line basis over the period of the lease.

(u) Dividends Final dividends proposed by the Board and unpaid at the end of the year are not recognised in the financial statements until they have been approved by the shareholders at the AGM. Interim dividends are recognised when they are paid.

(v) Capitalisation of finance costs Gross finance costs directly attributable to the construction of tangible fixed assets are capitalised as part of the cost of those assets until such a time as the assets are substantially ready for their intended use or sale.

(w) Provisions A provision is recognised in the balance sheet when the group has a present legal or constructive obligation as a result of a past event, 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, where appropriate, the risks specific to the liability.

A provision for onerous contracts is recognised when the expected benefits to be derived by the group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. Vacant properties for which an outstanding lease commitment exists and which cannot be sublet for at least the same rate fall within this category.

(x) Segment reporting A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographic segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

(y) Own shares held by ESOP trust Transactions of the group-sponsored ESOP trust are included in the group financial statements. In particular, the trust's purchases of shares in the company are debited directly to equity.

(z) New standards and interpretations not yet adopted A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2006, and have not been applied in preparing these consolidated financial statements:

(i) IFRS 7 'Financial Instruments : Disclosures' and the Amendment to IAS 1 'Presentation of Financial Statements : Capital Disclosures' require extensive disclosures about the significance of financial instruments for an entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. IFRS 7 and amended IAS 1, which becomes mandatory for the group's 2007 financial statements, will require extensive additional disclosures with respect to the group's financial instruments and share capital.

(ii) IFRIC 8 'Scope of IFRS 2 Share-based Payment' addresses the accounting for share based payment transactions in which some or all of goods or services received cannot be specifically identified. IFRIC 8, which becomes mandatory for the group's 2007 financial statements is not expected to have any impact on the consolidated financial statements.

(iii) IFRIC 9 'Reassessment of Embedded Derivatives' requires that a reassessment of whether embedded derivatives should be separated from the underlying host contract should be made only when there are changes to the contract. IFRIC 9, which becomes mandatory for the group's 2007 financial statements is not expected to have any impact on the consolidated financial statements.

2 Segmental analysis

Segment information is presented in respect of the group's business and geographical segments. The primary format, business segments, is based on the group's management and internal reporting structure.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Central items comprise of mainly corporate assets and expenses, loans and borrowings.

Inter-segment transfers and transactions are entered into under normal commercial terms and conditions that would also be available to unrelated third parties.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets that are expected to be used for more than one period.

Primary reporting format - Business segments

The group comprises the following main business segments:

Stratstone This segment comprises the group's luxury car brand encompassing the sale of new and used motor cars and motorbikes, together with associated aftersales activities of service, body repair and parts sales.

Evans Halshaw This segment comprises the group's volume car brand encompassing the sale of new and used motor cars, together with associated aftersales activities of service, body repair and parts sales.

Chatfields This segment comprises the group's truck and commercial vans brand encompassing the sale of new and used trucks and commercial vehicles, together with associated aftersales activities of service, body repair and parts sales.

Support This segment comprises the group's contract hire activities and ancillary businesses related to the motor segment which includes the group's parts distribution, dealer management system provider and shared service centre.

Year ended 31 December 2005	Stratstone £m	Evans Halshaw £m	Chatfields £m	Support £m	Central £m	**Total £m**
New vehicle revenue	788.4	736.4	165.7	-	-	**1,690.5**
Used vehicle revenue	640.9	479.0	16.5	-	-	**1,136.4**
Aftersales revenue	168.2	182.9	57.8	-	-	**408.9**
Contract hire and support revenue	-	-	-	143.5	-	**143.5**
Total gross segment revenue	1,597.5	1,398.3	240.0	143.5	-	**3,379.3**
Inter-segment revenue	-	(25.4)	-	(69.4)	-	**(94.8)**
Revenue from external customers	1,597.5	1,372.9	240.0	74.1	-	**3,284.5**
Operating profit before other income and exceptional items	55.2	21.6	8.4	13.6	-	**98.8**
Other income and exceptional items	-	(2.9)	-	-	7.4	**4.5**
Operating profit	55.2	18.7	8.4	13.6	7.4	**103.3**
Finance costs - net						**(39.6)**
Share of profit of joint venture						**0.1**
Profit before income tax						**63.8**
Income tax expense						**(20.7)**
Profit for year						**43.1**

Other items included in the income statement are as follows:	Stratstone £m	Evans Halshaw £m	Chatfields £m	Support £m	Central £m	**Total £m**
Depreciation	7.6	9.4	0.7	29.2	-	**46.9**
Amortisation	0.3	0.3	-	-	-	**0.6**
Share based payments	0.2	0.2	-	-	-	**0.4**
Impairment of goodwill	-	1.1	-	-	-	**1.1**

2 Segmental analysis (continued)

Year ended 31 December 2006	Stratstone £m	Evans Halshaw £m	Chatfields £m	Support £m	Central £m	**Total £m**
New vehicle revenue	1,083.3	1,539.1	135.4	-	-	**2,757.8**
Used vehicle revenue	868.7	804.3	14.7	-	-	**1,687.7**
Aftersales revenue	234.3	292.4	50.3	-	-	**577.0**
Contract hire and support revenue	-	-	-	146.3	-	**146.3**
Total gross segment revenue	2,186.3	2,635.8	200.4	146.3	-	**5,168.8**
Inter-segment revenue	-	(12.2)	-	(55.6)	-	**(67.8)**
Revenue from external customers	2,186.3	2,623.6	200.4	90.7	-	**5,101.0**
Operating profit before other income and exceptional items	55.7	53.6	6.1	19.9	-	**135.3**
Other income and exceptional items	-	(0.9)	-	-	29.2	**28.3**
Operating profit	55.7	52.7	6.1	19.9	29.2	**163.6**
Finance costs - net						**(67.6)**
Share of profit of joint venture						**0.4**
Profit before income tax						**96.4**
Income tax expense						**(28.9)**
Profit for year						**67.5**

Other items included in the income statement are as follows:	Stratstone £m	Evans Halshaw £m	Chatfields £m	Support £m	Central £m	**Total £m**
Depreciation	9.2	21.7	0.8	30.3	-	**62.0**
Amortisation	1.4	1.6	0.1	-	-	**3.1**
Share based payments	0.4	0.5	-	-	-	**0.9**
Impairment of goodwill	-	0.9	-	-	-	**0.9**

The segment assets and liabilities at 31 December 2005 and capital expenditure for the year then ended are as follows:

	Stratstone £m	Evans Halshaw £m	Chatfields £m	Support £m	Central £m	**Total £m**
Assets	533.0	614.8	84.4	137.9	13.7	**1,383.8**
Joint Venture	-	-	-	-	1.4	**1.4**
Gross assets	533.0	614.8	84.4	137.9	15.1	**1,385.2**
Gross liabilities	(331.5)	(294.4)	(57.8)	(114.4)	(149.7)	**(947.8)**
Operating assets	201.5	320.4	26.6	23.5	(134.6)	**437.4**
Current taxation						**(19.1)**
Deferred taxation						**(2.0)**
Net borrowings						**(177.0)**
Net assets						**239.3**
Capital expenditure	31.3	65.8	0.9	56.1	-	**154.1**

2 Segmental analysis (continued)

The segment assets and liabilities at 31st December 2006 and capital expenditure for the year then ended are as follows:

	Stratstone £m	Evans Halshaw £m	Chatfields £m	Support £m	Central £m	**Total £m**
Assets	815.2	896.8	65.3	192.7	35.1	**2,005.1**
Joint Venture	-	-	-	-	3.0	**3.0**
Gross assets	815.2	896.8	65.3	192.7	38.1	**2,008.1**
Gross liabilities	(399.3)	(366.8)	(37.6)	(165.0)	(302.2)	**(1,270.9)**
Operating assets	415.9	530.0	27.7	27.7	(264.1)	**737.2**
Current taxation						**(19.5)**
Deferred taxation						**(42.0)**
Net borrowings						**(369.7)**
Net assets						**306.0**
Capital expenditure	59.3	51.7	1.5	61.4	-	**173.9**

Capital expenditure comprises additions to property, plant and equipment and intangible assets, including additions resulting from acquisitions through business combinations.

Secondary reporting format - Geographic segments

The group's business segments operate in two main geographical areas and are managed on a worldwide basis. These segments are the UK and overseas. The overseas segment includes US and German operations combined on the basis of materiality.

Activities in the UK comprise all operating segments. Overseas operations comprise motor activities only.

Revenue

	2006 £m	2005 £m
UK	**4,843.7**	3,031.8
Overseas	**257.3**	252.7
Revenue from external customers	**5,101.0**	3,284.5

Revenue is allocated based on the country in which the customer is located.

Gross assets

	2006 £m	2005 £m
UK	**1,900.1**	1,301.8
Overseas	**105.0**	88.5
	2,005.1	1,390.3
Joint venture	**3.0**	1.4
	2,008.1	1,391.7

Total assets are based on where the asset is located.

2 Segmental analysis (continued)

Capital expenditure

	2006	2005
	£m	£m
UK	**168.1**	149.9
Overseas	**5.8**	4.2
	173.9	154.1

Capital expenditure is allocated based on where the asset is located.

3 Net operating expenses and exceptional items

	2006	2005
	£m	£m
Net operating expenses:		
Distribution costs	**(367.6)**	(243.9)
Administrative expenses	**(201.2)**	(129.1)
Rents received	**0.5**	1.2
	(568.3)	(371.8)

Expenses and income incurred or received during the year, which due to their size and nature of being items that are typically non-recurring, are drawn out for separate disclosure as exceptional items. During the year exceptional costs were £5.9m which comprised £4.0m in respect of integration costs arising following the acquisition of Reg Vardy plc which include redundancy payments made to the former directors, £1.0m is in respect of the abortive acquisition costs incurred in the unsuccessful bid for Lookers plc and £0.9m impairment of goodwill. An exceptional net gain was made of £9.9m during the year on curtailment of the defined benefit pension schemes. Exceptional costs incurred in the previous period were £2.9m which comprised of £1.1m goodwill impairment and £1.8m of redundancy and other asset write offs following the collapse of the MG Rover Group. In all respects these costs are included within operating expenses.

Other income, being the profit on disposal of businesses and property comprises £0.1m profit on the disposal of motor vehicle dealerships (2005 : £0.2m) and £24.2m profit on sale of properties (2005: £7.2m) after deducting £4.0m impairment losses on non current assets held for sale (2005 : £nil).

The following items have been charged to the income statement as operating expenses during the year:		**2006**	2005
		£m	£m
Depreciation of property, plant and equipment	owned	**59.9**	45.6
	held under finance leases	**2.1**	1.3
Amortisation of intangible assets		**3.1**	0.6
Impairment of goodwill		**0.9**	1.1
Operating lease rentals payable	hire of plant and machinery	**4.4**	2.5
	property rentals	**28.4**	20.0
Increase in provisions		**6.3**	0.2

	2006	2005
Auditors' remuneration :	**£000**	£000
Audit of these financial statements	**185.0**	163.0
Amounts receivable by the auditors and their associates in respect of:		
Audit of financial statements of subsidiaries pursuant to legislation	**349.5**	204.0
Other services relating to taxation	**85.5**	62.0
Valuation and actuarial services	**712.0**	529.0
Services relating to corporate finance transactions entered into	**838.3**	250.0
All other services	**74.5**	41.0
	2,244.8	1,249.0

Of the above, £552,000 (2005: £250,000) in relation to the corporate finance transactions entered into have been capitalised as part of the costs relating to these transactions.

4 Employees

The average number of people employed by the group in the following areas was:

	2006 Number	2005 Number
Sales	**5,181**	3,479
Aftersales	**8,744**	5,880
Administration	**2,267**	1,744
	16,192	11,103

Costs incurred in respect of these employees were :

	2006 £m	2005 £m
Wages and salaries	**334.8**	237.1
Social security costs	**31.9**	22.4
Contributions to defined contribution plans	**1.0**	0.4
(Decrease) / increase in liability for defined benefit plans	**(6.7)**	4.6
Share based payments	**0.9**	0.4
	361.9	264.9

5 Directors

Total emoluments of directors (including pension contributions) amounted to £2.0m (2005 : £2.3m).

