

FINANCIAL REVIEW

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

The 2005 interim financial statements have been prepared in accordance with the recognition and measurement principles of International Financial Reporting Standards (IFRS) expected to be adopted for use in the European Union by 31 December 2005. The 2004 comparatives have been restated in accordance with the prescribed conversion methodologies contained within the standards. All discussion within the review is on IFRS based financial statements.

The impact of IFRS is set out in detail in note 1. There is no impact on turnover and gross profit other than reclassifications between costs of sales and operating costs. Operating costs are impacted by the different accounting treatment for share based payment schemes and goodwill. The total impact of these adjustments in the six months to 30 June 2004 was to reduce operating profit by only €14,000. There have also been a small number of reclassifications within the balance sheet.

TURNOVER

Turnover growth for the six months to 30 June 2005 was 27.08% bringing turnover to €704.1m (2004: €554.1m). This reflects strong growth across all three divisions. Turnover in 2004 included approximately €12m on the Euro 2004 Football Championship. No replacement event took place in 2005.

– RETAIL

Retail turnover was €401.3m (2004: €340.4m) an increase of 17.89%. Retail turnover growth in Ireland and the UK was 14.12% and 59.79% respectively. Like-for-like turnover growth in Ireland was 10.5%. Average slip size for the total estate grew by 3.8% to €18.53 from €17.85. Slip volumes grew by 13.6% from 19.1m to 21.7m

– NON RETAIL

Telephone betting turnover grew by 20.6% from €105.8m to €127.6m with very strong growth in the Irish market. Growth rates in the UK were modest due to the continued repositioning of the business as noted below. Average stake was €88.73 (2004: €77.02) an increase of 15.20%. Bet volumes increased by 4.7% to 1.44m (2004: 1.37m). The work that commenced in 2004 to refocus the telephone business at the higher end of the mass market has resulted in strong underlying growth in this business as we encourage the lower staking customers to use the internet while focusing both our customer retention and acquisition efforts on higher staking customers. Total active customers (those who have bet in the last three months) were 21,433 (2004: 21,607). Of these 12,474 (2004: 12,539) were Irish and 8,959 (2004: 9,068) were from the UK.

Online turnover increased by 62.5% to €175.2m from €107.8m, an outstanding performance. In general, turnover on gaming product comprises the operator's 'hold', which represents 2% to 3% of the amount staked, while turnover from the

peer-to-peer products, including poker, represents the commission income (rake). The gross win percentage of this business is generally 100%. Conversely, bookmaking product and fixed odds games turnover represents the total amounts staked by customers while the gross win reflects turnover less winnings paid out. Consequently, turnover as a measure of growth, understates the underlying growth of the overall business as the level of gaming activity increases within the online division.

Turnover from the sportsbook was €153.8m (2004: €104.7m) an increase of 46.9%. Turnover from gaming activities totalled €21.4m (2004: €3.1m) an increase of 588.7%. Gaming activity includes the casino, poker, peer-to-peer games and various fixed odds games.

Average bet size in the sportsbook was €28.30 (2004: €25.63) an increase of 10.5%.

Total active online customers (those who have bet in the last three months) were 73,999 (2004: 54,349) an increase of 36.2%. Of these 69,097 bet on at least the sportsbook. 59,132 were solely sportsbook customers, and 14,867 were both sportsbook and gaming customers. Of the total customer base 26,818 (2004: 21,913) were Irish and 47,181 (2004: 32,436) were from the UK.

Customer retention continues to improve across all the non retail businesses and customer acquisition costs remain very competitive.

GROSS WIN AND GROSS PROFIT

Gross win is measured in sports betting and fixed odds games as amounts staked (excluding betting taxes and levies) less the amount returned to customers as winnings. For casino bets and poker rake the customer drop is recorded in both turnover and gross win at 100% margin. Overall gross win rose by 12.1% to €80.9m (2004: €72.2m).

