Marshalls

# Delivering long-term sustainable growth

**Marshalls plc** Annual Report and Accounts 2017

# Delivering long-term sustainable growth

Our primary objective is to improve profitability and to deliver long-term sustainable growth for our shareholders whilst taking into account the interests of all stakeholders.

**Strategic report**


**Corporate governance**


**Financial statements**


Find us on Facebook
**MarshallsGroup**

Follow us on Twitter
**@MarshallsGroup**

Follow us on LinkedIn
**Marshalls**

Follow us on YouTube
**MarshallsTV**


Find out more online:
**www.marshalls.co.uk**

Front Cover: Marshalls La Lina Paving at De Montfort University


Case study

## Marshalls Design Space in Central London

- Communication facilities in Central London - close to core customer base
- Continues to showcase the Group's brand leading capabilities
- Provides customers with new products, access to samples and technical advice
- Updated regularly – focus on Landscape Architect, Architect and Designer
- Focus on design, technical insights, technology, innovation and sustainability

# Continued progress has been made in the year to deliver the 2020 Strategy

The self help programme to support organic growth is progressing well and we continue to outperform our peers and gain market share.

**"The progress made on both the 2020 Strategy and the acquisition of CPM has allowed us to improve the level of our sustainable operating margins."**

The 2020 Strategy objectives are firmly aligned with delivering sustainable shareholder value and the Group's longer term strategy set out on pages 14 and 15.

Alternative Performance Measures are used consistently throughout the Annual Report and Accounts. These relate to like-for-like, EBITA, EBITDA and ROCE. For further details of their purpose, definition and reconciliation to the equivalent statutory measures see Note 1 to the Financial Statements.

▶ **Our strategy** pages 14 and 15
▶ **Key performance indicators** pages 18 and 19

## The 2020 Strategy remains on track

- EBITDA growth continues alongside improved ROCE and a strengthened brand
- Self help programme well advanced
- Organic capital investment continues
- Research and development expenditure increased in the period
- Focus on innovation, new product development and service to drive sales growth
- Focus on increasing profitability of the emerging UK businesses continues
- Wide-ranging digital strategy continues to drive real benefits across the business
- Continue to target selective bolt-on acquisition opportunities, after the acquisition of CPM
- Maintain a 2 times dividend cover policy, supported by supplementary dividends

## Financial highlights

- Revenue up 8% to £430.2 million (2016: £396.9 million)
- Profit before tax up 13% to £52.1 million (2016: £46.0 million), after charging approximately £1million of acquisition costs
- Return on capital employed ("ROCE") up 8% to 24.8% (2016: 23.0%) on a like-for-like basis
- EPS up 14% to 21.52 pence (2016: 18.95 pence)
- CPM has traded strongly since acquisition and its integration is in line with expectations
- The Group's strong cash generation has continued
- Net debt of £24.3 million (2016: £5.4 million cash) reflects cash outflow relating to the CPM acquisition of £41.4 million
- Final ordinary dividend increased by 17% to 6.80 pence (2016: 5.80 pence) per share
- Supplementary dividend of 4.00 pence per share
- Strong start to 2018 – sales up 18% including CPM (up 4% underlying)


## Case study

# Acquisition of CPM

- CPM is a specialist UK manufacturer of underground concrete pipes, conveyance and water management systems, targeting the Public Sector and Commercial end market.
- CPM has a comprehensive range of technical and innovative water management solutions.
- Manufacturing takes place at two sites – one at Mells (Somerset) and one at Pollington (East Yorkshire). There are ancillary offices in the Midlands and Scotland.
- The business has approximately 350 employees, with the majority based at the Somerset head office site.
- CPM is a growing business with a strong track record of quality and service.
- The business will trade initially as Marshalls CPM, within the wider Marshalls Group.

**Revenue (£'m)**

£430.2m
+8%

| | |
|---|---|
| **2017** | **430.2** |
| 2016 | 396.9 |
| 2015 | 386.2 |
| 2014 | 358.5 |
| 2013 | 307.4 |

**Operating profit (£'m)**

£53.4m
+12%

| | |
|---|---|
| **2017** | **53.4** |
| 2016 | 47.6 |
| 2015 | 37.5 |
| 2014 | 25.3 |
| 2013 | 16.1 |

**EPS (p)**

21.52p
+14%

| | |
|---|---|
| **2017** | **21.52** |
| 2016 | 18.95 |
| 2015 | 14.32 |
| 2014 | 10.13 |
| 2013 | 6.94 |

**Profit before tax (£'m)**

£52.1m
+13%

| | |
|---|---|
| **2017** | **52.1** |
| 2016 | 46.0 |
| 2015 | 35.3 |
| 2014 | 22.4 |
| 2013 | 13.0 |

**Return on capital employed (%)[1]**

24.8%
+8%

| | |
|---|---|
| **2017** | **24.8** |
| 2016 | 23.0 |
| 2015 | 19.0 |
| 2014 | 12.5 |
| 2013 | 8.1 |

**Final dividend recommended (p)**

6.80p
+17%

| | | |
|---|---|---|
| 2017 | 6.8 | 4.0 |
| 2016 | 5.8 | 3.0 |
| 2015 | 4.75 | 2.0 |
| 2014 | 4.0 | |
| 2013 | 3.5 | |

1 2017 ROCE has been calculated on a like-for-like the basis (excluding the impact of CPM).

# The UK's leading hard landscaping manufacturer

Marshalls is a leading brand with a significant market position. Our cornerstone themes of customer service, quality and sustainability put the customer at the very heart of our business model and investment proposition.

▶ **Business model** pages 10 and 11

## What we do

### Public Sector and Commercial

## Landscapes, gardens and seating

Marshalls is the leading innovator of hard landscaping solutions for the commercial construction sector, placing a focus on developing new and innovative products.

Marshalls focuses on developing products which help architects, local authorities and contractors to create better spaces, whether it is street furniture, natural stone paving for the internal or external environment, concrete block paving, water management or protective street furniture products.

**Customers**
Local authorities, commercial architects, specifiers, contractors, housebuilders and builders merchants.

**Products**
Paving, block paving, kerb, water management, natural stone cladding, street furniture, lighting, protective street furniture, walling and mortars.

### Domestic

## Gardens and driveways

Marshalls' Domestic customers range from DIY enthusiasts to professional landscapers, driveway installers and garden designers. Sales continue to be driven through the Marshalls Register of Accredited Landscapers and Driveway Installers.

For homeowners, Marshalls offers the inspiration they need for their garden and driveway projects.

**Customers**
National and independent builders merchants, DIY groups, professional landscapers, garden designer and patio, driveway installers and homeowners.

**Products**
Paving, block paving, paths, edgings, walling, drainage and decorative aggregates.

## Our investment case

### Growth agenda

Proven record of sustained growth with 5 year CAGR growth in PBT of 41 per cent.

### Strong market position

Unique national network of manufacturing sites ensures proximity to customers and an efficient logistics footprint. Wide-ranging mineral reserves with the "Marshalls Stone Standard" quality mark.

### Diversified group

Serving Public Sector, Commercial and Domestic markets. These have historically proved to offer security due to their counter cyclical profiles.

### Strong asset base and resources

Well invested manufacturing plants with continuing emphasis on high quality maintenance, technology improvements and re-investment. Capital investment of £22.5 million in 2017.


Case study

## Innovation and NPD framework

There is a critical relationship between product, process and materials for development of new products.

- The Group's innovation cycle combines intelligence, innovation and delivery, and is a driver of growth;
- Dedicated and focused resources;
- High level of technical competence in materials, automation, engineering and product design;
- Delivering a high degree of product complexity; and
- Excellent trial and development facilities.

## Acquisition of CPM

CPM is a pre-cast concrete manufacturer specialising in underground water management solutions. The acquisition will enable the Group to offer a broader product choice that complements our existing water management offering and is a significant step to providing a full water management capability.

## Innovation and new products

The continued focus on innovation and new product development ensures the development of the Group's project engineering and manufacturing capabilities, concrete and other materials technology innovations and extending the new product pipeline.

## Sustainability

The Group has a sustainable business plan and has set KPIs for the key areas of this plan. Sustainability and corporate responsibility are key elements of the Marshalls culture.

## Culture

The Group's core values of leadership, excellence, trust and sustainability underpin our culture along with our key objective of doing business responsibly.

# The Group's 2020 Strategy is well established with good momentum and considerable further benefits to come

**"The Group's core values of leadership, excellence, trust and sustainability underpin our culture along with our key objective of doing business responsibly."**


## Summary

- 2017 has been another year of good profit growth.
- Core values remain leadership, excellence, trust and sustainability.
- 14% increase in earnings per share reflecting continuing strength of the Marshalls brand.
- Strong balance sheet and prudent capital structure.
- Full-year dividend of 10.20 pence (up 17%) and a discretionary supplementary dividend of 4.00 pence.


## Overview

This is my last report to you as your Chairman and I am pleased to be leaving your Company in good shape, with 2017 having been another year of profitable growth. Cash performance has been strong and we are again able to propose an increased dividend and a further supplementary dividend, whilst continuing to invest in the business and maintain a prudent capital structure. The Group's 2020 Strategy is well established with good momentum and considerable further benefits to come. The acquisition of CPM Group Limited ("CPM") during the year was an important step forward. Doing business the right way has always been important to Marshalls as we seek to ensure we balance the interests of all our stakeholders and make a full and proper contribution to society.

## Contribution to Society

Marshalls is purpose led. Our products transform the built environment whether public spaces or private driveways and patios through strong aesthetics and fit for purpose. We target very high levels of customer service. New product development and digital are important elements of our strategy and we continue to invest strongly in the business. We employ over 2,600 people, many of whom have been with Marshalls for very long periods. We are a "Living Wage" company and our pay is positioned at the top end for the industry. We established a new improved defined contribution pension scheme for employees during the year with a larger pension contribution made by the Company. We encourage share ownership and sharing in success, and we place a high priority on employee engagement, training and development, building successful careers for our people, and health and safety. Many of our businesses and our people play a strong role in their local communities. In 2017 over £50,000 was raised by employees for MIND which was the Group's chosen national charity and the Company has matched this contribution. As you will see from this report the Board is committed to the highest standards of environmental, sustainability and governance practice. The Group has maintained its "Fair Tax Mark" status in 2017. Taking account not only of corporation tax but also of PAYE and NI paid on our employee wages, aggregates levy, VAT, fuel duty and business rates Marshalls has funded total taxation to the UK economy of £96 million, some 22 per cent of Group turnover.

## Results and dividends

Group revenue for the year was £430.2 million, an increase of 8 per cent on 2016. Excluding the contribution from CPM, like-for-like revenue was up 6 per cent. The Domestic end market performance was again strong with revenue growth of 12 per cent during the year.

Profit before tax of £52.1 million (2016: £46.0 million) is stated after charging £1.2 million of operational restructuring costs and £0.8 million of acquisition costs. EBITDA has grown by 12 per cent to £67.9 million and the Group's earnings per share, at 21.52 pence, is up 14 per cent.

Marshalls continues to have strong cash generation with year-end net debt of £24.3 million (2016: £5.4 million net cash), after funding the acquisition of CPM of £41.2 million.

The Group's policy is to pay a progressive dividend aimed at achieving up to 2 times cover over the business cycle. The Board is recommending a final dividend of 6.80 pence per share (2016: 5.80 pence per share) which, together with the interim dividend of 3.40 pence per share (2016: 2.90 pence per share), makes a combined dividend of 10.20 pence per share (2016: 8.70 pence per share), an increase of 17 per cent for the year.

The Board is also recommending a supplementary dividend of 4.00 pence per share for 2017 (2016: 3.00 pence per share). This supplementary dividend is discretionary. The payment of a supplementary dividend recognises the Board's objective of maintaining an efficient and prudent capital structure and providing increased returns for shareholders whilst at the same time retaining flexibility for capital and other investment opportunities.

## Strategy

Our vision is to establish Marshalls as a world-class hard landscape business and to grow our emerging businesses. The Group's strategic objective is to deliver sustainable growth in shareholder value whilst taking into consideration the interests of all our stakeholders and the wider contribution we make to society. The Group's 2020 Strategy is firmly aligned with this vision and our strategy is already focused on sustaining the delivery of our core objectives beyond this time horizon.

The Marshalls brand remains central to our strategy and we have again received "Superbrand" status for 2018. Our emphasis on customer service, the provision of new and innovative quality products and integrated solutions, the development of our digital strategy, and focus on those areas of the market with good growth potential all underpin the continuing development of the Marshalls brand.

## Culture

The Board fosters an open and transparent culture that is responsive to the expectations of stakeholders and the external environment. Corporate culture remains a priority and the Board is working with the help of external consultants to define clearly its vision of good company culture and to embed this successfully into its operations in 2018.

The Group's core values of leadership, excellence, trust and sustainability underpin our culture along with our key objective of doing business responsibly. The aim is to promote sustainable operations, minimise adverse environmental and social impacts and achieve high standards of customer service and health and safety. This is embedded in management and employee reward schemes, where achieving customer service and health and safety targets remain key performance parameters. Marshalls won the Corporate Social Responsibility Award at the prestigious PLC Awards in March 2017.

## Governance

We continue to comply with all the provisions of the UK Corporate Governance Code as outlined in our Corporate Governance Statement on pages 36 to 41. The Board remains committed to the highest standards of corporate governance and to operating in accordance with strong ethical and corporate social responsibility principles. A large proportion of management's remuneration is in shares which must be retained for up to 5 years. This ensures a strong alignment between the interests of management and our shareholders.

The Group continues to enhance its Annual Report disclosures to ensure they give a fair, balanced and understandable assessment of the Group's position and prospects.

The Board's priorities for 2017 included the continuing promotion of the 2020 Strategy, the development of Marshalls' corporate culture and good practice, and succession planning, both at Board and senior management level. These initiatives are explained in more detail in the Corporate Governance Statement on pages 36 to 41.

During 2017, an internal evaluation of Board performance was undertaken to follow the external evaluation in 2016. No areas of material concern were highlighted during the 2017 evaluation.

## Board changes

Mark Edwards retired from the Board following the Annual General Meeting in May 2017 having served as Non-Executive Director and Chairman of the Audit Committee since May 2010. Following Mark's retirement Graham Prothero was appointed Non-Executive Director and Chairman of the Audit Committee. Graham has a strong financial background with significant sector experience.

In October 2017, I announced my intention to step down as Chairman and retire from the Board after nearly 8 years as your Chairman and 15 years as a Non-Executive Director. I will step down immediately after the AGM when my successor will take over.

## People

During my time at Marshalls I have visited our operations on numerous occasions and have met and talked to large numbers of our people across the organisation. It is clear to me that our people are the enduring strength of the business. There is a real passion for what we do and a high level of decency that pervades everything.

I would like to thank all our staff for their commitment, hard work and continuing dedication to Marshalls and also for their considerable support to me.

## Outlook

The Group has again delivered strong profit growth year-on-year. Good progress has been made in the year executing the 2020 Strategy, notably the acquisition of CPM, and the ongoing self help programme to drive organic growth is progressing well. The underlying drivers have remained positive in our main end markets and our sales and order intake have been strong in the first 2 months of 2018.

We remain well placed to deliver continued growth and operational profit improvements.

**Andrew Allner**
Chairman

# The Group has continued to deliver strong profit growth in 2017

"We are now planning beyond 2020 to progress the development of our strategic objectives in the longer term."

- Profit before tax up 13% to £52.1 million after charging approximately £1 million of acquisition costs.
- The planned integration of CPM is on track with our expectations.
- The Group's positive cash generation has continued.
- Commitment to self help capital investment programme and new product development.
- Digital strategy development progressing well.

## Introduction

The Group has continued to deliver strong profit growth in 2017. Continued progress has been made in the year to deliver the 2020 Strategy and the self help programme to support organic growth is progressing well. Sales and order intake have remained strong in the first couple of months of 2018. Based on public indicators we believe we continue to outperform our peers and gain market share. The Group's 2020 Strategy is now in its third year and we have continued to deliver on its core aspects. We are now planning beyond 2020 to progress the development of our strategic objectives over the longer term.

As a result of our continued focus on strategic growth and operational efficiency initiatives, the Group has delivered an operating profit in 2017 of £53.4 million (2016: £47.6 million), an increase of 12 per cent. This result is after charging £1.2 million of operational restructuring costs and £0.8 million of acquisition costs.

CPM Group Limited ("CPM") was acquired on 19 October 2017. CPM is a precast concrete manufacturer which specialises in underground water management solutions and the acquisition is in line with our stated 2020 Strategy to complement our organic plans with targeted acquisitions. CPM has traded strongly since acquisition and the planned integration of CPM is in line with our expectations.

Marshalls is a leading brand with a significant market position. Our strong investment case is covered in more detail on pages 4 and 5. Marshalls remains a benchmark for excellence and the 3 cornerstone themes of customer service, quality and sustainability continue to put the customer at the very heart of our business model and investment proposition.

Your Chairman, Andrew Allner is retiring both from the Board, and as Chairman, after many years of service. On behalf of the Company, I would like to place on record my thanks to Andrew for his excellent stewardship and his significant contribution to the ongoing development and growth of Marshalls.

## 2017 trading summary

Group revenue for the year ended 31 December 2017 was up 8 per cent at £430.2 million (2016: £396.9 million). Group revenue includes £9.0 million from CPM. On a like-for-like basis, excluding the impact of CPM, Group revenue was up 6 per cent.

Sales in the Domestic end market, which represented approximately 32 per cent of Group sales, continue to outperform CPA forecasts, and were up 12 per cent compared with the prior year period. The survey of domestic installers at the end of February 2018 revealed order books of 10.8 weeks (2017: 11.0 weeks) which compared with 11.7 weeks at the end of October 2017.

Excluding CPM, sales in the Public Sector and Commercial end market, which represented approximately 61 per cent of Group sales, were up 2 per cent compared with 2016. The Group continues to target those parts of the market where higher levels of growth are anticipated including New Build Housing, Water Management and Rail.

The core Commercial and Domestic businesses continue to deliver benefits from operational efficiency improvements and our network of manufacturing sites remains a key competitive strength. Revenues in our Emerging UK Businesses increased by 2 per cent, compared with the prior year. The improved performance of our Street Furniture business has been particularly encouraging in 2017, and the growth in sustainable profitability of our Emerging UK Businesses remains a key part of the 2020 Strategy. The growth of protective security street furniture continues and this is explained in more detail on page 16.

International revenue grew by 19 per cent during 2017 and represents approximately 5 per cent of Group sales. Marshalls has made continued progress in developing the International business and trading performance has improved in line with the revenue growth. The Group continues to develop opportunities by improving its global supply chains and routes to market.

Profit before tax increased by 13 per cent to £52.1 million (2016: £46.0 million) and EBITDA increased by 12 per cent to £67.9 million (2016: £60.8 million). Basic EPS was 21.52 pence (2016: 18.95 pence), an increase of 14 per cent.

Profit before tax is stated after charging £1.2 million of operational restructuring costs and £0.8 million of acquisition costs in relation to the Group's acquisition of CPM.

Capital discipline remains a key priority and the Group's strong cash generation has continued. Net debt at 31 December 2017 was £24.3 million (2016: £5.4 million cash) and reflects the total cash outflow of £41.4 million in connection with the acquisition of CPM. Operating Cash flow was 100 per cent of EBITDA.

## Acquisition of CPM

Water Management is a key focus area for the Group and the acquisition of CPM is a significant step towards the Group's stated strategy of providing a full water management capability within its product range. CPM will enable us to offer customers a broader product choice that complements our existing water management offering. Previously, Marshalls did not trade in below ground UK drainage products, so the acquisition has extended the Group's product range below ground. CPM operates in the collect, conveyance, clean, hold and release, and recycle areas of the underground market and the product ranges include pipes, traditional and sealed manholes, attenuation tanks and flow control and rainwater harvesting systems.

## Current priorities and operational strategy

The Group's 2020 Strategy is now in its third year and we have again delivered on its core aspects. The Group's strategy remains to grow the business, deliver increasing operating margins in all businesses and improve the Group's return on capital employed ("ROCE"). We are now planning beyond 2020 so as to progress the development of our strategic objectives over the longer term.

During 2017, further progress has been made with the self help capital investment programme, the development of new products and the Group's digital strategy. These organic projects have been complemented by the acquisition of CPM and its planned integration is on track with our expectations. Both aspects have allowed us to improve the level of our sustainable operating margins with the Group reporting an increase from 12.0 per cent to 12.4 per cent during the year.

ROCE, defined as EBITA / shareholders' funds plus net debt, was 24.8 per cent for the year ended 31 December 2017, which was up 8 per cent year-on-year. This ROCE calculation excludes the impact of CPM and is therefore on a like-for-like basis.

Capital expenditure was £22.5 million in the year ended 31 December 2017, which included £8.6 million of additional "self help" investment. Capital expenditure of £28.0 million is planned for 2018. We continue to generate a good pipeline of capital investment projects that will drive future organic growth. In addition, increases in research and new product development expenditure continue to be made.

Notwithstanding the acquisition of CPM, we continue to target bolt-on acquisitions within our identified growth sectors of Water Management, Street Furniture and Minerals. Our approach remains cautious and any proposed acquisition target will be carefully assessed against strict criteria and will be thoroughly considered during the detailed due diligence phase.

Marshalls' digital strategy remains a key priority and continued investment is being directed to enhancing capability and to drive a "digital first" approach. The digital strategy is underpinned by continuous improvement driven by data analysis and customer insight. Our web and mobile applications enable customers to model their requirements and allow digital access to the registered installer base.

The Group's strategic initiatives are set out in detail in the Strategic Report on pages 2 to 33.

## Innovation and new product development

In the core Landscape Products business, the growth in revenue from new products continued strongly, increasing by 4.2 per cent during 2017. The objective is to deliver innovative market leading new products that are aligned with customer needs across all business areas. The development pipeline continues to be strong and the Group is committed to providing high performance product solutions. All the Group's premium driveway products now feature advanced surface performance technology; examples include "Drivesys" which has been designed to look and feel like natural stone and "Priora" which has been specifically engineered to manage heavy rainfall.

Further development includes project engineering to improve manufacturing efficiency and our specialist engineers and technicians deliver competitive advantage for Marshalls by combining machinery design and installation with process improvement. This enables Group to generate added value through innovation in materials, technology and product development.

## Improvements in operational efficiency

We are continuing to focus on improving operational and manufacturing efficiency. The Group adopts a flexible operating framework that aims to drive cost efficiency improvements across the controllable cost base and to develop flexible strategies within the supply chain. Our objective is to mitigate inflation on an ongoing basis to ensure sustainable business continuity and cost control. The Group network of 13 concrete manufacturing sites and quarries provides national geographic coverage and, with the implementation of best practice across the entire network, represents a key competitive advantage.

The Group's well invested sales and capital investment programmes provide the flexibility to manufacture products for both the Public Sector and Commercial and the Domestic end markets. This enhances operational flexibility which also remains a key priority. All the Group's operations are supported by a centrally managed logistics and distribution capability. Manufactured products from this network, together with ethically sourced natural stone products imported from India, China and Vietnam, are supplied to distributors' depots or direct to site.

## Health and safety

The Group is committed to safeguarding the health and safety of every employee and all stakeholders who may be affected by our undertakings. Maintaining the highest standards of health and safety remains a cornerstone of the Group's culture and we are committed to the continual improvement in health and safety performance.

During 2017, there was a 35 per cent reduction in days lost from workplace incidents, which is comfortably ahead of the Group's headline target. The Group has continued to invest in health and safety awareness training for all managers and supervisory staff and we promote a culture in which all managers visibly demonstrate health and safety leadership.

**Martyn Coffey**
Chief Executive

# How we do business

Marshalls is the UK's leading hard landscaping manufacturer supplying superior natural stone and innovative concrete products to the construction, home improvement and landscape markets since the 1890s.

## 1 Resources and inputs

### Responsible leadership
- Sustainable operations
- Values and culture

### Intellectual capital
- Superbrand
- Innovation and strong R&D / NPD

### People and skills
- Company culture
- Technical expertise
- Specialist skills
- Strong relationships

### High quality assets
- National coverage
- Efficient plants
- Diverse product range
- Mineral reserves

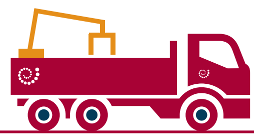
### Relationships
- Customers
- Supply chain
- Community

### Financial capital
- Robust balance sheet
- Prudent capital structure

### What we do
Marshalls is a complete external landscaping, interior design, paving and flooring products business – from planning and engineering, to guidance and delivery.

### Responding to the wider market
Marshalls seeks to understand the long-term drivers of market and product growth. Through detailed market analysis, we continue to drive new product development, particularly in the areas of New Build Housing, Water Management, Street Furniture and Rail. Product development focuses on meeting consumer needs and on increasing the speed and efficiency of product installation.

## 2 How we operate



### Sourcing
The Group's main raw materials are cement, sand, aggregates, pigments, fuel oil and utilities. We use the best materials we can source. Supply chain relationships include the ethical sourcing of natural stone from India, China and Vietnam. The Group also has extensive reserves of UK natural stone.

**RELATED RISKS**
- Macro-economic and political
- Cost and availability of raw materials
- Cyber security risks
- Environmental
- Ethical

### Manufacturing
The Group manufactures and supplies landscape, driveway and garden products from a range of materials, principally concrete and natural stone. Marshalls has a world-class Manufacturing, Innovation and Development team.

**RELATED RISKS**
- Competitor activity
- Threat from new technologies and business models
- IT infrastructure
- Legal and regulatory

### Distribution
Due to the scale of our operations, and our national network of regional centres, 97 per cent of our customers are less than 2 hours away. This continues to be a key competitive advantage.

**RELATED RISKS**
- Macro-economic and political
- IT infrastructure
- Cost inflation
- Environmental

**Our core values:** Leadership Excellence

- **Our markets** pages 12 and 13
- **Our strategy** pages 14 and 15
- **Key performance indicators** pages 18 and 19
- **Risk Management and principal risks** pages 20 to 24


## Key strengths

### Sustainability
- Commitment to producing new quality products that are better than any existing market offering
- Development of a digital strategy

### Customer service
- World-class Manufacturing, Innovation and Development team
- Skilled engineers and technicians
- Broad range of products

### Quality
- New and innovative products
- Patent protection
- Machinery design and installation

### Capital structure
- Strong and flexible capital structure
- Clear capital allocation policy


**Priorities for capital** page 28


### Innovation
- Benchmark for excellence, widely regarded as a leader in its field
- Marshalls is one of Britain's strongest Superbrands
- Sustainability credentials

## Customers

Our customers range from Domestic homeowners to Public Sector and Commercial. We seek to exceed the expectations of customers in all our markets.

**RELATED RISKS**
- Macro-economic and political
- Weather
- Cyber security risks
- Legal and regulatory

**Trust** **Sustainability**

## 3 Delivering stakeholder value

Our engagement with key shareholders is a key part of the Group Sustainability Strategy (Pages 30 to 33). Stakeholder engagement is focused on personal communication and ongoing collaboration.

### Employees
- Employee engagement through newsletter, intranet and workplace meetings
- Focus on safety
- Promote development and personal growth
- Living Wage Company

NEW APPRENTICESHIPS CREATED IN 2017

**50**

### Customers
- Centre of business model
- Quality, availability and "on-time" delivery
- Quality innovative products and exceptional service
- Development of solutions that can be efficiently and effectively installed

CUSTOMER SERVICE INDEX

**98.0%**

### Shareholders
- Face to face meetings, site visits and investor roadshows
- Progressive dividend policy
- Targeting 2 times dividend cover over business cycle

DIVIDEND PER SHARE

**14.20p**

### Communities
- Business in the Community
- Responsible business practices
- Total taxation to the UK economy – £96 million
- Charitable initiatives

DIRECT INVESTMENT IN THE COMMUNITY

**£200,000**

### Environment
- Responsible use of natural resources
- Reinvestment (research and development, capital expenditure)
- Drive growth and sustainability

REDUCTION IN $CO_2e$ EMISSIONS OVER LAST 5 YEARS

**13%**

### Suppliers
- Global supply chain with long-term partnerships
- Regular communication and fair terms
- Regular supply chain audits
- Ethical trading initiative

SUPPLIERS RECEIVING ANTI-BRIBERY AND MODERN SLAVERY TRAINING

**70%**

### Strategic objectives:
- Shareholder value
- Relationship building
- Brand development
- Sustainable profitability
- Organic expansion
- Effective capital structure and control framework

# Growth markets

Marshalls tracks a comprehensive set of market indicators and drivers to identify areas of sustainable market growth to not only focus current sales and marketing effort but also future product development.

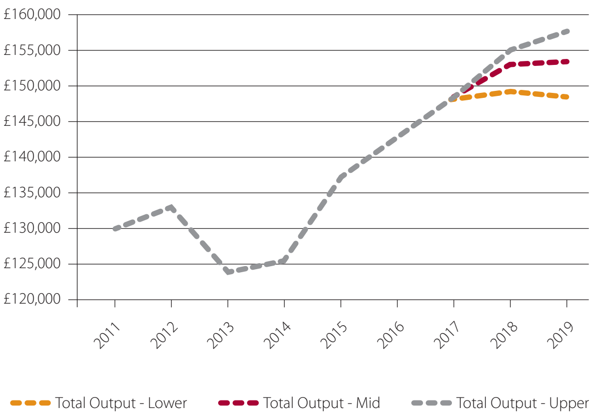
PUBLIC SECTOR & COMMERCIAL MARKETS

## Construction Market Growth

The CPA forecast Construction Output to rise by 0.2 per cent in 2018 and 1.7 per cent in 2019 and highlighted Brexit uncertainty in a wide scenario range. This top level view masks some significant variations in regional and sector growth forecasts.

**CPA – Total Construction Output**

Winter 2017/18 Forecasts




### OUR STRATEGIC RESPONSE

- Marshalls will target individual market sectors and focus on those areas with sustainable growth; and
- The Group's analysis goes further than the base forecasts and seeks to understand the long-term drivers of market growth.

### INNOVATION AND SERVICE

- The digital strategy will drive service and development.

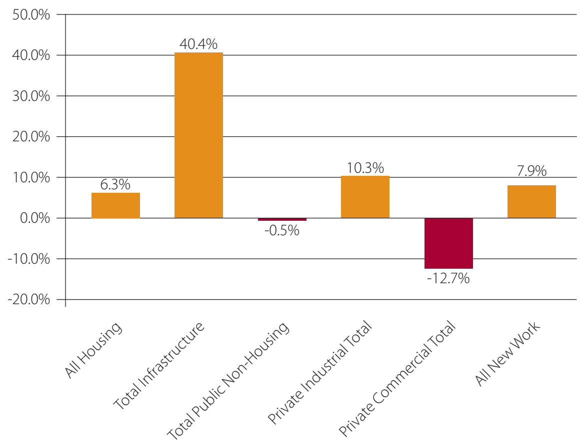

Find out more online:
**www.marshalls.co.uk/futurespaces**

PUBLIC SECTOR & COMMERCIAL MARKETS

## Sector Growth

Infrastructure projects, particularly rail & roads, feature strongly in new construction orders. HS2 work is expected to be seen on the ground from the end of 2018. For private housing, the largest sector by value, growth remains robust and is forecast to rise 3 per cent in 2018 and 2 per cent in 2019.

**ONS Construction Orders 2017 Q3 MAT Growth** %




### OUR STRATEGIC RESPONSE

- Marshalls will focus on targeted growth areas including New Build Housing, Water Management and Rail; and
- We continue to drive innovation and the introduction of new products and propositions.

### INNOVATION AND SERVICE

- Rail platform range.

Find out more online:
**www.marshalls.co.uk/rail**

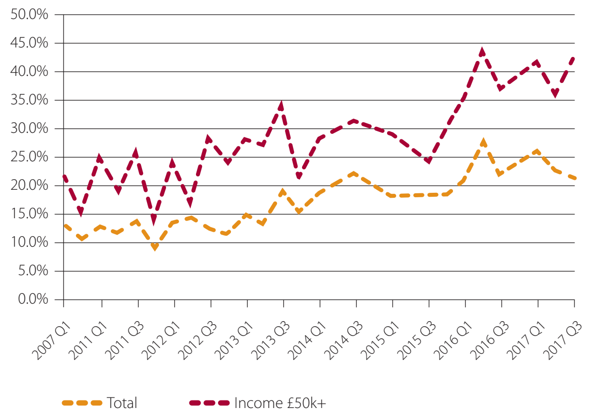
THE CONSUMER MARKETS

## Consumer Demand

There are some significant subtleties in the underlying consumer confidence data. 42 per cent of households, with income of more than £50,000, said they were planning a drive or garden project in the next 12 months, the second highest proportion in the last 10 years. Indeed older, wealthy, mortgage free, homeowners are improving their living environment.