Information relating to directors' emoluments, share options and pension entitlements is set out in the Directors' Remuneration Report on pages 27 to 34.

6 Finance costs

	2006 £m	2005 £m
Interest payable on bank borrowings	**30.0**	11.1
Interest payable on loan notes	**9.5**	8.9
Vehicle stocking plan interest	**25.5**	18.6
Interest payable on finance leases	**0.4**	0.1
Fair value losses - interest rate swaps	**1.0**	-
Unwinding of discounts in contract hire residual values	**2.7**	2.5
Interest on pension scheme obligations	**16.5**	13.8
	85.6	55.0
Less : interest capitalised	**(0.3)**	(0.1)
Total finance costs	**85.3**	54.9

Interest of £0.3m has been capitalised during the year at an average rate of 5.75% on assets under construction.

7 Finance income

	2006 £m	2005 £m
Fair value gains - interest rate swaps	**-**	0.4
Interest receivable on bank deposits	**0.8**	0.8
Interest on pension scheme assets	**16.9**	13.6
Other interest receivable	**-**	0.5
Total finance income	**17.7**	15.3

8 Taxation

	2006	2005
	£m	£m
UK corporation tax :		
Current tax on income for the year	20.1	17.0
Adjustments in respect of prior periods	(3.6)	(2.6)
	16.5	14.4
Overseas taxation :		
Current tax on income for the year	1.4	1.3
Adjustments in respect of prior periods	0.4	(0.4)
	1.8	0.9
Total current tax expense	18.3	15.3
Deferred tax expense :		
Origination and reversal of temporary differences	10.6	4.6
Benefit of tax losses recognised	-	0.8
	28.9	20.7

The total aggregate tax charges recognised in the income statement are analysed as:	2006	2005
	£m	£m
Current tax	18.3	15.3
Deferred tax	10.6	5.4
Total income tax expense in the income statement	28.9	20.7

Factors affecting the tax charge for the period:

The tax assessed is different than the standard rate of corporation tax in the UK (30%)

The differences are explained below :	2006	2005
	£m	£m
Profit before taxation	96.4	63.8
Tax on profit at UK rate of 30% (2005 : 30%)	28.9	19.1
Differences :		
Accounting depreciation for which no tax relief is due	0.3	0.7
Difference between accounts profits and taxable profits on capital asset disposals	(1.0)	0.8
Other disallowables	1.0	0.1
Unrecognised losses	0.7	1.0
Tax rate differential on overseas income	0.3	0.5
Movement in rolled over and held over chargeable gains	(0.4)	(0.2)
Asset impairment charge	0.3	0.3
Adjustments to tax charge in respect of previous periods	(1.2)	(1.6)
Total tax charge	28.9	20.7

Deferred tax (expense) / credit recognised directly in equity	2006	restated * 2005
	£m	£m
Relating to share based payments	1.5	3.4
Actuarial gains and losses	(5.4)	5.1
	(3.9)	8.5

8 Taxation (continued)

Factors affecting the future tax charge

The group operates in countries where the tax rates are different to that of the UK rate. Germany has a lower tax rate than the UK whilst the US tax rate is higher compared to the UK. As is common in the motor retail industry, the group also incurs a significant level of other expenses which are not tax deductible (mainly depreciation on showrooms and other non deductible capital expenditure). As a result, it is expected that the effective rate of tax on the group's trading profits will continue to be higher than the standard rate of UK corporation tax.

Unrecognised deferred tax assets

There are unutilised tax losses within the group of £15.5m (2005 : £13.0m) relating to overseas businesses for which no deferred tax asset has been recognised pending clarity of the availability of intra-EU losses.

Deferred tax assets / (liabilities)

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority. The offset amounts are as follows:

	2006 **£m**	restated * 2005 £m
Deferred tax assets	**26.5**	35.3
Deferred tax liabilities	**(68.5)**	(37.3)
	(42.0)	(2.0)

The movements in temporary differences for the year are as follows:

	restated * At 1 January 2005 £m	On acquisition £m	Charged / (credited) to consolidated income statement £m	Credited to equity £m	Charged to investment £m	Exchange differences £m	restated * **At 31 December 2005** **£m**
Property, plant and equipment	28.8	-	2.3	-	-	0.2	**31.3**
Rolled over and held over gains	6.6	-	(0.7)	-	-	-	**5.9**
Retirement benefit obligations	(23.9)	-	0.6	-	-	-	**(23.3)**
Share based payments	(2.1)	-	0.6	(3.4)	-	-	**(4.9)**
Actuarial gains and losses	(0.6)	-	-	(5.1)	-	-	**(5.7)**
Tax value of loss carry-forwards	(0.8)	-	0.8	-	-	-	**-**
Financial instruments	-	-	0.1	-	-	-	**0.1**
Provisions	(3.1)	-	1.7	-	-	-	**(1.4)**
Tax liabilities / (assets)	4.9	-	5.4	(8.5)	-	0.2	**2.0**

* See change in accounting policy - see note 1r

8 Taxation (continued)

	At 1 January 2006 £m	On acquisition £m	Charged / (credited) to consolidated income statement £m	Charged / (credited) to equity £m	Charged to investment £m	Exchange differences £m	**At 31 December 2006 £m**
Property, plant and equipment	31.3	19.7	1.8	-	5.9	(0.1)	**58.6**
Rolled over and held over gains	5.9	4.4	(0.4)	-	-	-	**9.9**
Intangible assets	-	0.6	(0.6)	-	-	-	**-**
Retirement benefit obligations	(23.3)	(4.6)	5.7	-	-	-	**(22.2)**
Share based payments	(4.9)	-	4.4	(1.5)	-	-	**(2.0)**
Actuarial gains and losses	(5.7)	-	-	5.4	-	-	**(0.3)**
Financial instruments	0.1	-	(0.3)	-	-	-	**(0.2)**
Provisions	(1.4)	(0.4)	-	-	-	-	**(1.8)**
Tax liabilities / (assets)	2.0	19.7	10.6	3.9	5.9	(0.1)	**42.0**

9 Earnings per share

	2006 Earnings per share pence	**2006 Earnings Total £m**	restated * 2005 Earnings per share pence	restated * 2005 Earnings Total £m
Basic earnings per share	**10.7**	**67.5**	7.0	43.1
Adjusting items :				
Profit on business and property disposals	**(3.9)**	**(24.3)**	(1.2)	(7.4)
Goodwill impairment	**0.1**	**0.9**	0.2	1.1
Abortive acquisition costs	**0.2**	**1.0**	-	-
Gain on curtailment of defined benefit pension schemes	**(1.6)**	**(9.9)**	-	-
Operating exceptional costs	**0.6**	**4.0**	0.3	1.8
Tax effect of adjusting items	**1.4**	**8.1**	0.4	2.8
Adjusted earnings per share	**7.5**	**47.3**	6.7	41.4
Diluted earnings per share	**10.6**	**67.5**	6.8	43.1

The calculation of basic, adjusted and diluted earnings per share is based on the following number of shares in issue (millions):

	2006 Number	restated * 2005 Number
Weighted average number of ordinary shares in issue	**629.0**	619.3
Weighted average number of dilutive shares under option	**10.7**	17.0
Weighted average number of shares in issue taking account of applicable outstanding share options	**639.7**	636.3

The directors consider that the adjusted earnings per share figure provides a better measure of comparative performance.

* The note has been restated following the subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

10 Intangible assets

	Goodwill £m	Other intangibles £m	**Total £m**
Cost			
At 1 January 2005	174.7	9.3	**184.0**
Additions through business combinations	1.7	-	**1.7**
Other additions	-	0.4	**0.4**
Exchange adjustments	1.2	-	**1.2**
Disposals	(8.3)	(0.2)	**(8.5)**
At 31 December 2005	169.3	9.5	**178.8**
At 1 January 2006	169.3	9.5	**178.8**
Additions through business combinations	272.5	3.2	**275.7**
Other additions	-	0.5	**0.5**
Exchange adjustments	(1.5)	-	**(1.5)**
Disposals	(0.9)	(0.5)	**(1.4)**
Classified as non-current assets held for sale	(1.7)	-	**(1.7)**
At 31 December 2006	437.7	12.7	**450.4**
Amortisation			
At 1 January 2005	1.9	7.7	**9.6**
Amortised during the year	-	0.6	**0.6**
Impairment	1.1	-	**1.1**
At 31 December 2005	3.0	8.3	**11.3**
At 1 January 2006	3.0	8.3	**11.3**
Amortised during the year	-	3.1	**3.1**
Impairment	0.9	-	**0.9**
Disposals	-	(0.1)	**(0.1)**
At 31 December 2006	3.9	11.3	**15.2**
Carrying amounts			
At 1 January 2005	172.8	1.6	**174.4**
At 31 December 2005	166.3	1.2	**167.5**
At 1 January 2006	166.3	1.2	**167.5**
At 31 December 2006	433.8	1.4	**435.2**

The amortisation charge is in respect of other intangibles is recognised within operating expenses in the income statement.

Impairment losses of £0.9m of goodwill attaching to business units pending closure where the future cash flows from these are not expected to recover the goodwill carrying value are recognised within operating expenses in the income statement (2005 : £1.1m recognised during the year are in respect of goodwill of MG Rover franchises impaired following the collapse of the manufacturer).

Goodwill is allocated across multiple cash-generating units and consequently a consistent approach in assessing the carrying value of this amount is taken. This value was determined by discounting the future cash flows generated from the continuing use of the unit and was based on the following key assumptions:

Cash flows were projected based on actual operating results and the current business plan with regard to the long term strategy of the group in terms of business representation. These were extrapolated over a 20 year period. Management believes that this forecast period was justified due to the long term outlook for the industry and the groups dominant position in the market place.

Whilst it is anticipated that the units will grow revenues in the future for the purpose of the impairment testing no growth has been assumed.

A pre tax discount rate of eight percent was applied in determining the recoverable amount of the units which the group have estimated to be the approximate weighted average cost of capital of the group.