The following gross win percentages were achieved:

Gross Win	H1 2005	H2 2004	H1 2004
Retail	12.4%	11.6%	14.2%
Telephone	8.6%	6.7%	10.4%
Online	11.6%	9.7%	12.0%

Gross win percentages in the sportsbook were exceptionally strong in the first six months of 2004 but reverted to their more normal levels in 2005, albeit lower than expected. This was primarily due to the adverse horse racing results throughout the period with a large number of big races being won by favourites. These results had the greatest impact on the retail division which is most exposed to horseracing.

Gross profit, measured as gross win less the cost of discounting bets, gross win taxes, data rights and third party profit shares rose by 11.4% to €68.7m from €61.6m.

FINANCIAL REVIEW

The following gross profit percentages were achieved:

Gross Profit	H1 2005	H2 2004	H1 2004
Retail	10.9%	10.2%	12.6%
Telephone	7.4%	6.0%	8.8%
Online	8.9%	8.1%	8.7%

OPERATING PROFIT

Operating profit fell by 2.4% to €17.8m (2004: €18.2m) with a significant increase in operating profit in the non retail business being offset by lower operating profit in the retail division. The non retail profit improvements were driven by the strong turnover growth in the sports betting business combined with the strong growth in gaming products. These more than compensated for the poor racing results and increased cost base. Non retail operating profit comprised 63% of operating profits.

Notwithstanding the strong like-for-like sales increase, retail profits fell due to the significantly poorer gross win percentages achieved in 2005 in comparison to 2004, together with the cost of further expansion of the retail estate in Ireland and the UK. This reflects the sensitivity of the retail business to large changes in gross win percentages and does not indicate any structural revenue or cost management issues.

Overall operating costs continue to grow with the expansion of the business and the commitment to investing up front in new businesses.

TAXES

The corporation tax charge for the six months to 30 June 2005 was €2.6m (2004: €2.7m), an effective rate of 14.0% (2004:14.5%). Paddy Power's effective rate is 1.5% above the Irish statutory rate due to a number of non-deductible expenses and its passive income which is taxed above the statutory rate.

CASH FLOW

Net cash flow from operating activities for the six months ended 30 June 2005 fell by 21% to €25.0m from €31.6m in 2004. While operating profits were broadly flat on 2004, the working capital contribution, while positive at €1.1m, was lower than the €9.4m generated in 2004. This was largely due to high Euro 2004 antepost betting in June 2004, and changes in the timings of payments such as taxes and other supplier payments between December 2003 and December 2004. The cash was applied acquiring fixed assets of €11.5m comprising the fit-out of new and relocated outlets as well as computer equipment. In addition, dividends of €6.3m, the funding of share purchases by the trustees of the long-term incentive plan of €2.6m, and corporation taxes of €2.4m were paid during the period. Cash received from the exercise of share options amounted to €0.1m. Cash balances at 30 June 2005 were €50.1m compared to € 47.2m at 31 December 2004. This includes cash balances held on behalf of customers of €6.9m (December 2004: €6.5m).

DIVIDENDS

The Board has decided to pay an interim dividend of 7.75c (2004: 6.2c) per share, an increase of 25% payable on 23 September 2005 to shareholders on the register at the close of business on 9 September 2005. This reflects the Board's desire to have a progressive dividend policy that is not impacted by short-term adverse sporting results.

OUTLOOK

Since 30 June 2005 gross win percentages have been disappointing in the sportsbook with percentages at 11.4%, 8.05% and 5.11% for the retail, online and telephone divisions respectively. Online gaming and poker have continued to grow in line with expectations, and the Group will continue to invest in people and marketing to develop these products during the remainder of the year.

As ever, the outturn for the year will depend on the gross win over the coming months. The Group remains confident of meeting its expansion plans for the year and is well positioned for continued growth in 2006.



Ross Ivers

Finance Director

30 August 2005