**GFK Consumer DIY Intentions Drive and / or Garden** (HL)

% of those questioned who are planning a Drive and / or Garden Project in the next 12 Months




OUR STRATEGIC RESPONSE

- Invest in new product development within the core landscaping product range of Domestic drives and patios; and
- We focus on consumer needs including increasing the speed and efficiency of installation.

INNOVATION AND SERVICE

- Drivesys® Patented Driveway Systems.

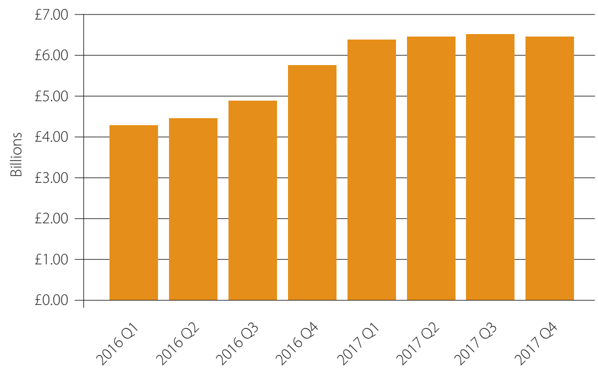
Find out more online:
**www.marshalls.co.uk/home**

THE CONSUMER MARKETS

## Project Funding

An older demographic, with housing and pension wealth, prefer to improve rather than move. Pension release has become a significant source of funding for home improvements with the value released stabilising during 2017. These triple locked consumers are more resistant to falls in real wages than new homeowners.

**Moving Annual Total Value** (£bn)
**of Flexible Payments from Pensions** (HMRC)




OUR STRATEGIC RESPONSE

- New product development for the Domestic homeowner tracks trends in lifestyles and aesthetics; and
- Marshalls operates the UK's largest approved garden and driveways installer team.

INNOVATION AND SERVICE

- Focus on customer service, quality and sustainability.

Find out more online:
**www.marshalls.co.uk/homeowners**

# Focused on growth

Marshalls continues to place emphasis on customer service and our enduring objective of providing quality products and integrated solutions. Delivering growth through technology, digitalisation and product innovation is a key element of the Group's strategy.

## Shareholder value

To deliver sustainable shareholder value by improving the long-term operating performance of the business.

ROCE of
24.8%

**WHAT WE HAVE ACHIEVED**

- ROCE of 24.8 per cent (on a like-for-like basis, excluding the impact of CPM).
- Market share gains.
- Supplementary dividend.

**2020 STRATEGY**

- To strengthen the Marshalls brand by developing systems-based solutions.
- To make strategic investments for organic growth and acquisitions.
- To have a progressive dividend policy supported by supplementary dividends, as appropriate.

**OUR FUTURE TARGETS**

- To grow EBITDA and ROCE.

## Sustainable profitability

To maintain a strong market position and grow the business profitability in all of the Group's end markets.

New products growth over last 3 years
14%

**WHAT WE HAVE ACHIEVED**

- 12 per cent growth in operating profit driven by sustainable efficiency improvements.
- Increase in operating profit percentage to 12.4 per cent (2016: 12.0 per cent).
- 4 per cent growth in sales of new products in the core business.

**2020 STRATEGY**

- To deliver new and innovative product solutions.
- To improve operational efficiency of manufacturing and distribution network.
- To drive through sustainable cost reductions.
- To continue to invest in the digital strategy.

**OUR FUTURE TARGETS**

- To deliver sustainable EPS and operating cash flow growth.

## Relationship building

To develop relationships with key stakeholders, customers and installers.

Registered installer teams now
approx. 1,900

**WHAT WE HAVE ACHIEVED**

- Strengthened customer relationships.
- 98 per cent customer service KPI.
- Integrated "landscaping solutions".
- Design Space office in Central London.
- 1,900 registered installer teams.

**2020 STRATEGY**

- To promote integrated product solutions.
- To focus on installer training, marketing and sales support.
- To develop the supply chain and maintain ethical and sustainable policies.
- To be a provider of integrated solutions and systems.

**OUR FUTURE TARGETS**

- To increase market share in our emerging UK businesses and to be an employer of choice.

- **Key performance indicators** pages 18-19
- **Risks** pages 20-24
- **Sustainability** pages 30-33
- **Remuneration** pages 50-63



## Organic expansion

To invest in organic expansion in existing and related markets and product categories to expand the business.

**Revenue**
£430.2m

**WHAT WE HAVE ACHIEVED**
- Revenue growth of 8 per cent to £430.2 million. On a like-for-like basis, excluding the impact of CPM, Group revenue was up 6 per cent.
- Significant growth in key focus areas whilst maintaining operational flexibility.
- 19 per cent growth in International revenue.

**2020 STRATEGY**
- To focus on increasing the profitability of the Emerging UK Businesses.
- To target growth areas such as New Build Housing, Water Management and Rail.
- To increase capital expenditure investment for organic growth.

**OUR FUTURE TARGETS**
- To optimise our national network of manufacturing and distribution sites.
- To develop our global supply chains and infrastructure.

## Brand development

To strengthen and extend the Marshalls brand by focusing on innovation, service and new product development.

**R&D investment of**
£3.9m

**WHAT WE HAVE ACHIEVED**
- "Superbrand" status.
- Continued development of Marshalls brand.
- Developed product range.
- Provision of innovative, quality products.

**2020 STRATEGY**
- To focus on innovation, customer service and product quality.
- To increase technical R&D.
- To maintain the highest health and safety standards.

**OUR FUTURE TARGETS**
- To maintain the Group's market-leading position.

## Effective capital structure and control framework

To maintain efficient and effective business controls and to ensure that the capital structure remains aligned with the Group's corporate growth objectives.

**Net debt: EBITDA**
0.35 ratio

**WHAT WE HAVE ACHIEVED**
- Strong balance sheet.
- Low gearing of 10 per cent at 31 December 2017.
- Efficient portfolio of bank facilities with extended maturities and realigned headroom.
- Continued focus on working capital management and efficient inventory control.

**2020 STRATEGY**
- To maintain a flexible capital structure that recognises cyclical risk, focusing on security, efficiency and liquidity.
- To deliver a capital allocation strategy that is fully aligned with this capital structure.

**OUR FUTURE TARGETS**
- To operate tight control over business, operational and financial procedures.
- To target a net debt to EBITDA ratio of between 0 and 1 times over the business cycle.

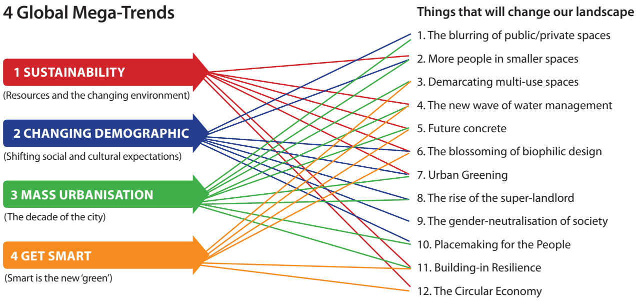
# Growth opportunities

The Group is constantly tracking the global mega trends, the shorter term trends in lifestyles and aesthetics and the developing requirements of our consumers and stakeholders.

## Future Spaces

### WHAT THIS MEANS?

Future Spaces is the result of intensive research with the aim of understanding how the format, planning, specification and materials used in the construction of public, private and commercial spaces, both indoors and outdoors, might look and function in 10 years time.




### LINK TO STRATEGY

We are using the 12 Future Spaces themes to give specific direction to our strategic objectives. These themes are being used to provide the strategic focus to:

- new product development;
- new services and propositions; and
- identify targeted acquisitions.

These themes are changing the nature of our built environment.

### ACTION TAKEN TO DATE

We are constantly engaging with all our stakeholder groups to ensure a fully collaborative approach to planning and development. We are focusing development expenditure and growth initiatives into the areas of New Build Housing, Water Management, Minerals and Rail. The digital approach transcends all our development projects.

### FUTURE DIRECTION

Already we are seeing the emergence of the following themes and these are being built into our strategic planning:

- the blurring of public and private spaces;
- place-making for the people;
- building in resilience; and
- the Circular Economy.

Find out more online
**www.marshalls.co.uk/futurespaces**

## International Security

### WHAT THIS MEANS?

In our lifetimes, the nature of terrorism has undergone significant change. The concept of terrorism describes the use of intentionally indiscriminate violence as a means to create terror and fear to achieve political, religious or ideological aim. The market for security barriers and bollards is developing as a response and is truly international.

### LINK TO STRATEGY

Only 15 per cent of people say that traditional concrete anti-terror barriers make them feel safer. Our strategy has been to use new technology to design solutions that Deter, Deflect and Defend, a three-tier strategy designed to reduce the threat long before vehicles are used to target assets.

### ACTION TAKEN TO DATE

Marshalls Landscape Protection is based on increasingly resistant new security products that use new technology. The increasing market demand for hostile vehicle mitigation is a specific growth opportunity.

### FUTURE DIRECTION

We believe that successful security should take a holistic approach and we are engaging with relevant stakeholder groups to drive effective new product development.

Find out more online
**www.marshalls.co.uk/landscapeprotection**

## Digitising the Customer Journey

**WHAT THIS MEANS?**

Over the last few years technology and software advancements have rapidly driven disruption and change to many industries. All businesses are now faced with the challenge of how best to utilise digital to transform their business. Our digital principles are designed to create an engaging customer experience.

**LINK TO STRATEGY**

In determining our strategic direction for digital development, we have identified 6 core principles which are firmly aligned with our strategic objectives:

- Design for the customer
- Collaboration
- Data driven
- Promote agility
- Open and transparent
- Robust governance


**ACTION TAKEN TO DATE**

The digital initiatives that have been taken to date all put the interests of stakeholders and the requirements of customers as the key priority. For example, web and mobile applications enable customers to model their requirements and allow full digital access.


**FUTURE DIRECTION**

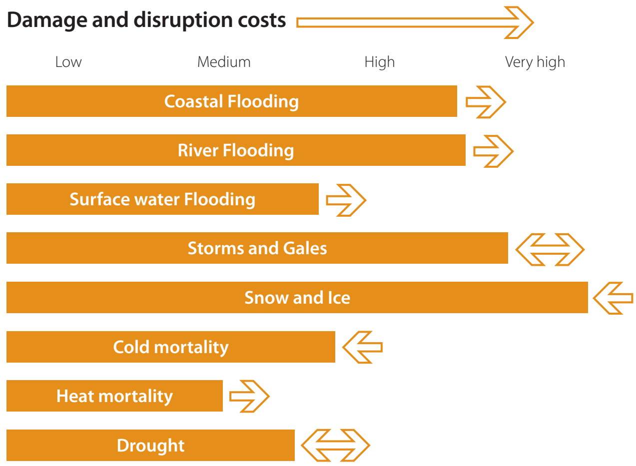
The Group's future direction is to embrace a "digital first" approach. The strategic direction is "digital by default" which seeks to apply the digital principles referred to above to People, Process and Technology such that digital is part of the Group's culture.

Find out more online
**www.marshalls.co.uk**

## Climate Change

**WHAT THIS MEANS?**

The Government's latest climate change risk assessment identifies flood risk, and particularly flooding from heavy downpours, as one of the key climate threats for the UK. This must be viewed alongside stresses on water resources, threats to biodiversity and natural habitats, and the repercussions for the UK from climate change impacts abroad.




**LINK TO STRATEGY**

Water Management is a specific growth area and to ensure that our development initiatives are in line with our strategic objectives, the Group has determined that all new products must:

- improve sustainability;
- improve functionality;
- improve installation;
- improve aesthetics; and
- reduce whole life costs.

**ACTION TAKEN TO DATE**

The strategic objective is to provide a full water management capability and the acquisition of CPM is an important step in that direction. CPM's product range serves the "below ground" drainage market, whereas Marshalls had previously only been able to offer an "above ground" linear drainage proposition.

**FUTURE DIRECTION**

The Group's water management strategy is designed to deliver long-term sustainable value. Future growth objectives will cover above and below ground systems and will include "collect", "convey", "clean" and "hold / release"systems.

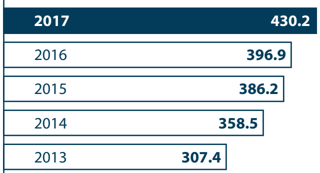
Find out more online
**www.marshalls.co.uk**

# Measuring our performance

The Group's KPIs monitor progress towards the achievement of its objectives. All of the Group's strategic KPIs have moved forward strongly during 2017.

## Revenue (£'m)

£430.2m
+8%




**LINK TO STRATEGY**

Delivering growth is key to the 2020 Strategy.

**2017 PERFORMANCE**

Group revenue has increased by 8 per cent in 2017. Growth in Domestic revenue was particularly strong at 12 per cent.

**STRATEGIC TARGETS**

The aim continues to be to outperform the market and maintain or grow market share.

**REMUNERATION LINKAGE**

Sustainable revenue growth is the driver of EPS and Operating Cash Flow ("OCF") growth.

**RISK MANAGEMENT**

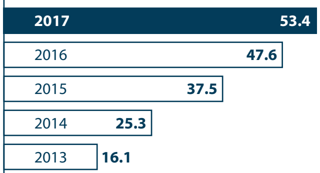
The Group closely monitors trends and lead indicators and continues to benefit from the diversity of its business and end markets.

**STAKEHOLDER LINKAGE**

Customers
Suppliers
Employees
Communities

## Operating profit (£'m)

£53.4m
+12%




**LINK TO STRATEGY**

The sustainable improvement in profitability is a strategic priority.

**2017 PERFORMANCE**

Operating profit has increased by 12 per cent to £53.4 million in 2017. The Group's strong operational gearing has driven an increase in reported operating margin from 12.0 per cent to 12.4 per cent.

**STRATEGIC TARGETS**

Sustainable improvement in profitability.

**REMUNERATION LINKAGE**

EPS and OCF are both remuneration performance targets.

**RISK MANAGEMENT**

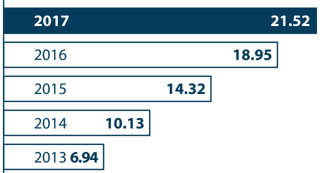
The Group focuses on innovation and new product development in order to improve product mix and increase value-added sales.

**STAKEHOLDER LINKAGE**

Shareholders
Employees

## EPS (p)

21.52p
+14%




**LINK TO STRATEGY**

The delivery of long-term sustainable profitability for shareholders is a strategic priority.

**2017 PERFORMANCE**

Group EPS has increased by 14 per cent in 2017 to 21.52 pence.

**STRATEGIC TARGETS**

Significant EPS growth is a strategic target.

**REMUNERATION LINKAGE**

EPS growth is a remuneration performance target.

**RISK MANAGEMENT**

The Group focuses on sales opportunities and strategic growth opportunities.

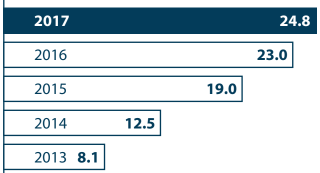
**STAKEHOLDER LINKAGE**

Shareholders
Employees

## Return on capital employed (%)

24.8%

(on a like-for-like basis, excluding the impact of CPM)




**LINK TO STRATEGY**

ROCE remains an important indicator of sustainable shareholder value.

**2017 PERFORMANCE**

Group ROCE is 24.8 per cent for the year ended 31 December 2017, on a like-for-like basis (excluding the impact of CPM). ROCE is defined as EBITA / shareholders' funds plus cash / net debt.

**STRATEGIC TARGETS**

The strategic target is to continue to grow ROCE.

**REMUNERATION LINKAGE**

ROCE provides the control and balance between the profit and cash flow performance targets.

**RISK MANAGEMENT**

The Group continues to focus on strategic investment for both organic and acquisitive growth.

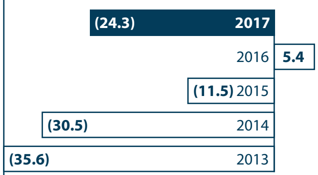
**STAKEHOLDER LINKAGE**

Shareholders
Employees

**Strategic objectives:** Shareholder value · Sustainable profitability · Relationship building · Organic expansion · Brand development · Effective capital structure and control framework

**Net debt (£'m)**

# £24.3m




**LINK TO STRATEGY**

Marshalls continues to support a prudent capital structure.

**2017 PERFORMANCE**

Significant cash generation has continued and, notwithstanding the acquisition of CPM, gearing remains low at 10 per cent at 31 December 2017. Net debt was £24.3 million at 31 December 2017.

**STRATEGIC TARGETS**

The Group's strategic target is for the ratio of net debt to EBITDA to be between 0 and 1 times over the business cycle.

**REMUNERATION LINKAGE**

OCF is a remuneration performance target.

**RISK MANAGEMENT**

The Group maintains a conservative financial profile that recognises cyclical risk and a flexible capital structure that can respond to market changes.

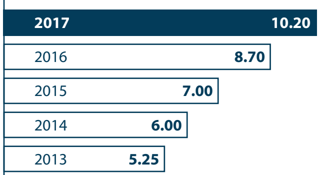
**STAKEHOLDER LINKAGE**

Shareholders
Employees
Customers
Suppliers

**Dividend per share (recommended, p)**

# 10.20p

+17%




**LINK TO STRATEGY**

A progressive dividend policy remains a key objective.

**2017 PERFORMANCE**

The ordinary dividend per share increased by 17 per cent to 10.20 pence. On an IFRS basis, the dividends declared in the year ended 31 December 2017 are 12.20 pence, an increase of 26 per cent.

**STRATEGIC TARGETS**

The continuing strategy is to maintain up to 2 times cover over the business cycle.

**REMUNERATION LINKAGE**

Remuneration targets are aligned with shareholder value.

**RISK MANAGEMENT**

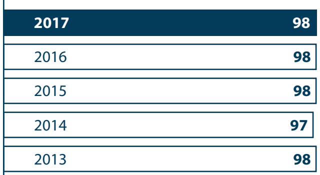
Risk management remains a key factor in the delivery of the Group's strategic objectives and risk appetite is aligned with the delivery of long-term sustainable value.

**STAKEHOLDER LINKAGE**

Shareholders

**Customer service index**

# 98.0%




**LINK TO STRATEGY**

Customer service lies at the heart of the Marshalls brand. The Group's customer service index combines measures of product availability, on-time delivery performance and administrative and delivery accuracy.

**2017 PERFORMANCE**

The combined customer service measure continued to be in excess of 98 per cent throughout 2017.

**STRATEGIC TARGETS**

The Group's customer service index target is 95 per cent.

**REMUNERATION LINKAGE**

Customer service is a remuneration performance target.

**RISK MANAGEMENT**

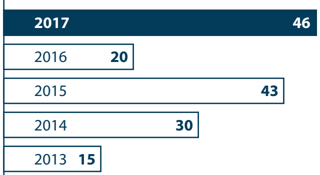
The Group focuses on quality, service, reliability and ethical standards that differentiate Marshalls from its competitors.

**STAKEHOLDER LINKAGE**

Customers
Communities
Environment

**Health and safety (reduction in working days lost, %)**

# 46.0%




**LINK TO STRATEGY**

Marshalls remains committed to meeting the highest health and safety standards for all its employees and continually strives to improve the quality and safety of the working environment.

**2017 PERFORMANCE**

In 2017 there was a 46 per cent reduction in days lost from workplace incidents compared with the target benchmark.

**STRATEGIC TARGETS**

The headline target for 2017 was to achieve an accident rate for the year no higher than the 2015 actual results.

**REMUNERATION LINKAGE**

Health and safety performance is a remuneration performance target.

**RISK MANAGEMENT**

The Group's compliance procedures and policies seek to ensure that local, national and international health and safety controls are fully complied with.

**STAKEHOLDER LINKAGE**

Employees
Communities
Environment

# Managing risk to deliver strategic objectives

Managing risk is key to the delivery of long-term sustainable improvement in shareholder value. All risks are aligned with the Group's strategic objectives.

## Achievements in 2017

In addition to the delivery of ongoing process and system enhancements that are designed to mitigate risk, the Group's risk function has placed particular emphasis on the following areas during the year:

- Cyber risk has continued to be a major focus area for risk assessment. A further internal audit project has been undertaken by KPMG and continued improvements have been made to mitigate risk and improve IT security, business continuity and disaster recovery.
- Health and safety continues to be a focus area as the Group continually strives to reduce health and safety risk and improve performance. Additional staff training was undertaken in 2017.
- Proactive supply chain management continues to be a focus area for the Group and an internal audit project has been undertaken by KPMG in 2017. This covered the adequacy of the Group's policies, procedures and systems and the operation of key controls.
- A detailed annual review of the Group's capital structure has been undertaken to ensure it remains aligned with corporate growth objectives and the external market risk environment.
- The maintenance of a conservative capital structure with a strong balance sheet and comfortable headroom against bank facilities provides significant mitigation against potential funding risk.

## Priorities for 2018

The priorities for the Group's risk function in 2018 include the following areas of focus:

- The rapid pace of change in the wider environment necessitates cyber risk remaining a key priority for 2018. Further assignments and penetration tests are planned to ensure that the Group remains proactive in this area.
- The completion of a number of targeted projects will again be a major focus for KPMG. In 2018, projects covering inventory management, GDPR and human resource systems and procedures are planned.
- Following the acquisition of CPM in October 2017, the successful integration of the business into the Group is a major focus area. The risk that the integration takes longer than anticipated and impacts financial performance has been included as a key item on the Group's Risk Register. A post integration review is to be undertaken by KPMG.
- Health and safety remains a major focus area. Significant increases in the financial penalty regime have increased the potential impact of health and safety incidents.

### Approach to risk management

Risk management is the responsibility of the Board and is a key factor in the delivery of the Group's strategic objectives. The Board establishes the culture of effective risk management and is responsible for maintaining appropriate systems and controls. The Board sets the risk appetite and determines the policies and procedures that are put in place to mitigate exposure to risks.

### Process

There is a formal ongoing process to identify, assess and analyse risks and those of a potentially significant nature are included in the Group Risk Register. The conclusion of the Group's internal auditor, KPMG, is that the process continues to be a robust mechanism for monitoring and controlling the Group's principal risks.

The Group Risk Register is reviewed and updated at least every 6 months and the overall process is the subject of regular review. Risks are recorded with a full analysis and risk owners are nominated who have authority and responsibility for assessing and managing the risk. All risks are aligned with the Group's strategic objectives and each risk is analysed for impact and probability to determine exposure and impact to the business and the determination of a "gross risk score" enables risk exposure to be prioritised. External risks include the weather, political and economic conditions, the effect of legislation or other regulatory actions, the actions of competitors, foreign exchange, raw material prices and pension funding. Internal risks include investment in new products, new business strategies and acquisitions. In particular, during 2017, the potential impact of Brexit and wider economic uncertainty has been considered in the assessment of risk 1 on page 22.

The Group seeks to mitigate exposure to all forms of strategic, financial and operational risk, both external and internal. The effectiveness of key mitigating controls is continually monitored and such controls are subjected to internal audit and periodic testing in order to provide independent verification where this is deemed appropriate. The effectiveness and impact of key controls are evaluated and this is used to determine a "net risk score" for each risk. The process is used to develop action plans that are used to manage, or respond to, the risks and these are monitored and reviewed on a regular basis by the Group's Audit Committee.

In addition, the Group has established a formal framework for the ongoing assessment of operational, financial and IT-based controls. The overriding objective is to gain assurance that the control framework is complete and that the individual controls are operating effectively. Additional independent verification checking of key controls and reconciliations are undertaken on a rolling basis. Such testing includes key controls over access to, and change permissions on, base data and metadata.

## Framework

**The Board:**
- determines the Group's approach to risk, its policies and the procedures that are put in place to mitigate exposure to risk.

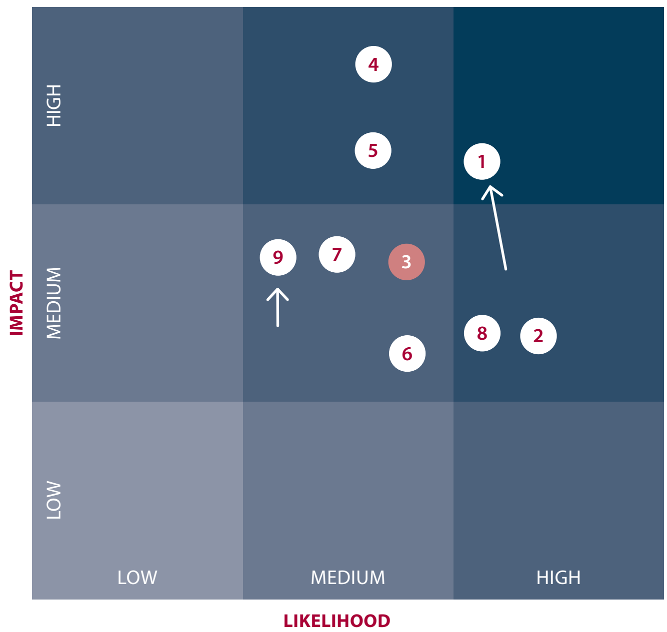
**The Audit Committee:**
- has delegated responsibility from the Board to oversee risk management and internal controls;
- reviews the effectiveness of the Group's risk management and internal control procedures; and
- monitors the effectiveness of the internal audit function and the independence of the external audit.

**Executive Directors:**
- are responsible for the effective maintenance of the Group's Risk Register;
- oversee the management of risk;
- monitor risk mitigation and controls; and
- monitor the effective implementation of action plans.

**Internal audit:**
- independently reviews the effectiveness of internal control procedures;
- reports on effectiveness of management actions; and
- provides assurance to the Audit Committee.

**Operational managers:**
- are responsible for the identification of operational and strategic risks;
- are responsible for the ownership and control of specific risks; and
- are responsible for establishing and managing the implementation of appropriate action plans.

## Risk heatmap




1 Macro-economic and political
2 Cyber security risks
3 Integration of CPM (New risk)
4 Weather
5 Customers
6 Competitor activity
7 Threat from new technologies and business models
8 Cost and availability of raw materials
9 Corporate, legal and regulatory

## Risk appetite

The Group is prepared to accept a certain level of risk to remain competitive but continues to adopt a conservative approach to risk management. The risk framework is robust and provides clarity in determining the risks faced and the level of risk that we are prepared to accept. Marshalls continues to put in place detailed plans to manage all risks through strategies that are designed to either treat, transfer or terminate the source of the identified risk.

## Viability Statement

After considering the principal risks overleaf, the Directors have assessed the prospects of the Group over a longer period than the period of at least 12 months required by the "going concern" basis of accounting. The Directors consider that the Group's risk management process satisfies the requirements of provision C.2.2 of the UK Corporate Governance Code.

The Board considers annually, and on a rolling basis, a 3-year strategic plan, which is assessed with reference to the Group's current position and prospects, the strategic objectives and the operation of the procedures and policies to manage the principal risks that might threaten the business model, future performance and target capital structure. In this assessment, security, flexibility and efficiency are the guiding principles that underpin the Group's capital structure objectives.

The Board continues to believe that 3 years is an appropriate period of assessment and, aligned with the Group's strategic plan, the Directors also consider that they have reasonable visibility of the market over a 3-year period to 31 December 2020. A 3-year period is consequently considered appropriate for the Viability Statement. The Group's strategic plan includes an integrated model that incorporates income statement, balance sheet and cash flow projections. Key KPIs and financial ratios are reviewed along with the ongoing appropriateness of all assumptions used. Scenario planning is undertaken along with stress testing against downside sensitivities. The stress testing reflects the principal risks that could conceivably threaten the Group's ability to continue operating as a going concern and has critically assessed downside scenarios that might give rise to sales volume reductions, deteriorating operating margins and increases in interest rates. None of the individual sensitivities applied impact the Directors' assessment of viability. The stress testing applied in 2017 reflects a cautious economic outlook and remains a key part of the Group's detailed approach to capital structure and forecasting. A significant stress test sensitivity has been applied to reflect a dramatic economic downturn and the Group's updated Risk Register continues to identify external market factors as being the key risk. The stress testing has aimed to replicate the financial impact of the last recession as the core sensitivity, with significantly reduced sales volumes giving rise to a 33 per cent decrease in revenue over the next 3 years.

Based on this assessment, the Directors confirm that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due for the next 3 years.

## Principal risks and uncertainties

The Directors have undertaken a robust, systematic assessment of the Group's principal risks. These have been considered within the timeframe of 3 years, which aligns with our Viability Statement above.

## 1 Macro-economic and political

**LINK TO STRATEGY**

**NATURE OF RISK**

The Group is dependent on the level of activity in its end markets. Accordingly, it is susceptible to economic downturn, the impact of Government policy and any political and economic uncertainty in relation to Brexit.

**POTENTIAL IMPACT**

The potential impact of Brexit and wider global macro-economic uncertainty could lead to lower activity levels which could reduce sales and production volumes. This could have an adverse effect on the Group's financial results. The impact of exchange rate fluctuations could also have an adverse impact on material costs.

**MITIGATING FACTORS**

- The Group closely monitors trends and lead indicators, invests in market research and is an active member of the CPA.
- The Group benefits from the diversity of its business and end markets.
- The Group focuses on sales opportunities and strategic growth initiatives, together with quality, service and its supply chain.
- The Group focuses on its supplier relationships, flexible contracts and the use of hedging instruments.

**CHANGE IN RISK IN THE YEAR**

Given the perception of increased global economic uncertainty, this risk has increased and this is reflected in wider economic forecasts. The CPA forecasts have softened slightly in recent months.

There continues to be growth potential in certain focus areas, e.g. New Build Housing, Water Management and Rail. Forward indicators in the core business remain positive.

The proactive development of the product range continues to offer protection.

## 2 Cyber security risks

**LINK TO STRATEGY**

**NATURE OF RISK**

Inadequate controls and procedures over the protection of intellectual property, sensitive employee information and market influencing data.

The failure to improve controls against cyber security risk quickly enough, given the rapid pace of change and the continuing introduction of new threats.

**POTENTIAL IMPACT**

Risk of data loss causing financial and reputational risk.

**MITIGATING FACTORS**

- Use of IT security policies.
- The undertaking of regular cyber security risk audits by specialists and the quick introduction of mitigation controls and other recommended procedure updates.
- Sensitive data is currently restricted to selected senior and experienced employees who are used to handling such data.
- Where sensitive data is made available to third parties, it is done under confidentiality agreements with reputable suppliers.
- A rolling programme of awareness training for staff.

**CHANGE IN RISK IN THE YEAR**

This remains a high profile area and considerable focus is being given to promoting awareness of IT security policies.

Appropriate tools and training procedures are in place to protect sensitive data when stored and transmitted between parties (e.g. encryption of hard drives, restricted USB devices, secure data transmission mechanisms and third party security audits).

## 3 Integration of CPM

**LINK TO STRATEGY**

**NATURE OF RISK**

The successful integration of CPM into the Marshalls Group is a significant business issue for 2018.

**POTENTIAL IMPACT**

There is a risk that the integration of CPM could take longer than expected. This could impact the expected financial performance and reduce the positive impact of potential synergy benefits.

**MITIGATING FACTORS**

- Certain ongoing legal and regulatory matters were identified during due diligence and the sale and purchase agreement included risk mitigation by requiring £12 million to be paid into an escrow account pending the resolution of these issues. The Group has a right of reimbursement of amounts held in the escrow account to the extent that any liability crystallises in respect of these ongoing legal and regulatory matters.
- The Group has a detailed integration plan which covers all business areas and is focused on risk reduction and maximising opportunity.
- The integration plan has Executive level focus and is being administered by a dedicated Integration Manager.
- A post integration review is to be undertaken by KPMG in Q3 2018.

**CHANGE IN RISK IN THE YEAR**

The acquisition of CPM in October 2017 has created a new risk for the Group, although the integration project is receiving significant management focus.