10 Intangible assets (continued)

Goodwill by segment	**2006**	2005
	£m	£m
Stratstone	**158.8**	52.8
Evans Halshaw	**236.7**	93.7
Chatfields	**12.9**	12.9
Support	**0.9**	0.9
Contract Hire	**24.5**	6.0
	433.8	166.3

11 Property, plant and equipment

	Land & buildings £m	Plant & equipment £m	Motor vehicles £m	**Total £m**
Cost				
At 1 January 2005	332.8	42.5	173.1	**548.4**
Additions through business combinations	16.9	1.4	-	**18.3**
Other additions	19.2	12.1	122.8	**154.1**
Exchange adjustments	0.9	0.2	-	**1.1**
Disposal of businesses	(4.5)	(1.0)	(0.4)	**(5.9)**
Other disposals	(91.6)	(4.1)	(113.4)	**(209.1)**
Classified as non-current assets held for sale	(20.2)	-	-	**(20.2)**
At 31 December 2005	253.5	51.1	182.1	**486.7**
At 1 January 2006	253.5	51.1	182.1	**486.7**
Additions through business combinations	198.8	11.0	46.2	**256.0**
Other additions	28.6	13.8	131.5	**173.9**
Exchange adjustments	(1.6)	(0.4)	(0.1)	**(2.1)**
Disposal of businesses	(0.4)	(0.4)	-	**(0.8)**
Other disposals	(212.4)	(9.8)	(143.6)	**(365.8)**
Classified as non-current assets held for sale	(31.4)	(0.2)	-	**(31.6)**
At 31 December 2006	235.1	65.1	216.1	**516.3**
Depreciation				
At 1 January 2005	5.7	21.4	49.5	**76.6**
Exchange adjustments	0.1	0.1	-	**0.2**
Charge for the year	4.0	6.7	36.2	**46.9**
Disposal of businesses	(0.7)	(0.6)	(0.2)	**(1.5)**
Other disposals	(0.5)	(0.9)	(26.8)	**(28.2)**
Classified as non-current assets held for sale	(1.3)	-	-	**(1.3)**
At 31 December 2005	7.3	26.7	58.7	**92.7**
At 1 January 2006	7.3	26.7	58.7	**92.7**
Exchange adjustments	(0.2)	(0.3)	-	**(0.5)**
Charge for the year	4.4	11.3	46.3	**62.0**
Disposal of businesses	-	(0.3)	-	**(0.3)**
Other disposals	(2.4)	(7.4)	(47.3)	**(57.1)**
Classified as non-current assets held for sale	(0.9)	-	-	**(0.9)**
At 31 December 2006	8.2	30.0	57.7	**95.9**

11 Property, plant and equipment (continued)

Carrying amounts	Land & buildings £m	Plant & equipment £m	Motor vehicles £m	**Total £m**
At 1 January 2005	327.1	21.1	123.6	**471.8**
At 31 December 2005	246.2	24.4	123.4	**394.0**
At 1 January 2006	246.2	24.4	123.4	**394.0**
At 31 December 2006	226.9	35.1	158.4	**420.4**

Included in the amounts for plant, equipment and motor vehicles above are the following amounts relating to leased assets and assets acquired under hire purchase contracts:

	Land & buildings £m	Plant & equipment £m	Motor vehicles £m	**Total £m**
Depreciation				
Charge for the year	-	0.4	1.7	**2.1**
Carrying amounts				
At 31 December 2005	0.6	1.8	0.4	**2.8**
At 31 December 2006	0.6	-	8.2	**8.8**

Interest of £0.3m has been capitalised during the year at an average rate of 5.75% on assets under construction.

Cumulative interest charges of £0.4m (2005 : £0.7m) have been capitalised as construction costs and included in land and buildings.

Land and buildings include £4.5m (2005 : £7.6m) in respect of building projects currently under construction for which no depreciation has been charged during the year. Future capital expenditure which has been contracted for but not yet provided in the financial statements amounted to £2.9m (2005 : £10.9m).

12 Interest in joint venture

The group has a 51% ordinary share capital interest in a joint venture PPH0 Limited, a company that is incorporated and trading in the United Kingdom, whose principal activity is that of a property company. The joint venture is accounted for under the equity accounting method and included in the consolidated financial statements as a non-current asset of £3.0m (2005: £1.4m) that represents the group's interests in the assets and liabilities of the joint venture which is analysed below. The group's share of revenues and expenses of the joint venture included in the income statement is also presented:

	2006 £m	2005 £m
Non-current assets	**162.2**	41.9
Current assets	**23.9**	7.2
Non-current liabilities	**(166.0)**	(41.0)
Current liabilities	**(17.1)**	(6.7)
	3.0	1.4
Income	**3.7**	0.5
Expenses	**(3.2)**	(0.4)
Income tax expense	**(0.1)**	-
	0.4	0.1

The group, whilst holding a 51% holding in the ordinary share capital of PPH0 Limited, holds by way of a contractual agreement 50% of the voting rights attaching to that company, thereby giving the group joint control.

PPH0 Limited has borrowings secured on its land and buildings. At 31 December 2006 PPH0 Limited has no contractual capital commitments.

13 Inventories

	2006 £m	2005 £m
New and used vehicles	**671.9**	490.1
Consignment vehicles	**124.7**	109.1
Vehicle parts and other inventories	**53.6**	42.6
	850.2	641.8

Inventories recognised as an expense during the year	**4,321.0**	2,765.6
Inventories stated at fair value less costs to sell	**3.2**	2.7
Carrying value of inventories subject to retention of title clauses	**637.1**	503.7

During the year £0.1m was recognised as an net credit to expenses in respect of the write down of vehicle parts inventories due to general obsolescence (2005 : £0.8m expense).

14 Trade and other receivables

	2006 £m	2005 £m
Trade receivables	**140.9**	99.9
Other receivables	**110.2**	49.0
Other taxation and social security	**-**	4.2
Prepayments	**9.8**	8.5
	260.9	161.6

At 31 December 2006 trade receivables are shown net of an allowance for doubtful debts of £1.4m (2005: £0.3m). The expense recognised for bad debts during the year was £0.5m (2005: £0.4m).
All amounts are due within one year.

15 Trade and other payables

	2006 £m	2005 £m
Trade payables	**810.8**	641.0
Consignment vehicle liabilities	**124.7**	109.1
Payments received on account	**15.9**	15.6
Other taxation and social security	**26.3**	3.4
Accruals	**194.1**	86.4
	1,171.8	855.5

As at 31 December 2006, the outstanding commitment to purchase ex-contract vehicles that were not supplied by the company amounted to £15.5m (2005: £21.8m). Expected losses in respect of these commitments of £3.0m (2005: £7.0m) are included in accruals.

16 Interest bearing loans and borrowings

	2006	2005
	£m	£m
Non-current liabilities		
Unsecured bank loans	**262.0**	123.6
Unsecured loan notes	**102.5**	129.8
Finance lease liabilities (see note 25)	**6.5**	2.6
	371.0	256.0
Current liabilities		
Unsecured bank loans	**-**	-
Unsecured other loans	**4.0**	4.0
Unsecured loan notes	**1.3**	-
Finance lease liabilities (see note 25)	**5.1**	0.9
	10.4	4.9

Note 17 sets out the maturity profile of non-current liabilities.

17 Financial instruments and derivatives

Financial risk management

Treasury policy and procedures

Group treasury matters are managed within policy guidelines set by the Board with prime areas of focus being liquidity, interest rate and foreign exchange exposure. Management of these areas is the responsibility of the group's central treasury function. Derivative financial instruments are utilised to reduce exposure to movements in foreign exchange rates and interest rates. The Board does not permit the speculative use of derivatives.

Funding and liquidity management

The group is financed primarily by loan notes, bank loans, vehicle stocking credit lines and operating cash flow. Committed facilities have a range of maturities, are maintained at levels in excess of planned requirements and are in addition to short term uncommitted facilities that are also available to the group.

Each business within the group is responsible for its own day to day cash management and the overall cash position is monitored on a daily basis by the group treasury department. Where our overseas subsidiaries borrow to fund their businesses they do so independently of and without recourse to the UK parent company.

Interest rate risk management

The objective of the group's interest rate policy is to minimise interest costs whilst protecting the group from adverse movements in interest rates. Borrowings issued at variable rates expose the group to cash-flow interest rate risk whereas borrowings issued at fixed rates expose the group to fair value interest rate risk. The group does not actively manage cash flow interest rate risk as the Board believes that the retail sector in which the group operates provides a natural hedge against interest rate movements. Consequently, it is group policy to borrow on a floating rate basis and all fair value interest rate risk arising from fixed rate borrowings entered into by the group are managed by swaps into floating rate.

17 Financial instruments and derivatives (continued)

Foreign exchange risk management

The group faces currency risk in respect of its net assets denominated in currencies other than sterling. On translation into sterling movements in currency will affect the value of these assets. The group's policy is therefore to match, where possible, net assets in overseas subsidiaries which are denominated in a foreign currency with borrowings in the same currency. Similarly, where the group borrows in a foreign currency to finance assets denominated in sterling the borrowings are swapped into sterling. In line with these policies the group has swapped all of its fixed rate loan notes denominated in US dollars into floating rate sterling and has borrowed Euro 10.0m (2005 : Euro 17.0m) and USD 49.0m (2005 : USD 46.0m) against its net assets held in overseas subsidiaries.

Credit risk management

The group is exposed to credit risk primarily in respect of its trade receivables and financial assets. Trade receivables are stated net of provision for estimated doubtful receivables. Exposure to credit risk in respect of trade receivables is mitigated by the group's policy of only granting credit to certain customers after an appropiate evaluation of credit risk. Credit risk arises in respect of amounts due from manufacturers in relation to bonuses and warranty receivables. This risk is mitigated by the range of manufacturers dealt with, the group's procedures in effecting timely collection of amounts due and management's belief that it does not expect any manufacturer to fail to meet its obligations. Financial assets comprise cash balances and assets arising from transactions involving derivative financial instruments. The counterparties are banks with sound credit ratings and management does not expect any counterparty to fail to meet its obligations. The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet.

Accounting for derivative financial instruments and hedging activities

The group holds derivative financial instruments to hedge currency and interest risks arising from its activities. Derivative financial instruments are measured at fair value at each balance sheet date. Where a derivative financial instrument hedges the changes in fair value of recognised assets or liabilities, any gain or loss is recognised in the income statement. The hedged item is also stated, separately from the derivative, at fair value in respect of the risk being hedged with any gain or loss also recognised in the income statement. This will result in variations in the balance sheet values of the hedged item and the offsetting derivatives as the market value fluctuates. The fair value of derivatives and hedged items is the estimated amount receivable or payable to terminate the contract determined by reference to calculations provided by financial institutions utilising market prices prevailing at the balance sheet date.

Hedges

Fair value hedges of interest rate and currency risk

The group classifies its interest rate and currency swaps as fair value hedges and states them at fair value. The fair value of interest rate and currency swaps at 1 January 2005 was adjusted against opening retained earnings. The net fair value of swaps used as hedges of the group's USD and GBP loan notes is set out below:

Fair value hedge	**Assets carrying value & fair value 2006 £m**	**Liabilities carrying value & fair value 2006 £m**	Assets carrying value & fair value 2005 £m	Liabilities carrying value & fair value 2005 £m
Currency and interest swap (USD 110m /GBP : fixed rate to floating rate) expiring 2011	**-**	**(4.8)**	3.4	-
Currency and interest swap (USD 67m / GBP : fixed rate to floating rate) expiring 2014	**-**	**(2.9)**	2.5	-
Interest swap (GBP 17m : fixed rate to floating rate) expiring 2014	**-**	**(0.3)**	0.6	-
Total	**-**	**(8.0)**	6.5	-

All derivative financial instrument assets and liabilities are non-current. The critical terms of the derivative financial instrument and the hedged item match (i.e. currency, notional amount, and timing of rate resets and payments) and therefore changes in the fair value attributable to the risk being hedged are expected to be offset by the hedging derivative financial instrument.

17 Financial instruments and derivatives (continued)

Hedges of net investments in overseas operations

Included within bank borrowings are balances denominated in US dollar and euro which are each designated as hedges of the net investment in the group's US and German subsidiaries respectively. The aggregate fair value of these borrowings was £31.8m at 31 December 2006. Foreign exchange gains of £3.2m on translation of the borrowings to sterling at the balance sheet date are recognised within the translation differences reserve in equity, net of exchange losses of £3.4m in respect of the net investments being hedged.

Cash and cash equivalents

Bank balances and bank overdrafts set out below are stated net of legal rights of set-off resulting from pooling arrangements operated by individual banks.

	Carrying value & fair value 2006 £m	Carrying value & fair value 2005 £m
Bank balances and cash equivalents	**19.7**	82.1
Bank overdrafts	-	(4.7)
	19.7	77.4

Borrowings	**Carrying value & fair value 2006 £m**	Carrying value & fair value 2005 £m
Non-current		
Bank borrowings	**262.0**	123.6
5.65% USD 110 million loan notes 2011	**53.2**	60.8
5.95% USD 67 million loan notes 2014	**32.4**	37.4
5.95% GBP 17 million loan notes 2014	**16.7**	17.6
Other loan notes	**0.2**	14.0
Finance leases	**6.5**	2.6
Total non-current	**371.0**	256.0
Current:		
Other loan notes	**1.3**	-
Finance leases	**5.1**	0.9
Other loans	**4.0**	4.0
Total borrowings	**381.4**	260.9

The effective interest rates for all borrowings after taking into account derivative financial instruments are all based on LIBOR for the relevant currency. Finance leases are effectively held at fixed rates of interest with a weighted average rate of 6%. Information regarding classification of balances and interest, the range of interest rates applied in the year to 31 December 2006 and repricing periods, is set out in the table overleaf.

17 Financial instruments and derivatives (continued)

	Carrying value & fair value £m	Classification	Interest classification	Interest rate range	Effect of interest rate and currency swaps	Swapped interest rate range	Repricing periods
Bank balances and cash equivalents	**19.7**	Amortised cost	Floating GBP	4.50% - 5.00 %	N/A	N/A	6 months or less
Bank overdrafts	**-**	Amortised cost	Floating GBP	5.50% - 6.00 %	N/A	N/A	6 months or less
	19.7						
Borrowings							
Non-current							
Bank borrowings	**262.0**	Amortised cost	Floating GBP	3.67% - 6.60 %	N/A	N/A	6 months or less
5.65% USD 110 million loan notes 2011	**53.2**	Fair value	Fixed USD	5.65 %	Floating GBP	6.44% - 6.95 %	6 months or less
5.95% USD 67 million loan notes 2014	**32.4**	Fair value	Fixed USD	5.95 %	Floating GBP	6.22% - 6.73 %	6 months or less
5.95% GBP 17 million loan notes 2014	**16.7**	Fair value	Fixed GBP	5.95 %	Floating GBP	6.22% - 6.73 %	6 months or less
Other loan notes	**0.2**	Amortised cost	Floating GBP	12.50 %	N/A	N/A	6 months or less
Finance leases	**6.5**	Amortised cost	Fixed GBP	4.71% - 6.36 %	N/A	N/A	See note 25
Total non-current	**371.0**						
Current:							
Finance leases	**5.1**	Amortised cost	Fixed GBP	4.71% - 6.36 %	N/A	N/A	See note 25
Other loan notes	**1.3**	Amortised cost	Floating GBP	4.11% - 4.51 %	N/A	N/A	6 months or less
Other loans	**4.0**	Amortised cost	Floating GBP	5.07% - 5.73 %	N/A	N/A	6 months or less
Total borrowings	**381.4**						

In addition, included within trade payables (see note 15) is £45.7m (2005: £43.1m) in respect of contract hire vehicle lease liabilities. These are stated at amortised cost with fixed interest rates that average 6.0%.

The carrying amounts of the Group's borrowings are denominated in the following currencies:

	2006 £m	2005 £m
Pound sterling	**339.5**	212.3
US dollar	**35.2**	37.0
Euro	**6.7**	11.6
	381.4	260.9

The maturity of non-current borrowings is as follows:

	2006 £m	2005 £m
Between 1 and 2 years	**56.7**	126.7
Between 2 and 5 years	**211.8**	11.2
Over 5 years	**102.5**	118.1
	371.0	256.0

The group has the following undrawn borrowing facilities:

	2006 £m	2005 £m
Expiring in more than one year but not more than two years	**-**	151.8
Expiring in more than two years	**268.2**	1.2
	268.2	153.0

The group has a £550m revolving credit facility which is subject to covenants with respect to debt / EBITDA and fixed charge coverage. Similar covenants are also in place for the group's USD and GBP loan notes expiring 2011/2014.

18 Provisions

The movements in provisions for the year are as follows :	Warranty service provision £m	Vacant property £m	**Total £m**
At 31 December 2005	-	1.9	**1.9**
Reclassified from accruals and deferred income	1.7	-	**1.7**
Provisions made during the year	6.4	0.1	**6.5**
Provisions assumed from business combinations	6.5	0.7	**7.2**
Provisions used during the year	(4.4)	(0.8)	**(5.2)**
Provisions reversed during the year	-	(0.2)	**(0.2)**
At 31 December 2006	10.2	1.7	**11.9**
Non-current	6.5	1.1	**7.6**
Current	3.7	0.6	**4.3**
	10.2	1.7	**11.9**

The provision on warranty service contracts relates to future repair costs expected against income received in advance, on products sold during the last three years. It is expected this expenditure will be incurred within three years of the balance sheet date.

The vacant property provision is comprised of the future costs of vacated properties, being predominantly future lease commitments. The present value of future lease commitments is calculated using an 8% discount rate and assumes that any sub-let properties will remain so until the end of the sub-lease.

19 Called up share capital

On 22 December 2006, in order to increase the number of ordinary shares in issue and consequently to reduce the price at which the ordinary shares are traded, the ordinary shares of 25p each were subdivided in to five new ordinary shares of 5p each.

	Number	**£m**
Authorised shares of 25p each at 31 December 2005	160,000,000	**40.0**
Subdivision of shares	640,000,000	-
Authorised shares of 5p each at 31 December 2006	800,000,000	**40.0**
Allotted, called up and fully paid shares of 25p each at 31 December 2005	131,201,720	**32.8**
Subdivision of shares	524,806,880	**-**
Issued during the year	18,750	**-**
Allotted, called up and fully paid shares of 5p each at 31 December 2006	656,027,350	**32.8**

During the year 18,750 (2005 : 69,750) ordinary shares at an aggregate nominal value of £938 (2005 : £3,488) were issued for a total cash consideration of £1,905 (2005 : £10,382). The shares were issued pursuant to the 1989 Executive Share Option Scheme.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the company. All shares rank equally with regard to the company's residual assets.

20 Reserves

Reconciliation of movement in capital and reserves

	Share capital £m	Share premium £m	Capital redemption reserve £m	Other reserves £m	Translation reserve £m	restated * Retained earnings £m	restated * **Total £m**
Balance at 1 January 2005	32.8	56.8	2.5	12.6	(0.3)	116.4	**220.8**
Impact of change in accounting policy	-	-	-	-	-	(1.3)	**(1.3)**
Balance at 1 January 2005, restated *	32.8	56.8	2.5	12.6	(0.3)	115.1	**219.5**
Total recognised income and expense for 2005	-	-	-	-	0.2	31.1	**31.3**
Dividends	-	-	-	-	-	(15.6)	**(15.6)**
Share based payments	-	-	-	-	-	3.8	**3.8**
Disposal of own shares in share trusts	-	-	-	-	-	0.3	**0.3**
Balance at 31 December 2005	32.8	56.8	2.5	12.6	(0.1)	134.7	**239.3**
Balance at 1 January 2006	32.8	56.8	2.5	12.6	(0.1)	134.7	**239.3**
Total recognised income and expense for 2006	-	-	-	-	(0.2)	80.2	**80.0**
Dividends	-	-	-	-	-	(17.4)	**(17.4)**
Share based payments	-	-	-	-	-	2.4	**2.4**
Disposal of own shares in share trust	-	-	-	-	-	1.7	**1.7**
Balance at 31 December 2006	32.8	56.8	2.5	12.6	(0.3)	201.6	**306.0**

* See change in accounting policy - see note 1r

Capital redemption reserve

The capital redemption reserve has arisen following the purchase by the company of its own shares and comprises the amount by which distributable profits were reduced on these transactions in accordance with Chapter VII of Part V of the Companies Act 1985.

Other reserves

Other reserves comprise the amount of demerger reserve arising on the demerger of the company from Williams Holdings PLC in 1989.

The market value of the investment in the company's own shares at 31 December 2006 was £21.0m (2005 : £35.6m), being 21.0m (2005 : 35.0m) shares with a nominal value of 5p each, acquired at a cost of between £0.08 and £0.43 each. The amounts deducted from retained earnings for shares held by ESOP trusts at 31 December 2006 was £7.9m (2005 : £9.6m). The investment in own shares represents shares in the company held by Pendragon Quest Trustees Limited and Investec Trust Guernsey Limited (employee share ownership trusts) which may subsequently be awarded to Executive Directors and employees under the Pendragon 1999 Approved Executive Share Option Scheme, Pendragon 1999 Unapproved Executive Share Option Scheme and the 1998 Pendragon Sharesave Scheme. Details of the plans are given in the Directors' Remuneration Report on pages 27 to 34.

Dividends on the shares owned by the trusts, the purchase of which were funded by interest free loans to the trusts from Pendragon PLC, are waived. All expenses incurred by the trusts are settled directly by Pendragon PLC and charged in the accounts as incurred.

The trusts are regarded as quasi subsidiaries and their assets and results are consolidated into the financial statements of the group.

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the net investment in foreign operations as well as from the translation of liabilities held to hedge the respective net investment in foreign operations.

21 Dividends

	2006	2005
	£m	£m
Ordinary shares		
Final dividend in respect of 2005 of 1.32p per share (2004 : 1.20p)	**8.2**	7.4
Interim dividend in respect of 2006 of 1.45p per share (2005 : 1.32p)	**9.2**	8.2
	17.4	15.6

A final dividend in respect of 2006 of 2.00p (2005: 1.32p) per share amounting to a total of £12.7m (2005: £8.2m) is proposed by the Board. The dividend proposed will not be accounted for until it has been approved at the Annual General Meeting.

Dividends on the 21.0m shares held by Pendragon Quest Trustees Limited and Investec Trust Guernsey Limited are waived.

The note has been restated following the subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

22 Business combinations

Reg Vardy plc

On 14 February 2006 the group acquired all of the shares in Reg Vardy plc for a total consideration including costs of £504.2m in cash. Reg Vardy plc is the parent company of a group of companies involved in motor vehicle retailing and repair.

In the 10 1/2 months to 31 December 2006 the subsidiary contributed profit of £32.4m.

Net assets at date of acquisition:

	Book value £m	Fair value adjustments £m	**Fair value £m**
Property, plant and equipment	205.6	48.2	**253.8**
Intangible assets	1.1	2.1	**3.2**
Non-current assets classified as held for sale	12.2	6.3	**18.5**
Inventories	306.9	0.1	**307.0**
Trade and other receivables	67.4	0.1	**67.5**
Trade and other payables	(350.7)	(4.9)	**(355.6)**
Cash and cash equivalents	49.1	-	**49.1**
Retirement benefit obligations	(15.0)	(0.9)	**(15.9)**
Bank loans	(50.0)	-	**(50.0)**
Obligations under finance leases	(10.8)	-	**(10.8)**
Tax liabilities	(6.7)	0.5	**(6.2)**
Provisions	(7.2)	-	**(7.2)**
Deferred tax liabilities	(5.1)	(14.6)	**(19.7)**
	196.8	36.9	**233.7**
Goodwill			**270.5**
Consideration (including costs)			**504.2**

Consideration satisfied by cash and cash equivalents	**498.0**
Costs of acquisition	**6.2**
Fair value of consideration paid	**504.2**

Following an investigation into the Reg Vardy plc acquistion by the Office of Fair Trading the group gave undertakings to dispose of four motor vehicle dealerships to avoid referral to the Competition Commission under section 73 of the Enterprise Act 2002. At the balance sheet date one of these businesses had been disposed with the other three due to complete in early 2007.

22 Business combinations (continued)

Other acquisitions

During the year the group also acquired the trade and certain assets and liabilities of a number of retail motor vehicle businesses from a number of different vendors which included:

Date	Business acquired	Consideration £m
17 February 2006	Edinburgh Peugeot	**0.7**
10 March 2006	Speeds Motor Group	**7.1**
22 September 2006	Darlington Citroen and Peugeot	**1.0**
13 December 2006	Peugeot Huddersfield, Leeds and York	**2.1**
		10.9

In the period from acquisition to 31 December 2006 the businesses contributed profit of £0.1m.

Net assets at date of acquisition:

	Book value £m	Fair value adjustments £m	Fair value £m
Property, plant and equipment	2.3	(0.1)	**2.2**
Inventories	6.7	-	**6.7**
Trade and other receivables	0.2	-	**0.2**
Trade and other payables	(0.1)	(0.1)	**(0.2)**
	9.1	(0.2)	**8.9**
Goodwill			**2.0**
Consideration (including costs)			**10.9**

Consideration satisfied by cash and cash equivalents	**10.6**
Costs of acquisition	**0.3**
Fair value of consideration paid	**10.9**

Total fair value of consideration paid on business combinations made in the year	**515.1**

Net cash outflow arising on acquisition

	£m
Cash consideration	**515.1**
Cash and cash equivalents acquired	**(49.1)**
	466.0

Net cash outflow arising on acquistions from the previous period was £35.1m.