**Strategic objectives:** Shareholder value Sustainable profitability Relationship building Organic expansion Brand development Effective capital structure and control framework

## 4 Weather

**LINK TO STRATEGY**

**NATURE OF RISK**
The Group is exposed to the impact of prolonged periods of bad weather.

**POTENTIAL IMPACT**
Adverse working conditions could give rise to disruption and delays that might reduce short-term activity levels. This could reduce sales and production volumes and therefore have an adverse effect on the Group's financial results.

**MITIGATING FACTORS**
- The Group has a continuing focus on new product development, including landscape water management.
- The Group is developing its internal flooring offer and International strategy in order to diversify its activities.
- The development of the Group's Water Management business is a significant opportunity. The acquisition of CPM has significantly moved the Group forward in this area and the acquisition has been a significant step in the stated strategy of providing a full water management capability.

**CHANGE IN RISK IN THE YEAR**

Weather conditions are beyond the Group's control.

## 5 Customers

**LINK TO STRATEGY**

**NATURE OF RISK**
The UK business has a number of key customers, in particular the national merchants. This is partly as a result of the consolidated nature of this market.

**POTENTIAL IMPACT**
The loss of a significant customer may give rise to a significant adverse effect on the Group's financial results.

**MITIGATING FACTORS**
- The Group focuses on brand and new product development, quality and customer service improvement.
- The Group maintains a national network of manufacturing and distribution sites.
- The Group undertakes ongoing reviews of trading policies and relationships and maintains constant communication with customers.

**CHANGE IN RISK IN THE YEAR**

Although the underlying risk continues, the effective management of key relationships and the ongoing diversification of the business are serving to mitigate the risk.

## 6 Competitor activity

**LINK TO STRATEGY**

**NATURE OF RISK**
The Group has a number of existing competitors who compete on range, price, quality and service.

Potential new low cost competitors may be attracted into the market through increased demand for imported natural stone products.

**POTENTIAL IMPACT**
The increased competition could reduce volumes and margins on manufactured and traded products.

**MITIGATING FACTORS**
- The Group has unique selling points that differentiate the Marshalls branded offer.
- The Group focuses on quality, service, reliability and ethical standards that differentiate Marshalls from competitor products.
- The Group continues to have the lowest cost to market.
- The Group has a continuing focus on new product development.

**CHANGE IN RISK IN THE YEAR**

The more uncertain market environment has not led to any significant changes in competitive pressure.

## 7 Threat from new technologies and new business models

**LINK TO STRATEGY**

**NATURE OF RISK**

Reduction in demand for traditional products. Risk of new competitors and new substitute products appearing. Failure to react to market developments.

**POTENTIAL IMPACT**

The increased competition could reduce volumes and margins on traditional products.

**MITIGATING FACTORS**

- Good market intelligence.
- Flexible business strategy able to embrace new technologies.
- Significant focus on research and development and new products.
- Development of a digital strategy.

**CHANGE IN RISK IN THE YEAR**

The ongoing diversification of the business, the continued development of the Marshalls brand and the focus on new products and greater manufacturing efficiency continue to mitigate the risk.

## 8 Cost and availability of raw materials

**LINK TO STRATEGY**

**NATURE OF RISK**

The Group is susceptible to significant increases in the price of raw materials, utilities, fuel oil and haulage costs and decreases in vehicle availability.

As demand increases, the Group is potentially more exposed to the risk of temporary raw material shortages.

**POTENTIAL IMPACT**

The increased costs could reduce margins and may be further impacted in the event of imbalances in the mix of regional activity.

The risk of market demand exceeding raw material supply could lead to inefficient production, which could reduce margins.

**MITIGATING FACTORS**

- The Group benefits from the diversity of its business and end markets.
- The Group focuses on its supplier relationships, flexible contracts and the use of hedging instruments.
- The Group utilises sales pricing and purchasing policies designed to mitigate the risks.
- The Group uses specialist delivery vehicles.

**CHANGE IN RISK IN THE YEAR**

Cost inflation remains a risk as demand for raw materials increases against a backdrop of increased economic uncertainty. All importers are faced with the same issues.

The risk of temporary shortages is mitigated by proactive supply chain management and the use of alternative suppliers.

## 9 Corporate, legal and regulatory

**LINK TO STRATEGY**

**NATURE OF RISK**

The Group may be adversely affected by an unexpected reputational event, e.g. an issue in its ethical supply chain or due to a health and safety incident.

The impact of the "Environmental Protocol" leads to the need for increasingly expensive processes.

**POTENTIAL IMPACT**

An incident could lead to a disruption to production and the supply of products for customers. This could increase costs and have a potential negative impact on the Group's reputation.

An environmental contamination event may lead to a prosecution and to reputational loss.

Significant increases in the penalty regime have increased the potential financial impact of health and safety as well as environmental incidents.

**MITIGATING FACTORS**

- The Group employs compliance procedures, policies and independent audit processes which seek to ensure that local, national and international regulatory and compliance procedures are fully complied with.
- The Group uses professional specialists covering carbon reduction, water management and biodiversity.
- The Group focuses on the implementation of ISO standards.
- The Group has a formal Group sustainability strategy focusing on impact reduction.

**CHANGE IN RISK IN THE YEAR**

The Group continues to improve compliance procedures within the supply chain.

Health and safety and the potential impact of the Bribery Act continue to be high profile risk areas. These areas are receiving additional management focus, but the impact of the underlying risk has increased.

The Group is unable to predict future changes in environmental laws or policies or the ultimate cost of compliance with such laws or policies.

**Strategic objectives:** Shareholder value · Sustainable profitability · Relationship building · Organic expansion · Brand development · Effective capital structure and control framework

# Continuing to deliver the 2020 Strategy objectives



## "Growth in all key financial metrics."

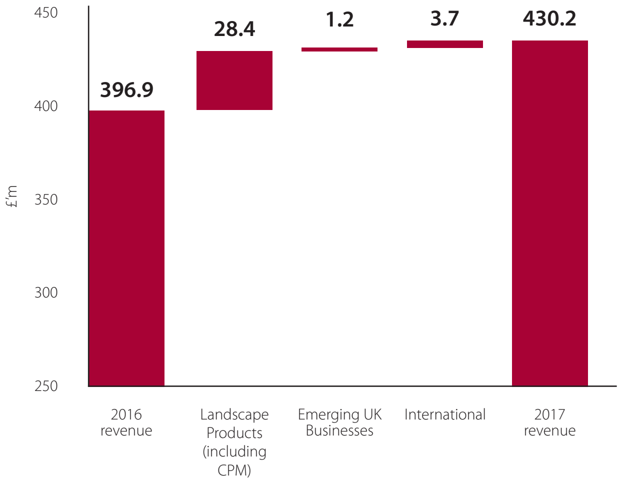
- Operating profit up 12% to £53.4 million.
- EBITDA up 12% to £67.9 million.
- Acquisition of CPM in October 2017.
- Consistently strong return on capital employed at 24.8% (excluding CPM).
- Strong operating cash flow at 100% of EBITDA.
- Significant headroom for investment.
- Increase in final ordinary dividend of 17%.
- Additional supplementary dividend of 4.00 pence per share.

## Trading summary

**Revenue**

Revenue for the year ended 31 December 2017 was £430.2 million (2016: £396.9 million), which represented an increase of 8.4 per cent. Group revenue includes £9.0 million from CPM for the period since its acquisition on 19 October 2017. On a like-for-like basis, excluding the impact of CPM, Group revenue was up 6.1 per cent.

**Revenue variance analysis 2016/2017 (£'m)**




Analysis of revenue by end market is summarised in the table below:

| Analysis of revenue by end market | **2017 £'m** | 2016 £'m | Change % |
|---|---|---|---|
| UK Domestic | **135.4** | 120.8 | 12.1 |
| Public Sector and Commercial (including CPM) | **271.8** | 256.8 | 5.8 |
| International | **23.0** | 19.3 | 19.3 |
| | **430.2** | 396.9 | 8.4 |
| | **%** | % | |
| UK Domestic | **31.5** | 30.5 | |
| Public Sector and Commercial (including CPM) | **63.2** | 64.6 | |
| International | **5.3** | 4.9 | |

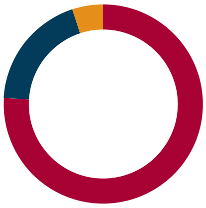
# Financial Review *continued*

### Revenue by end market

| | |
|---|---|
| UK Domestic | 32% |
| Public Sector and Commercial | 63% |
| International | 5% |

### Revenue by area

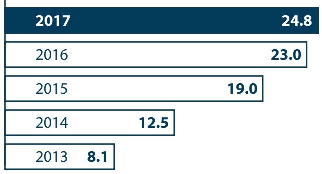
| | |
|---|---|
| Landscape Products | 79% |
| Emerging UK businesses | 16% |
| International | 5% |



### Return on capital employed (%)

24.8%(1)

**(20.8% on a reported basis)**




1 On a like-for-like basis (excluding the impact of CPM)

## Trading summary *continued*

### Public Sector and Commercial

Excluding CPM, sales in the Public Sector and Commercial end market were up 2.3 per cent compared with 2016. Including the post-acquisition contribution of CPM, sales in the Public Sector and Commercial end market were up 5.8 per cent and represented 63 per cent of Group sales.

Marshalls' strategy is to offer sustainable integrated solutions to customers, architects and contractors. The Group's technical and sales teams remain particularly focused on those market areas where future demand is considered to be greatest including New Build Housing, Water Management and Rail. The Group is outperforming the market in these areas. Our "Design Space" office in Central London continues to showcase the Group's brand leading capabilities and provides customers with information about new products, access to samples and technical advice.

The Group's unique national network of manufacturing sites remains a core strength and, as far as our mineral reserves are concerned, the "Marshalls Stone Standard" quality mark gives customers full assurance that all Marshalls' natural stone not only meets, but exceeds the base technical levels outlined in BS7533.

### Domestic

Revenue in the Domestic end market grew strongly, increasing by 12.1 per cent. Sales to the UK Domestic end market now represent approximately 32 per cent of Group sales.

Installer order books at the end of February 2018 were 10.8 weeks (February 2017: 10.9 weeks), compared with 11.7 weeks at the end of October 2017. The Group continues to receive good feedback from its customers and installers for the consistency and quality of service and we remain focused on enhancing the overall customer experience by extending digitisation and commitment to innovation. The Group's industry leading standards remained high in 2017 with a combined customer service measure of 98 per cent (2016: 98 per cent).

The Group's strategy continues to be to drive more sales through quality installers. The Marshalls Register of approved domestic installers is unique and comprises approximately 1,900 teams. The objectives continue to be to develop the Marshalls' brand, improve the product mix, ensure a consistently high standard of quality, excellent customer service and marketing support and maintain good geographical coverage.

### International

Sales to International markets increased by 19.3 per cent and represents approximately 5 per cent of Group sales. The Group continues to develop its global supply chains and infrastructure to ensure that international operations are aligned with market opportunities. Revenue growth has been strong in the US during 2017 and the new sales office in Dubai has delivered further sales growth in the Middle East.

### Acquisition of CPM

Water Management is a strategic focus for Marshalls and the acquisition of CPM on 19 October 2017 is a significant step forward for the Group, extending the product range into the new area of below ground drainage. CPM has a comprehensive range of technical and innovative water management solutions and has a strong track record of quality and service.

The acquisition of CPM has contributed £9.0 million to Group revenue and sales for the full 12 month period ended 31 December 2017 were £55.3 million. Recent growth has been driven by an expansion in production capabilities and the sites at Mells, in Somerset, and Pollington, in East Yorkshire, are both able to produce around 170,000 tonnes per annum. The provision of bespoke "off-site" solutions is a particular growth area.

The acquisition has been funded from existing facilities and an additional £20 million debt facility was established to maintain headroom capacity.

### Operating profit

| Trading results | **2017 £'m** | 2016 £'m | Change % |
|---|---|---|---|
| EBITDA | **67.9** | 60.8 | 11.7 |
| Depreciation / amortisation | **(14.5)** | (13.2) | |
| Operating profit | **53.4** | 47.6 | 12.2 |

Operating profit was £53.4 million (2016: £47.6 million), which represents an increase of 12.2 per cent. This is after charging £1.2 million of operational restructuring costs and £0.8 million of acquisition costs. EBITDA increased by 11.7 per cent to £67.9 million (2016: £60.8 million) and EPS was 21.52 pence (2016: 18.95 pence), an increase of 13.6 per cent.

ROCE remained strong and, notwithstanding the acquisition of CPM in October 2017, was 20.8 per cent (2016: 23 per cent), on a reported basis, at 31 December 2017. Capital employed has increased by 23.8 per cent to £261.8 million (2016: £211.7 million) following the acquisition of CPM. On a like-for-like basis, excluding the impact of CPM, ROCE was up 8 per cent at 24.8 per cent. This reflects the Group's tight control and management of inventory and monetary working capital.

### Profit margins

The Group has continued to strengthen its market position and operating margin has increased to 12.4 per cent (2016: 12.0 per cent).

| Margin analysis | Revenue £'m | Reported operating profit £'m | Margin impact % |
|---|---|---|---|
| 2016 | 396.9 | 47.6 | 12.0 |
| Landscape Products | 28.4 | 5.1 | 0.4 |
| Emerging UK Businesses | 1.2 | 0.4 | 0.1 |
| International | 3.7 | 0.3 | (0.1) |
| **2017** | **430.2** | **53.4** | **12.4** |

The table illustrates the impact of operational gearing in the UK businesses and shows that growth has continued to be ahead of CPA forecasts. The Group's Landscape Products business is a reportable segment servicing both the UK Public Sector and Commercial and UK Domestic end markets. Revenue increased by £28.4 million and operating profit grew by £5.1 million in the Landscape Products business.

There has been continued development of the Emerging UK Businesses during 2017 and revenue increased by 2 per cent compared with the prior year period. The emerging UK businesses include Street Furniture and Mineral Products and they continue to be a key strategic focus and a positive driver for growth.

### Continued development of the 2020 Strategy

During 2017, capital investment in property, plant and equipment (including software) totalled £22.5 million (2016: £13.9 million). This compares with depreciation of £14.5 million (2016: £13.2 million). This includes a significant increase in self help capital projects to deliver new, innovative products and to drive through sustainable cost reductions and improvements in operational efficiency. We continue to have a strong pipeline of such projects and capital expenditure of £28 million is planned for 2018.

Research and development expenditure in the year ended 31 December 2017 amounted to £3.9 million (2016: £3.4 million). Investment in research and development covers a number of areas including the development of the Group's project engineering and manufacturing capabilities, concrete and other materials technology innovations and extending the new product pipeline. Revenue from new products increased by 4.2 per cent during 2017 in the core Landscape Products business and over the last 3 years has increased by 14 per cent.

Further investment continues to be made to develop our wide-ranging digital strategy, encompassing digital trading, digital marketing and digital business. More details are provided on page 17.

### Net financial expenses

Net finance costs were £1.4 million (2016: £1.6 million) and interest was covered 38.5 times (2016: 29.9 times). Interest charges on bank loans totalled £1.0 million (2016: £1.1 million) and, including scheme administration costs, there was an IAS 19 notional interest charge of £0.4 million (2016: £0.5 million) in relation to the Group's Pension Scheme. The IAS 19 notional interest includes interest on obligations under the defined benefit section of the Marshalls plc Pension Scheme, net of the expected return on Scheme assets.

### Taxation

The effective tax rate was 19.1 per cent (2016: 18.5 per cent), the prior year having benefited from a deferred tax credit arising principally in relation to the settlement of share-based payments. The Group has paid £10.5 million (2016: £7.1 million) of corporation tax during the year. Deferred tax of £0.1 million in relation to the actuarial gain arising on the defined benefit Pension Scheme in the year has been taken to the Consolidated Statement of Comprehensive Income.

Marshalls has again been awarded the Fair Tax Mark, which recognises social responsibility and transparency in a company's tax affairs. The Group's tax approach has long been closely aligned with the Fair Tax Mark's objectives and this is supported by the Group's tax strategy and fully transparent tax disclosures.

**Case study**

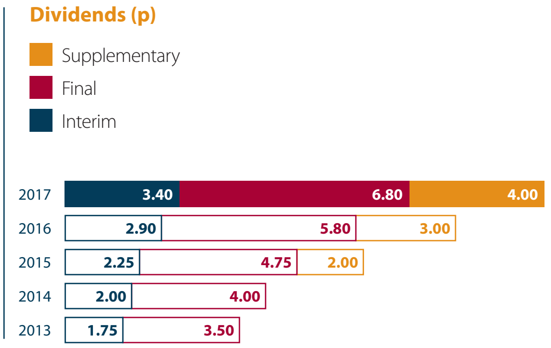
## Self help capital expenditure

- Self help capital expenditure is additional to ongoing spend;
- Must be "value added", targeting volume growth areas and cost reduction and efficiency opportunities;
- Objective is <3 years payback and a healthy IRR;
- Self help capital expenditure of £8.6 million in 2017, with a similar level planned for 2018;
- New investment in a modern production facility in Natural Stone Paving;
- £3 million investment in saws, automation and optimisation of stone processing; and
- Significant improvement in yields and efficiency.

## **Trading summary** *continued*

### Dividends

The recommended "supplementary dividend" of 4.00 pence (2016: 3.00 pence) per share is discretionary and non-recurring and recognises that the business has sufficient capital both to finance increased investment and to maintain a conservative and flexible capital structure. When added to the normal full year dividend of 10.20 pence, this gives a total dividend for the year of 14.20 pence, which represents an increase against the prior year of 21 per cent. The incremental cash outflow in 2017 in relation to the supplementary dividend has been £5.9 million and will be approximately £7.9 million in 2018.




### Balance sheet

| Group balance sheet | **2017 £'m** | 2016 £'m |
|---|---|---|
| Non-current assets | **249.1** | 193.4 |
| Current assets | **166.3** | 139.7 |
| Current liabilities | **(106.9)** | (87.1) |
| Non-current liabilities | **(70.9)** | (28.9) |
| Net assets | **237.6** | 217.1 |
| Net (debt) / cash | **(24.3)** | 5.4 |

Net assets at 31 December 2017 were £237.6 million (2016: £217.1 million). The Group has a strong balance sheet with a good range of medium-term bank facilities available to fund investment initiatives to generate growth.

### Credit management

The Group continues to prioritise the close control of inventory and the effective management of working capital. Debtor days remain industry leading due to continued close control of credit management procedures. The Group maintains credit insurance which provides excellent intelligence to minimise the number and value of bad debts and ultimately provides compensation if bad debts are incurred.

### Pension

The balance sheet value of the Group's defined benefit Pension Scheme was a surplus of £4.1 million (2016: £4.3 million). The amount has been determined by the Scheme actuary. The fair value of the Scheme assets at 31 December 2017 was £354.7 million (2016: £360.1 million) and the present value of the Scheme liabilities is £350.6 million (2016: £355.8 million). These changes have resulted in an actuarial gain, net of deferred taxation, of £0.3 million (2016: £1.4 million actuarial gain) and this has been recorded in the Consolidated Statement of Comprehensive Income. The Company has previously agreed with the Trustee that no cash contributions are now payable under the funding and recovery plan.

**Case study**

## Capital allocation

The Group's capital allocation strategy is to maintain a strong balance sheet and flexible capital structure that recognises cyclical risk, while focusing on security, efficiency and liquidity.

The capital allocation strategy prioritises organic capital investment, supported by an increase in new product development and research and development expenditure. The strategy also targets selective bolt-on acquisition opportunities. In addition, the objective is to maintain a dividend cover of 2 times earnings over the medium term and to give consideration to supplementary dividends.

**Priorities for capital**

1. **Organic growth**
   Capital investment in growth projects. Plan £28 million in 2018.
2. **R&D and NPD**
   Increase research and development and new product development.
3. **Ordinary dividends**
   Maintain dividend cover of 2 times earnings over the business cycle.
4. **Selective acquisitions**
   Target selective bolt-on acquisition opportunities in Water Management, Street Furniture and Minerals.
5. **Supplementary dividends**
   Supplementary dividends when appropriate. Discretionary and non-recurring.

**Case study**

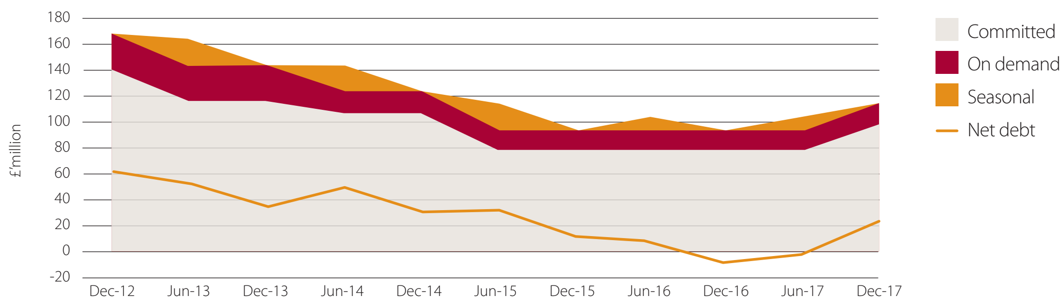
## Self help capital expenditure

**Investment in**

- New kerb and edging press facilities servicing the South East – to eliminate logistics cost of transferring product between regions;
- Investment in facemix and other technologies to produce value-added products;
- Investment in automatic guided vehicles – along with vision systems and monitoring cameras; and
- Investment in auto-wash systems and in DISAB vacuum system soda blast cleaning equipment – to reduce downtime and assist maintenance.

STRATEGIC REPORT

### Banking facility headroom




### Analysis of net debt

| Analysis of net (debt) / cash | **2017 £'m** | 2016 £'m |
|---|---|---|
| Cash and cash equivalents | **19.8** | 20.7 |
| Bank loans | **(43.8)** | (14.9) |
| Finance leases | **(0.3)** | (0.4) |
| | **(24.3)** | 5.4 |

Net debt at 31 December 2017 was £24.3 million, which reflects the payment of consideration totalling £38.2 million in relation to the acquisition of CPM, together with the impact of CPM's net borrowings taken on of £3.0 million. This compares with a positive cash position of £5.4 million at 31 December 2016. The ratio of net debt to EBITDA was 0.35 times at 31 December 2017 which is comfortably within our target range, of between 0 to 1 times, and well below covenant levels.

Cash management continues to be a high priority with continuing focus on the close control of inventory and the effective management of working capital. The key working capital metrics are in line with plan.

### Borrowing facilities

On 17 August 2017, the Group renewed its short-term working capital facilities of £25.0 million. This includes a seasonal working capital facility of £10.0 million which is available between 1 February and 31 August each year. On 16 October 2017 the Group took out an additional committed facility of £20.0 million. The Group continues its policy of having a range of committed bank facilities in place with a positive spread of medium-term maturities that now extends to 2022. The Group's committed facilities are all revolving credit facilities with interest charged at a variable rate based on LIBOR.

The total bank borrowing facilities at 31 December 2017 amounted to £115.0 million (2016: £95.0 million) of which £71.1 million (2016: £80.0 million), remained unutilised. Interest cover and net debt to EBITDA covenants in the facilities were comfortably met at the year end. The bank facilities are unsecured save for inter-company guarantees between the Group and its subsidiary undertakings in favour of the facility banks.

| Expiry date | Facility £'m | Cumulative facility £'m |
|---|---|---|
| **Committed facilities** | | |
| Q3 2022 | 20 | 20 |
| Q3 2021 | 20 | 40 |
| Q3 2020 | 20 | 60 |
| Q3 2019 | 20 | 80 |
| Q3 2018 | 20 | 100 |
| **On-demand facilities** | | |
| Available all year | 15 | 115 |
| Seasonal (February to August inclusive) | 10 | 125 |

### Cash generation

The Group is significantly cash generative. In the year ended 31 December 2017 net cash flow from operating activities was £57.3 million (2016: £49.4 million).

| Group cash flow | **2017 £'m** | 2016 £'m |
|---|---|---|
| Net cash from operating activities | **57.3** | 49.4 |
| Net cash from investing activities | **(58.0)** | (10.0) |
| Net cash from financing activities | **(28.5)** | (20.2) |
| Movement in net debt in the year | **(29.2)** | 19.2 |
| Foreign exchange | **(0.5)** | (2.3) |
| Net cash / (debt) at beginning of year | **5.4** | (11.5) |
| **Net (debt) / cash at end of year** | **(24.3)** | 5.4 |

| Analysis of cash utilisation | **2017 £'m** | 2016 £'m |
|---|---|---|
| Net cash from operating activities | **57.3** | 49.4 |
| Capital expenditure | **(20.7)** | (13.9) |
| Proceeds from sale of property assets | **3.9** | 3.8 |
| Payments to acquire own shares / other | **(1.1)** | (1.1) |
| Acquisition of subsidiary undertaking | **(44.5)** | – |
| Dividends | **(24.1)** | (19.0) |
| **Movement in net debt** | **(29.2)** | 19.2 |

Cash outflow on capital expenditure in the year was £20.7 million (2016: £13.9 million). This includes self help growth expenditure and the replacement of existing assets, business improvements and new process technology. Proceeds from the sale of targeted property assets contributed £3.9 million (2016: £3.8 million). The increase in net debt arising on the acquisition of CPM comprises the cash outflow in connection with the acquisition and the fair value of borrowings acquired. Dividend payments in the year were £24.1 million (2016: £19.0 million).

**Jack Clarke**
Finance Director

# At the heart of all we do

By being a responsible business we are leveraging sustainability to drive competitive advantage for our business.

## Human Rights

**OBJECTIVES**

Marshalls supports human rights consistent with the Universal Declaration of Human Rights. In conducting business across the globe we respect these rights and seek to uphold, preserve and promote them. Our corporate responsibility to respect human rights means acting with due diligence to avoid infringing upon the rights of others, and addressing any issues that do occur. We recognise that our responsibility applies across all business activities, including business relationships with third parties and those within our supply chain.

**2018 PRIORITIES**

- Continue to focus on the issue of modern slavery and improve compliance procedures within the supply chain; and
- Continue to collaborate with multiple stakeholders.

**PROGRESS**

Human rights regulation for business continues on an upward trajectory and the issue of modern slavery rightly remains firmly in the spotlight. We are working with multiple stakeholders across the world to help make our business operations and supply chains as toxic as possible to the organised criminals who seek to exploit vulnerable individuals and corporations. We are collaborating with governments, UN agencies, human rights observers, suppliers, workers and communities. Our human rights due diligence and monitoring and implementation is extremely dynamic reflecting the nature of the human rights arena. Our active global supply chain risk mapping processes together with our Ethical Risk Index further guide our robust decision making processes.

**Detailed ethical risk indices are in place for 44 natural stone product supply chains.**

**FUTURE GOALS**

- Further develop the Group's global supply chain risk mapping processes; and
- Continue to develop our Ethical Risk Index methodology and procedures.

## Labour Rights

**OBJECTIVES**

From living wages in the UK to the elimination of child labour in India, we are committed to ensuring that what is good for business is good for society. Our approach to labour rights is driven by the Ethical Trading Initiative ("ETI") Base Code which we adopted in 2005. To ensure that the Base Code is embedded within operations and supply chains we have social auditors in India, China and Vietnam.

**2018 PRIORITIES**

- Continue to promote ETI membership, peer reviews and our "Hope for Justice" Strategic Partnership;
- Conduct ETI Base Code social and ethical audits in India, China and Vietnam; and
- Develop the use of social auditors in India, to complement the ETI ethical audits.

**PROGRESS**

We continue to be members of the ETI and our new ETI Strategic Plan has been developed to support, strengthen and maximise our continued drive to uphold and strengthen labour rights across the globe. The Plan honours our commitment to ETI Base Code implementation and will further embed and integrate ethical trade into business activities and decision making; ultimately it will seek to improve conditions for workers, their families and communities.

**Marshalls have been accredited by the Living Wage Foundation since 2015.**

**FUTURE GOALS**

- Further embed and integrate ethical trade into business practice;
- Promote procurement principles that comply with the UN Global Compact and ETI base code;
- Continue to improve conditions for workers, their families and communities; and
- Maintain commitment to the abolition of slavery in all its forms.

### Sustainability overview

Corporate responsibility, awareness and mitigation of adverse impacts on the environment, and positive engagement with our community and employees have long been core values of Marshalls. We aim to align our business values, purpose and strategy with the social, economic and environmental needs of our stakeholders, embedding responsible and ethical business policies and practices in everything we do.

FTSE4Good

Find out more online:
**www.marshalls.co.uk/sustainability**

Climate Change Policy
**www.marshalls.co.uk/ccp**

Carbon Disclosure Project
**www.cdp.net**

Environmental
**www.marshalls.co.uk/sustainability/environment**

## The Environment

**OBJECTIVES**

Our environmental objectives and targets are driven by a strong commitment to compliance coupled with mitigation plans to address legislative and physical business risks, whilst maximising opportunities against a corporate strategic commitment to be a sustainable business. At the heart of Marshalls' sustainable business model is an approach which combines key business issues and key performance indicators with third party verification, legislation and industry standards including ISO14001 for environmental management and ISO50001 for energy management.

**2018 PRIORITIES**

- Continue to focus on the Group's Sustainability Strategy, including key focus areas such as eSight energy monitoring systems and increasing use of rainwater capture;
- Further develop detailed site energy usage and carbon intensity analysis and action plans; and
- Maintain adherence to all legislative and ISO requirements for environmental and energy management.

**PROGRESS**

We have clear environmental, energy and climate change policies in place and are on track to meet our policy commitments. Key environmental issues for us are climate change, water and biodiversity. Marshalls' successful management of environmental issues has been recognised by third parties such as Business in the Community.

**Over 2,500 individual product carbon footprints.**

**FUTURE GOALS**

- Continue to develop environmental targets as key business drivers to increase sustainability, cost efficiency and shareholder value;
- Ensure that environmental targets are aligned with operational and strategic planning; and
- Invest in smart systems that allow real time monitoring of energy consumption in relation to carbon reduction measures.

## Responsible Business

**OBJECTIVES**

Marshalls is committed to conducting business with the utmost integrity and in accordance with the principles set out in the Bribery Act 2010. Greater transparency leads to increased trust. This in turn provides the solid foundations required for sustainable growth. By making our financial, social, environmental and ethical data transparent we can inspire trust which will lead to customers buying more of our products, investors purchasing more of our stock, and engaged employees working harder and smarter.

**2018 PRIORITIES**

- Further develop the Group's ongoing monitoring, training and compliance procedures;
- Continue to ensure that appropriate training is undertaken in relation to responsible business practice, including the Group's anti-bribery and corruption policies and procurement procedures; and
- Continue to maintain our Fair Tax Mark accreditation and to be open and transparent about the Group's tax affairs. Our commitment to responsible tax practice ensures that we seek to pay the right amount of tax at the right time in the right place.

**PROGRESS**

We are clear that bribery is not a victimless crime and that it discourages effective trading by diverting funds away from projects designed to build communities and help the most disadvantaged in our society. We have a clear Anti-Bribery & Corruption Policy and have launched and effectively communicated Marshalls' Supplier Code of Conduct. This has been further embedded, with employees and suppliers, through a new IT training platform.

**Marshalls is making a significant contribution to the implementation of the Sustainable Development Goals.**

**FUTURE GOALS**

- Continue to promote the UN Global Compact's commitment to sustainable development and the implementation of the UN's 17 Sustainable Development Goals;
- To make an increasing impact in the implementation of these goals – especially those goals where Marshalls is particularly well-placed to make a significant contribution.

### Marshalls' sustainable business model

Empowered by our brand values of leadership, excellence, trust and sustainability we work passionately and diligently to uphold the United Nations Global Compact pillars of human rights, labour, environment and anti-corruption. The Group has a sustainable business plan and has set KPIs for the key areas of this plan. It addresses economic, social and environmental aspects of Marshalls' operations.

## Carbon emissions – disclosure

Marshalls' Energy and Climate Change Policy confirms the Group's commitment to reducing the energy and carbon impact of its business. Our target is to reduce Group absolute $CO_2$e emissions in line with the UK Government's targets (37 per cent by 2020 and 80 per cent by 2050 from a 1990 baseline). The progress indicates that reductions are in line with the 2020 and 2050 targets.

The Group complied with its legal obligation under the Government's Carbon Reduction Commitment Energy Efficiency Scheme ("CRC") by submitting its Annual Report and surrendering appropriate Carbon allowances for the period April 2016 to March 2017 within the time limit imposed by the legislation. The Group continues to be certified to the Carbon Trust Standard. The Group's approach to the Energy Savings Opportunity Scheme ("ESOS") legislation was to define its energy management in compliance with the international standard for energy management ISO50001, gaining accreditation in November 2015 and maintaining this through 2017. The Group continues to voluntarily disclose data to the "Carbon Disclosure Project" receiving a B rating for its 2017 submission. This disclosure includes the wider carbon management performance over time and also provides an insight for shareholders regarding the Group's energy, carbon and climate change impact management programme.

Marshalls has a mandatory duty to report its annual Greenhouse Gas Emissions ("GHG") under the Companies Act 2006 (Strategic and Directors' Reports) Regulations 2013 and the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008. Marshalls uses The Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard (revised edition) and the August 2017 Department for Business, Energy and Industrial Strategy (BEIS) published $CO_2$e conversion factors to measure its GHG emissions.

The Group has conducted an audit of its UK fugitive emissions and found these to be 0.6 per cent of the Group total emissions; accordingly these are excluded from the report.

The chart below (left) illustrates the Group's UK absolute $CO_2$e emissions in tonnes, including transport activities, between 2013 and 2017.

The chart below (right) illustrates the Group's $CO_2$e intensity emissions as a proportion of production output, including transport activities between 2013 and 2017.

A number of factors have contributed to the Group's energy performance during the year including reduction in carbonisation of the electricity grid supply, product mix, weather (temperature impacting on the use of heating / cooling fuel) and energy management activities. Two increases in emissions during the year have resulted from the acquisition of CPM Group, which had added (absolute) 760 tonnes and (intensity) 11.44 kg per tonne production, to the annual data and an increase in the LGV fleet by 11 per cent full time equivalent vehicles to satisfy customer requirements.

The Group reports that it is responsible for the GHG emissions of Marshalls NV. The $CO_2$ emission from Marshalls NV activities (using the latest International Energy Associations Emission Factor) in 2017 was (absolute) 520 tonnes and (intensity) 10.60 kg per tonne production.

Marshalls aims to publish its environmental KPI performance for the financial year in a separate document, the Marshalls' Environmental KPI 2018 Report. This will cover the energy performance in more detail, together with reporting of the environmental governance, policies, management and key environmental impact areas such as waste, water and packaging. The Environmental KPI 2018 Report will also detail our work with internationally recognised expert bodies such as the Carbon Trust and the RSPB.

This section of the Annual Report has been audited by a qualified verifier on behalf of BSI. On the basis of the work undertaken this carbon statement is considered to be a fair reflection of the Group's performance during 2017 and contains no misleading information.

## Health and safety

Marshalls is committed to meeting the highest safety standards for all its employees, reinforcing and developing its safety processes, and developing a competent workforce with a view to achieving long-term improvement gains. This remains a key priority for the business.

The achievement of annual health and safety improvement targets is directly linked to the remuneration of the Executive Directors and senior management, as explained in the Remuneration Report on pages 50 to 63.

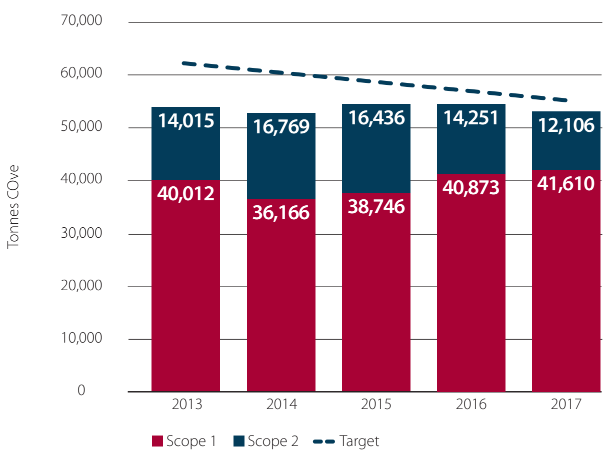
The headline target for 2017 was to maintain days lost resulting from workplace incidents at a figure no higher than the 2015 actual result. The actual results achieved were:

- 46 per cent reduction in days lost resulting from all accidents frequency rate;
- 11 per cent reduction in all incident frequency rate;

**Scope 1 and 2 emissions (Tonnes $CO_2$e)**

Scope 1 41,610 tonnes $CO_2$e

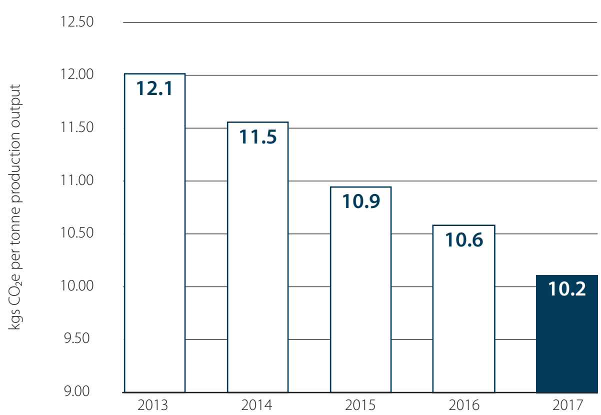
Scope 2 12,106 tonnes $CO_2$e




**Relative $CO_2$e emissions for Scope 1 and 2 from UK operations (kg $CO_2$e per tonne of production)**

# 10.17kg $CO_2$e/T

**-3.7%**



- 20 per cent reduction in lost time incidents ("LTI's") frequency rate; and
- 12 per cent reduction in incidents reportable to the HSE under the Reporting of Injuries, Diseases and Dangerous Occurrence Regulations ("RIDDOR").

The primary target for 2018 will be to achieve an accident rate for the year no higher than the 2015 actual result. The table below shows the KPIs used by the Group to monitor performance, and progress against those KPIs over the last 5 years.

**Accident frequency and severity rates (per 1 million hours worked)**

| | 2013 | 2014 | 2015 | 2016 | **2017** |
|---|---|---|---|---|---|
| All accidents | 65.6 | 59.1 | 48.8 | 49.2 | **43.4** |
| All lost time accidents | 12.2 | 7.2 | 5.1 | 5.6 | **4.1** |
| All RIDDORs | 3.6 | 3.3 | 1.6 | 2.3 | **1.4** |
| All days lost | 114.6 | 80.7 | 45.8 | 38.0 | **24.6** |
| Average UK headcount | 2,055 | 2,132 | 2,237 | 2,253 | **2,307** |

In 2017, the Executive Board agreed a formal 5-year Health and Safety strategy with set objectives. This strategy clearly demonstrates the commitment of the business to take the safety of its employees to the highest level.

The business also introduced a Safety, Health, Environmental and Quality ("SHEQ") concerns reporting process. The SHEQ concerns system not only gives all employees the tools to report concerns, but also ensures management identifies the root causation ensuring the right actions are taken to prevent a re-occurrence.

In 2018 the main Health and Safety initiatives will include:

- The implementation of Marshalls' mental health awareness programme. This involves the introduction of a mental health policy and support network, all management in the business receiving mental health awareness training and the Company appointing and training company mental health champions who will deliver mental health training to all employees;
- A programme whereby all first line supervisors within the business will complete a new, recently developed, Marshalls Health and Safety stage 2 training programme;
- The integration of CPM into the Marshalls Health and Safety Management system and culture; and
- The introduction of safety observations to all management teams across the business.

These initiatives will enhance the already high standard the Company demands in Health and Safety and take it to a completely new level.

## Equality and diversity

The ability to recruit, retain and develop the right people is fundamental to the future success of the business. The Company believes that attracting a suitably diverse range of individuals with the appropriate skills and experience will help us to achieve its goals.

As such, the Group has policies that promote equality and diversity and is committed to providing equal opportunities to employees and potential employees irrespective of gender, ethnicity, age, sexual orientation, disability or religious beliefs. The Company opposes all forms of discrimination and reinforces this through communication, awareness training and policy.

## Employees

The Company continues to be a "Living Wage Employer", underscoring its commitment to fairness and integrity towards our employees. Our recruitment policies are geared towards giving full and fair consideration towards creating a more diverse workforce and it is clear that there is much to be done in making the Company more attractive to both younger people and females in what has been historically a highly male dominated sector and workplace. The Company will be considering pro-active ways to encourage the attraction and promotion of these groups as part of our wider diversity and inclusion policy.

We also welcome and give full and fair consideration to applications from persons with recognised disabilities, providing equal opportunities for promotion and development and making adjustments to ensure that such individuals are not disadvantaged in the workplace.

### Employee engagement and development

Improving employee engagement throughout the Group continues to be an important priority in order for the business to deliver on its strategy and objectives as well as providing a fulfilling and rewarding place of work for our people. Initiatives to improve this included various charitable events across the Group raising in total over £100,000 for our nominated charity, MIND. The business also used the "Best Companies" framework to conduct another employee survey across all of the Group during 2017, achieving a response rate of 70 per cent. This will have been the fifth survey of this type as we continue to strive to improve our working environments and capture the valuable feedback from our employees and devise improvement plans as a result. The Company operates Sharesave and share purchase plans to encourage employee participation in the Company's success.

The engagement programme is supported by an annual Group-wide communication "roadshow" programme of senior management visits travelling around the business with the objective of meeting as many of our employees as possible face to face. This provides the Directors and senior management team with an unparalleled opportunity to explain to our employees how the business is performing, how our strategy is working, and what the priorities and objectives are, as well as providing information of concern to employees generally, taking soundings on employee views and answering questions in an open forum.

As a business, we are committed to investing in our employees. The ongoing training and development of our employees to develop our future managers and leaders is of major importance to the business. There is a range of online learning programmes accessible to all employees, and, in addition, to the management training programme for our first line managers, in which over 100 employees have now participated, we have added an additional 3 management development programmes. These programmes are geared towards emerging and middle management and facilitated through the University of Salford, Ashridge Business School and Cranfield School of Management.

We also continue to try and make our organisation an attractive place of work for young people through our ongoing apprenticeship programmes. We now have a good mix of apprenticeships spanning everything from engineering through to 4 year apprenticeships in areas such as marketing and Information Systems. We will continue to build on these schemes to increase our intake in 2018 and widen the range of options for prospective employees. We have strong community connections, particularly in locations near our offices and factories, and we plan to develop closer relations with local schools and colleges in order to encourage young people into the industry as well as the business.

Good progress has been made in the year with the development of our new HR system platform which will improve our operational efficiency and reliability of data in personnel and payroll administration. This, in conjunction with our project on job evaluation, will ensure that we are in a position to facilitate better decision making and create a more transparent system for the equal treatment of employees.

The system will also serve as the foundation to develop our future people strategy and complement our wider Group objectives through improved resource planning, performance management, recruitment and talent development initiatives with a view to ensuring that we attract and retain the best people in an open and fair way.

# Board of Directors and Secretary

## Andrew Allner

Chairman

**BOARD COMMITTEES**
Remuneration; Nomination (Chairman).

**TERM OF OFFICE**
Joined the Board in July 2003; appointed as Chairman in May 2010. Last re-elected in May 2017, and will retire in May 2018. Also chairs the Nomination Committee.

**LENGTH OF SERVICE**
14 years 6 months
(7 years 6 months as Chairman)

**INDEPENDENT**
Yes (on appointment as Chairman)

**SKILLS AND EXPERIENCE**
Significant current listed company Board experience, as Chairman and as a Non-Executive Director. Previous Executive roles include Group Finance Director of RHM plc, taking a lead role in its flotation in July 2005 on the London Stock Exchange, and CEO of Enodis plc. Also held senior Executive positions with Dalgety plc, Amersham International plc and Guinness plc.

Chartered Accountant, former partner of Price Waterhouse. Graduate of the University of Oxford.

**EXTERNAL APPOINTMENTS**
Non-Executive Director and Chairman of SIG plc; Non-Executive Director and Chairman of The Go-Ahead Group plc and Fox Marble Holdings plc, and Non-Executive Director at Northgate plc.

## Martyn Coffey

Chief Executive

**BOARD COMMITTEES**
None.

**TERM OF OFFICE**
Joined the Company and appointed to the Board in September 2013. Last re-elected in May 2017.

**LENGTH OF SERVICE**
4 years 4 months

**INDEPENDENT**
No

**SKILLS AND EXPERIENCE**
Wide Executive leadership experience: previously Divisional Chief Executive Officer of BDR Thermea Group BV, a leading manufacturer and distributor of domestic and industrial heating and hot water systems operating in 70 countries and with a turnover of €1.8 billion, formed in 2009 from the merger of Baxi and De Dietrich Remeha. Prior to the merger, he was Chief Executive of the private equity-owned Baxi Group. Also held the position of Managing Director of Pirelli Cables where he spent 14 years in the UK, Australia and North America. Holds a BSc in Mathematics.

**EXTERNAL APPOINTMENTS**
Officer of the Construction Products Association. Director of the Mineral Products Association. Non-Executive Director and Chair of Remuneration Committee at Eurocell plc.

## Jack Clarke

Finance Director

**BOARD COMMITTEES**
None.

**TERM OF OFFICE**
Joined the Company and appointed to the Board on 1 October 2014. Last re-elected in May 2017.

**LENGTH OF SERVICE**
3 years 3 months

**INDEPENDENT**
No

**SKILLS AND EXPERIENCE**
Chartered Accountant. Joined Marshalls from AMEC Foster Wheeler plc, where he was Executive Vice President and Director of Change Management. He has extensive experience in managing international operations, having previously served as CFO of AMEC's £850 million power and process division and its US$1.5 billion environment and infrastructure division. He has extensive M&A experience. Previous experience includes senior finance and operational management roles with Halliburton and Mobil Oil. Holds an MSc (Civil Engineering) and BA (Economics and Management).

**EXTERNAL APPOINTMENTS**
None.

## Janet Ashdown

Senior Independent Non-Executive Director

**BOARD COMMITTEES**
Audit; Remuneration (Chair); Nomination.

**TERM OF OFFICE**
Appointed in March 2015. Last re-elected in May 2017.

**LENGTH OF SERVICE**
2 years 9 months

**INDEPENDENT**
Yes

**SKILLS AND EXPERIENCE**
Non-Executive Director of SIG Plc: other appointments include Non-Executive member of the Board of the Nuclear Decommissioning Authority (since 2015) and Non-Executive Director of Victrex plc (appointed February 2018). Previous Executive experience included 30 years with BP plc, most recently as Director, BP Oil UK Limited, and Head of UK Retail and Commercial Fuels. Between 2010 and 2012 she was CEO of Harvest Energy.

**EXTERNAL APPOINTMENTS**
Non-Executive Director of SIG Plc, Victrex plc (from February 2018) and the Nuclear Decommissioning Authority.

## Graham Prothero

Non-Executive Director

**BOARD COMMITTEES**
Audit (Chair); Remuneration; Nomination.

**TERM OF OFFICE**
Appointed in May 2017.

**LENGTH OF SERVICE**
8 months

**INDEPENDENT**
Yes

**SKILLS AND EXPERIENCE**
Graham Prothero is a Chartered Accountant and is an Executive Director and Group Chief Financial Officer of Galliford Try plc. He is also on the Board of the Jigsaw Trust, a charitable trust. Prior to joining Galliford Try plc in 2013, he was Group Finance Director at leading property developer Development Securities PLC (now U+I), having previously held senior finance positions at Taylor Woodrow, the FTSE 100 listed housebuilder, and at Blue Circle Industries plc. Graham also spent 7 years as a partner in the Real Estate, Hospitality and Construction Group of Ernst & Young LLP.

**EXTERNAL APPOINTMENTS**
Group Chief Financial Officer of Galliford Try plc.

## Tim Pile

Non-Executive Director

**BOARD COMMITTEES**
Audit; Remuneration; Nomination.

**TERM OF OFFICE**
Appointed in October 2010. Last re-elected in May 2017.

**LENGTH OF SERVICE**
7 years 3 months

**INDEPENDENT**
Yes

**SKILLS AND EXPERIENCE**
Formerly Chairman of Cogent Elliott, the leading independent marketing agency and was Chief Executive Officer of Sainsbury's Bank. Previous Non-Executive Director roles include Cancer Research UK.

**EXTERNAL APPOINTMENTS**
Deputy Chairman of the Royal Orthopaedic Hospital and Immediate Past-President of the Greater Birmingham Chambers of Commerce and Chair of Greater Birmingham and Solihill LEP. He is also a Non-Executive Director of the City of Birmingham Symphony Orchestra.

## Mark Edwards

Non-Executive Director (retired May 2017)

**BOARD COMMITTEES**
Audit (Chair); Remuneration; Nomination (retired May 2017).

**TERM OF OFFICE**
Appointed in October 2010, and retired from the Board and as a Non-Executive Director in May 2017.

**LENGTH OF SERVICE**
7 years

**INDEPENDENT**
Yes

**SKILLS AND EXPERIENCE**
Chartered Accountant with a strong operating background gained in the USA, Europe and Asia. CEO of AIM Altitude, a leading supplier of cabin interiors for Boeing and Airbus aircraft on the world's leading airlines.

Formerly CEO of the Baxi Group and Vice President of the Construction Products Association.

**EXTERNAL APPOINTMENTS**
Chief Executive of AIM Aviation Holdings (which trades as AIM Altitude) and its group of companies, and Chairman of Atlas Fine Wines.

## Cathy Baxandall

Group Company Secretary

**TERM OF OFFICE**
Appointed in July 2008.

**SKILLS AND EXPERIENCE**
In addition to her role as Company Secretary, Cathy is General Counsel to the Marshalls Group and has responsibility for compliance and risk management. She has previous experience as Company Secretary and Group Counsel with Silentnight Group, Thistle Hotels plc and Jacuzzi (UK). Qualified as a solicitor with Clifford Chance before becoming a partner in a national law firm, specialising in banking and corporate law. Graduate of the University of Oxford.

**EXTERNAL APPOINTMENTS**
Charity Trustee and Board member of Ilkley Literature Festival, the Open College of the Arts (part of the University for the Creative Arts); Chair of the Bedales Grants Trust Fund.

# Planning for the future

> "The Board is strongly focused on promoting a positive and dynamic corporate culture for the benefit of all its stakeholders."

**BOARD OBJECTIVES 2017**

- Maintain strategic vision while developing a strong and resilient organisation;
- Focus on succession planning at Board and senior level to ensure the right mix of skills, experience and diversity to support our vision for 2020 and beyond; and
- Develop our corporate culture agenda, improving communication of our shared vision and values supported by action on engagement.

**WHAT WE ACHIEVED**

- Robust capital structure and strong risk management processes have been supported by a detailed internal audit programme throughout the year; notable progress in particular areas such as cyber-risk and security, and the application and testing of our anti-bribery policies and procedures;
- Detailed evaluation of CPM Group acquisition in October 2017, and subsequent integration;
- Further strengthened the Board through the appointment of Graham Prothero to succeed Mark Edwards in accordance with agreed succession plan: currently finalising the appointment of a new Chair to succeed Andrew Allner on his retirement from the Board in 2018;
- Placed culture firmly on the Board and senior management agenda, with a strategy day and the appointment of external consultants to support our communication strategy, and help develop policies that will reinforce and embed recognised good corporate culture;
- New HR system, is expected to facilitate harmonisation of recruitment, training and personal development for our employees across the Group; new all-employee retirement and savings pension plan also launched during 2017; and
- Contributed to BEIS Green Paper consultation on corporate governance designed to improve transparency, accountability and responsible corporate behaviours; appointed Janet Ashdown as Non-Executive Director with primary responsibility for engagement programme with workforce on remuneration matters.

**KEY THEMES FOR 2018**

- Successful recruitment and induction of new Chair while maintaining Board balance;
- Ensure diversity principles are fully incorporated into recruitment process at Board and senior management level; development of recruitment and promotion strategies to support greater diversity (e.g. gender, ethnicity, age), as well as company culture and values;
- Extend 2020 vision, with additional KPIs to measure and monitor progress in key growth areas; also develop effective measurement of progress towards strategic objectives relating to values and culture;
- Review risk appetite and mitigation strategies in relation to significant external risks (e.g. economic downturn, impact of Brexit);
- Consider the Board's responsibilities to all stakeholders: review Board performance and priorities with these in mind. Ensure that the business contribution to wider society is fully understood and communicated; and
- Develop an employee engagement programme (led by Janet Ashdown) that reflects new corporate governance guidance and requirements and supports the Group's culture and values, helping to embed good practice.

▶ **Nomination Committee Report** pages 42 - 43
▶ **Statement of Directors' Responsibilities** pages 44 - 45
▶ **Audit Committee Report** pages 46 - 49
▶ **Remuneration Committee Report** pages 50 - 63

# Dear Shareholder

This Corporate Governance Statement, together with the Reports of the Audit, Nomination and Remuneration Committees on pages 42 to 63, explains how Marshalls' governance framework works and how we apply the principles of business integrity, high ethical values and professionalism in all our activities. As a Board, we recognise that we are accountable to shareholders for good corporate governance, and we seek to promote consistently high standards of governance throughout the Group that are recognised and understood by all.

## Good governance

Good governance depends on good and effective leadership and a healthy corporate culture, supported by robust systems and processes and a good understanding of risk and risk appetite. Your Board has continued throughout the year to engage with shareholders and other stakeholders, to maintain constructive dialogue and challenge and to focus on strategy and value. As a Board, we keep abreast of developments in good governance and practice and participated in the Hampton-Alexander report on gender balance in 2017 as well as providing a detailed submission to the Government's consultation on its Green Paper on Corporate Governance published in November 2016. The outcome of these and other initiatives are expected to lead to greater transparency and responsible corporate behaviour, which we fully support. The Board and the Executive Committee spent time on evaluating Marshalls' culture and values, recognising that a healthy corporate culture will both protect and generate value. The Board has a leading role in fostering and influencing the positive culture and values of the Group by ensuring a consistency of approach and message from the top. The work of our Board Committees, explained in this report, demonstrates our commitment to openness and accountability, acknowledging the value of diversity and good succession planning, how we align reward with our values and strategy and how as an organisation we seek to embed our values across the business, while also recognising that there is further work to do.

## Board evaluation

During 2017, the Board carried out an evaluation of its performance led by the Company Secretary and the Chairman. This concluded that the Board composition continued to be appropriate for the business, with a good balance of skills and experience, ensuring a well balanced and effective Board with a clear and inclusive strategy and a high degree of respect and trust at individual and collective level. The summary of our 2017 objectives, how we performed against them, and the objectives we have set for 2018 following the 2017 evaluation process, appears on the first page of this report. These priorities are closely linked to the strategic objectives of the business.

## Diversity

Marshalls' policy is that no employee or job applicant will be treated less favourably on the grounds of race, colour, nationality, ethnic or national origin, gender (including gender reassignment), pregnancy, marital or civil partner status, sexual orientation, religious belief, age or disability, or on any other grounds which cannot be justified on job-related terms. We do not discriminate on grounds of age, gender or background, and we are committed to equality within our business and in our dealings with other organisations. These policy principles are supported by our Code of Conduct.

The Board is committed to achieving diversity in the widest sense. We ensure that briefs to external recruitment agencies and search consultants are aimed at improving diversity ratios and balance both at Board and senior management level and more widely within the business, while also reflecting the changing strategic needs of the Group. We will continue to support positively opportunities for talented individuals regardless of gender, ethnicity, age or social background.

As a Board, we are fully engaged with the initiatives within the business in this area, although we recognise that there is much work to do to achieve true gender balance and greater diversity. The Remuneration Report contains details of our gender ratios and gender pay gap data (pages 58 and 59), and the Nomination Committee report (pages 42 and 43) explains in more detail how we implement our policy and how we aim to achieve improvements.

## The UK Corporate Governance Code

This Corporate Governance Statement, which is part of the Directors' Report, has been prepared in accordance with the principles of the UK Corporate Governance Code published in April 2016 (the "Code"), but also recognises the recommendations in the FRC's proposed new Corporate Governance Code expected to come into force from January 2019. The Company is supportive of the changes that will result from the application of that new Code. The Board has carried out a review of how the Code principles have been applied, together with the processes and procedures adopted by the Company to support the Code. The Board considers that the Company has complied with the relevant provisions of the Code throughout the year in all material respects. I can also confirm that in the opinion of the Directors these Annual Financial Statements present a fair, balanced and understandable assessment of the Group's position and prospects and provide the information necessary for shareholders to assess the Group's position and performance, business model and strategy. The respective responsibilities of the Directors and the Auditor in connection with the Financial Statements are explained in the Statement of Directors' Responsibilities and the Auditor's Report on pages 44 to 45 and 66 to 71 respectively.

**Andrew Allner**
Chairman

### Case study

## Culture

- Constant theme of stakeholder engagement.
- The Group's culture is underpinned by the core values of leadership, excellence, trust and sustainability and undertaking "responsible business".
- Recent initiatives support the corporate culture:
  - Ethical training
  - Charitable giving
  - Anti-bribery training
  - Employee training and development
  - Apprenticeships
  - Community engagement
  - Fair reward packages
  - Fair Tax Mark

# Corporate Governance Statement *continued*

## Role of the Board

The Board currently comprises an Independent Non-Executive Chairman, 3 Non-Executive Directors and 2 Executive Directors who are equally responsible for the proper stewardship and leadership of the Company. Their biographical details are on pages 34 and 35.

Among the written Schedule of Matters Reserved for the Board, which is reviewed annually, are:

- approving and monitoring progress of strategy, business plans and budgets;
- approving any changes to capital, constitution or corporate structure;
- approving the annual and half-yearly accounts, and the approval and monitoring of the internal financial control system, risk management, health and safety and anti-bribery policies and procedures;
- Board appointments and succession planning, and setting Terms of Reference for Board Committees;
- approving transactions of significant value or major strategic importance; and
- remuneration matters, including major changes to pension schemes, the introduction of share and incentive schemes, and the general framework of remuneration.

The Board has delegated specific responsibilities to the Audit, Remuneration and Nomination Committees. The Audit Committee Report on pages 46 to 49 provides details of how the Board applies the Code in relation to financial reporting, risk management and internal controls. The Nomination Committee Report on pages 42 and 43 reports on the work done, particularly in relation to Board and senior management succession planning, diversity and Board development. The Remuneration Report on pages 50 to 63 gives details of how the Group's Remuneration Policy has been implemented, and of Directors' remuneration for 2017. It also includes details of gender pay and balance. Other Board Committees are established periodically for particular purposes. For example, during the year, Board Committees were established to approve the acquisition of CPM Group Limited as well as the preliminary and half-yearly results.

Day-to-day management and the implementation of strategies agreed by the Board are delegated to the Executive Directors. The Group's reporting structure below Board level is designed so that all decisions are made by the most appropriate people in a timely manner. Management teams report to members of the Executive Committee; this currently consists of 7 senior managers, including the 2 Executive Directors. The Board receives regular updates from the Executive Committee in relation to business issues and developments. These policies and procedures collectively enable the Board to make informed decisions on a range of key issues including strategy and risk management. The charts below show the frequency of how Board meetings, and the Board interacts with the Executive and the business.

## Board meetings and attendance

Key = ● – Present ○ – Absent

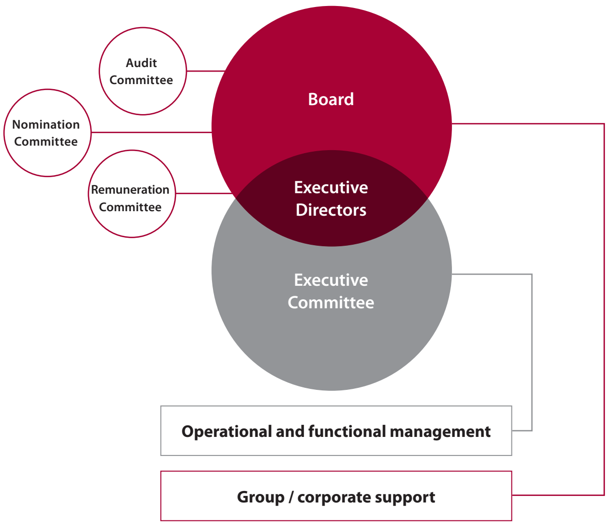
| | Board | Audit Committee | Remuneration Committee | Nomination Committee |
|---|---|---|---|---|
| Andrew Allner (Non-Executive) | ●●●●●●● | – | ●●●●● | ●● |
| Janet Ashdown (Non-Executive) | ●●●●●●● | ●●●● | ●●●●● | ●● |
| Jack Clarke | ●●●●●●● | – | – | – |
| Martyn Coffey | ●●●●●●● | – | – | – |
| Graham Prothero (Non-Executive) | ●●●●○○○ | ●●●○ | ●●●○○ | ○○ |
| Mark Edwards (Non-Executive) | ●●●○○○○ | ●○○○ | ●●○○○ | ●○ |
| Tim Pile (Non-Executive) | ●●●●●●● | ●●●● | ●●●●● | ●● |

The Board met 7 times in full session during 2017. In addition, the Audit Committee met 4 times, the Remuneration Committee met 5 times and the Nomination Committee met twice during the year. There were also Board Committee meetings in connection with the issue of financial results and the acquisition of CPM Group Limited.

The Chief Executive and the Finance Director are usually invited to attend Audit Committee meetings, although the Audit Committee also meets the auditor without any Executive Director being present. The Chief Executive is invited to attend Remuneration Committee meetings where appropriate. The Company Secretary is also Secretary to the Board Committees and attends meetings for this purpose.

Mark Edwards retired from the Board in May 2017 and attended all meetings up to the date of his retirement. Graham Prothero attended all meetings after the date of his appointment. In 2018 there are 7 Board, 4 Audit Committee and 4 Remuneration Committee meetings scheduled, with an additional day set aside for strategy. There are two scheduled Nomination Committee meetings and others will be arranged as necessary in relation to new Board appointments. Outside this formal Board schedule, Board members are expected to participate in site visits, and are invited to other events such as the Group's two-day annual management conference.

### Interaction between Board and management bodies




Chairman and CEO Terms of Reference
www.marshalls.co.uk

Committee Terms of Reference
www.marshalls.co.uk

## Roles of the Chairman, Chief Executive and Non-Executive Directors

There is a clear division of responsibilities between the Chairman and Chief Executive, each of whom has annually reviewed written Terms of Reference. The Chairman leads the Board and sets its agenda, ensuring that adequate time is available for discussion of all agenda items, in particular strategic issues, making sure all Directors, particularly the Non-Executive Directors, are able to contribute, and maintaining a constructive relationship between the Executive and the Non-Executive Directors. The Chief Executive has responsibility for all operational matters which include the implementation of strategy and policies approved by the Board.

The Senior Independent Director, who also has written Terms of Reference, is responsible for providing a sounding board for the Chairman and is an intermediary for other Non-Executive Directors. She is available to shareholders if they have concerns which are not resolved through the normal channels of contact.

The Chairman and the Non-Executive Directors were independent on appointment, and the Board considers each of the Non-Executive Directors to be independent in character and judgement in accordance with the principles of the Code.

At least once a year the Chairman holds a meeting with the Non-Executive Directors without the Executive Directors being present. The Non-Executive Directors also meet annually without the Chairman being present to appraise the Chairman's performance.

Directors are able to ensure that any concerns they raise about the running of the Company or a proposed action are recorded in the Board minutes. If a Non-Executive Director did have any such concerns on resignation the Chairman would invite that Director to provide a written statement for circulation to the Board.

## Conflicts of interest

The Board has adopted procedures for the authorisation of existing situations and for considering (and authorising where appropriate) new situations which may give rise to a conflict of interest. These are recorded in a Conflicts Register, reviewed by the Nomination Committee at least annually. Currently, the only situations authorised are the holding by Directors of directorships or similar offices with companies or organisations not connected with the Company where the Board has not identified any actual conflict of interest. The Board has reviewed the procedures and is satisfied that they are operating effectively.

## Board composition, commitment and election of Directors

The Nomination Committee leads the process for Board appointments and makes recommendations to the Board. We believe our Board is of sufficient size and has an appropriate balance of skills and experience to meet the needs of the business. Individual Director evaluations, succession planning and the work of the Nomination Committee are commented on further in the Nomination Committee Report.

On appointment, Board members, in particular the Chairman and the Non-Executive Directors, disclose their other commitments and agree to allocate sufficient time to the Company to discharge their duties effectively and ensure that these other commitments do not affect their contribution. The current Board commitments of the Chairman and of the remaining members of the Board are shown on pages 34 and 35. Any conflicts of interest are dealt with in accordance with the Board conflicts procedures.