If the acquisitions had occurred on 1 January 2006, group revenues would have been £5,482.1m and group profit attribuatble to equity holders of the parent would have been £64.9m.

Goodwill arising in the year through business combinations represents the value attributed to the future profitability of the acquired businesses together with the associated benefits from economies of scale facilitated by the business combination, the scale of the acquired assembled workforce and franchise arrangements, which cannot be separately identified or measured.

An intangible asset has been recognised in respect of the fair value of the order book which existed on the date of acquisition. This intangible asset has been amortised over the period the orders are fulfilled.

No business combinations have been made between the balance date and the date of this report.

23 Business disposals

Net assets at date of disposal

	Net book value £m
Property, plant and equipment	**0.5**
Non-current assets classified as held for sale	**18.5**
Inventories	**4.2**
Trade and other receivables	**0.2**
Trade and other payables	**(0.4)**
	23.0
Profit on sale of businesses	**0.1**
Proceeds on sale satisfied by cash and cash equivalents	**23.1**

No cash was disposed as part of a business disposal during the year.

Proceeds on sale satisfied by cash and cash equivalents for previous period was £16.2m.

Included within the above business disposals were five motor vehicle dealerships acquired with Reg Vardy plc, the non-current assets of which are disclosed in the business combination table in note 22 as non-current assets held for resale. These assets are therefore excluded from the non-current asset movements in note 11.

24 Cash and cash equivalents

	2006 £m	2005 £m
Bank balances and cash equivalents	**19.7**	82.1
Bank overdrafts	**-**	(4.7)
Cash and cash equivalents in the statement of cash flows	**19.7**	77.4

25 Obligations under finance leases

	Minimum lease payments		Present value of minimum lease payments	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Amounts payable under finance leases:				
Within one year	**5.4**	0.9	**5.1**	0.9
In the second to fifth years inclusive	**5.9**	1.4	**4.9**	1.1
After five years	**8.5**	8.6	**1.6**	1.5
	19.8	10.9	**11.6**	3.5
Less: future finance charges	**(8.2)**	(7.4)	**-**	-
Present value of lease obligations	**11.6**	3.5	**11.6**	3.5
Amount due for settlement within one year			**5.1**	0.9
Amount due for settlement in over one year			**6.5**	2.6
			11.6	3.5

The group's obligations under finance leases comprise certain items of plant and equipment, the average lease term of which is 2 to 3 years and three properties on long term leases with a lease term of between 61 and 86 years. The effective interest rates were in the range of 4.71% to 6.36% (2005 : 6.0%). The group's obligations under finance leases are secured by the lessors' charges over the leased assets.

All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments.

26 Operating lease arrangements

The group as lessee

At the balance sheet date, the group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2006	2005
	£m	£m
Within one year	**69.5**	22.5
In the second to fifth years inclusive	**177.0**	79.2
After five years	**510.7**	216.7
	757.2	318.4

The group leases a number of properties, the majority of which are motor vehicle showrooms with workshop and parts retail facilities, with varying lease periods. None of these leases includes contingent rentals. In addition there are other leases in respect of items of plant and equipment which includes the rental of motor vehicles hired for short term usage typically as courtesy cars.

The group as lessor

Property rental income earned during the year was £0.5m (2005 : £1.2m). No contingent rents were recognised in income (2005 : £nil).
At the balance sheet date, the group had contracted with tenants for the following future minimum lease payments:

	2006	2005
	£m	£m
Within one year	**0.9**	1.1
In the second to fifth years inclusive	**3.1**	2.6
After five years	**5.6**	4.8
	9.6	8.5

In addition, the group is a lessor in respect of vehicle sales with committed repurchase terms. There are no future minimum lease payments outstanding.

27 Employee benefits

Share schemes

The number and weighted average exercise prices of share options is as follows:

	Weighted average exercise price 2006	**Number of options millions 2006**	restated * Weighted average exercise price 2005	restated * Number of options millions 2005
Outstanding at beginning of period	31.70 p	38.3	27.12 p	36.2
Lapsed during the period	38.33 p	(5.0)	32.04 p	(3.6)
Exercised during the period	24.70 p	(16.0)	11.98 p	(4.6)
Granted during the period	68.68 p	7.0	60.40 p	10.3
Outstanding at the end of the period	45.55 p	24.3	37.44 p	38.3
Exercisable at the end of the period	28.00 p	5.1	17.75 p	0.6

* The note has been restated following the subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

The options outstanding at 31 December 2006 have an exercise price in the range of 9.1 pence to 130.6 pence and a weighted contractual life of 2.7 years. All share options are settled in equity.

27 Employee benefits (continued)

Movements in the number of options to acquire ordinary shares under the group's various share option schemes, together with exercise prices and the outstanding position at 31 December 2006 were as follows :

Exercise period	Date of grant	Scheme Description	Exercise price per share	31 December 2005 Number	Granted Number	Exercised Number	Lapsed Number	31 December 2006 Number
17 March 2001 to 16 March 2008	17 March 1998	1989 Executive Scheme	24.6 p	125,000	-	-	(18,750)	106,250
9 October 2001 to 8 October 2008*	9 October 1998	1989 Executive Scheme	10.2 p	125,000	-	(18,750)	-	106,250
1 July 2006 to 31 December 2006	1 July 1999	1998 Sharesave Scheme	13.6 p	243,105	-	(199,890)	(43,215)	-
21 June 2002 to 20 June 2009	21 June 1999	1999 Executive Scheme	13.0 p	50,000	-	(37,500)	-	12,500
1 July 2007 to 31 December 2007	1 July 2000	1998 Sharesave Scheme	9.1 p	602,930	-	-	-	602,930
9 March 2004 to 8 March 2011	9 March 2001	1999 Executive Scheme	18.7 p	335,745	-	(184,200)	-	151,545
1 July 2006 to 31 December 2006	1 July 2001	1998 Sharesave Scheme	18.0 p	311,820	-	(311,820)	-	-
1 July 2008 to 31 December 2008	1 July 2001	1998 Sharesave Scheme	18.0 p	71,585	-	-	(2,630)	68,955
24 March 2006 to 23 March 2013	24 March 2003	1999 Executive Scheme	23.4 p	13,774,950	-	(10,250,500)	(375,000)	3,149,450
1 July 2006 to 31 December 2006	1 July 2003	1998 Sharesave Scheme	24.6 p	4,024,450	-	(3,756,765)	(242,175)	25,510
1 July 2008 to 31 December 2008	1 July 2003	1998 Sharesave Scheme	24.6 p	1,724,840	-	(13,365)	(202,875)	1,508,600
1 July 2010 to 31 December 2010	1 July 2003	1998 Sharesave Scheme	24.6 p	556,310	-	-	(47,675)	508,635
30 September 2006 to 29 September 2013	30 September 2003	1999 Executive Scheme	40.2 p	2,910,000	-	(1,215,445)	(195,000)	1,499,555
20 September 2007 to 19 September 2014	20 September 2004	1999 Executive Scheme	60.2 p	3,875,000	-	-	(250,000)	3,625,000
1 July 2008 to 31 December 2008	1 July 2005	1998 Sharesave Scheme	60.4 p	5,206,335	-	(23,560)	(1,198,060)	3,984,715
1 July 2010 to 31 December 2010	1 July 2005	1998 Sharesave Scheme	60.4 p	3,657,065	-	(2,490)	(1,346,720)	2,307,855
1 July 2012 to 31 December 2012	1 July 2005	1998 Sharesave Scheme	60.4 p	745,540	-	-	(154,220)	591,320
1 July 2009 to 31 December 2009	1 July 2006	1998 Sharesave Scheme	130.6 p	-	3,027,195	-	(343,780)	2,683,415
1 July 2011 to 31 December 2011	1 July 2006	1998 Sharesave Scheme	130.6 p	-	3,015,400	-	(393,815)	2,621,585
1 July 2013 to 31 December 2013	1 July 2006	1998 Sharesave Scheme	130.6 p	-	931,155	-	(137,670)	793,485
				38,339,675	6,973,750	(16,014,285)	(4,951,585)	24,347,555

* Parallel grant

The share option arrangements scheduled above include a number of arrangements granted before 7 November 2002. The recognition and measurement principles in IFRS 2 have not been applied to those grants in accordance with the transitional provisions of IFRS 1 and IFRS 2.

On 1 July 2006 options over 6,973,750 ordinary shares of 5p were granted pursuant to the 1998 Pendragon Sharesave Scheme at an exercise price of 130.6p per share.

The grants of share options under the 1989 and 1999 Schemes prescribed an earnings per share performance criterion. It is a pre-condition to the exercise of grants made under the 1989 and 1999 Schemes that the growth in the company's earnings per share over the prescribed three year period must exceed by at least 3 per cent per annum (for 1999 scheme) and 2 percent per annum (for the 1989 scheme) compound the annual rate of inflation as shown by the RPI Index.

The weighted average share price at the date of exercise for share options exercised in the year was 25.7 pence (2005 : 63.0 pence).

The vesting conditions attaching to the 1998 Pendragon Sharesave schemes are that the option holder must be employed by the group on the date of exercise.

All options are settled by physical delivery of shares.

27 Employee benefits (continued)

The fair value of services received in return for share options is measured by reference to the fair value of the options granted. The estimate of the fair value of the services received in respect of share option and share save schemes is measured using the Black-Scholes option pricing model. The estimate of the fair value of services received in respect of the Long Term Incentive Plan (LTIP) (see Directors Renumeration Report) is measured using a stochastic model which incorporates the discount factor required for the total shareholder return performance condition. The weighted average fair value of the options at the date of grant for those that are outstanding at 31 December 2006 is 19.2 pence (2005: 6.0 pence). There were no executive share options granted during 2006 to any team members. The average assumptions input into the models for options granted under the share save schemes and LTIP in the year were as follows:

	Share save scheme		Long term incentive plan	
	2006	2005	**2006**	2005
Number of share options granted in year	**6,973,750**	10,345,235	**1,502,525**	-
Weighted average share price (pence)	**130.6**	60.4	**1.21**	-
Weighted average exercise price (pence)	**130.6**	60.4	**-**	-
Expected volatility (%)	**32.8%**	31.7%	**33.5%**	-
Expected life (years)	**4.4**	4.1	**3.0**	-
Risk free rate (%)	**4.7%**	4.0%	**4.7%**	-
Expected dividend yield (%)	**2.6%**	5.1%	**2.2%**	-

Expected volatility was determined by calculating the historical volatility of the group's share price over the corresponding historical period. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of exercise restrictions and team member turnover.

The group recognised a total expense of £0.9m (2005 : £0.4m) related to equity-settled share based payment transactions, of which £0.3m (2005: £nil) was in respect of the LTIP.

The note has been restated following the subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

Pension obligations

The group operates seven defined benefit pension schemes (four of which have defined contribution sections) which closed to future benefits from 30 September 2006 and employees were offered membership of a defined contribution scheme. The asset values shown do not include those of the defined contribution sections. Actuarial gains and losses are recognised directly in equity immediately. Actuarial gains and losses consist of differences between actual and expected returns on scheme assets during the year, experience losses on scheme liabilites and the impact of any changes in assumptions. Details of the last independent statutory actuarial valuation and assumptions are set out below by scheme.

The group increased it's level of contributions to all of the schemes and five of the schemes will have formal actuarial valuations as at April 2006 under the UK Government's new Scheme Specific Funding arrangements. The group has agreed funding plans with the seven schemes which aim to eliminate the current deficits over a five year period.

Pendragon Pension Plan

The Pendragon Pension Plan is a funded defined benefit scheme with a defined contribution section. The last actuarial valuation of the Plan was carried out as at 6 April 2003 using the defined accrued benefit method. At this date the market value of the Plan's assets relating to the defined benefit section was £50.4m; these assets represented 85% of the value of accrued liabilities. The main assumptions used for this valuation were that the annual rate of return on existing investments would be between 5.6% - 8.6%, the annual rate of earnings increases would be 5%, and the annual rate of pension increases would be between 2.6% - 3.5%.