The Company's Articles of Association contain powers of removal, appointment, election and re-election of Directors and provide that at least one-third of the Board must retire at each Annual General Meeting and each Director must retire by rotation every 3 years. In practice, the Company requires all Non-Executive Directors and Executive Directors to stand for re-election at each Annual General Meeting. All Directors except Andrew Allner will stand for re-election or election at the 2018 Annual General Meeting. The terms of appointment of the current Directors and the Directors' biographical details on pages 34 and 35 show their length of service on the Board.

## Board induction, development and support

New Directors receive a full, formal and tailored induction on joining the Board. There is an induction pack for new Directors incorporating the Company's constitutional and governance documents, Group policies and other key information, and training is provided on the use of our active "virtual boardroom" board reporting tools. During 2017, Non-Executive Directors were trained to carry out site safety inspections as part of the Group's health and safety programme. Other tailored training may be arranged to meet individual needs, for example to update knowledge of developments in regulatory compliance. Typically, a new Director will meet the Chairman and other Non-Executive Directors in one-on-one sessions; he or she will have meetings with key management, briefings with external advisers and shareholders, and a programme of site visits will be arranged at which the Director meets site-based staff to gain a full understanding of the business.



### Case study

## Induction of Graham Prothero to the Board

Graham held one-to-one meetings with all Directors and the Company Secretary as part of his recruitment and induction. On appointment he received a detailed information pack containing relevant constitutional documents, key policies and procedures, essential Company facts and a corporate history and contact details.

A comprehensive programme of site visits and meetings with key advisers was arranged for Graham throughout 2017. By December, he had been to a number of key operating sites and had held meetings with auditors, internal auditors and the Company's City advisers.

Commenting on his induction, Graham said: "The process was very thorough and gave me an excellent introduction to the Company. I was impressed by the support given by the executive team and their staff and the warm welcome from my Board colleagues."

**Case study**

## Linking governance and operational strategy: Acquisition of CPM

- The Board commissioned an external review of value-enhancing acquisition targets in 2015, and management followed this up with exploratory discussions designed to nurture good relations with certain prospective target businesses. When management considered the time was right, supported by a strong business case, the proposal to pursue formal discussions with the shareholders of CPM Group Limited was tabled for Board consideration in early 2017.
- Board presentations were reviewed in both June and August 2017, during which the Board challenged and scrutinised the rationale for the proposed acquisition to ensure it was in line with the Group's strategy and would be value enhancing.
- The Board authorised a Board Committee to approve heads of terms and commence detailed due diligence in July 2017 and PwC and Herbert Smith Freehills were commissioned to provide financial and legal advice in connection with the acquisition.
- The Board considered detailed due diligence reports covering all aspects of CPM's business (including financial, legal, property, health and safety, IT, procurement, sales and operations) and held meetings with the project teams. The Board review covered various issues, including funding, risk analysis, expected returns and the post-acquisition integration plan.
- Having concluded its investigation and negotiated the detailed terms of the acquisition, the Board approved management's recommendation to acquire CPM on 18 October 2017, and the acquisition was completed on 19 October 2017.

### Board induction, development and support *continued*

Directors are expected to attend external courses and seminars as appropriate to maintain and develop their Board competencies. Training is also built into the annual Board programme, which is designed to cover a range of topics of particular relevance to the business. During 2017, there were Board briefings relating to health and safety and the Board also received senior management presentations in relation to customer initiatives, developments in HR, manufacturing operations and the Group's marketing strategy. Non-Executive Directors took the opportunity to meet senior managers to discuss areas of particular interest. Training needs are identified through the Board evaluation process and through the individual one-to-one reviews between the Directors and the Chairman.

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

The Board has an approved procedure for all Directors to take independent professional advice at the Company's expense. Board Committees are provided with sufficient resources to undertake their duties, including the option to appoint external advisers when they deem it appropriate.

### Indemnities and insurance

The Company maintains directors' and officers' liability insurance to cover legal proceedings against its Directors and Officers acting in that capacity. The Group has also granted indemnities to its Directors to the extent permitted by law (which are qualifying third party indemnities within the meaning of Section 236 of the Companies Act 2006), and these remained in force during the year in relation to certain losses and liabilities that the Directors may incur to third parties in the course of action as Directors or employees of the Company, any subsidiary or associated company, or as a Director of the pension scheme trustee board. Neither the liability insurance nor the indemnities provide cover in the event of proven fraudulent or dishonest activity.

### Board evaluation

The Company carries out a full evaluation of Board performance and that of its 3 principal Committees annually. The independent assessment provided by Equity Communications in 2016 confirmed that the Board was working very effectively and that the internally-led Board evaluation process in previous years had been successful in improving Board effectiveness. Accordingly, the Board decided to return to an internal process for its 2017 evaluation, led by the Chairman and the Company Secretary. The evaluation was carried out using a questionnaire, followed by one-to-one interviews between each of the Directors and the Company Secretary. The questionnaire was designed to stimulate thought and discussion rather than to deliver scores, and included questions about the effectiveness of Executive and Non-Executive Directors, and the performance of the Chairman. The Senior Independent Director separately reviewed the Chairman's performance with other Non-Executive Directors. The results of the evaluation were then reviewed by the Chairman and the Company Secretary and discussed by the Board. The Board also reviewed progress against the priorities identified for 2017 from the 2016 evaluation process. The outcomes of the evaluation process and the themes that have emerged for focus in 2018 are highlighted on page 36.

### How we assess our performance, prospects and viability

The Group has in place a comprehensive financial review process, including detailed annual budgets, business plans and regular forecasting. There are a range of performance indicators which are tracked by management on a daily, weekly and monthly basis, as appropriate, and addressed through a programme of operational meetings and action plans. All Directors receive regular and timely information to enable them to perform their duties, including information on the Group's operational and financial performance, customer service, health and safety performance and forward trends.

The Board reviews at each regular Board meeting the monthly financial results, taking account of performance indicators and the detailed annual business plan and budget. The Board also considers forward trends and performance against other key indicators, including areas where performance departs from forecasts, and contingency plans. The Board reviews and discusses medium and long-term strategy on a regular basis and meets at least annually with the Executive Committee to review strategy. It also holds separate meetings with individual members of senior management to ensure the Board receives regular updates on current business and strategic issues.

**Case study**

## Investor communications strategy

Marshalls' investor communications strategy combines personal contact with integrated reporting through the IR website, regular presentations and the Annual Report. During 2017, 80 meetings were held with current or prospective shareholders, together with additional analyst meetings, investor roadshows and site visits. Marshalls continues to enhance and align all reporting channels focusing on strategy, key business drivers, risks and the investment case.

- Our main purpose is to articulate a clear corporate strategy in a way that is easy to understand;
- We seek to give a consistent message and style across all the communication channels;
- There is an emphasis on personal contact and individual dialogue – with significant time commitment for shareholder and investor meetings;
- We arrange regular analyst presentations and site visits;
- We have invested in Corporate Reporting in recent years – with particular focus on the Strategic Report and Corporate Governance Reporting;
- There are regular and consistent presentations to facilitate understanding and clarity of message;
- Results Presentation by CEO and CFO is filmed and available on the IR website;
- We have re-designed and upgraded the Investor Relations website; and
- PR consultants (MHP Communications) provide ongoing support for the communications strategy.

In this way, the Board assesses the prospects of the Group using all the information at its disposal, and considering historic performance, forecast performance for the current year, and longer-term forecasts over the 3-year business planning cycle as appropriate. In approving these accounts the Board has considered these matters in detail in order to be able to give the Viability Statement on page 21. The Board has adopted the going concern basis in preparing these Financial Statements and has a reasonable expectation that the Group is able to continue in operation and meet its liabilities as they fall due for at least the next 12 months.

### Risk management and internal control

The Board acknowledges its responsibility for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives, and for the Group's system of internal control. The Board has during 2017 carried out a review of the effectiveness of the Group's risk management and internal controls systems covering all material controls, including financial, operational and compliance controls. The Strategic Report comments in detail (pages 20 to 24) on the nature of the principal risks facing the Group, in particular those that would threaten our business model, future performance, solvency or liquidity and the measures in place to mitigate them. In conducting its review, the Board has included a robust assessment of these risks, particularly operational risks that might affect the assessment of the Group's viability. The Board's risk review also incorporates an element of stress testing, by envisaging scenarios that might arise during the financial year and / or the planning cycle, and considering, with financial impact modelling where appropriate, the likely effect in the business and its prospects. The Audit Committee Report on pages 46 to 49 describes the internal control system and how it is managed and monitored. The Board acknowledges that such systems are designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material mis-statement or loss.

### Relations with shareholders

The Board places great emphasis on good communications with shareholders. The Chief Executive and the Finance Director meet regularly with major shareholders to discuss the Group's performance, strategic issues and shareholder investment objectives, and also periodically arrange site visits for investors. Reports of these meetings and any shareholder communications during the year are provided to the Board. During 2017, 80 such meetings were held, at which 75 per cent of the Group's institutional shareholders were represented. This approach ensures the views of major shareholders are understood by all Directors.

The Board also regularly receives copies of analysts' and brokers' briefings. The Chairman is available to meet major shareholders on request to discuss governance and strategy. The Senior Independent Director is also available to meet shareholders separately if requested. When appropriate, the Non-Executive Directors attend meetings or site visits with major shareholders and would be available to meet major shareholders if a meeting were requested.

There is a regular reporting and announcement schedule to ensure that matters of importance affecting the Group are communicated to investors, and the Annual and Half-yearly Reports, together with the Marshalls website, are substantial means of communication with all shareholders during the year.

### Annual General Meeting

The Notice of Annual General Meeting is dispatched to shareholders, together with explanatory notes or a circular on items of special business, at least 20 working days before the meeting. It is the Company's practice to propose separate resolutions on each substantially separate issue, including a resolution relating to the Report and Accounts, and to put all resolutions to an electronic poll at the Annual General Meeting. All Directors normally attend the meeting, including the Chairs of the Audit, Remuneration and Nomination Committees, who are available to answer questions. The Board welcomes questions from shareholders who have an opportunity to raise issues informally or formally before or at the Annual General Meeting.

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

All valid proxy appointments are properly recorded and counted. Information on the number of shares represented by proxy, the proxy votes for and against each resolution, and the number of shares in respect of which the vote was withheld for each resolution, together with the voting result, are given at the meeting and made available on the Company's website.

**Andrew Allner**
Chairman
14 March 2018

# Nomination Committee Report

> **"Succession plans for the appointment of a new Board Chair in 2018 are well advanced."**

## Role of the Nomination Committee

The Board's Nomination Committee fulfils a vital role in terms of succession planning and Board performance. Its Terms of Reference include:

- Board succession planning, including size, composition and balance of skills and experience, giving due weight to the achievement of diversity in its widest sense;
- recruitment and induction of candidates for appointment to the Board;
- reviewing individual performance evaluation outcomes for Directors standing for election or re-election in advance of the Annual General Meeting; and
- monitoring conflicts, reviewing the Board conflicts policy, maintaining the conflicts register and considering any new notifications.

The performance of the Committee was evaluated as part of the externally led Board evaluation process in 2017, and the Committee Terms of Reference were also reviewed.

During the year the Nomination Committee held two scheduled meetings, and additional meetings and discussions in connection with succession planning and recruitment were held by telephone. Attendance at meetings is shown on page 38.

**NOMINATION COMMITTEE MEMBERS**

- Andrew Allner – Chair
- Janet Ashdown
- Graham Prothero
- Tim Pile

**HIGHLIGHTS OF 2017**

- The Board succession plans were re-tested against the Group's 2020 Strategy objectives.
- Successful recruitment of Graham Prothero to succeed Mark Edwards as Chair of Audit Committee and Non-Executive Director.
- Plans put in place for the recruitment of a new Chair to succeed Andrew Allner, who announced his intention to retire at the 2018 AGM, and the process is well advanced.

**OUR FUTURE TARGETS**

- Recruit and induct new Chair of the Board: maintain board balance while ensuring smooth transition.
- Recruitment and succession planning will be designed to incorporate fully the Group's inclusivity and diversity objectives.
- Recruitment and succession planning will be aligned with a healthy and well understood corporate culture.

## Dear Shareholder

I am pleased to report to shareholders on the main activities of the Committee and how it has performed its duties during 2017, as well as commenting on the Committee's role in the appointment of my successor as Chair of the Board. As current Chair, I also chair Nomination Committee meetings, except where the Committee is dealing with my own re-appointment or replacement as Chair.

### Recruitment and succession planning

The philosophy of the Nomination Committee is that recruitment and succession planning should reflect the changing strategic needs and objectives of the Group, both now and in the future, as well as being an important factor in the development of a strong corporate culture. In this context, we are wholly committed to achieving diversity in its widest sense in the composition of the Board and senior management, and we welcome the increased focus on diversity from shareholders and other commentators. The Group's policies are designed to support positively the widening of opportunity for talented individuals regardless of gender, ethnicity or social background. The Remuneration Report includes details of current gender ratios and some of the measures that have been taken in 2017 and that are planned in future to help achieve our objectives. These are disclosed on pages 58 and 59.

During 2017, the Committee reviewed its written succession plan and individual performance and development at Board level. Having concluded in 2016 that the composition and current Board size were appropriate, and that the range of skills and experience was well balanced, we were pleased to welcome Graham Prothero to the Board and as Audit Chair to succeed Mark Edwards in May 2017. Graham's recruitment was carried out using the services of Lygon, who have no other connection with the Group, following a detailed and objective selection process. Graham is a valuable addition to the Board and the induction and handover process worked well.

During 2017, the Committee also commenced the recruitment process for a new Board Chair. A competitive tender resulted in the appointment of The Inzito Partnership to support the process, who are not otherwise connected with the Group. The brief was clear on the need to take into account our commitments to inclusivity and diversity objectives both at Board and senior management level, as well as keeping a good balance and "fit" with the existing Board. The process has been led by Tim Pile and is well advanced, with a very strong field of candidates. We expect to conclude the selection and make an announcement very shortly. The Committee has also engaged with ongoing initiatives in the business as a whole to improve diversity ratios and gender balance, through meetings and discussions with management, monitoring progress and ensuring that these principles are followed in briefs to external recruitment agencies and search consultants.

Non-Executive Directors, including the Chair, are appointed for specific terms, subject to re-appointment and the Company's Articles of Association and subject to the Companies Act provisions relating to the removal of a Director. The Committee's framework for succession planning is designed to phase future recruitment so that the composition of the Board can be refreshed whilst ensuring continuity.

### Re-appointment of Directors

Each Non-Executive Director was, on joining, provided with a detailed description of his or her role and responsibilities, and received a detailed business induction. All Directors have an annual one-to-one development review meeting with the Chair to appraise performance, set personal objectives and discuss any development and training needs to enable them to continue to add value to the Board, with an assessment of individual and collective performance with contributions from senior management and other business stakeholders.

Before any Director is proposed for re-election, or has their appointment renewed, the Committee considers the outcome of these reviews to ensure that the Director continues to be effective and demonstrates commitment to the role. The Chair provides an explanation to shareholders as to why the Director should be re-elected and confirming that a formal performance evaluation has taken place when the resolution to re-elect is circulated.

It is the Company's policy that Executive Directors can only hold 1 external listed company Non-Executive directorship. Voluntary service on the governing board of a social, trade or charitable organisation is also permitted. Details of the external appointments held by the Executive Directors are included in the biographical notes on pages 34 and 35.

I expect to step down as Chair in May 2018, immediately following the AGM, at which time it is expected that my replacement will take office.

### Governance

The Committee has acted in accordance with the principles of the Code in developing and applying its succession plans and policies. The Committee's effectiveness, including the effective application of those principles, is assessed as part of the annual Board evaluation process. The framework for the refreshment of skills, experience and diversity to support the needs of the business and its stakeholders in the future is transparent and well understood.

**Andrew Allner**
Chair of the Nomination Committee
14 March 2018

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

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

Company law requires the Directors to prepare Group and Parent Company Financial Statements for each financial year. Under that law they are required to prepare the Group Financial Statements in accordance with IFRSs as adopted by the European Union and Article 4 of the IAS Regulation, and have elected to prepare the Parent Company Financial Statements in accordance with UK Accounting Standards, including FRS 101 *"Reduced Disclosure Framework"*.

Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and Parent Company Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting 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.

In preparing the Group Financial Statements, IAS 1 requires that Directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and 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 2006. 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 Strategic Report, 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.

## Responsibility statement of the Directors on the annual financial report

The Directors who held office at the date of approval of this Directors' Report and whose names and functions are listed on pages 34 and 35 confirm that, to the best of each of their knowledge:

- the Financial Statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit of the Company and the undertakings included in the consolidation taken as a whole;
- the Strategic Report contained in this Annual Report includes a fair review of the development and performance of the business and the position of the Company and the Group taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the Annual Report and Financial Statements, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

## Disclosure of information to the auditor

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

## Going concern

The Directors have adopted the going concern basis in preparing these Financial Statements in accordance with the Financial Reporting Council's "Guidance on Risk Management, Internal Control and Related Financial and Business Reporting", issued in September 2014. The Directors considered that it was appropriate to do so, having reviewed any uncertainties that may affect the Company's ability to continue as a going concern for at least the next 12 months from the date these Financial Statements were approved.

## Cautionary statement and Directors' liability

This Annual Report 2017 has been prepared for, and only for, the members of the Company, as a body, and no other persons. Neither the Company nor the Directors accept or assume any liability to any person to whom this Annual Report is shown or into whose hands it may come except to the extent that such liability arises and may not be excluded under English law. Accordingly, any liability to a person who has demonstrated reliance on any untrue or misleading statement or omission shall be determined in accordance with Section 90A of the Financial Services and Markets Act 2000.

This Annual Report contains certain forward-looking statements with respect to the Group's financial condition, results, strategy, plans and objectives. These statements are not forecasts or guarantees of future performance and involve risk and uncertainty because they relate to events and depend upon circumstances that will occur in the future.

There are a number of factors that could cause actual results or developments to differ materially from those expressed, implied or forecast by these forward-looking statements. All forward-looking statements in this Annual Report are based on information known to the Group as at the date of this Annual Report and the Group has no obligation publicly to update or revise any forward-looking statements, whether as a result of new information or future events. Nothing in this Annual Report should be construed as a profit forecast.

## Annual General Meeting

The Notice convening the Annual General Meeting to be held at the Holiday Inn, Clifton Village, Brighouse HD6 4HW at 11.00 am on Wednesday 9 May 2018, together with explanatory notes on the resolutions to be proposed, is contained in a circular to be sent to shareholders with this Annual Report.

By Order of the Board:

**Cathy Baxandall**
Group Company Secretary
14 March 2018

# Audit Committee Report

> The Committee's focus is to ensure the Group has an effective system of risk management and control and for ensuring it continues to meet the necessary standards."

## Role of the Audit Committee

The key responsibilities of the Committee are:

- to keep under review the Group's financial and other systems and controls and financial reporting procedures;
- to agree the plan and scope of the annual audit and half-yearly audit review, receive audit reports and review financial statements, taking account of accounting policies adopted and applicable reporting requirements;
- to review the Annual Report and Financial Statements and advise the Board on whether they give a fair, balanced and understandable explanation of the Company's business and performance over the relevant period;
- to conduct a detailed review of internal controls and the internal audit process and report findings at least twice yearly to the Board;
- to review and update the Company's Risk Register;
- to review external auditor independence and audit and non-audit fees, to review and monitor the appropriateness of the provision of non-audit services by the auditor, and make recommendations regarding audit tender and the appointment and remuneration of the auditor;
- to monitor and review the effectiveness of the internal audit function and the internal audit programme; and
- to review the Anti-Bribery Code and procedures, the Serious Concerns Policy and other policies relevant to financial security, compliance and business ethics.

The Audit Committee is the body appointed by the Board with responsibility for carrying out the functions required by the Listing Rules DTR 7.1.3R. The Committee's Terms of Reference are reviewed annually and approved by the Board.

### AUDIT COMMITTEE MEMBERS

- Graham Prothero – Chair
- Janet Ashdown
- Tim Pile

### HIGHLIGHTS OF 2017

- The Committee reviewed the significant financial judgements made during the year and in the preparation of the 2017 Financial Statements. The significant areas considered by the Committee in 2017 were inventory provisioning, accounting for the acquisition of CPM and the potential for management override of controls.
- The Committee provided assurance to the Board on whether the 2017 Annual Report and Financial Statements, taken as a whole, are fair, balanced and understandable.
- Reviews of cyber security controls and IT security were undertaken by KPMG LLP as part of a wider Cyber Security Review. A number of recommendations have been, or are in the process of being, addressed. The ongoing focus of the Committee is to ensure that IT controls remain appropriate and robust.
- During the year the Committee commissioned KPMG LLP to undertake internal audit reviews in a number of areas. These included reviews in relation to taxation, supply chain controls and process and GDPR readiness. A review of the Group's budget procedures was also undertaken. A number of recommendations have been addressed.
- During the year a high level review of strategic risk was undertaken by the Committee which was subsequently integrated into the overall Risk Register.

### OUR FUTURE TARGETS

- Continue to oversee the significant financial judgements made by management.
- Continue to assess the effectiveness of risk management systems and internal control processes.
- Continue to review the delivery of the external and internal audit and monitor progress.
- Continue to assess and improve cyber security controls and to ensure that IT controls remain appropriate and robust. This will involve further cyber security audits.
- Continue to review the findings from internal audit reviews undertaken by KPMG LLP and monitor the implementation of recommendations made in these reports and the status of progress made against previously agreed actions. There are 8 individual internal audit reviews planned for 2018 and these include:
  - a review of the integration procedures, processes and controls following the acquisition of CPM;
  - ongoing cyclical reviews of key financial processes, including inventory; supplier payments and expenses;
  - update reviews of the Group's General Data Protection Regulation ("GDPR") and anti-bribery controls and procedures; and
- Continue to monitor changes in external regulatory environment and best practice.

## Dear Shareholder

I am pleased to present my first report as Chairman of the Audit Committee. In this report I set out the Audit Committee's objectives and responsibilities and also explain the activities undertaken during 2017 and the priorities for 2018. This report, which is part of the Directors' Report, explains how the Audit Committee has discharged its responsibilities during 2017.

The role of the Audit Committee is to oversee financial reporting and to review the ongoing effectiveness of the Group's internal controls. The Committee provides assurance on the Group's risk management processes and assesses information received from the external and internal audit functions. This report explains the Group's procedures in relation to internal control, risk management and financial reporting.

KPMG LLP, who were appointed as internal auditors in 2015, conducted 8 separate detailed reviews during 2017 and reported to the Committee with recommendations, all of which have been implemented or will be implemented during the coming year. One of our key priorities remains to monitor the risk management and control environment, ensuring that it aligns with best practice and that any improvements are implemented in a timely and efficient way. Cyber security continued to be a key priority and other areas of focus for the Committee are provided in this report.

The Committee has reviewed the Group's Financial Statements contained in this Annual Report and, following its review, is satisfied that the Committee has provided assurance to the Board that they present a fair, balanced and understandable assessment of the Group's position and prospects.

### How the Audit Committee operates

During the year, the Audit Committee held 4 formal meetings and there were also meetings between the Audit Committee Chairman, the Finance Director and the external auditor.

The Committee meets both the external and internal auditor independently of management, giving the opportunity to ensure that it has full visibility of matters that have been the subject of particular discussions. The Committee also reports to the Board in relation to the going concern statement and the viability statement and whether the accounts are fair, balanced and understandable.

### Effectiveness of the Audit Committee

During the year an internal evaluation of the Committee's performance was undertaken as part of the Board evaluation process. The review found the Committee to be effective and well run. No areas of concern were highlighted during this review.

The Chairman of the Committee is a Chartered Accountant and the Board is satisfied he is independent and has recent and relevant financial experience as required by the Code. Other members also have relevant sectoral and financial experience. Their biographical details are on pages 34 and 35, and attendance at meetings is shown on page 38.

### Financial reporting

The Committee has reviewed, with both management and the external auditor, where the more significant judgements have been made and the quality and appropriateness of the Group's accounting policies. The Committee has also reviewed the assumptions and provided assurance to support the long-term viability statement.

### Risk management and internal control

The Board is responsible for reviewing the effectiveness of the system of risk management and control, and for ensuring that it continues to meet the necessary standards. The systems and controls are also subject to a regular rolling programme of review, the results of which are periodically reported to the Board.

The Group's Risk Committee, comprising the Executive Directors and members of senior management with Executive accountability for particular risk areas, meets at least twice yearly to identify, evaluate and consider steps to manage any material risks which might threaten the Group's business objectives.

The Group has an established internal control framework, the key features of which include clearly defined reporting lines and authorisation procedures and a comprehensive budget and monthly reporting system. The internal control framework governs the internal financial reporting process of the business, with checks and balances built into the system that are designed to reduce the likelihood of material error or fraud.

Within the internal control framework, policies and procedures are reviewed on an ongoing basis. During the year, a more formal process has been adopted for the ongoing assessment of operational financial and IT based controls. The overriding objective is to gain assurance that the control framework is complete and that individual controls are operating effectively. A rolling programme of independent internal checking of key controls and reconciliations has been established during the year. This programme includes key controls over access and change permissions on base data and metadata.

## Significant issues related to the Financial Statements

When reviewing the annual and half-yearly results, the Committee exercises its judgement in relation to matters drawn to its attention by the Finance Director from the internal audit function, the Risk Committee and the Group's external auditor. The significant areas considered by the Committee for 2017 were:

- **The risk of management override of controls** – management's assessment of the control framework including authorisation controls and segregation of duties. The Committee considered those areas where management applies judgement in determining the appropriate accounting and discussed this with the external auditor. The external auditor presented its findings with regard to the audit testing of journals to the Committee. This testing included the use of data analytics to profile the entire journal population.
- **Inventory provisioning** – management's assessment of the appropriate level of provisioning against inventory obsolescence. The gross levels of finished goods inventory held and the provisions recorded against obsolescence and in respect of items that might be sold at lower than cost were reviewed by the Committee. The review included meetings with operational management to discuss the inventory provisioning strategy. The external auditor presented its findings with regard to the audit testing over inventory valuation and the Committee concurred with management's assessment of the carrying value of Group inventories.
- **Acquisition accounting in relation to the purchase of CPM** – management's assessment of the appropriate accounting treatment and the exercise of judgement in the identification and valuation of intangible assets within the acquired business. The Committee considered those areas where management applied judgement in delivering the appropriate accounting treatment and discussed this with the external auditor. The external auditor presented its findings with regards to the audit work undertaken to assess this area.

## Fair, balanced and understandable

The Committee has considered whether, in its opinion, the 2017 Annual Report and Financial Statements is, taken as a whole, fair, balanced and understandable, and whether it provides the information necessary for shareholders to assess the Group's position, performance, business model and strategy. In making this assessment, the Committee has advised the Board in relation to the statement required by the UK Corporate Governance Code.

The Committee has concluded that the disclosures, and the process and controls underlying their production, were appropriate to enable it to determine that the 2017 Annual Report and Financial Statements are fair, balanced and understandable.

## Risk management and internal control

The Audit Committee has carried out an assessment of the effectiveness of the Group's risk management and internal control system, covering all material controls including its financial, operational and compliance controls and risk management systems for the year to 31 December 2017.

The Group maintains a written Risk Register that identifies the Group's key risk areas, the probability of these risks occurring and the impact they would have on the Group. Against each risk, the effectiveness of the controls that exist to manage and, where possible, minimise or eliminate those risks are also listed. The Risk Register process identifies areas for action and independent audit assessment in order to test the effectiveness of the Group's risk control systems. Information relating to the management of risks and any changes to the assessment of key risks is regularly reported to the Board, and the Risk Register is updated to reflect changes. To the extent that any failings or weaknesses are identified during the review process, appropriate measures are taken to remedy these. The key risks affecting the Group, how they relate to strategy and how they changed during the year, together with a description of the controls and mitigation associated with such risks, are highlighted in the Strategic Review on pages 20 to 24.

## External audit, auditor independence and objectivity

The Audit Committee has primary responsibility for making a recommendation to the Board on the appointment, re-appointment and removal of the external auditor. It keeps under review the scope and results of the audit, its cost effectiveness and the independence and objectivity of the auditor. The Group's current auditor, Deloitte LLP, has processes in place designed to maintain independence, including regular rotation of the audit partner. Deloitte LLP was appointed in May 2015 as statutory auditor following a tender process, and Christopher Robertson has acted as audit partner since the appointment of Deloitte LLP as auditor in May 2015. The Company has complied with the Competition and Markets Authority's Order for the financial year under review.

The Committee has adopted policies to safeguard the independence of its external auditor. It is the policy of the Company that the external auditor should not provide non-audit services other than those of a "de minimis" value of less than £5,000 in aggregate in any financial year. Any other non-audit services, require the specific approval of the Committee. Where the Committee perceives that the independence of the auditor could be compromised, the work will not be awarded to the external auditor. Details of amounts paid to the external auditor for audit and non-audit services in 2017 are analysed in Note 3 on page 89. Other than the auditor's Half-yearly review of Marshalls plc, no amounts were paid for non-audit work. The aggregate amount paid to other firms of accountants for non-audit services in the same period was £368,000 (2016: £245,000).

## Internal audit

The Committee has responsibility for monitoring the effectiveness of internal controls and reviews these on an ongoing basis. The internal audit process of reviewing and reporting on the internal control system is carried out by KPMG LLP, appointed by the Committee in 2015 to act as internal auditor for the Group. The annual internal audit programme is derived from a risk-based assessment that takes into account the Risk Register and management input. This risk-based assessment is reviewed and approved by the Audit Committee. This process is overseen by the Finance Director. KPMG LLP are independent from the Company's external auditor and have no other connection with the Group.

The Company operates a self-certification internal control process to support the internal audit process throughout the year. The internal audit programme includes both regular audit checks and assignments to look at areas of critical importance. These assignments form part of a much wider programme of independently audited aspects of the Group's operations. Any areas of weakness that are identified through this process prompt a detailed action plan and a follow-up audit check to establish that actions have been completed. Instances of fraud or attempted fraud (if any) and preventative action plans are also reported to the Committee and recorded in a fraud register.

During the year, in addition to the regular internal control process, KPMG LLP conducted specific reviews on cyber security risk and the policies and procedures in operation to manage the supply chain. Other reviews included reviews in relation to taxation, budget procedures and GDPR.

The Committee is pleased to report that, although the wider risk of cyber fraud continues to increase, no significant failings or weaknesses were identified during the year. There were no incidences of fraud that significantly affected the Group's business during 2017. A rolling programme of cyber security awareness training is undertaken and external presentations were made to selected groups of employees by specialists from the Group's banking partners.

## Effectiveness of the external audit

An annual review of external audit effectiveness was undertaken by the Committee in 2017. The conclusion of the review was that the external auditor had conducted a comprehensive, appropriate and effective audit. Communication, at all levels, had been open and constructive and areas where the external auditor could work more effectively, in respect of each phase of the audit, were identified.

## Effectiveness of the internal audit

An annual review of internal audit effectiveness and of the performance of KPMG LLP as independent internal auditor was undertaken by the Committee in 2017.

The conclusion was very positive and was that the current internal audit process continues to be an efficient and effective means of managing the internal audit function. The Committee has considered, with KPMG LLP, how this process can be developed further and further improvements have been reflected in the 2018 plan.

## Whistleblowing and bribery

The Audit Committee monitors any reported incidents under the Serious Concerns Policy (our whistleblowing policy), which is available to all employees. This policy is displayed on operating site noticeboards and on the Company's intranet, and sets out the procedure for employees to raise legitimate concerns about any wrongdoing without fear of criticism, discrimination or reprisal. The Serious Concerns Policy was reviewed during the year and the Committee was satisfied that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.

The Audit Committee also takes responsibility for reviewing the policies and procedures adopted by the Company to prevent bribery. The Company is committed to a zero-tolerance position with regard to bribery, made explicit through its Anti-Bribery Code and supporting guidance for its employees, agents and contractors on hospitality and gifts. The policy and procedures are published on the Company website and displayed on operating site noticeboards. Online training is available to all employees via the Group's internal learning zone to reinforce the Anti-Bribery Code and procedures, and classroom-based training sessions are also held throughout the year. All employees in decision-making roles with potential exposure to bribery risk have completed the training and must self-certify annually that they continue to comply. There is a maintained register of employee interests and a gifts and hospitality record. The internal audit review programme included a review of the adequacy of the Company's procedures in relation to the prevention of bribery, and recommendations from the internal audit process have been implemented.