The employer contributions paid to the defined benefit section of the Plan during the year were £4.3m, based upon actuarial advice.

Stripestar Pension Scheme

The Stripestar Pension Scheme is a funded defined benefit scheme with a defined contribution section. The last actuarial valuation of the Scheme was carried out as at 6 April 2004 using the defined accrued benefit method. At this date the market value of the Scheme's assets relating to the defined benefit section was £5.15m; these assets represented 73% of the value of accrued liabilities. The main assumptions used for this valuation were that the annual rate of return on existing investments would be between 4.9% - 6.9%, the annual rate of earnings increases would be 5%, and the annual rate of pension increases would be 3%.

The employer contributions paid to the defined benefit section of the Scheme during the year were £0.5m, based upon actuarial advice.

27 Employee benefits (continued)

CD Bramall Pension Scheme

The CD Bramall Pension Scheme is a funded defined benefit scheme. The last actuarial valuation was carried out as at 5 April 2003 using the attained age method. At the valuation date, the market value of assets was £10.1m; these assets represented 62% of the value of accrued liabilities, after allowing for expected future increases in earnings. The main assumptions used for this valuation were that the annual rate of return on existing investments would be between 5.75% - 6.75%, the annual rate of earnings increases would be 4%, and the annual rate of pension increases would be 2.5%.

The employer contributions paid to the Scheme during the year were £1.5m, based upon actuarial advice.

CD Bramall Dealerships Limited Pension Scheme

The CD Bramall Dealerships Limited Pension Scheme is a funded defined benefit scheme. The last actuarial valuation was carried out as at 5 April 2003 using the attained age method.

At the valuation date, the market value of assets was £13.4m; these assets represented 64% of the value of accrued liabilities, after allowing for expected future increases in earnings. The main assumptions used for this valuation were that the annual rate of return on existing investments would be between 5.75% - 6.75%, the annual rate of earnings increases would be 4%, and the annual rate of pension increases would be 2.5%.

The employer contributions paid to the Scheme during the year were £1.3m, based upon actuarial advice.

CD Bramall Retirement Benefits Scheme

The CD Bramall Retirement Benefits Scheme is a funded defined benefit scheme with a defined contribution section. The last actuarial valuation was carried out as at 31 March 2003 using the attained age method. At the valuation date, the market value of assets relating to the defined benefit section was £2.84m; these assets represented 60% of the value of accrued liabilities, after allowing for expected future increases in earnings. The main assumptions used for this valuation were that the annual rate of return on existing investments would be between 5.75% - 6.75%, the annual rate of earnings increases would be 4%, and the annual rate of pension increases would be 2.5%.

The employer contributions paid to the Scheme during the year were £0.4m, based upon actuarial advice.

Quicks Pension Scheme

The Quicks Pension scheme is a funded defined benefit scheme. The last actuarial valuation was carried out as at 6 April 2005 using the defined accrued benefit method. At the valuation date, the market value of assets was £51.8m; these assets represented 67% of the value of accrued liabilities. The main assumptions used for this valuation were that the annual rate of return on existing investments would be between 5.4% - 6.4%, the annual rate of earnings increases would be 3.9% and the annual rate of pension increases would be between 2.9% - 3.2%.

The employer contributions paid to the Scheme during the year were £6.9m, based upon actuarial advice.

Reg Vardy plc Retirement Scheme

The Reg Vardy plc Retirement Scheme is a funded defined benefit scheme. An actuarial valuation was performed as at 30 April 2004 and used the projected unit method. The main actuarial assumptions were an investment return of 6.6% per annum, salary increases of 3% per annum, a yield of 5.5.% underlying the capitalisation of pensions from and during retirement, and Limited Price Indexation pension increases of 2.5% per annum.

The employer contributions paid to the Scheme during the year were £1.4m, based upon actuarial advice.

Stakeholder arrangements

With effect from April 2006, new contributions to the defined contribution sections of the schemes ceased. For the employees affected the group offered to pay contributions to a new stakeholder arrangement with Friends Provident. This arrangement was also made available to the employees affected by the closure of the defined benefit sections of the schemes on 30 September 2006. Total contributions paid by the group in 2006 to the stakeholder arrangement were £0.9m.

27 Employee benefits (continued)

IAS19 assumptions

The principal assumptions used by the independent qualified actuaries for the purposes of IAS19 for all schemes were:

	2006	2005	2004
Inflation	**2.90 %**	2.80 %	2.80 %
Rate of increase in salaries	**n/a**	4.10 %	4.10 %
Rate of increase to pensions in payment	**2.90 %**	2.80 %	2.80 %
Discount rate	**5.20 %**	4.80 %	5.50 %
Mortality table assumption	**PA92YOB****	PA92C2005**	PA92C2005**

The expected long term rates of return on the main asset classes were:

	2006	2005	2004
Equities	**8.60 %**	8.10 %	8.50 %
Bonds	**4.70 %**	4.50 %	5.00 %
Cash	**4.60 %**	4.10 %	4.50 %

The weighted average expected long term rates of return were:

	2006	2005	2004
	7.66 %	7.32 %	7.83 %

The overall expected return on assets reflects the Directors' long term view of future returns taking into account market conditions at the year end and asset allocation of the schemes.

The assumptions used by the actuary are the best estimates chosen from a range of possible acturial assumptions which, due to the timescale covered, may not necessarily be borne out in practice. The IAS assumptions have been updated at 31 December 2006 and differ from those used for the earlier independent statutory actuarial valuations explained above.

** The mortality table assumption implies the following expected future lifetime from age 65:

	2006 years	2005 years	2004 years
Males aged 45	**20.9**	18.5	18.5
Females aged 45	**23.9**	21.5	21.5
Males aged 65	**19.6**	18.5	18.5
Females aged 65	**22.7**	21.5	21.5

The fair value of the schemes' assets which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the value of the schemes' liabilities, which is derived from cash flow projections over long periods and thus inherently uncertain, are:

Scheme assets and liabilities

	2006 £m	restated * 2005 £m	restated * 2004 £m
Equities	**215.9**	165.8	137.5
Bonds	**59.9**	39.0	28.3
Cash	**8.0**	5.7	3.6
Fair value of scheme assets	**283.8**	210.5	169.4
Present value of funded defined benefit obligations	**(349.0)**	(300.9)	(249.6)
Net liability on the balance sheet	**(65.2)**	(90.4)	(80.2)

27 Employee benefits (continued)

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

	2006 £m	restated * 2005 £m
Net liability for defined benefit obligations at 1 January	**(90.4)**	(80.2)
Contributions received	**16.3**	11.5
Expense recognised in the income statement	**6.7**	(4.6)
Actuarial gains and losses recognised in equity	**18.1**	(17.1)
Deficit assumed in a business combination	**(15.9)**	-
Net liability for defined benefit obligations at 31 December	**(65.2)**	(90.4)

	2006 £m	2005 £m
Actual return on assets	**27.0**	35.0
Expected contributions in following year	**18.6**	13.7

Total expense recognised in the income statement

	2006 £m	2005 £m
Current service cost	**3.6**	4.4
Interest on obligation	**16.5**	13.8
Expected return on assets	**(16.9)**	(13.6)
Gains on curtailments	**(9.9)**	-
	(6.7)	4.6

The expense is recognised in the following line items in the income statement:

	2006 £m	2005 £m
Administrative expenses	**(6.3)**	4.4
Finance costs	**16.5**	13.8
Finance income	**(16.9)**	(13.6)
	(6.7)	4.6

Actuarial gains and losses recognised directly in equity

	2006 £m	restated * 2005 £m
Cumulative amount at 1 January	**(19.0)**	(1.9)
Recognised during the period	**18.1**	(17.1)
Cumulative amount at 31 December	**(0.9)**	(19.0)

Amounts recognised in the statement of recognised income and expense

	2006 £m	2005 £m
Difference between actual and expected return on scheme assets	**10.1**	21.4
Experience (loss) / gain on scheme liabilities	**(12.3)**	0.2
Changes in assumptions underlying the present value of scheme obligations	**20.3**	(38.7)
	18.1	(17.1)

27 Employee benefits (continued)

Changes in the present value of the defined benefit obligation

	2006 £m	2005 £m
Opening present value of defined benefit obligation	**300.9**	249.6
Current service cost	**3.6**	4.4
Interest cost	**16.5**	13.8
Actuarial (gains) / losses	**(8.0)**	38.5
Gains on curtailments	**(9.9)**	-
Liabilities assumed in a business combination	**53.3**	-
Employee element of service cost	**1.1**	1.5
Less benefits paid	**(8.5)**	(6.9)
Closing present value of defined benefit obligation	**349.0**	300.9

Movement in fair value of scheme assets during the period

	2006 £m	2005 £m
Opening fair value of assets	**210.5**	169.4
Expected return on assets	**16.9**	13.6
Actuarial gains on assets	**10.1**	21.4
Contributions by employer	**16.3**	11.5
Assets acquired in a business combination	**37.4**	-
Employee contributions	**1.1**	1.5
Less benefits paid	**(8.5)**	(6.9)
End of period	**283.8**	210.5

History of experience adjustments

	2006 £m	2005 £m	2004 £m
Present value of defined benefit obligation	**349.0**	300.9	249.6
Fair value of scheme assets	**283.8**	210.5	169.4
Deficit in schemes	**65.2**	90.4	80.2
Experience adjustments on scheme liabilities			
Amount	**(8.0)**	38.5	10.1
Percentage of scheme liabilities (%)	**(2.3%)**	12.8 %	4.0 %
Experience adjustments on scheme assets			
Amount	**10.1**	21.4	8.3
Percentage of scheme liabilities (%)	**2.9%**	7.1 %	3.3 %

*See change in accounting policy- see note 1r.

28 Related party transactions

Subsidaries

The group's ultimate parent company is Pendragon PLC. A listing of all principal trading subsidaries is shown within the financial statements of the company on page 82.

Joint venture

The group has a 51% ordinary share capital interest in a joint venture PPH0 Limited, whose principal activity is that of a property company. The group occupies properties owned by PPH0 Limited and it's group on short term leases.

During the year the group entered into transactions with it's related party and has balances outstanding at 31 December as follows:

	2006	2005
	£m	£m
Rent paid to related party	**7.2**	1.0
Proceeds of property sold to related party	**262.2**	-
Management fee received from related party	**0.1**	-
Amounts owed to related party	**1.0**	-
Amounts owed from related party	**27.1**	-

Transactions with key management personnel

The key management personnel of the group comprise the executive and non-executive directors. The details of the remuneration, long term incentive plans, shareholdings, share option and pension entitlements of individual directors are included in the Directors' Remuneration Report on pages 27 to 34.

Directors of the company and their immediate relatives control 5.5% of the ordinary shares of the company.

During the year the key management personnel compensation was as follows:	**2006**	2005
	£m	£m
Short term employee benefits	**1.8**	2.1
Post-employment benefits	**0.2**	0.2
Share based payments	**0.4**	0.1
	2.4	2.4

In addition to services as a non-executive director, Mr N G Hannah provides commercial property advice to the group under a retainer arrangement. In 2006 he earned benefits to the value of £30,000 (2005 : £30,000) in the form of fees. As chairman and a shareholder of commercial property surveyors Innes England Limited, Mr Hannah is interested in contracts for the provision of their services to the group, which during the year had an aggregate value of £30,000 (2005 : £89,000). Mr Hannah retired as non-executive director in December 2006.

29 Deferred Income

The group entered into a sale and leaseback arrangement in December 2006 with its joint venture company PPH0 Limited, in which a number of properties were disposed of generating total proceeds of £250.1m. The arrangement entitles PPH0 Limited to lease back those properties to the group over a period of over 25 years, a factor resulting in the group receiving a consideration in excess of the deemed fair value as at the date of disposal, when measured under an open market valuation in accordance with IFRS. The proceeds received were estimated to be greater than the fair value of the properties by £22.0m and as required by IAS 17 'Leases' this excess over fair value is deferred and amortised over the period of the leases. Of the remaining profit on disposal of the properties of £37.3m before costs, £18.3m was allocated to realised profit and £19.0m to investment in joint ventures, being the unrealised element.