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

**Graham Prothero**
Chair of the Audit Committee
14 March 2018

# Remuneration Committee Report

> **"Engagement with our employees and other stakeholders on remuneration is an important feature of our commitment to fairness and transparency."**

## Role of the Remuneration Committee

The Committee's responsibilities include:

- setting remuneration policy for Executive Directors;
- determining specific remuneration packages for Executive Directors and for the Chairman;
- operating the Company's employee share incentive arrangements;
- providing guidance on remuneration for senior employees who report to the CEO; and
- considering the broader remuneration policies for Group employees below Board level.

The Board determines the remuneration of the Non-Executive Directors. No Director plays a part in any decision about his / her own remuneration. Janet Ashdown, Tim Pile and Graham Prothero are all Independent Non-Executive Directors within the definition of the Code, and Andrew Allner satisfied the independence condition on his appointment as Non-Executive Chairman in 2010. None of them have any personal financial interest (other than as shareholders) in matters to be decided, nor do they have any conflicts of interest from cross-directorships or any day-to-day involvement in running the business.

### REMUNERATION COMMITTEE MEMBERS

- Janet Ashdown – Chair
- Andrew Allner
- Tim Pile
- Graham Prothero

### HIGHLIGHTS OF 2017

- Remuneration Policy reviewed against best practice and approved by 96 per cent of voting shareholders at 2017 AGM.
- Strong Group performance resulting in achievement of Executive incentive targets that are well-aligned with shareholder and stakeholder objectives, with significant element of variable award in shares or share equivalents.
- Committee has responded to recommendations in the Green Paper and changes proposed by the FRC to the UK Corporate Governance Code; appointment of Janet Ashdown as Non-Executive Director with responsibility for employee engagement on remuneration matters.
- Committee monitoring of the Group's 2017 gender pay gap statistics, as part of commitment to ensuring recruitment and reward structures support diversity objectives.

### DECISIONS MADE DURING THE YEAR

- Review and approval of Remuneration Policy, tabled to 2017 AGM for shareholder approval.
- Approval of Executive incentive awards following 2016 results announcement.
- Setting Executive Director remuneration packages for 2018, having taken into account pay and benefits among the wider workforce and in the comparator group: also noting and monitoring senior management remuneration below Board level.
- Setting incentive scheme targets for 2018 using stretching financial and non-financial measures designed to align with strategic objectives and shareholder interests.
- Appointment of Non-Executive Director with responsibility for employee engagement on remuneration matters (Janet Ashdown).

### OUR FUTURE TARGETS

- Develop action plan for engagement with employees and other stakeholders on remuneration, to be rolled out during 2018.
- Review pay and benefit structures for Executive Directors and senior management against results of gender pay analysis, using new HR systems and associated benchmarking to improve understanding of the underlying factors and develop action plans to address any imbalance.
- Review incentive schemes for Executive Directors and their direct reports to ensure they are aligned with latest best practice. Current management incentive plan ("MIP") expires in 2020, commence design of replacement scheme for approval in 2019.

### APPLICATION OF THE POLICY FOR 2018

- Current MIP scheme is in line with good governance guidance from the Investment Association and other voting institutions. Continue to set stretching and relevant incentive targets that are closely aligned with Group strategy and reward success in a measured and sustainable way through a combination of shorter and longer-term incentives.
- Focus on fairness and transparency: take account of feedback through our planned employee engagement programme and reflect in future pay reviews and benchmarking.
- Ensure the application of remuneration policy and resulting packages support the Group's initiatives on strategy, diversity and the strengthening of values and culture.

# Dear Shareholder

I am writing to you as the Chair of Marshalls' Remuneration Committee and am pleased to set out in this report how the Committee has carried out its objectives and responsibilities during 2017.

This report is divided into two; an introduction and "at a glance" summary of our activities and our Annual Remuneration Report, showing how our Policy was applied during the year and outcomes for our executives.

## Wider workforce considerations

Marshalls is committed to creating an inclusive working environment and to rewarding our employees throughout the organisation in a fair manner. In making decisions on executive pay, the Remuneration Committee considers wider workforce remuneration and conditions. We believe that employees throughout the Company should be able to share in the success of the Company and, in 2015, we introduced a tax advantaged Save-As-You-Earn plan for this purpose. We also believe that employees should have the opportunity to save for their futures and to this end we introduced a new defined contribution scheme during 2017. This provides a much improved pension savings mechanism for all employees. We are proud to be a Living Wage Employer and believe that fair working conditions should extend throughout not just our own organisation but also along our supply chain. Marshalls has worked closely with external organisations to evaluate our business and supply chain against the principles now embodied in the Modern Slavery Act 2015 to eliminate slavery in all its forms.

As part of our commitment to fairness, we have introduced a new section to this report (see pages 58 and 59) which sets out more information on our wider workforce pay conditions, our CEO to employee pay ratio, our gender pay statistics and our diversity initiatives. Whilst we recognise there is much work still to do, we believe that transparency is an important first step towards making improvements in relation to these issues.

## Board changes

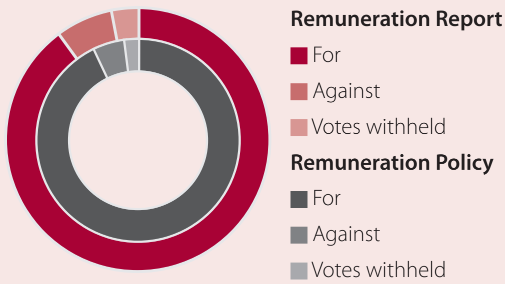
The Committee was delighted to welcome its newest member, Graham Prothero, following the 2017 AGM. Graham brings a wealth of insight from his experience in professional services and, more recently, as Group CFO of Galliford Try plc.

## Shareholders

I would like to thank our shareholders for their continued support during the year. I will be available at the Company's Annual General Meeting on 9 May 2018 to answer any questions in relation to this Remuneration Report.

**Janet Ashdown**
Chair of the Remuneration Committee
14 March 2018

## Voting outcomes 2017




At the 2017 AGM, 96 per cent of shareholders voted in favour of the Remuneration Policy, and 95 per cent of shareholders voted in favour of the Remuneration Report.

## External advisers

The Company has appointed external remuneration advisers, PricewaterhouseCoopers LLP ("PwC"). PwC attends meetings of the Committee by invitation. The Chief Executive attends as appropriate but may not participate in discussions about his own remuneration. The Company Secretary acts as Secretary to the Committee and attends Committee meetings.

PwC's fees are agreed by the Remuneration Committee according to the work performed. The terms of engagement are available on request from the Company Secretary. PwC also provided advice to the Group during the year in relation to the DC pension scheme reforms and the acquisition of CPM Group Limited. The Committee is satisfied that the advice from PwC is independent based on the separation of the team advising the Committee from any other work undertaken by PwC and the fact that PwC is a signatory to the Remuneration Consultants' Group's Code of Conduct. PwC's work relating to Executive remuneration during 2017 included: assistance in the preparation of the Remuneration Committee Report; the triennial review of Remuneration Policy; benchmarking of total remuneration in respect of the Company and its comparator group; and general advice on remuneration trends, regulations and best practice. The amount paid to PwC in respect of remuneration advice received during 2017 was £40,000 (2016: £25,000).

Our Remuneration Report has been prepared in accordance with the Companies Act 2008 and Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. It also meets the requirements of the UK Corporate Governance Code and the UK Listing Authority's Listing Rules and Disclosure and Transparency rules.

# Remuneration Committee Report *continued*

## At a glance

### 2017 remuneration outcomes

The tables below set out how we performed against targets for the Management Incentive Plan ("MIP") in 2017. Pages 61 and 62 set out further information regarding performance measures and targets, which are linked to the key strategic objectives highlighted on pages 18 and 19 of the Strategic Report.

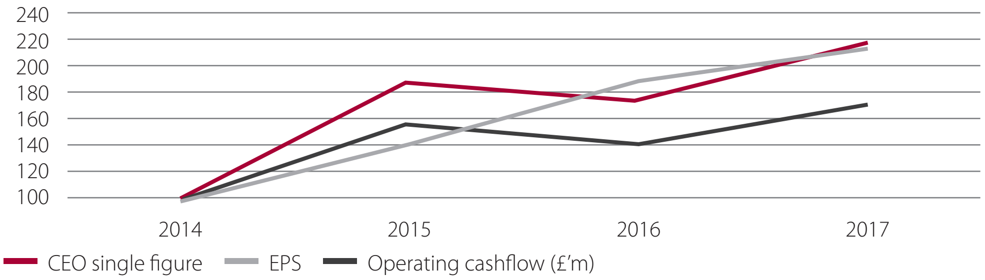
MIP Element A: 100 per cent of maximum (2016: 96.9 per cent of maximum) was awarded to the Chief Executive Officer and Chief Financial Officer.

MIP Element B: 100 per cent of maximum (2016: 96.9 per cent of maximum) was awarded to the Chief Executive Officer and Chief Financial Officer.

| | Minimum (0% payable) | Maximum (100% payable) | Actual (2017) | Percentage of target achieved | Percentage of salary earned (Element A) | Percentage of salary earned (Element B) |
|---|---|---|---|---|---|---|
| EPS | 18.86p | 21.73p | 22.41p | 100% | 112.5% | 75.0% |
| Operating cash flow / EBITDA | £52.2m | £68.4m | £68.7m | 100% | 37.5% | 25.0% |
| Non-financial targets (Customer Service and Health and Safety) | | | | 100% | No deduction | No deduction |

### Long-term performance

The following chart shows the single figure of remuneration for the CEO over the last 3 financial years compared to the Company's EPS and operating cash flow over the same period. The chart demonstrates a strong correlation between Company performance demonstrated by these measures and the remuneration paid to the CEO.




### Link to strategy

The following table sets out the Company's KPIs and how they are reflected in the operation of the MIP:

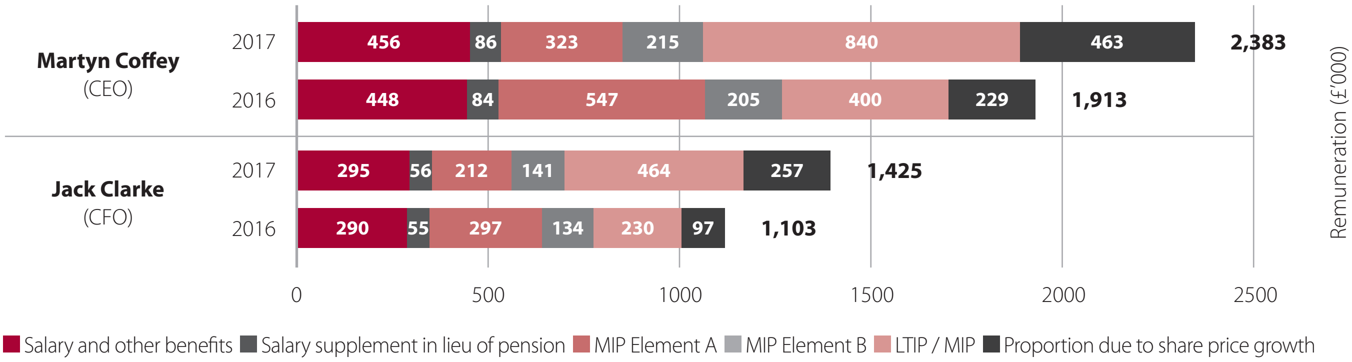
| Strategic KPI | Revenue | Profit | ROCE | Net debt | Customer service | Health and safety |
|---|---|---|---|---|---|---|
| Measure | EPS / OCF | EPS / OCF | EPS / OCF | OCF | Index KPI | Target KPI |
| Remuneration element | MIPA / MIPB | MIPA / MIPB | MIPA / MIPB | MIPA / MIPB | MIPA / MIPB | MIPA / MIPB |

Full details of the Company's strategy are set out in the Strategic Report on pages 2 to 33.

### 2016 / 17 single figure

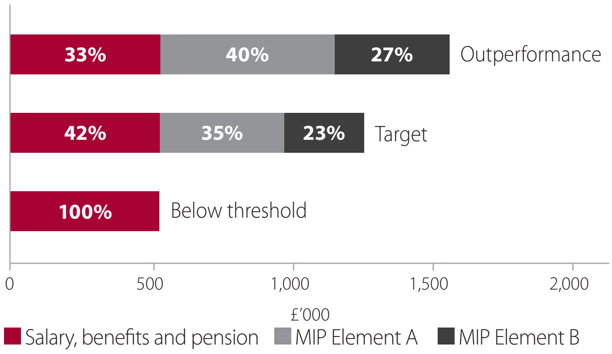
The following charts summarise the single figure of remuneration for 2017 in comparison with 2016 and with the minimum, target and maximum remuneration scenarios from the 2017 Remuneration Policy to show how the actual remuneration compares to the Policy remuneration. For those elements of remuneration provided in shares in 2016 and 2017, we have separated out their original value on grant and the additional value generated due to share price growth over the vesting period. It is the Committee's view that one of the key objectives of equity based remuneration is to align executives' interests and those of shareholders. The increase in value of awards due to share price growth over the vesting periods is another demonstration of this alignment.

Explanatory notes on the single figure can be found in the Annual Report on Remuneration (page 60).

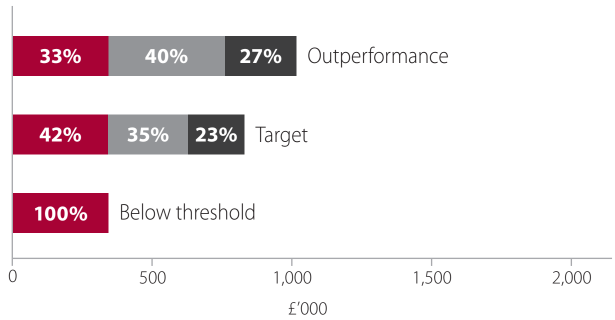


Total remuneration opportunity under the Policy for each of the Executive Directors at 3 different levels of performance is shown below:

**Chief Executive**




**Finance Director**




Notes:

(a) Base salary, benefits and pension information is taken from the single figure remuneration table in the 2016 Annual Remuneration Report. The benefits value reflects a fully expensed company car, medical insurance and any other taxable benefits and pension includes the level of pensions allowance paid instead of contractual employer pension contributions.

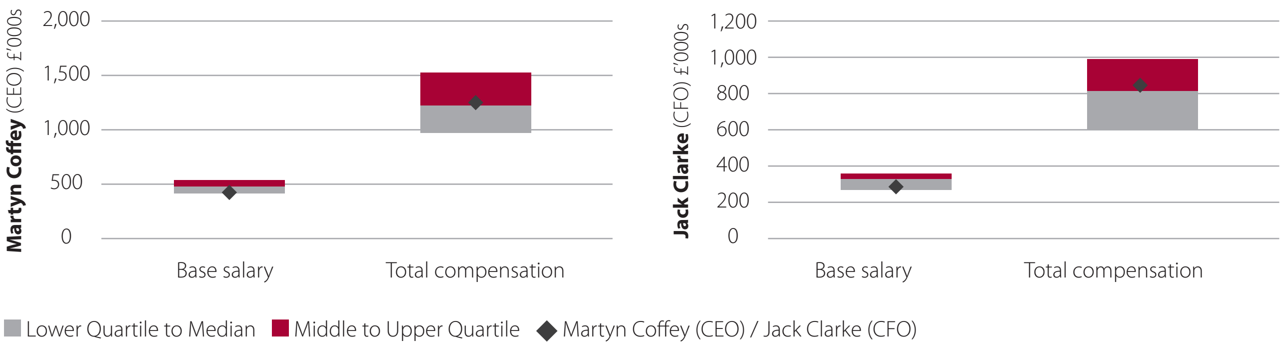
(b) Achievement of performance targets in line with expectations will result in 70 per cent of the annual award under the MIP.

(c) The minimum assumes a performance that fails to meet the threshold for Element A and Element B so is the level below which no variable pay under the MIP is earned.

(d) The maximum represents the full 250 per cent of salary potential under the MIP.

## Comparison to peers

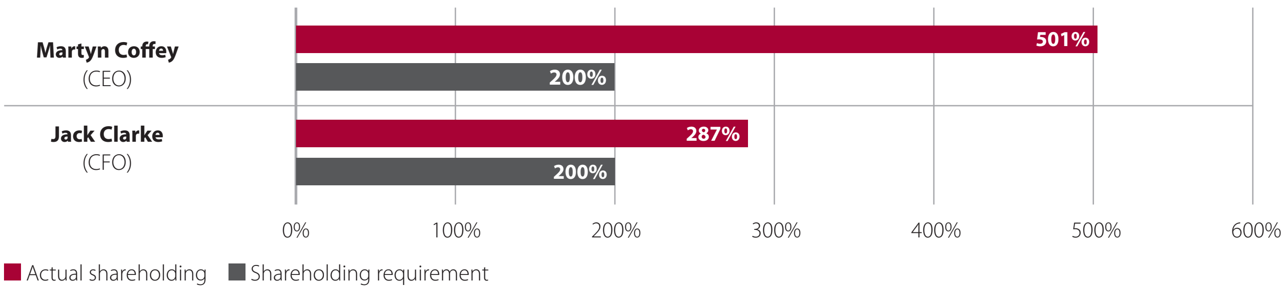
The following chart shows the relative position of base salary and total compensation for our Executive Directors compared to our peers.




The chart demonstrates the Committee's policy that salary and benefits should be set at or below the market level, with variable incentives allowing an overall above-market positioning when the Company has performed well. The variable element assumes an "on-target" performance under relevant incentive schemes.

## Shareholding requirement

The minimum shareholding requirement for Executive Directors is set out below. It must be built up over a 5-year period and then subsequently held at an equivalent of 200 per cent of base salary.



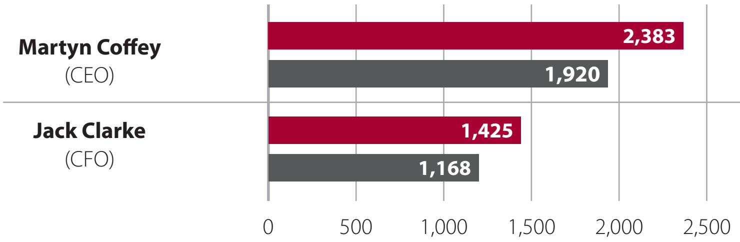

## Remuneration, equity and reward of the Executive Directors

It is the Committee's view that it is important when considering the remuneration paid in the year under the single figure to take a holistic view of the Director's total reward linked to the performance of the Company. In the Committee's opinion, the impact on the total reward of the Director is more important than the single figure in any one year. This approach encourages Directors to take a long-term view of the sustainable performance of the Company, which is critical in a cyclical business. The ability for the Directors to gain and lose, dependent on the share price performance of the Company, at a level which is material to their total remuneration is a key facet of the Company's Remuneration Policy.

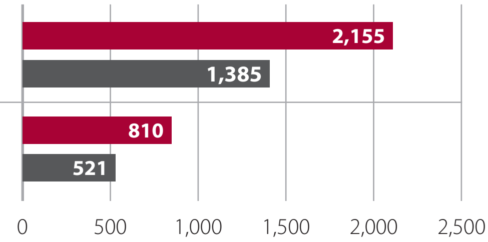
## At a glance *continued*

The following table sets out the single figure for 2017, the number of shares held by the Executive Directors at the beginning and end of the financial year and the impact on the value of these shares taking the opening price and closing price for the year.

**Impact of share price appreciation on single figure remuneration**




**Impact of share price appreciation on value of shares held**




■ Full impact of share price appreciation ■ Assuming no share price appreciation

## Implementation of policy in 2017 and 2018

| Element and link to strategy | Period over which earned 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|---|---|
| **Salary and benefits**<br>Base salary recognises the market value of the Executive's role, skills, responsibilities, performance and experience.<br>Typically, the base salaries of Executive Directors in post at the start of the Policy period and who remain in the same role throughout the Policy period will be increased by a similar percentage to the average annual percentage increase in salaries of all other employees in the Group. Benefits include company car / allowance, private medical cover and health screening. | → | → | | | | | | |
| **Pension**<br>To enable Executive Directors to make appropriate provision for retirement. | → | → | | | | | | |
| **MIP Element A**<br>Enabling the successful implementation of Group strategy through setting relevant annual targets to measure Executive Director performance. Aligns the interests of Executive Directors with shareholders and contributes to the retention of key individuals by ensuring that Executive Directors take part of their annual bonus in shares or share-linked units rather than cash.<br>Upon assessment of performance by the Committee, a contribution will be made by the Company into the participant's plan account and 50 per cent of the cumulative balance will be paid in cash. Any remaining balance will be converted into shares or share-linked units.<br>100 per cent of the balance in the final year of the plan will normally be paid in shares to the participant. During the plan period, 50 per cent of the retained balance is at risk of forfeiture based on a minimum threshold level of performance determined annually by the Committee. | → | → | → | → | → | | | |
| **MIP Element B**<br>To promote long-term shareholding in the Company and strengthen alignment between interests of Executive Directors and those of shareholders.<br>To link variable pay to achievement of annual financial and business objectives.<br>Awards are made annually in shares. Awards normally vest after three years, subject to continued employment.<br>Once vested (net of tax), the shares may not be sold for a further 2 years.<br>There is a minimum threshold which, if not achieved at the end of the 3 year vesting period, results in the forfeiture of up to 50 per cent of unvested awards. | — | — | — | — | → | → | | |

| How we implemented the policy in 2017 | How we will implement the policy in 2018 |
|---|---|
| Executive Director salaries for 2017 were as follows:<br>CEO – £430,000<br>CFO – £282,000<br>Salary increases were 2 per cent in 2017, in line with inflation and increases for UK employees generally. | A salary increase of 3.5 per cent will be applied at the salary review date. From 1 January 2018, Executive Director salaries will be:<br>CEO – £445,000<br>CFO – £292,000<br>The general employee base salary increase was 3.5 per cent from 1 January 2018. |
| The maximum Company contribution or pension allowance is 20 per cent of salary. | No change. |
| Maximum opportunity in 2017 was as follows:<br>CEO – 150 per cent of base salary<br>CFO – 150 per cent of base salary<br>The performance measures were:<br>EPS (75 per cent);<br>operating cash flow (25 per cent); and<br>non-financial targets (which, if not met, result in a 10 per cent deduction for each missed target from amount earned under financial measures).<br><br>The outcome level for 2017 was as follows:<br>CEO – 100 per cent award<br>CFO – 100 per cent award<br>The performance measures are the same for Element A and Element B in 2017. | No change to opportunities under the MIP.<br>Our strategic priorities for 2018 are focused on improving profit margins, growing our business and developing our brand, while also remaining innovative and operating sustainably with the highest standards of health, safety and social responsibility. The Committee believes that EPS and the ratio of OCF to EBITDA remain the most appropriate criteria for measuring achievement of our financial objectives and that a combination of financial and non-financial criteria avoids inadvertently motivating irresponsible behaviour.<br>The weighting for 2018 awards under the MIP will be: EPS: 75 per cent; and OCF to EBITDA: 25 per cent. Targets are set between a minimum (0 per cent) and maximum (100 per cent) range in each case, with on-target (budget) performance expected to deliver 70 per cent of maximum. There will also be non-financial performance conditions, to reflect our focus on brand, customers and employees. Customer service must remain at or above 95 per cent and the rate of lost time due to workplace accidents must not fall below an agreed threshold, benchmarked by reference to the "base" year (2015). If the non-financial criteria are not met, there is a reduction of award value earned by 10 per cent in relation to each of these additional conditions.<br>Element A awards have a forfeiture threshold set annually at the time of the award. If this is breached, 50 per cent of the deferred balance in a participant's Element A MIP account is forfeited. Element B awards also have a long-term financial underpin based on a minimum EPS threshold that must be maintained over the 3 years from the date of grant. If this is breached, 50 per cent of the Element B award is forfeited. Element B awards are granted after the end of the financial period by reference to which they have been earned and the underpin is set at the time of grant. The measurement period under the MIP by reference to which these targets must be met will be the full financial year ending 31 December 2018. It is the view of the Committee that the targets for 2018 MIP awards are commercially sensitive as they are primarily related to budgeted future profit and debt levels in the Company and therefore their disclosure in advance is not in the interests of the Company or shareholders. The Committee will, however, provide full retrospective disclosure to enable shareholders to judge the level of award against the targets set.<br>There are malus and clawback provisions in the MIP rules which apply to both 2017 and 2018 awards. |

## Implementation of policy in 2017 and 2018 *continued*

### Non-Executive Directors

The Board also approved an increase in the fees of 3.5 per cent from 1 January 2018, in line with Executive Directors and UK employees. Non-Executive Directors reclaim business expenses incurred in the performance of their duties retrospectively against duly presented invoices.

| Director | **1 January 2018 £'000** | 1 January 2017 £'000 | Percentage increase |
|---|---|---|---|
| Andrew Allner (Chairman) | **148.3** | 143.3 | 3.5 |
| Janet Ashdown (SID) | **54.5** | 52.7 | 3.5 |
| Graham Prothero | **51.6** | – | 3.5 |
| Tim Pile | **46.3** | 44.7 | 3.5 |

## Fairness, diversity and wider workforce considerations

### Competitive pay and cascade of incentives

The Committee ensures that pay is fair throughout the Company and makes decisions in relation to the structure of executive pay in the context of the cascade of pay structures throughout the business. The Committee's remit includes setting remuneration for Executive Directors and overseeing remuneration levels and structure of rewards for senior management. Targets under the MIP and the Bonus Share Plan ("BSP") scheme use the same measurements. In addition, there are incentive opportunities for employees (other than Executive Directors and senior management) that are job related.

| Level (number) | Participation in Element A of the MIP (percentage range) | Participation in Element B of the MIP (percentage range) | Participation in other bonus or commission plans | Participation in employee share plans (Sharesave / SPP) |
|---|---|---|---|---|
| Executive Directors (2) | 150% of salary | 100% of salary | X | ✓ |
| Executive Committee (5) | 85% to 120% of salary | 55% to 70% of salary | X | ✓ |
| Senior Management (12) | 45% to 55% of salary | 30% to 35% of salary | X | ✓ |
| Employees in BSP (49) | | | 15% to 45% +5% bonus shares | ✓ |
| Employees in other job related bonus or commission schemes (460) | | | Sales bonuses | ✓ |

### Living wage employer

Marshalls is proud to be a "Living Wage Employer", underscoring its commitment to its employees. Marshalls benchmarked its average salaries against other similar companies (as part of the review of job evaluations carried out by external consultants in connection with the HR system implementation) and this showed that its average pay rates for equivalent jobs were generally competitive or at the higher end of the comparable range.

### Saving for the future

In 2017 the Group established a new defined contribution scheme within a Master Trust operated by Aviva, and increased its overall employer pension contribution, benefiting the majority of employees. This will provide an improved pension savings mechanism for employees.

### Bonus Share Plan

The Bonus Share Plan approved in 2015 provides the opportunity for those in the BSP to earn "free" bonus shares of up to 5 per cent of salary, which vest after 3 years subject to continued employment.

### Sharesave Scheme / Share Purchase Plan

The Marshalls 2015 Sharesave Scheme encourages wider ownership of Marshalls plc shares across the entire workforce, which ensures that the employees are able to participate in the Group's success in a way that aligns their interests with those of shareholders. The Share Purchase Plan allows employees to purchase shares on a monthly basis out of gross salary, another way of incentivising investment by employees in the Company's shares.

### Fairness throughout our supply chain

From living wages in the UK to the elimination of child labour in India, we are committed to ensuring that what is good for business is good for society. Our approach to labour rights is driven by the ETI Base Code which we adopted in 2005. To ensure that the Base Code principles are embedded within operations and supply chains, we employ social auditors in India, China and Vietnam, who regularly carry out checks and audits to ensure that the Base Code is being upheld and to report any concerns or violations so that we can take swift action should we need to. Marshalls has also worked closely with external organisations to evaluate our business and supply chain against the principles now embodied in the Modern Slavery Act 2015 to eliminate slavery in all its forms. Our Modern Slavery Statement can be found on the Company's website (www.marshalls.co.uk). Marshalls was the first company in its sector to belong to the ETI and is committed to the ETI Base Code.

### Pay comparisons

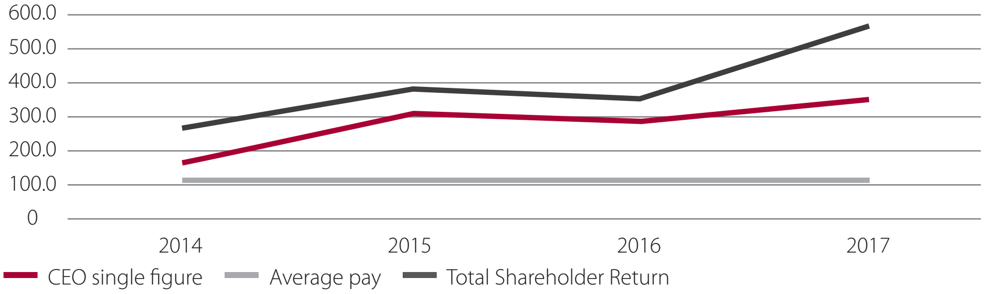
**CEO ratio**

Our CEO to average employee pay ratio for 2017 is 64.1. This is measured as the ratio of CEO single figure pay realised in the year to average (mean) employee pay. To give context to this ratio, we have included a chart tracking CEO pay and average employee pay since Martyn Coffey's appointment alongside Marshalls' TSR performance over the same period. The Remuneration Committee has always been committed to ensure that CEO reward is commensurate with performance. The chart shows a clear alignment between shareholder returns and CEO single figure pay. The CEO single figure for 2013 was affected by the retiring CEO's 2012 and 2013 LTIP awards vesting early on a pro-rata basis owing to his good leaver status.

The factors leading to the increase in the ratio over the last 3 years is the strong performance of the Company reflected in the total shareholder return which has resulted in high levels of vesting of share-based incentives granted to the CEO. The value of these incentives has also materially increased over the performance period due to share price growth, as shown in the charts on pages 53 and 54. Shareholders expect the CEO to have a significant proportion of his pay based on performance and paid in shares. It is this element of his package which provides the volatility in CEO remuneration and the variations in the ratio.

| | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | **2017** |
|---|---|---|---|---|---|---|---|---|
| Ratio of single figure total remuneration to average employee | 21.5x | 23.6x | 30.6x | 98.1x | 32.0x | 60.0x | 51.4x | **64.1x** |

## CEO / average pay against TSR




## CEO pay in the last 8 years

This table shows how pay for the CEO role has changed in the last 8 years:

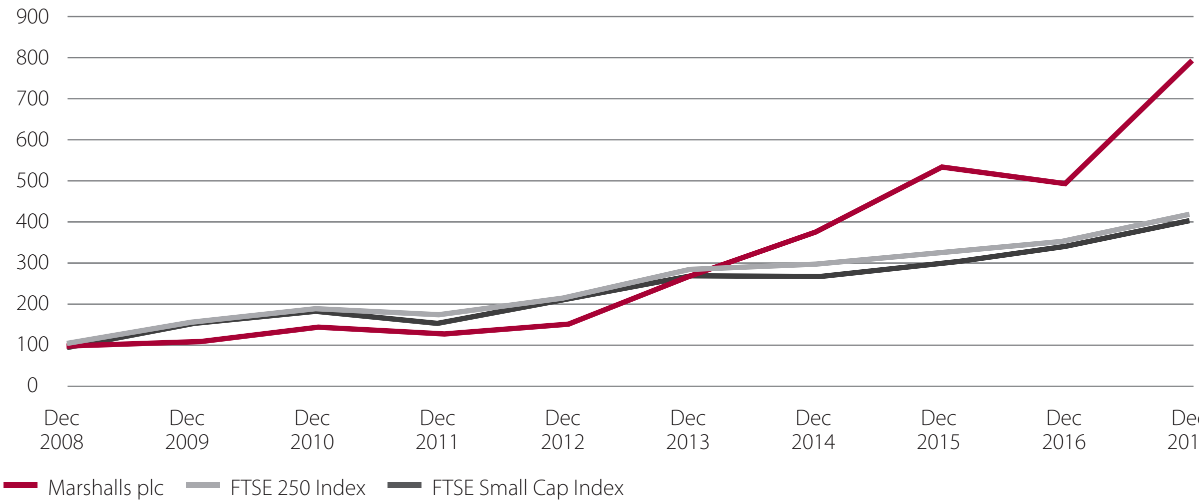
| Year | 2010<br>£'000 | 2011<br>£'000 | 2012<br>£'000 | 2013<br>(Note b)<br>£'000 | 2014<br>£'000 | 2015<br>£'000 | 2016<br>£'000 | **2017<br>£'000** |
|---|---|---|---|---|---|---|---|---|
| Single figure remuneration | 671 | 752 | 938 | 3,143 | 1,101 | 2,064 | 1,913 | **2,383** |
| % of maximum annual bonus earned | 38.6% | 78.1% | 33.0% | 63.6% | 99.3% | 100% | 96.9% | **100%** |
| % of maximum LTIP awards vesting | 0 | 0 | 0 | 63.0% | 0 | 100% | 100% | **100%** |

Notes:

(a) The years up to 2013 show the previous CEO's (Graham Holden's) remuneration.