30 Non-current assets classified as held for sale

The group holds a number of freehold properties and items of plant and equipment that are currently being marketed for sale which are expected to be disposed during 2007. Impairment losses of £4.0m on the remeasurement of these assets to the lower of their carrying amount and their value less costs to sell have been recognised in the income statement within Other income - gains on the sale of businesses and property.

During the year non-current assets classified as held for sale disposed realised a profit of £10.9m which is included on the income statement under Other income - gains on the sale of businesses and property.

These properties form part of central segment assets.

31 Accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Critical accounting judgements when applying the group's accounting policies

Certain critical accounting judgements in applying the group's accounting policies are described below:

Goodwill impairment

The carrying value of Goodwill is tested annually for impairment by using cash flow projections for each cash generating unit. These projections are based upon actual and short term planned results extrapolated over a 20 year period. A discount rate of 8.0% is used.

Intangible assets

Management undertook a review of intangible assets that are pertinent to the motor business. This included consideration of customer lists, franchise rights, brands and other intangible assets. The review concluded that for acquisitions undertaken since 1 January 2004 no intangible assets or rights had been acquired with the exception of the value attaining to the order book that existed at the point of acquisition.

Repurchase commitments

The group enters into leasing arrangements whereby it agrees to repurchase vehicles from lessees or providers of lease finance at the end of the lease agreement, typically two to four years in the future. The repurchase price is determined at the time the agreement is entered into based on the then estimate of a vehicle’s future residual value. The actual value of the vehicles at the end of the lease contract, and therefore the proceeds that can be realised from eventual sale, can vary materially from these estimates. Annual reviews are undertaken to reappraise residual values.

	Notes	2006 £m	2005 £m
Fixed assets			
Investments	5	**1,020.5**	499.6
Current assets			
Debtors (2005 includes £7.0m due after more than one year)	6	**8.1**	19.7
Cash at bank and in hand		**94.0**	5.9
		102.1	25.6
Creditors: amounts falling due within one year	7	**(573.3)**	(138.3)
Net current liabilities		**(471.2)**	(112.7)
Total assets less current liabilities		**549.3**	386.9
Creditors: amounts falling due after more than one year	8	**(362.1)**	(242.8)
Net assets		**187.2**	144.1
Capital and reserves			
Called up share capital	10	**32.8**	32.8
Share premium account	11	**56.8**	56.8
Capital redemption reserve	11	**2.5**	2.5
Other reserves	11	**13.9**	13.9
Profit and loss account	11	**81.2**	38.1
Equity shareholders' funds		**187.2**	144.1

Approved by the Board of Directors on 15 February 2007 and signed on its behalf by:

T G Finn

Chief Executive

D R Forsyth

Finance Director

The notes on pages 79 to 85 form part of these financial statements.

RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS YEAR ENDED 31 DECEMBER 2006

	Note	2006 £m	2005 £m
Profit for the financial year		**57.2**	11.2
Dividends	4	**(17.4)**	(15.6)
		39.8	(4.4)
Share based payments		**1.6**	-
Disposal of own shares in share trusts		**1.7**	0.3
Net additions / (reduction) to shareholders' funds		**43.1**	(4.1)
Opening shareholders' funds		**144.1**	147.8
Adoption of FRS26 on 1 January 2005		**-**	0.4
Closing shareholders' funds		**187.2**	144.1

The notes on pages 79 to 85 form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS OF THE COMPANY

1 Accounting policies

(a) Accounting convention The financial statements have been prepared in accordance with applicable UK accounting standards using the historical cost convention. The financial statements have been prepared on a going concern basis.

(b) Deferred taxation Full provision is made for deferred taxation on all timing differences which have arisen but have not reversed at the balance sheet date, except as follows:

(i) tax payable on the future remittance of the past earnings of subsidiaries is provided only to the extent that dividends have been accrued as receivable or a binding agreement to distribute all past earnings exists;

(ii) deferred tax assets are recognised only to the extent that it is more likely than not that they will be recovered.

Deferred tax is measured on a non discounted basis at the tax rates that are expected to apply in the periods in which the timing differences reverse, based on tax rates and laws substantively enacted at the balance sheet date.

(c) Financial instruments The company holds derivative financial instruments to hedge currency and interest risks arising from its activities. Derivative financial instruments are recognised initially at cost, if any, and are subsequently re-measured at fair value. Any gain or loss on remeasurement is recognised in the profit and loss account. However, the treatment of gains or losses arising from derivatives which qualify for hedge accounting depends on the nature of the hedged item itself. The fair value of derivatives is the estimated amount receivable or payable to terminate the contract determined by reference to the market prices prevailing at the balance sheet date.

In accordance with its treasury policy, the company has swapped its fixed rate USD liabilities into floating rate GBP liabilities by utilising cross currency interest rate swaps.

As permitted by Financial Reporting Standard 26 'Financial Instruments: Measurement' these policies were adopted on 1 January 2005.

Fair value hedges

Where a derivative financial instrument hedges the changes in fair value of recognised assets or liabilities, any gain or loss is recognised in profit and loss. The hedged item is also stated, separately from the derivative, at fair value in respect of the risk being hedged with any gain or loss also recognised in profit and loss. This will result in variations in the balance sheet values of the gross debt and the offsetting derivatives as the market value fluctuates.

(d) Investments Investments held as fixed assets are stated at cost less any impairment losses.

(e) Employee Benefits – Share Based Payments The company operates a number of employee share option schemes. The fair value at the date at which the share options are granted is recognised in profit and loss on a straight line basis over the vesting period, taking into account the number of options that are expected to vest. The number of options that are expected to become exercisable is reviewed at each balance sheet date and if necessary estimates are revised. In accordance with the transitional provisions of FRS20, no profit and loss expenses are recorded in respect of grants of share options made prior to 7 November 2002.

(f) Cash flow statement As the ultimate holding company of the Pendragon group, the company has relied upon the exemption in FRS 1 (revised) and has not included a cash flow statement as part of its own financial statements.

(g) Pensions The Company participates in a group wide defined contribution pension scheme. The assets of the scheme are held separately from those of the Company in an independently administered fund. The amount charged to the profit and loss account represents the contributions payable to the scheme in respect of the accounting period.

The Company participates in a group wide 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.

(h) Related parties Under FRS 8 the company has relied upon the exemption not to disclose related party transactions with other group undertakings as they are all included in the Pendragon PLC consolidated financial statements.

(i) Dividends Dividends proposed by the Board and unpaid at the end of the year are not recognised in the financial statements until they have been approved by the shareholders at the Annual General Meeting. Interim dividends are recognised when they are paid.

(j) Own shares held by ESOP trust Transactions of the group-sponsored ESOP trust are included in the company financial statements. In particular, the trust's purchases of shares in the Company are debited directly to equity.

(k) Contingent liabilities Where Pendragon PLC, the company enters into financial guarantee contracts to guarantee the indebtedness of other companies within its 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.

2 Profit and loss account of the company

In accordance with the exemption allowed by Section 230 (4) of the Companies Act 1985, the profit and loss account of the company is not presented. The profit after taxation attributable to the company dealt with in its own accounts for the year ended 31 December 2006 is £57.2m (2005 : £11.2m).

3 Directors

Total emoluments of directors (including pension contributions) amounted to £2.0m (2005 : £2.3m).
Information relating to directors' emoluments, share options and pension entitlements is set out in the Directors' Remuneration Report on pages 27 to 34.

The directors are the only employees of the company.

4 Dividends

	2006	2005
	£m	£m
Ordinary shares		
Final dividend in respect of 2005 of 1.32p per share (2004 : 1.20p)	**8.2**	7.4
Interim dividend in respect of 2006 of 1.45p per share (2005 : 1.32p)	**9.2**	8.2
	17.4	15.6

A final dividend in respect of 2006 of 2.00p (2005 : 1.32p) per share amounting to a total of £12.7m (2005 : £8.2m) is proposed by the Board. The dividend proposed will not be accounted for until it has been approved at the Annual General Meeting.

The note has been restated following the subdivision of the ordinary shares of 25p each into five new ordinary shares of 5p each.

5 Investments

Company	Shares in joint venture £m	Shares in subsidiary undertakings £m	Loans to subsidiary undertakings £m	**Total £m**
At 31 December 2005	6.5	403.1	90.0	**499.6**
Additions	15.1	505.8	-	**520.9**
At 31 December 2006	21.6	908.9	90.0	**1,020.5**

Shares in jointly controlled undertakings represent a 51 per cent holding of the issued ordinary share capital of PPH0 Limited, a property holding company incorporated and trading in the United Kingdom.

The company acquired the entire share capital of Reg Vardy plc for a total consideration of £504.2m during the year and share based payments on behalf of subsidiary undertakings was £1.6m.

Shares in subsidiary undertakings are stated at cost. Pendragon PLC owns directly or indirectly 100 percent of the issued ordinary share capital of the following principal subsidaries.

5 Investments (continued)

Name	Activity
Incorporated in Great Britain:	
Alloy Racing Equipment Limited	Motor vehicle dealer
Andre Baldet Limited	Motor vehicle dealer
Bramall Contracts Limited	Contract hire and fleet management
Bramall Quicks Dealerships Limited	Motor vehicle dealer
Bridgegate Limited	Motor vehicle dealer
Cadillac GB Limited	Motor vehicle dealer
Car Fleet Control Limited	Computer systems and services
CD Bramall (York) Limited	Motor vehicle dealer
CD Bramall Dealerships Limited	Motor vehicle dealer
CD Bramall Motors Limited	Motor vehicle dealer
Charles Sidney Holdings Limited	Motor vehicle dealer
Chatfield Martin Walters Limited	Motor vehicle dealer
Derwent Vehicles Limited	Motor vehicle dealer
Evans Halshaw (Chesham) Limited	Motor vehicle dealer
Evans Halshaw Motors Limited	Motor vehicle dealer
Executive Motors Limited	Motor vehicle dealer
Extra Leasing Limited	Plant leasing and rentals
Pendragon Contracts Limited	Contract hire and fleet management
Pendragon Javelin Limited	Motor vehicle dealer
Pendragon Management Services Limited	Management services
Pendragon Motor Group Limited	Motor vehicle dealer
Pendragon Motorcycles Limited	Motor vehicle dealer
Pendragon Orient Limited	Motor vehicle dealer
Pendragon Premier Limited	Motor vehicle dealer
Pendragon Property Holdings Limited	Property holdings
Pendragon Sabre Limited	Motor vehicle dealer
Pendragon Viking Limited	Motor vehicle dealer
Petrogate Limited	Property holdings
Pinewood Technologies PLC *	Computer systems and services
Reg Vardy (AMC) Limited	Motor vehicle dealer
Reg Vardy (Fleet) Limited	Motor vehicle dealer
Reg Vardy (MML) Limited	Motor vehicle repairs
Reg Vardy (Property Management) Limited	Property holdings
Reg Vardy (TMC) Limited	Motor vehicle dealer
Reg Vardy (VMC) Limited	Motor vehicle dealer
Reg Vardy Limited *	Motor vehicle dealer
Stripestar Limited	Motor vehicle dealer
Trust Properties Limited	Property holdings
Vardy (Continental) Limited	Motor vehicle dealer
Vardy Marketing Limited	Marketing Services
Vertcell Limited	Motor vehicle parts distribution
Victoria (Bavaria) Limited	Motor vehicle dealer