(b) The 2013 single figure is made up of the previous CEO's base salary and benefits up to 10 October 2013 and Martyn Coffey's proportionate entitlement to salary, benefits and annual bonus for his period of service in 2013. It also includes the various incentive payments that crystallised as a result of Graham Holden being a "good leaver" by reason of retirement in 2013 (see 2013 Remuneration Report for full details).

## Total shareholder return




This chart shows the Group's total shareholder return ("TSR") performance compared to (i) the FTSE Small Cap Index and (ii) the FTSE 250. TSR is defined as share price growth plus reinvested dividends. Marshalls plc was a constituent of the FTSE Small Cap Index for the period from January 2009 to August 2015 and became a constituent of the FTSE 250 in August 2015. This chart shows the value at 31 December 2017 of £100 invested in Marshalls plc on 1 January 2009 compared with the value of £100 invested in (i) the FTSE Small Cap Index and (ii) the FTSE 250. The other plotted points are the intervening financial year ends. Marshalls' TSR performance was 232 per cent better than the overall performance of the FTSE Small Cap Index and 239 per cent better than the FTSE 250 in 2017.

## Fairness, diversity and wider workforce considerations *continued*

### Percentage change in CEO's remuneration

The table below shows how the percentage change in the CEO's salary, benefits and bonus between 2016 and 2017 compares with the percentage change in the average of each of those components of pay for the UK-based employees of the Group as a whole.

| | Salary £'000 | | Percentage change (Note a) | Taxable benefits £'000 | | Percentage change | Bonus (Note b) £'000 | | Percentage change |
|---|---|---|---|---|---|---|---|---|---|
| | **2017** | 2016 | % | **2017** | 2016 | % | **2017** | 2016 | % |
| **CEO pay** | **430** | 422 | 1.9 | **26** | 26 | – | **538** | 752 | (28.5) |
| UK total pay | **81,571** | 78,450 | 4.0 | **2,517** | 2,337 | 7.7 | **3,372** | 4,207 | (19.8) |
| Number of employees | **2,306** | 2,252 | 2.4 | **365** | 361 | 1.1 | **527** | 432 | 22.0 |
| Average per employee | **35.4** | 34.8 | 1.5 | **6.9** | 6.5 | 6.5 | **6.4** | 9.7 | (34.3) |

Notes:

(a) Martyn Coffey's salary was increased on 1 January 2017 by 2 per cent, the same percentage increase as given to the workforce as a whole.

(b) The bonus is the non-deferred amount earned for the relevant year taken from the single figure remuneration table on page 60.

(c) A 2 per cent increase was awarded to the workforce on 1 January 2017. The table above shows, however, that the average salary increase per employee for 2017 was slightly lower. This was due to variations in overtime in the current year and specific variations relating to the impact and timing of leavers and new starters.

(d) The table above shows that the average bonus per employee decreased by 34.3 per cent in 2017 compared with the prior year. This is due to the impact of the participation of senior management (other than Executive Directors) in the 2017 MIP. In 2017, the MIP bonus comprised the first year of cycle 2 of the Scheme, with no elements carried forward from cycle 1 resulting in a fall against the previous year. Amounts carried forward from earlier years for Executive Directors are disclosed in the long-term incentive column of the single figure remuneration table on page 60. In 2016, the final LTIP awards also vested.

### Gender balance and pay

At the end of 2017 our total workforce comprised 2,603 employees with the following gender balance:

| | Male | Female |
|---|---|---|
| Total workforce | 83% | 17% |
| Senior managers | 86% | 14%[1] |
| Directors | 83% | 17% |

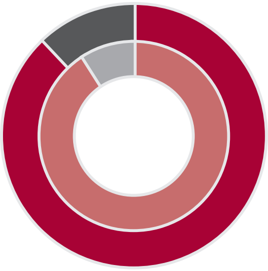
1 Senior managers comprise those in positions of management or control within the business as reflected in job bandings and measured consistently with previous years. The Company has also provided data to the Hampton-Alexander reporting initiative in relation to the gender balance at the levels of Board, Executive and their direct reports. This showed a slightly higher female percentage at Executive Committee level (19.4 per cent) based on the smaller Hampton-Alexander reporting sample.

The UK Government Equalities Office legislation requires employers with more than 250 employees to disclose information on their gender pay gap annually. The first such disclosure is based on amounts paid in the April 2017 payroll. The bonus gap is based on incentives paid in the year to 31 March 2017. The Marshalls Group has two employing companies: Marshalls plc (which has less than 250 employees, mostly at Director/Senior Manager level) and Marshalls Group Limited, which employs all remaining employees. The charts show the consolidated results for Marshalls plc and Marshalls Group Limited, which provides a more accurate overview of pay balance; however, the separate information that is required by the legislation in relation to Marshalls Group Limited is also included below. This information will also be posted on Marshalls' website. CPM Group Limited was acquired in October 2017, and will report separately for 2017 as it remains a separate employer.

Marshalls is committed to equal pay and opportunities for men and women throughout the Group. The gender pay gap analysis is based on a calculation of the average hourly pay and bonus of all our employees, irrespective of what job they do. This shows that as at April 2017 there is a median gender pay gap of 19.3 per cent (consolidated) (20.7 per cent: Marshalls Group Limited), and a mean gender pay gap of 15.7 per cent (consolidated) (17.8 per cent: Marshalls Group Limited). Our recruitment policies, salary and bonus structures are designed to be gender-neutral, and for male and female employees in similar roles, the rates of pay and bonus are the same. However, as the gender split analysis shows, more than 80 per cent of our workforce are male, and there are more males than females in every pay band across the organisation. This is representative of the construction sector generally.

We are evaluating the 2017 results to develop our understanding of the detailed contributory factors. In broad terms, because the construction sector has traditionally attracted more men than women, a majority of our longer-serving employees (for example in middle management or shift leader positions) are male, and most of the senior roles, attracting the highest pay and bonus, are also currently held by men, we believe these are the main reasons for the difference. With the assistance of PwC, we will be analysing the results in detail so that we are able to develop our processes. A breakdown pay gap by quartile is shown opposite:

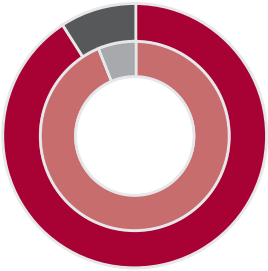
**Quartile A (Highest)**



**Consolidated**
Male 88% Female 12%

**Marshalls Group Limited**
Male 91% Female 9%

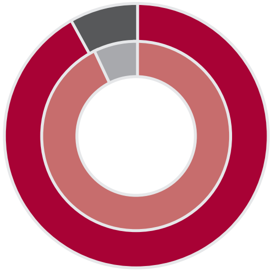
**Quartile B**



**Consolidated**
Male 91% Female 9%

**Marshalls Group Limited**
Male 94% Female 6%

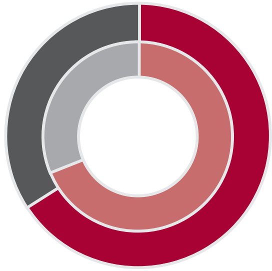
**Quartile C**



**Consolidated**
Male 92% Female 8%

**Marshalls Group Limited**
Male 93% Female 7%

**Quartile D (Lowest)**



**Consolidated**
Male 66% Female 34%

**Marshalls Group Limited**
Male 69% Female 31%

When analysing bonus outcomes, the same factors are relevant. We know our bonus awards are gender-neutral, and across our consolidated workforce more women than men participate in a bonus scheme: however, the predominance of men in senior roles carrying higher base pay means that we are also reporting a gender pay gap in mean and median bonus.

| | Male | Female |
|---|---|---|
| **Percentage receiving bonus** | | |
| Consolidated | 14% | 36% |
| Marshalls Group Limited | 13% | 42% |

| | |
|---|---|
| **Mean bonus gap** | |
| Consolidated | 82.8% |
| Marshalls Group Limited | 74.2% |
| **Median bonus gap** | |
| Consolidated | 78.3% |
| Marshalls Group Limited | 77.8% |

The introduction during 2017 of our new HR system, together with a pay benchmarking exercise across all jobs within the organisation, will, for the first time, allow us to develop consistent control monitoring of recruitment policies and pay. This in turn will lead to better alignment of pay with job grades, which are scored in a gender-neutral way. We are also engaged in initiatives to make our employment opportunities more attractive to female applicants to address gender imbalance, for example in outreach programmes in schools and colleges to support women in engineering, in reviewing and improving flexible working policies for all our workforce and in ensuring that recruitment fosters applications from individuals of diverse backgrounds to improve the gender mix.

## Diversity initiatives

The Group has policies that promote equality and diversity in the workforce as well as prohibiting discrimination in any form. The Group launched a Code of Conduct during 2017, initially focusing on its supply chain, which clearly states its commitment to these principles and requires a similar commitment from its business partners.

Marshalls is supportive of the initiatives reflected in the Hampton-Alexander, Parker, and McGregor-Smith reviews to improve ratios in gender and ethnic diversity at Board and senior management level as well as in the wider workforce. Aligning pay and recruitment policies with these principles forms a key element of our planning for 2018 and beyond.

The Remuneration Committee Chair's engagement programme is expected to include a focus on initiatives to eliminate unconscious bias, if it is found, and to ensure our pay and performance policies are fair and transparent with measures to encourage applications from talented and motivated individuals regardless of gender, ethnicity, degree of physical ability or background. Retention of such people by giving fair consideration to flexible working policies where appropriate, and ensuring incentive schemes are fairly distributed will also be key elements of our diversity strategies. We aim to make progress on these objectives in moving towards the 2020 target of at least 33 per cent of our Board and senior management being female.

We welcome and give full and fair consideration to applications from individuals with recognised disabilities to ensure they have equal opportunity for employment and development in our business. Wherever practicable we offer training and make adjustments to ensure disabled employees are not disadvantaged in the workplace.

More information on our employees, gender diversity and our social and ethical policies can be found on page 33.

## Annual Remuneration Report

This report covers the reporting period from 1 January 2017 to 31 December 2017 and explains how the Remuneration Policy has been implemented. Comparative figures for the 2016 financial year have also been provided.

| | Fixed (£'000) | | | | | | Performance related (£'000) | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | Annual bonus | | | | Long-term incentives | | | |
| | Salary | | Other benefits | | Salary supplement in lieu of pension | | MIP Element A | | MIP Element B | | LTIP / MIP | | Total | |
| | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 |
| Martyn Coffey | **430** | 422 | **26** | 26 | **86** | 84 | **323** | 547 | **215** | 205 | **1,303** | 629 | **2,383** | 1,913 |
| Jack Clarke | **282** | 277 | **13** | 13 | **56** | 55 | **212** | 297 | **141** | 134 | **721** | 327 | **1,425** | 1,103 |
| Total | **712** | 699 | **39** | 39 | **142** | 139 | **535** | 844 | **356** | 339 | **2,024** | 956 | **3,808** | 3,016 |
| | | | Note a | | Note b | | Note c | | | | Notes d and e | | | |

Notes:

(a) Benefits are car / car allowance, fuel / fuel allowance, private medical insurance, life insurance and travel and accommodation expenses.

(b) All Directors received salary supplement allowance in lieu of contributions into the Group's pension scheme throughout the year. No Director had any entitlement under the defined benefit section of the pension scheme and no additional benefit was received as a result of early retirement.

(c) The annual bonus column shows 50 per cent of the total bonus contribution earned under the MIP Element A in respect of 2017 performance, and 50 per cent of the total value of Element B shares awarded which are deferred but are not subject to further performance conditions (other than continued employment). The remaining 50 per cent in respect of 2017 Element A is deferred into shares in the MIP account which are subject to performance and employment-based forfeiture for a further holding period. The remaining 50 per cent of 2017 Element B shares is subject to performance and employment-based forfeiture for a 3-year deferred period. These deferred elements will be disclosed in the long-term incentive column when the conditions are satisfied. The deferred shares in relation to both Element A and Element B may change in value during the holding period depending on the Marshalls' share price.

(d) The long-term incentive column shows the aggregate value of sums released from MIP or LTIP account balances from earlier years that are no longer subject to deferral and forfeiture risk.

(e) For 2017, the LTIP column comprises the aggregate value of sums released from the MIP, at the end of the first cycle, in relation to Element A and Element B. Of these amounts, the Remuneration Committee have determined that MIP Element A will be settled in cash and MIP Element B will be settled in shares. For 2016, the LTIP comprises the 2014 Performance Share Award under the 2005 LTIP that vested and was settled during 2017.

### Setting pay in context

The following graphs illustrate the relationship between total expenditure on remuneration and other disbursements from profit over the past 3 years.

The 4 elements represent the most significant outgoings for the Company during the financial year. In addition to staff pay and shareholder distributions, capital investment and taxation are shown for the following reasons:

- investment – the Company's strategy is to increase capital investment to take advantage of market demand and in order to ensure that the business grows in a sustainable manner with a corresponding long-term benefit for all stakeholders; and
- tax – the Company is a UK taxpayer and feels that it is beneficial to demonstrate to all its stakeholders its total UK tax contribution. The most significant elements of the Company's UK tax contribution are VAT, employer's NI, corporation tax, fuel duty and aggregates levy. As profitability increases, corporation tax will also increase. In 2017 the Group was re-accredited with the Fair Tax Mark.

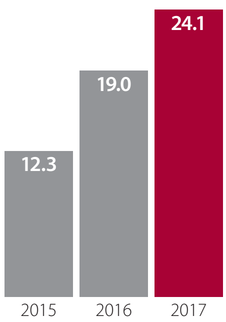
### Relative importance of spend on pay (percentage change)

**Staff pay** (£'m)

+ 2.4%

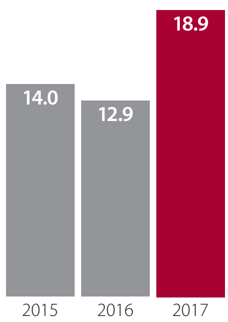

**Distributions to shareholders** (£'m)

+ 26.6%




**Capital investment** (£'m)

+ 46.0%




**Tax** (£'m)

+ 4.7%

## Outcomes of incentive schemes in 2017 (audited)

This section explains how 2017 performance is reflected in rewards earned by the Executive Directors under the Company's incentive schemes.

### MIP

The MIP incorporates:

- Element A, an annual bonus award carrying a maximum of 150 per cent of salary, of which 50 per cent must be deferred into shares or share-linked units; and
- Element B, an award normally in the form of a nil-cost option to acquire shares, carrying a maximum of 100 per cent of salary, conditional on continued employment for 3 years from grant and 50 per cent of which is also subject to a financial condition over the 3-year period. Element B shares must be held for a further 2 years after vesting.

Both awards depend on achievement of the performance conditions set by the Remuneration Committee at the date of award. The table below shows the 2017 performance conditions and the extent to which they have been satisfied.

| Measurement | Percentage of maximum contribution based on measurement | Minimum target | Maximum target | **2017 actual** | Percentage of target achieved | Percentage of salary earned (Element A) | Percentage of salary earned (Element B) |
|---|---|---|---|---|---|---|---|
| EPS | 75% | 18.86p | 21.73p | **22.41p** | 100% | 112.5% | 75.0% |
| Operating cash flow (before restructuring costs) | 25% | £52.2m | £68.4m | **£68.7m** | 100% | 37.5% | 25.0% |
| Non-financial targets | 20% deduction if not met | 95% (customer service) To match or improve on 2015 performance (health and safety) | N/A | **Both achieved** | 100% | No deduction | No deduction |

Performance conditions were set at the beginning of 2017 and the Committee took account of both internal budgets and external factors such as the market consensus of investors for the full year 2017. During the year, cash flow from sales improved significantly and pre-tax profit grew by 13 per cent. This performance meant that the stretching EPS and OCF targets were both met in full, resulting in a combined 100 per cent achievement against target. The share price rose by 56 per cent during the year (31 December 2016: 292.5 pence; 31 December 2017: 454.9 pence), which means the underlying value of share and share-linked awards from previous years also increased.

### EPS

EPS relates to our strategic objective to grow profits. The Group's profit before tax increased by 13 per cent from £46.0 million to £52.1 million. Reported EPS improved by 14 per cent from 18.95 pence in 2016 to 21.52 pence in 2017. EPS and operating cash flow are both measured using International Financial Reporting Standards ("IFRSs") based on the audited results of the Group and subject to the discretion of the Committee with regard to one-off items. For the 2017 remuneration outcomes the Committee applied adjustments for one-off items relating to the acquisition of CPM Group Limited and certain operational restructuring items. These adjustments gave rise to an EPS figure of 22.41 pence for the purpose of remuneration outcomes.

### Operating cash flow

Operating cash flow is relevant for measurement of cash flow and overall sustainability. The Group's operating cash flow to EBITDA ratio for the year ended 31 December 2017 was at the top of the target range set by the Committee at the beginning of the year.

### Additional performance conditions

Our customers are at the heart of our business model, and our measurement of customer service uses factors such as product availability, on-time delivery performance and administrative and delivery accuracy to assess performance. The Group's average customer service performance, assessed monthly, exceeded its minimum target of 95 per cent throughout 2017. The Group also continued its excellent performance against its stated objective of keeping days lost to accidents to a minimum, by reference to the 2015 rate. Days lost to accidents year on year actually reduced by a further 35 per cent. Had either of these targets not been met, the overall level of MIP award would have reduced by 10 per cent; the achievement of these measures means that no reduction factor will apply.

### MIP awards 2017

#### Element A

| Plan accounts | Martyn Coffey | Jack Clarke |
|---|---|---|
| Opening balance (number of shares) (Note a) | 190,344 | 103,238 |
| 2017 contribution (percentage of salary earned) | 150% | 150% |
| Value | £645,492 | £423,428 |
| 2017 element released (Note b) | £(1,183,598) | £(678,622) |
| Closing balance (deferred into shares) | £322,746 | £211,714 |
| Number of shares represented by closing balance (Note c) | 73,341 | 48,110 |

## Annual Remuneration Report *continued*

### MIP awards 2017 *continued*

**Element B**

| | Martyn Coffey | Jack Clarke |
|---|---|---|
| Number of shares awarded | 97,788 | 64,146 |
| Percentage of salary | 100% | 100% |
| Value | £430,328 | £282,285 |
| EPS forfeiture threshold (Note d) | 14.32p | 14.32p |

Notes:

(a) 50 per cent of the earned Element A award is released to the participant as annual bonus; the remaining 50 per cent is deferred into the participant's MIP account and converted into shares. The previously deferred proportion of the 2016 Element A award was converted into shares by reference to the mid-market average value for the 30-day period ending on 31 December 2016. Dividends paid during the year are also added to the carried-forward plan account. The chart above shows the opening balance in shares at the start of the year and the closing balance after release of the 2017 entitlement, calculated by reference to the mid-market average value for the 30-day period ended 31 December 2017 and adding the value of dividends of 12.20 pence per share paid during 2017.

(b) The earned Element A award for 2017 is added to the individual's plan account, and 50 per cent of the resulting balance is released to the participant as an annual bonus; the remaining 50 per cent is deferred into the participant's MIP account and converted into shares. The deferral is repeated in each subsequent year up to the final year. In the final year, subject to any forfeiture provisions, 100 per cent of any balance in the MIP account is released. As 2017 was the final year of the first 4-year cycle, the full balances for years 1-4 plan accounts were released. At the same time, Year 1 awards for performance in 2017 were made.

(c) The carried-forward balance is converted back into shares by reference to the mid-market average value for the 30-day period ended 31 December 2017 (440.06 pence).

(d) If the actual EPS falls below the forfeiture threshold over the 3 years before vesting, 50 per cent of the balance of the award is forfeited. Once Element B shares have vested, they must normally be held for a further 2 years. Element B shares lapse on cessation of employment except in "good leaver" circumstances, in which case they vest on leaving and must normally be held for 2 years from the date of leaving.

(e) As 2017 was the final year of the first 4-year cycle, the full balances for years 1- 4 plan accounts was released. At the same time, year 1 awards for performance in 2017 were made.

### Single total figure of remuneration: Non-Executive Directors (audited)

Non-Executive Directors do not participate in any of the Company's incentive arrangements. Their fees are reviewed periodically and were last reviewed in November 2017. The Chairman's fees are set by the Committee and the CEO; other Non-Executive Directors' fees are set by the Board as a whole. The Non-Executive Directors also received travel and accommodation expenses associated with attendance at Board meetings, and where this is a taxable benefit it is shown below as a grossed-up taxable amount.

| | Board fee £'000 | | Committee fees £'000 | | Expenses £'000 | | Total £'000 | |
|---|---|---|---|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 |
| Andrew Allner<br>Chairman and Chairman of Nomination Committee | **143** | 141 | **–** | – | **2** | 1 | **145** | 142 |
| Janet Ashdown<br>Senior Independent Director, Chairman of Remuneration Committee and member of Audit and Nomination Committees | **45** | 45 | **8** | 4 | **1** | 1 | **54** | 50 |
| Graham Prothero<br>Chairman of Audit Committee and member of Remuneration and Nomination Committees | **29** | – | **4** | – | **1** | – | **34** | – |
| Tim Pile<br>Member of Audit, Remuneration and Nomination Committees | **45** | 44 | **–** | – | **2** | 1 | **47** | 45 |
| Mark Edwards (retired 10 May 2017) | **17** | 45 | **2** | 6 | **–** | 1 | **19** | 52 |
| Alan Coppin (retired 18 May 2016) | **–** | 17 | **–** | 3 | **–** | 1 | **–** | 21 |
| Total | **279** | 292 | **14** | 13 | **6** | 5 | **299** | 310 |

The fees were increased by 3.5 per cent from 1 January 2018 in line with other Group employees. Graham Prothero became Chair of the Audit Committee in May 2017 on the retirement of Mark Edwards.

The Non-Executive Directors reclaim travel and expenses incurred in the performance of their duties.

## Statement of implementation of Remuneration Policy in the following financial year (2018)

See page 55.

## Directors' shareholdings and share interests

The following table sets out, in respect of each of the Directors:

- the number of shares the Director holds unconditionally;
- the number of deferred and conditional shares held under the incentive schemes that will vest following the 2017 results; and
- the number of shares subject to unvested incentive awards.

| | Shareholding requirement | | Beneficially owned | Shares that will vest following 2017 results (Note b) | Deferred shares (Note c) | Deferred and contingent share interests (Note d) | Total interests in shares (including contingent interests) |
|---|---|---|---|---|---|---|---|
| Director | % of salary | Number of shares required (Note a) | Number of shares | Number of shares | Number of shares | Number of shares | Number of shares |
| **Executive** | | | | | | | |
| Martyn Coffey | 200 | 189,198 | 288,202 | 185,427 | 183,531 | 256,872 | 914,032 |
| Jack Clarke | 200 | 124,109 | 71,508 | 106,620 | 115,248 | 163,358 | 456,734 |
| **Non-Executive** | | | | | | | |
| Andrew Allner | – | – | 57,246 | – | – | – | 57,246 |
| Janet Ashdown | – | – | 11,210 | – | – | – | 11,210 |
| Graham Prothero | – | – | – | – | – | – | – |
| Tim Pile | – | – | 44,740 | – | – | – | 44,740 |

Notes:

(a) The closing price on 31 December 2017 of 454.9 pence per share has been used to measure the number of shares required.

(b) This comprises Element B awards granted in March 2015 (based on 2014 performance) that will vest 3 years from grant (i.e March 2018) (before deduction of any tax and NIC). These must be held for a minimum of 2 further years.

(c) This column includes the 50 per cent of share interests awarded in 2015, 2016 and 2017 under Element B of the MIP in the form of nil-cost options or conditional shares that may be exercised after the 3-year vesting period but where vesting is only dependent on continuing employment throughout the 3-year period with no other performance conditions.

(d) This column comprises share interests awarded under the MIP (Element A deferred shares and Element B deferred shares) that remain subject to a financial performance condition as well as to continued employment over the relevant deferral period. 50 per cent of Element A awards and 100 per cent of Element B awards shown in this column may be forfeited if the financial condition is not satisfied.

(e) Share interests under Element A and Element B of the MIP are calculated by reference to the mid-market average value for the 30-day period ended 31 December 2017 (440.06 pence).

(f) The table above includes the interests of "persons closely associated" as defined under the Financial Services and Markets Act (Market Abuse) Regulations 2016.

## Service contracts and policy on termination payments

Each Executive Director has a service contract with the Company which is terminable by the Company on not more than 12 months' notice and by the Director on 6 months' notice. Non-Executive Directors, including the Chairman, are appointed under letters of appointment, usually for a term of 3 years. Either the Company or the Non-Executive Director may terminate the appointment before the end of the current term on 6 months' notice. If the unexpired term is less than 6 months, notice does not need to be served. No compensation is payable if a Non-Executive Director is required to stand down.

All Directors are subject to annual re-election.

Copies of Directors' service contracts and letters of appointment are available for inspection at the Company's registered office on application to the Company Secretary and will also be on display at the Company's AGM.

| Element | Executive Directors | | Non–Executive Directors | | | |
|---|---|---|---|---|---|---|
| Term | Martyn Coffey | Jack Clarke | Andrew Allner | Janet Ashdown | Tim Pile | Graham Prothero |
| Date of contract / appointment | September 2013 | October 2014 | July 2003 (renewed in July 2013 and May 2016) | March 2015 | October 2010 (renewed in July 2013 and May 2016) | May 2017 |
| Notice period in months | | | | | | |
| Company | 12 | 12 | 6 | 6 | 6 | 6 |
| Director | 6 | 6 | 6 | 6 | 6 | 6 |

There were no payments made to past directors and no payments to any directors were made for loss of office during 2017.

**Janet Ashdown**
Chair of the Remuneration Committee
14 March 2018

# Directors' Report – Other Regulatory Information

The information required by the Listing Rules (DTR 4.1.8R) is contained in the Strategic Report and the Directors' Report. Marshalls plc is registered with company number 5100353.

The Directors of the Company are listed on pages 34 and 35.

**Political donations:** The Group made no donations during the year to any political party or political organisation or to any independent election candidate, whether in the European Union or elsewhere (2016: £nil).

**Risk management:** The Group's risk management objectives, its approach to managing risk generally and its use of financial instruments are described in the Strategic Report on pages 20 to 24. Further details of the Group's risk management in relation to financial risks and its use of financial instruments to mitigate such risks are set out in Note 16 on pages 97 to 102.

**Greenhouse gas emissions:** The Group's $CO_2$ (greenhouse gas) emissions in 2017 are disclosed in the Strategic Report on page 32.

**Employees:** The Company's policies in relation to disabled employees and employee involvement and communication are explained in the Strategic Report on page 33.

**Corporate governance:** Details of how the Group complies with the UK Corporate Governance Code are set out on pages 36 to 41.

**Post-balance sheet events of importance since 31 December 2017:** There have been no important events affecting the Group since the end of the financial year.

**Research and development:** Activity and likely future developments for the business are described in the Strategic Report on pages 2 to 33.

## Dividends

The Board is recommending a final dividend of 6.80 pence (2016: 5.80 pence) per share which, together with the interim dividend of 3.40 pence (2016: 2.90 pence) per share, makes a combined dividend of 10.20 pence (2016: 8.70 pence) per share. The Board is also recommending payment of a supplementary dividend of 4.00 pence per share, which is discretionary and non-recurring. Payment of the final dividend and the supplementary dividend, if approved at the Annual General Meeting, will be made on 29 June 2018 to shareholders registered at the close of business on 8 June 2018. The ex-dividend date will be 7 June 2018.

The dividend paid in the year to 31 December 2017 and disclosed in the Consolidated Income Statement is 12.20 pence (2016: 9.65 pence) per share, being the previous year's final dividend of 5.80 pence (2016: 4.75 pence) per share, the interim dividend of 3.40 pence (2016: 2.90 pence) per share in respect of the year ended 31 December 2017 and the prior year supplementary dividend of 3.00 pence per share. The 2016 final and supplementary dividends were paid on 30 June 2017 and the 2017 interim dividend was paid on 6 December 2017.

## Share capital and authority to purchase shares

The Company's share capital at 1 January 2018 was 199,378,755 Ordinary Shares of 25 pence. There has been no change between 31 December 2017 and 14 March 2018. Details of the share capital are set out in Note 20 on page 108.

The Ordinary Shares of the Company carry equal rights to dividends, voting and return of capital on the winding up of the Company, as set out in the Company's Articles of Association. There are no restrictions on the transfer of securities in the Company and there are no restrictions on any voting rights or deadlines, other than those prescribed by law, nor is the Company aware of any arrangement between holders of its shares which may result in restrictions on the transfer of securities or voting rights, nor any arrangement whereby a shareholder has waived or agreed to waive dividends (other than the EBT – see below).

The Marshalls plc Employee Benefit Trust ("EBT") holds shares for the purposes of satisfying future awards that may vest under the Company's share-based incentive schemes. The EBT may purchase shares in the Company from time to time to satisfy awards granted to Directors and Senior Executives subject to the achievement of performance targets under the Company's incentive schemes. At 31 December 2017 the EBT held 1,770,354 Ordinary Shares in the Company (2016: 2,127,022 shares) in respect of future incentive awards under the Company's employee share schemes. Details of outstanding awards are set out in Note 17 on pages 105 and 106. The EBT has waived its right to receive dividends on shares that it holds beneficially in respect of future awards. The Trustee of the EBT exercises any voting rights on such shares in accordance with the Directors' recommendations.

UK-based employees of the Group with more than 6 months' service may participate in the Marshalls plc Share Purchase Plan during any offer period. Employees purchase Ordinary Shares in the Company with their pre-tax salary. The shares are purchased in the market and then held in trust by Yorkshire Building Society. Employees receive dividends on these shares and may give voting instructions to the Trustee.

At the Annual General Meeting in May 2017 shareholders gave authority to the Directors to purchase up to 29,886,875 shares, representing approximately 14.99 per cent of the Company's issued share capital in the Company, in the market during the period expiring at the next Annual General Meeting at a price to be determined within certain limits. No Ordinary Shares in the Company were purchased during the year or between 31 December 2017 and 14 March 2018 under this authority, which will expire at the Annual General Meeting in May 2018. The Directors will seek to renew the authority at that meeting.

## Contracts of significance and related parties

There were no contracts of significance between any member of the Group and (a) any undertaking in which a Director has a material interest, or (b) a controlling shareholder (other than between members of the Group). There have been no related party transactions between any member of the Group and a related party since the publication of the last Annual Report.

There are a number of agreements that take effect, alter or terminate upon a change of control of the Group. None of these are considered to be significant in terms of their likely impact on the business of the Group as a whole.

## Articles of Association

The Company's Articles of Association give powers to the Board to appoint Directors. Newly appointed Directors are required to retire and submit themselves for re-election by shareholders at the first Annual General Meeting following their appointment.

The Board of Directors may exercise all the powers of the Company, subject to the provisions of relevant laws and the Company's Memorandum and Articles of Association. These include specific provisions and restrictions regarding the Company's power to borrow money. Powers relating to the issuing and buying back of shares are included in the Articles of Association and such authorities are renewed by shareholders each year at the Annual General Meeting.

The Articles of Association may be amended by Special Resolution of the shareholders.

**Directors' indemnities** are referenced on page 40 of the Corporate Governance section of the Directors' Report. The Group has not indemnified any Director under the indemnities currently in place.