5 Investments (continued)

Name	Activity
Incorporated in Germany:	
Autohus Avalon Darmstadt GmbH	Motor vehicle dealer
Autohaus Avalon Frankfurt GmbH	Motor vehicle dealer
Autohaus Avalon Munchen GmbH	Motor vehicle dealer
Jaguar Autohaus Kronberg GmbH	Motor vehicle dealer
Incorporated in the United States of America:	
Bauer Motors Inc.	Motor vehicle dealer
Penegon West Inc.	Motor vehicle dealer
South County Inc.	Motor vehicle dealer
Lincoln Irvine Inc.	Motor vehicle dealer
Penegon Mission Viejo Inc.	Motor vehicle dealer
Penegon Newport Beach Inc.	Motor vehicle dealer

* Direct subsidiary of Pendragon PLC

6 Debtors

	2006 £m	2005 £m
Amounts due within one year:		
Corporation tax	**5.1**	9.1
Other debtors	**3.0**	3.6
	8.1	12.7
Amounts after more than one year:		
Deferred tax (see note 9)	**-**	0.5
Derivative financial instruments	**-**	6.5
	-	7.0
	8.1	19.7

7 Creditors : amounts falling due within one year

	2006 £m	2005 £m
Unsecured loan notes	**1.3**	-
Amounts due to subsidiary undertakings	**569.9**	137.8
Other creditors and accruals	**2.1**	0.5
	573.3	138.3

8 Creditors : amounts falling due after more than one year

	2006 £m	2005 £m
Unsecured bank loans (repayable between one and two years)	**40.0**	113.2
Unsecured loan notes (repayable between one and two years)	**-**	13.8
Unsecured bank loans (repayable between two and five years)	**211.8**	-
Unsecured loan notes (repayable after five years)	**102.3**	115.8
Derivative financial instruments	**8.0**	-
	362.1	242.8

8 Creditors : amounts falling due after more than one year (continued)

Unsecured loan notes (repayable after five years) comprise:	**2006**	2005
	£m	£m
5.65% USD 110 million loan notes 2011	**53.2**	60.8
5.95% USD 67 million loan notes 2014	**32.4**	37.4
5.95% GBP 17 million loan notes 2014	**16.7**	17.6
	102.3	115.8

9 Deferred tax

The movements in the deferred tax asset for the year is as follows:

	Deferred tax
	£m
At 31 December 2005	0.5
Profit and loss account	(0.5)
At 31 December 2006	-

Deferred tax asset is shown within debtors (see note 6)

The amount of deferred tax asset in the financial statements is as follows:

	2006	2005
	£m	£m
Other timing differences	**-**	0.5

10 Called up share capital

On 22 December 2006, in order to increase the number of ordinary shares in issue and consequently to reduce the price at which the ordinary shares are traded, the ordinary shares of 25p each were subdivided into five new ordinary shares of 5p each.

	Number	**£m**
Authorised shares of 25p each at 31 December 2005	160,000,000	**40.0**
Subdivision of shares	640,000,000	**-**
Authorised shares of 5p each at 31 December 2006	800,000,000	**40.0**
Allotted, called up and fully paid shares of 25p each at 31 December 2005	131,201,720	**32.8**
Subdivision of shares	524,806,880	**-**
Issued during the year	18,750	**-**
Allotted, called up and fully paid shares of 5p each at 31 December 2006	656,027,350	**32.8**

During the year 18,750 (2005 : 69,750) ordinary shares at an aggregate nominal value of £938 (2005 : £3,488) were issued for a total cash consideration of £1,905 (2005 : £10,382). The shares were issued pusuant to the 1989 Executive Share Option Scheme.

Movements in the number of options to acquire ordinary shares under the group's various share option schemes, together with exercise prices and the outstanding position at 31 December 2006 are fully disclosed above on page 70 of this report.

11 Reserves

	Share premium account £m	Capital redemption reserve £m	Other reserves £m	Profit and loss account £m
At 31 December 2005	56.8	2.5	13.9	38.1
Retained profit for the year	-	-	-	39.8
Disposal of own shares in share trusts	-	-	-	1.7
Share based payments	-	-	-	1.6
At 31 December 2006	56.8	2.5	13.9	81.2

The market value of the investment in the company's own shares at 31 December 2006 was £21.0m (2005 : £35.6m), being 21.0m (2005 : 35.0m) shares with a nominal value of 5p each, acquired at a cost of between £0.08 and £0.43 each. The amounts deducted from retained earnings for shares held by ESOP trusts at 31 December 2006 was £7.9m (2005 : £9.6m). The investment in own shares represents shares in the Company held by Pendragon Quest Trustees Limited and Investec Trust Guernsey Limited (employee share ownership trusts) which may subsequently be awarded to Executive Directors and employees under the Pendragon 1999 Approved Executive Share Option Scheme, Pendragon 1999 Unapproved Executive Share Option Scheme and the 1998 Pendragon Sharesave Scheme. Details of the plans are given in the Directors' Remuneration Report on pages 27 to 34.

Dividends on the shares owned by the trusts, the purchase of which were funded by interest free loans to the trusts from Pendragon PLC, are waived. All expenses incurred by the trusts are settled by Pendragon PLC and charged in the accounts as incurred.

12 Financial instruments and derivatives

	2006 £m	2005 £m
Changes in fair value (charged) / credited to profit and loss	**(1.0)**	0.4

Details of valuation techniques and fair values of each category of financial instruments are given above in note 17 to the consolidated financial statements on page 61 in the section headed 'Fair value hedges of interest rate and currency risk'.

13 Pensions

The company is a member of a funded group wide pension scheme (Pendragon Pension Plan) providing benefits based on final pensionable pay. The company is unable to identify its share of the scheme assets and liabilties on a consistent and reasonable basis and as permitted by FRS 17 'Retirement Benefits', the scheme has been accounted for in these financial statements as if the scheme was a defined contribution scheme. At 31 December 2006 the scheme had a deficit on an FRS 17 basis of £19.8m (2005: £28.1m).

The latest full actuarial valuation was carried out at 6 April 2003 and was updated for FRS 17 purposes to 31 December 2006 by a qualified independent actuary, KPMG.

The company has no outstanding pension contributions (2005: £nil).

14 Contingent liabilities

(a) The company has entered into cross-guarantees with its bankers whereby it guarantees payment of bank borrowings in respect of UK subsidiary undertakings.

(b) The company has given performance guarantees in the normal course of business in respect of subsidiary undertaking obligations.

Stock classification

The ordinary shares of the company are traded on the London Stock Exchange. Information concerning the day to day movement of the share price can be found on the London Stock Exchange's website under the code PDG. Users of GlobalTOPIC Trader and Reuters can identify the stock by the code PDG.L, and Bloomberg users by the code PDG LN.

Financial calendar

Ex-dividend date for 2006 proposed final dividend	4 April 2007
Record Date for 2006 proposed final dividend	10 April 2007
Annual General Meeting	27 April 2007
Payment date for 2006 proposed final dividend	2 May 2007
Interim results for 2007 announced	August 2007
Interim dividend for 2007 payable	October 2007
Final results for 2007 announced	February 2008
Final dividend for 2007 payable	April 2008

Share dealing service

The following companies offer private investors a quick and easy telephone share dealing service for dealings in the company's shares.

Barclays Stockbrokers Limited will purchase and sell shares at the following commission rates plus stamp duty and PTM Levy of £1 where applicable, subject to the minimum dealing charge of £15.00 per transaction.
1.5% commission on first £5,000
0.85% commission on the next £5,000
0.15% commission thereafter

Details of the service may be obtained by telephoning 0845 702 3021 (calls are charged at local rates and this telephone number can be accessed only from within the United Kingdom). For your protection, to check instructions and to maintain high quality service standards, Barclays Stockbrokers may record and monitor calls made to or from them.

Capita Registrars, a Trading Division of Capita IRG Trustees Limited, will purchase and sell shares at the following commission rates plus stamp duty and PTM Levy where applicable. Online (via www.capitadeal.com) at commission of 1% of the value of the trade, minimum £25/maximum £102.50 dealing charge, or by telephone on 0870 458 4577 at commission of 1.25% of the value of the trade, minimum £20/maximum £50 dealing charge.

Further details of the services including full Terms and Conditions may be obtained by telephoning 0870 458 4577 (calls charged at national rates).

In so far as this statement constitutes a financial promotion it has been approved for the purpose of Section 21 (2) (b) of the Financial Services and Markets Act 2000 only by Capita IRG Trustees Limited who are authorised and regulated by the Financial Services Authority (Register Number 184113)

This is not a recommendation to buy, sell or hold shares in Pendragon PLC. If you are unsure of what action to take, you should contact a financial advisor authorised under the Financial Services and Markets Act 2000. Please note that share values may go down as well as up, which may result in you receiving less than the amount originally invested.

Where the document containing this Shareholder Information on share dealing services has been received in a country where the provision of such a service would be contrary to local laws or regulations, this should be treated as for information only.

PENDRAGON PLC
(Incorporated in England with Registered No. 2304195)

Notice is hereby given that the nineteenth Annual General Meeting of Pendragon PLC (the "Company") will be held at Loxley House, 2 Oakwood Court, Little Oak Drive, Annesley, Nottinghamshire, NG15 0DR on Friday, 27 April 2007 at 10.30 am for the following purposes:

As ordinary business:

1. To receive the annual accounts of the Company for the year ended 31 December 2006, together with the Directors' Report and the Auditors' Report on those accounts and on the auditable part of the Directors' Remuneration Report.
2. To receive and approve the Directors' Remuneration Report (advisory vote).
3. To declare a final dividend.
4. To re-elect Mr M T Davies as a director.
5. To re-elect Miss H C Sykes as a director.
6. To re-elect Mr T G Finn as a director.
7. To re-elect Mr W W Rhodes as a director.
8. To re-appoint KPMG Audit Plc as auditors and to authorise the directors to determine their remuneration.

As special business:

To consider and if thought fit to pass the following resolution, which will be proposed as as a special resolution:

9. THAT the Company be and it is hereby generally and unconditionally authorised pursuant to article 1(K) of the articles of association of the Company and section 166 of the Companies Act 1985 (in substitution for all existing and unexercised authorities granted to the Company pursuant to the said article 1(K) and section 166, which authorities are hereby revoked) to make market purchases (within the meaning of section 163(3) of the Companies Act 1985) of its own ordinary shares on a recognised stock exchange of up to an aggregate of 65,602,735 ordinary shares of 5p each at a price per share which is not more than five per cent above the average of the middle market quotation for shares of the same class derived from the London Stock Exchange Daily Official List during the five dealing days immediately prior to the date of purchase of such shares nor less than the nominal value of the shares, provided that the authority conferred by this resolution shall, unless previously varied, revoked or renewed, expire on 27 October 2007 or at the conclusion of the Annual General Meeting of the Company held in 2008, whichever is the earlier, except in relation to a purchase of shares a contract for which shall have been made before that time.

By order of the Board
H C Sykes
Secretary
15 February 2007

Loxley House
2 Oakwood Court
Little Oak Drive
Annesley
Nottingham
NG15 0DR

A member entitled to attend and vote at the meeting is entitled to appoint one or more proxies to attend and vote on a poll instead of him. A proxy need not be a member of the Company. A proxy form is enclosed and to be effective must reach the Company's registrars, Capita Registrars, The Proxy Processing Centre, Telford Road, Bicester OX26 4LD not less than 48 hours before the time appointed for holding the meeting.

The completion and return by a member of a duly completed form of proxy will not preclude any such member who wishes to do so from attending in person and voting at the Annual General Meeting convened by the above notice.

To be entitled to attend and vote at the meeting (and for the purposes of the determination by the Company of the number of votes they may cast), members must be entered on the Company's register of members by 10.30 am on Wednesday, 25 April 2007. If the meeting is adjourned then, to be so entitled, members must be entered on the Company's register of members at the time which is 48 hours before the time fixed for the adjourned meeting.

Copies of the directors' service contracts and the register of directors' interests maintained under section 325 of the Companies Act 1985 are available for inspection at the Company's registered office during normal business hours on any weekday (excluding Saturdays, Sundays and public holidays) and will also be available for inspection at the place of the meeting for at least 15 minutes before and during the meeting.

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