## Directors' interests

Details of Directors' remuneration, their interests in the share capital of the Company and the share-based payment awards are contained in the Remuneration Committee Report on pages 50 to 63. No change in the interests of the Directors has been notified between 31 December 2017 and the date of this report.

## Listing Rule requirements

The applicable requirements of Listing Rule 9.8.4R in respect of long-term incentive schemes (pages 105 and 106) and contracts of significance (page 64) are included in this Annual Report.

## Substantial shareholdings

The Company has no controlling shareholder. As at 14 March 2018, the Company had been notified, in accordance with DTR Rule 5, of the following disclosable interests of 3 per cent or more in its voting rights:

| | **As at 14 March 2018 %** | As at 31 December 2017 % |
|---|---|---|
| Aberdeen Standard Investments | **10.81** | 10.84 |
| Majedie Asset Management | **8.64** | 8.82 |
| BlackRock | **5.83** | 5.99 |
| JP Morgan Asset Management | **4.69** | 4.08 |
| Montanaro Investment Managers | **4.47** | 4.47 |
| Royal London Asset Management | **4.34** | 4.20 |
| Old Mutual Global Investors | **3.93** | 3.70 |
| RWC Partners | **2.86** | 2.78 |
| M&G Investment Management | **2.82** | 3.06 |

The Directors' Report, comprising the Strategic Report, the Corporate Governance Report and the reports of the Audit, Remuneration and Nomination Committees, has been approved by the Board and signed on its behalf by:

**Cathy Baxandall**
Group Company Secretary
14 March 2018

# Independent Auditor's Report

**to the members of Marshalls plc**

## Opinion

In our opinion:

- the Financial Statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2017 and of the Group's profit for the year then ended;
- the Group Financial Statements have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union;
- the Parent Company Financial Statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 101 *"Reduced Disclosure Framework"*; and
- the Financial Statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group Financial Statements, Article 4 of the IAS Regulation.

We have audited the Financial Statements of Marshalls plc (the "Parent Company'" and its subsidiaries (the "Group") which comprise:

- the Consolidated Income Statement;
- the Consolidated statement of Comprehensive Income;
- the Consolidated and Parent Company balance sheets;
- the Consolidated and Parent Company statements of changes in equity;
- the Consolidated Cash Flow Statement; and
- the related notes 1 to 42.

The financial reporting framework that has been applied in the preparation of the Group Financial Statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the Parent Company Financial Statements is applicable law and United Kingdom Accounting Standards, including FRS 101 *"Reduced Disclosure Framework"* (United Kingdom Generally Accepted Accounting Practice).

## Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the Financial Statements section of our report.

We are independent of the Group and the Parent Company in accordance with the ethical requirements that are relevant to our audit of the Financial Statements in the UK, including the FRC's Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Parent Company.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## Summary of our audit approach

| | |
|---|---|
| **Key audit matters** | The key audit matters that we identified in the current year were:<br>• the carrying value of inventory; and<br>• acquisition accounting, in particular the identification and valuation of intangible assets within the CPM Group Limited acquisition and the determination of other fair value adjustments to the net assets within the acquired business..<br>Within this report, any new key audit matters are identified with ↑ and any key audit matters which are the same as the prior year identified with →. |
| **Materiality** | The materiality that we used for the Group Financial Statements was £2.5 million which was determined on the basis of 5 per cent of profit before tax. |
| **Scoping** | The Group audit team performed the audit of all UK components of the Group which accounted for 95 per cent of Group revenues, 99 per cent of Group net assets and 100 per cent of profit before tax.<br>Marshalls NV, the subsidiary based in Belgium, was audited by Deloitte Antwerp under the supervision of the Group audit team. |
| **Significant changes in our approach** | The Group acquired CPM Group Limited during the year and our audit scope has been extended to include the audit of this company and we have identified an additional significant audit risk for the current year relating to the acquisition accounting for this transaction, in particular the identification and valuation of intangible assets within the acquired business. There have been no other significant changes in our audit approach since the prior year. Taking account of our past experience from our audit work relating to the completeness of customer rebate expense, including the historical accuracy of management estimates of year-end rebate accruals and the relatively factual process of calculating these accruals, we concluded that this area was no longer a key audit matter for our 2017 audit. There have been no other significant changes in our audit approach since the prior year. |

## Conclusions relating to going concern, principal risks and viability statement

### Going concern

We have reviewed the Directors' Statement in Note 1 to the Financial Statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Group's and Company's ability to continue to do so over a period of at least twelve months from the date of approval of the Financial Statements.

We are required to state whether we have anything material to add or draw attention to in relation to that statement required by Listing Rule 9.8.6R(3) and report if the statement is materially inconsistent with our knowledge obtained in the audit.

**We confirm that we have nothing material to report, add or draw attention to in respect of these matters.**

### Principal risks and viability statement

Based solely on reading the Directors' Statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the Directors' assessment of the Group's and the Company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to:

- the disclosures on pages 20 to 24 that describe the principal risks and explain how they are being managed or mitigated;
- the Directors' confirmation on page 21 that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity; or
- the Directors' explanation on page 21 as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We are also required to report whether the Directors' statement relating to the prospects of the Group required by Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.

**We confirm that we have nothing material to report, add or draw attention to in respect of these matters.**



## Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Statements of the current period and include the most significant assessed risks of material mis-statement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the Financial Statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

## Carrying value of inventory ➔

**Key audit matter description**

The Group is primarily involved in the manufacture and sale of landscape and natural stone products, selling to Public Sector, Commercial and Domestic end users. It records inventory at the lower of cost and net realisable value, carrying a large amount of inventories in order to meet customer needs on demand. The Group offers a wide range of non-perishable products that are manufactured and subsequently stored in large quantities at various locations, and therefore carries a high level of inventories at any given point.

A risk exists that the sales prices of inventories, particularly those which are aged or in excess of specific customer requirements, may need to be discounted before they can be sold. The risk of discounting, combined with potential costs to move the inventories to a location where demand exists, may result in the inventories being sold at below cost.

The Directors are responsible for making judgements surrounding:

- the length of time required to sell inventories;
- the level of discounts necessary to sell inventories;
- whether inventories will need to be discounted below their cost price; and
- the appropriateness of standard costs and the level of provisioning applied.

The carrying value of the Group's finished goods inventory is £77.9 million, as disclosed in Note 11, and is noted as an area considered by the Audit Committee in their report on page 48.

# Independent Auditor's Report *continued*

**to the members of Marshalls plc**

## Carrying value of inventory *continued* ➔

| | |
|---|---|
| **How the scope of our audit responded to the key audit matter** | We have:<br>• reviewed business processes surrounding the recording of inventory quantities and management's review of the valuation and provisioning of inventory items;<br>• tested the design, implementation and operating effectiveness of certain key controls relating to purchasing, recording of inventory quantities and inventory provisioning across the Group;<br>• attended inventory counts at key locations to observe the count procedure being undertaken and inspect the condition of inventories;<br>• selected a sample of inventory items and agreed key inputs in the valuation such as materials costs, rebates, shipping costs, the overheads absorbed and expected sales prices to supporting documentation;<br>• tested the calculation of overheads absorption into inventory compared to actual overhead costs incurred; and<br>• used data analytic techniques to compare sales by product line to inventory cost to identify any inventory sold for less than its cost. |
| **Key observations** | The results of our testing were satisfactory. We concur with the basis of valuation of inventory and are satisfied that the level of inventory provisions is appropriate. |

## Acquisition accounting ↑

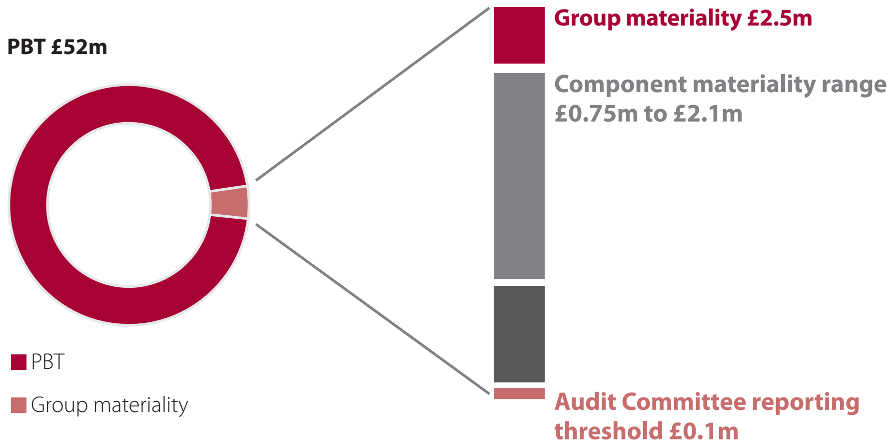
| | |
|---|---|
| **Key audit matter description** | The Group completed the acquisition of the entire share capital of CPM Group Limited during the year. The acquisition is accounted for in accordance with the requirements of IFRS 3 *"Business Combinations"* and this requires judgement to be applied in the process of identification and valuation of intangible assets and the determination of other fair value adjustments to the net assets within the acquired business. This process is inherently complex and a risk exists that intangible assets may be incorrectly identified and valued.<br><br>As described in Note 22 to the Financial Statements, the provisional fair value of the net assets acquired has been estimated at £1.1 million and intangible assets have been identified and valued at £7.2 million. |
| **How the scope of our audit responded to the key audit matter** | We have:<br>• evaluated the design and implementation of key controls relating to management's process for identification and valuation of intangible assets and for determining other fair value adjustments;<br>• reviewed the accounting entries recorded by agreeing to management's acquisition accounting paper and workings and the sale and purchase agreement ("SPA");<br>• agreed cash paid in respect of consideration to bank statements and confirmed the total amount of consideration by reference to the SPA;<br>• reviewed the SPA for any unusual clauses that may have accounting consequences and assessed the completeness of acquisition adjustments;<br>• tested the significant fair value adjustments recorded in respect of the business acquired by reference to supporting third party evidence;<br>• used our valuation specialists to review and challenge the process applied by management for determining the separable intangible assets and to assess the appropriateness of the valuation methodologies adopted and the discount rate applied in the valuation calculations; and<br>• assessed the basis upon which management determine the useful economic life of each intangible asset, considering any contradictory evidence and benchmarking against external evidence. |
| **Key observations** | Based on our procedures we concur that the judgements made by management in identifying and valuing intangible assets within the acquired business, and for determining fair value adjustments, are reasonable. |

## Our application of materiality

We define materiality as the magnitude of mis-statement in the Financial Statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the Financial Statements as a whole as follows:

| | Group Financial Statements | Parent Company Financial Statements |
|---|---|---|
| **Materiality** | £2.5 million (2016: £2.3 million). | £1.0 million (2016: £1.0 million). |
| **Basis for determining materiality** | 5 per cent (2016: 5 per cent) of pre-tax profit. | 0.5 per cent of net assets which is capped at 40 per cent (2016: 40 per cent) of Group materiality. |
| **Rationale for the benchmark applied** | In our professional judgement, profit before tax is a principal benchmark within the Financial Statements that is relevant to users of the Financial Statements. | As a holding company, net assets are considered to be a primary benchmark. |




We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £100,000 (2016: £100,000) for the Group, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the Financial Statements.

CORPORATE GOVERNANCE

# Independent Auditor's Report *continued*

**to the members of Marshalls plc**

## An overview of the scope of our audit

Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls, and assessing the risks of material mis-statement both at the Group and component level. In the current year, the scope of our work has been extended to take into account the acquisition of CPM Group Limited. The Group and Parent Company audits are performed at the Group's head office in Elland, West Yorkshire. All subsidiaries of the Group except Marshalls NV, based in Belgium, and CPM Group Limited, based in Somerset are accounted for and audited in the UK at the Group's head office. The Group audit team performed the audit of all UK components including CPM Group Limited, which accounted for 95 per cent (2016: 96 per cent) of Group revenue, 99 per cent (2016: 98 per cent) of Group net assets and 100 per cent (2016: 98 per cent) of Group profit before tax.

Marshalls NV accounted for the remaining revenue, net assets and profit before tax of the Group and was audited by Deloitte Antwerp under the supervision of the Group audit team to a component materiality of £0.75 million.

The senior statutory auditor has been involved in the planning, risk assessment and reporting procedures for all of the Group's components including the Group's Belgium subsidiary and members of the Group audit team have participated in the detailed group planning and close meetings for the Belgium subsidiary.

## Other information

The Directors are responsible for the other information. The other information comprises the information included in the Annual Report, other than the Financial Statements and our Auditor's Report thereon.

**We have nothing to report in respect of these matters.**

Our opinion on the Financial Statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the Financial Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Financial Statements or our knowledge obtained in the audit or otherwise appears to be materially mis-stated.

If we identify such material inconsistencies or apparent material mis-statements, we are required to determine whether there is a material mis-statement in the Financial Statements or a material mis-statement of the other information. If, based on the work we have performed, we conclude that there is a material mis-statement of this other information, we are required to report that fact.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

**Fair, balanced and understandable** – the statement given by the Directors that they consider the Annual Report and Financial Statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or

**Audit committee reporting** – the section describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee; or

**Directors' statement of compliance with the UK Corporate Governance Code** – the parts of the Directors' Statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the Auditor in accordance with Listing Rule 9.8.10R (2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

## Responsibilities of Directors

As explained more fully in the Directors' Responsibilities Statement, the Directors are responsible for the preparation of the Financial Statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors determine is necessary to enable the preparation of Financial Statements that are free from material mis-statement, whether due to fraud or error.

In preparing the Financial Statements, the Directors are responsible for assessing the Group's and the Parent Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or the Parent Company or to cease operations, or have no realistic alternative but to do so.

## Auditor's responsibilities for the audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the Financial Statements as a whole are free from material mis-statement, whether due to fraud or error, and to issue an Auditor's Report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material mis-statement when it exists. Mis-statements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Financial Statements.

A further description of our responsibilities for the audit of the Financial Statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our Auditor's Report.

## Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. 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.

## Report on other legal and regulatory requirements

**Opinions on other matters prescribed by the Companies Act 2006**

In our opinion the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the Financial Statements are prepared is consistent with the Financial Statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Group and the Parent Company and their environment obtained in the course of the audit, we have not identified any material mis-statements in the Strategic Report or the Directors' Report.

**Matters on which we are required to report by exception**

**Adequacy of explanations received and accounting records**

**We have nothing to report in respect of these matters.**

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the Parent Company Financial Statements are not in agreement with the accounting records and returns.

**Directors' remuneration**

**We have nothing to report in respect of these matters.**

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of Directors' remuneration have not been made or the part of the Directors' Remuneration Report to be audited is not in agreement with the accounting records and returns.

**Other matters**

**Auditor tenure**

Following the recommendation of the Audit Committee, we were appointed by the Board on 20 May 2015 to audit the Financial Statements for the year ending 31 December 2015 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and re-appointments of the firm is 3 years, covering the years ending 31 December 2015 to 31 December 2017.

**Consistency of the Auditor's Report with the additional report to the Audit Committee.**

Our audit opinion is consistent with the additional report to the Audit Committee we are required to provide in accordance with ISAs (UK).

**Christopher Robertson (Senior Statutory Auditor)**
for and on behalf of Deloitte LLP
Statutory Auditor
Manchester, UK
14 March 2018

# Consolidated Income Statement

**for the year ended 31 December 2017**

| | Notes | **2017 £'000** | 2016 £'000 |
|---|---|---|---|
| **Revenue** | 2 | **430,194** | 396,922 |
| Net operating costs | 3 | **(376,755)** | (349,283) |
| **Operating profit** | 2 | **53,439** | 47,639 |
| Financial expenses | 5 | **(1,388)** | (1,594) |
| Financial income | 5 | **–** | 1 |
| **Profit before tax** | 2 | **52,051** | 46,046 |
| Income tax expense | 6 | **(9,925)** | (8,539) |
| **Profit for the financial year** | | **42,126** | 37,507 |
| **Profit for the year** | | | |
| **Attributable to:** | | | |
| **Equity shareholders of the Parent** | | **42,503** | 37,350 |
| **Non-controlling interests** | | **(377)** | 157 |
| | | **42,126** | 37,507 |
| **Earnings per share** | | | |
| Basic | 7 | **21.52p** | 18.95p |
| Diluted | 7 | **21.37p** | 18.61p |
| **Dividend** | | | |
| Pence per share | 8 | **12.20p** | 9.65p |
| Dividends declared | 8 | **24,105** | 19,034 |

All results relate to continuing operations.

# Consolidated Statement of Comprehensive Income

**for the year ended 31 December 2017**

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| **Profit for the financial year** | **42,126** | 37,507 |
| **Other comprehensive income / (expense)** | | |
| *Items that will not be reclassified to the Income Statement:* | | |
| Remeasurements of the net defined benefit liability | **328** | 1,394 |
| Deferred tax arising | **(56)** | (237) |
| **Total items that will not be reclassified to the Income Statement** | **272** | 1,157 |
| *Items that are or may in the future be reclassified to the Income Statement:* | | |
| Effective portion of changes in fair value of cash flow hedges | **146** | 1,123 |
| Fair value of cash flow hedges transferred to the Income Statement | **(385)** | 1,681 |
| Deferred tax arising | **35** | (561) |
| Exchange difference on retranslation of foreign currency net investment | **179** | 2,729 |
| Exchange movements associated with borrowings | **(638)** | (2,641) |
| Foreign currency translation differences – non-controlling interests | **371** | 169 |
| **Total items that are or may be reclassified subsequently to the Income Statement** | **(292)** | 2,500 |
| **Other comprehensive (expense) / income for the year, net of income tax** | **(20)** | 3,657 |
| **Total comprehensive income for the year** | **42,106** | 41,164 |
| **Attributable to:** | | |
| **Equity shareholders of the Parent** | **42,112** | 40,838 |
| **Non-controlling interests** | **(6)** | 326 |
| | **42,106** | 41,164 |

# Consolidated Balance Sheet

**at 31 December 2017**

| | Notes | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Assets** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 9 | **169,093** | 146,995 |
| Intangible assets | 10 | **73,079** | 40,093 |
| Trade and other receivables | 12 | **–** | 208 |
| Employee benefits | 17 | **4,127** | 4,276 |
| Deferred taxation assets | 19 | **2,775** | 1,821 |
| | | **249,074** | 193,393 |
| **Current assets** | | | |
| Inventories | 11 | **77,859** | 68,713 |
| Trade and other receivables | 12 | **68,221** | 49,010 |
| Cash and cash equivalents | 13 | **19,845** | 20,681 |
| Assets classified as held for sale | | **–** | 624 |
| Derivative financial instruments | 16 | **447** | 657 |
| | | **166,372** | 139,685 |
| **Total assets** | | **415,446** | 333,078 |
| **Liabilities** | | | |
| **Current liabilities** | | | |
| Trade and other payables | 14 | **97,552** | 79,646 |
| Corporation tax | | **9,299** | 7,388 |
| Interest-bearing loans and borrowings | 15 | **35** | 34 |
| | | **106,886** | 87,068 |
| **Non-current liabilities** | | | |
| Interest-bearing loans and borrowings | 15 | **44,107** | 15,234 |
| Provisions | 18 | **11,840** | – |
| Deferred taxation liabilities | 19 | **14,986** | 13,655 |
| | | **70,933** | 28,889 |
| **Total liabilities** | | **177,819** | 115,957 |
| **Net assets** | | **237,627** | 217,121 |
| **Equity** | | | |
| **Capital and reserves attributable to equity shareholders of the Parent** | | | |
| Called-up share capital | 20 | **49,845** | 49,845 |
| Share premium account | | **22,695** | 22,695 |
| Own shares | | **(2,359)** | (3,622) |
| Capital redemption reserve | | **75,394** | 75,394 |
| Consolidation reserve | | **(213,067)** | (213,067) |
| Hedging reserve | | **386** | 590 |
| Retained earnings | | **303,274** | 283,821 |
| **Equity attributable to equity shareholders of the Parent** | | **236,168** | 215,656 |
| **Non-controlling interests** | 21 | **1,459** | 1,465 |
| **Total equity** | | **237,627** | 217,121 |

Approved at a Directors' meeting on 14 March 2018.

On behalf of the Board:

**Martyn Coffey**
**Chief Executive**

**Jack Clarke**
**Finance Director**

The Notes on pages 78 to 111 form part of these Consolidated Financial Statements.

# Consolidated Cash Flow Statement

**for the year ended 31 December 2017**

| | Notes | **2017 £'000** | 2016 £'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| **Profit for the financial year** | | **42,126** | 37,507 |
| Income tax expense | 6 | **9,925** | 8,539 |
| **Profit before tax** | | **52,051** | 46,046 |
| Adjustments for: | | | |
| Depreciation | 9 | **13,314** | 12,146 |
| Amortisation | 10 | **1,142** | 1,009 |
| Gain on sale of property, plant and equipment | 3 | **(948)** | (609) |
| Equity settled share-based payments | | **2,382** | 2,884 |
| Financial income and expenses (net) | | **1,388** | 1,593 |
| **Operating cash flow before changes in working capital** | | **69,329** | 63,069 |
| Decrease / (increase) in trade and other receivables | | **5,334** | (4,602) |
| Increase in inventories | | **(4,252)** | (2,419) |
| (Decrease) / increase in trade and other payables | | **(320)** | 1,868 |
| Operational restructuring costs paid | 3 | **(1,217)** | (476) |
| Acquisition costs paid | | **(193)** | – |
| **Cash generated from operations** | | **68,681** | 57,440 |
| Financial expenses paid | | **(911)** | (940) |
| Income tax paid | | **(10,465)** | (7,107) |
| **Net cash flow from operating activities** | | **57,305** | 49,393 |
| **Cash flows from investing activities** | | | |
| Proceeds from sale of property, plant and equipment | | **3,891** | 3,839 |
| Financial income received | | **–** | 1 |
| Acquisition of subsidiary undertaking | 22 | **(41,227)** | – |
| Acquisition of property, plant and equipment | | **(18,895)** | (12,939) |
| Acquisition of intangible assets | | **(1,750)** | (934) |
| **Net cash flow from investing activities** | | **(57,981)** | (10,033) |
| **Cash flows from financing activities** | | | |
| Payments to acquire own shares | | **(1,068)** | (1,175) |
| Net decrease in other debt and finance leases | | **(3,407)** | (40) |
| Increase / (decrease) in borrowings | | **28,226** | (23,791) |
| Equity dividends paid | | **(24,105)** | (19,034) |
| **Net cash flow from financing activities** | | **(354)** | (44,040) |
| **Net decrease in cash and cash equivalents** | | **(1,030)** | (4,680) |
| Cash and cash equivalents at the beginning of the year | | **20,681** | 24,990 |
| Effect of exchange rate fluctuations | | **194** | 371 |
| **Cash and cash equivalents at the end of the year** | | **19,845** | 20,681 |

# Consolidated Statement of Changes in Equity

**for the year ended 31 December 2017**

| | Attributable to equity holders of the Company | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital £'000 | Share premium account £'000 | Own shares £'000 | Capital redemption reserve £'000 | Consolidation reserve £'000 | Hedging reserve £'000 | Retained earnings £'000 | Total £'000 | Non-controlling interests £'000 | Total equity £'000 |
| **Current year** | | | | | | | | | | |
| At 1 January 2017 | **49,845** | **22,695** | **(3,622)** | **75,394** | **(213,067)** | **590** | **283,821** | **215,656** | **1,465** | **217,121** |
| **Total comprehensive income for the year** | | | | | | | | | | |
| Profit for the financial year attributable to equity shareholders of the Parent | – | – | – | – | – | – | **42,503** | **42,503** | **(377)** | **42,126** |
| **Other comprehensive income / (expense)** | | | | | | | | | | |
| Foreign currency translation differences | – | – | – | – | – | – | **(459)** | **(459)** | **371** | **(88)** |
| Effective portion of changes in fair value of cash flow hedges | – | – | – | – | – | **146** | – | **146** | – | **146** |
| Net change in fair value of cash flow hedges transferred to the Income Statement | – | – | – | – | – | **(385)** | – | **(385)** | – | **(385)** |
| Deferred tax arising | – | – | – | – | – | **35** | – | **35** | – | **35** |
| Defined benefit plan actuarial gain | – | – | – | – | – | – | **328** | **328** | – | **328** |
| Deferred tax arising | – | – | – | – | – | – | **(56)** | **(56)** | – | **(56)** |
| **Total other comprehensive income** | – | – | – | – | – | **(204)** | **(187)** | **(391)** | **371** | **(20)** |
| **Total comprehensive income for the year** | – | – | – | – | – | **(204)** | **42,316** | **42,112** | **(6)** | **42,106** |
| **Transactions with owners, recorded directly in equity** | | | | | | | | | | |
| **Contributions by and distributions to owners** | | | | | | | | | | |
| Share-based payments | – | – | – | – | – | – | **2,382** | **2,382** | – | **2,382** |
| Deferred tax on share-based payments | – | – | – | – | – | – | **885** | **885** | – | **885** |
| Corporation tax on share-based payments | – | – | – | – | – | – | **306** | **306** | – | **306** |
| Dividends to equity shareholders | – | – | – | – | – | – | **(24,105)** | **(24,105)** | – | **(24,105)** |
| Purchase of own shares | – | – | **(1,068)** | – | – | – | – | **(1,068)** | – | **(1,068)** |
| Disposal of own shares | – | – | **2,331** | – | – | – | **(2,331)** | – | – | – |
| **Total contributions by and distributions to owners** | – | – | **1,263** | – | – | – | **(22,863)** | **(21,600)** | – | **(21,600)** |
| **Total transactions with owners of the Company** | – | – | **1,263** | – | – | **(204)** | **19,433** | **20,512** | **(6)** | **20,506** |
| **At 31 December 2017** | **49,845** | **22,695** | **(2,359)** | **75,394** | **(213,067)** | **386** | **303,274** | **236,168** | **1,459** | **237,627** |

| | Attributable to equity holders of the Company | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital £'000 | Share premium account £'000 | Own shares £'000 | Capital redemption reserve £'000 | Consolidation reserve £'000 | Hedging reserve £'000 | Retained earnings £'000 | Total £'000 | Non-controlling interests £'000 | Total equity £'000 |
| **Prior year** | | | | | | | | | | |
| At 1 January 2016 | 49,845 | 22,695 | (5,529) | 75,394 | (213,067) | (1,653) | 263,894 | 191,579 | 1,139 | 192,718 |
| **Total comprehensive income for the year** | | | | | | | | | | |
| Profit for the financial year attributable to equity shareholders of the Parent | – | – | – | – | – | – | 37,350 | 37,350 | 157 | 37,507 |
| **Other comprehensive income / (expense)** | | | | | | | | | | |
| Foreign currency translation differences | – | – | – | – | – | – | 88 | 88 | 169 | 257 |
| Effective portion of changes in fair value of cash flow hedges | – | – | – | – | – | 1,123 | – | 1,123 | – | 1,123 |
| Net change in fair value of cash flow hedges transferred to the Income Statement | – | – | – | – | – | 1,681 | – | 1,681 | – | 1,681 |
| Deferred tax arising | – | – | – | – | – | (561) | – | (561) | – | (561) |
| Defined benefit plan actuarial gain | – | – | – | – | – | – | 1,394 | 1,394 | – | 1,394 |
| Deferred tax arising | – | – | – | – | – | – | (237) | (237) | – | (237) |
| **Total other comprehensive income** | – | – | – | – | – | 2,243 | 1,245 | 3,488 | 169 | 3,657 |
| **Total comprehensive income for the year** | – | – | – | – | – | 2,243 | 38,595 | 40,838 | 326 | 41,164 |
| **Transactions with owners, recorded directly in equity** | | | | | | | | | | |
| **Contributions by and distributions to owners** | | | | | | | | | | |
| Share-based payments | – | – | – | – | – | – | 2,884 | 2,884 | – | 2,884 |
| Deferred tax on share-based payments | – | – | – | – | – | – | 122 | 122 | – | 122 |
| Corporation tax on share-based payments | – | – | – | – | – | – | 442 | 442 | – | 442 |
| Dividends to equity shareholders | – | – | – | – | – | – | (19,034) | (19,034) | – | (19,034) |
| Purchase of own shares | – | – | (1,175) | – | – | – | – | (1,175) | – | (1,175) |
| Disposal of own shares | – | – | 3,082 | – | – | – | (3,082) | – | – | – |
| **Total contributions by and distributions to owners** | – | – | 1,907 | – | – | – | (18,668) | (16,761) | – | (16,761) |
| **Total transactions with owners of the Company** | – | – | 1,907 | – | – | 2,243 | 19,927 | 24,077 | 326 | 24,403 |
| **At 31 December 2016** | 49,845 | 22,695 | (3,622) | 75,394 | (213,067) | 590 | 283,821 | 215,656 | 1,465 | 217,121 |

# Notes to the Consolidated Financial Statements

## 1 Accounting policies

### Significant accounting policies

Marshalls plc (the "Company") is a Public Company limited by shares, incorporated in the United Kingdom under the Companies Act and is registered in England and Wales. The Consolidated Financial Statements of the Company for the year ended 31 December 2017 comprise the Company and its subsidiaries (together referred to as the "Group").

The Consolidated Financial Statements were authorised for issue by the Directors on 14 March 2018.

The Company's registered address is Landscape House, Premier Way, Lowfields Business Park, Elland, HX5 9HT.

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

The Consolidated Financial Statements have been prepared in accordance with IFRSs as adopted for use in the EU and therefore the Group Financial Statements comply with Article 4 of the EU IAS Regulations. The Group has applied all accounting standards and interpretations issued by the IASB and International Financial Reporting Committee relevant to its operations and which are effective in respect of these Financial Statements.

### Amendments to IFRSs that are mandatorily effective for the current year

In the current year, the Group has applied a number of amendments to IFRSs issued by the International Accounting Standards Board ("IASB") that are mandatorily effective for an accounting period that begins on or after 1 January 2017. Their adoption has not had any material impact on the disclosures or on the amounts reported in these Financial Statements.

| | |
|---|---|
| Amendments to IAS 7 – *"Disclosure Initiative."* | The Group has adopted the amendments to IAS 7 for the first time in the current year. The amendments require an entity to provide disclosures that enable users of Financial Statements to evaluate changes in liabilities arising from financing activities, including both cash and non-cash changes. The Group's liabilities arising from financing activities consist of borrowings (Note 15) and certain derivatives (Note 16). A reconciliation between the opening and closing balances of these items is provided in Note 16. Consistent with the transition provisions of the amendments, the Group has not disclosed comparative information for the prior year. Apart from the additional disclosure in Note 24, the application of these amendments has had no impact on the Group's Consolidated Financial Statements. |
| Amendments to IAS 12 *"Recognition of Deferred Tax Assets for Unrealised Losses."* | The Group has adopted the amendments to IAS 12 for the first time in the current year. The amendments clarify how an entity should evaluate whether there will be sufficient future taxable profits against which it can utilise a deductible temporary difference. The application of these amendments has had no impact on the Group's Consolidated Financial Statements as the Group already assesses the sufficiency of future taxable profits in a way that is consistent with these amendments. |
| *"Annual Improvements to IFRSs 2014-2016 Cycle."* | The Group has adopted the amendments to IFRS 12 included in the "Annual Improvements to IFRSs 2014-2016 Cycle" for the first time in the current year. The other amendments included in this package are not yet mandatorily effective and they have not been early adopted by the Group. IFRS 12 states that an entity need not provide summarised financial information for interests in subsidiaries, associates or joint ventures that are classified (or included in a disposal group that is classified) as held for sale. The amendments clarify that this is the only concession from the disclosure requirements of IFRS 12 for such interests. |

### New and revised IFRSs in issue but not yet effective

At the date of authorisation of these Financial Statements, the Group has not applied the following new or revised IFRSs that have been issued but are not yet effective and, in some cases, have not yet been adopted by the EU:

| | |
|---|---|
| IFRS 9 | *"Financial Instruments";* |
| IFRS 15 | *"Revenue from Contracts with Customers (and the related Clarifications)";* |
| IFRS 16 | *"Leases";* |
| IFRS 17 | *"Insurance Contracts";* |
| IFRS 2 (amendments) | *"Classification and Measurement of Share-based Payment Transactions";* |
| IFRS 4 (amendments) | *"Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts";* |
| IAS 40 (amendments) | *"Transfers of Investment Property";* |
| IFRS 10 and IAS 28 (amendments) | *"Sale or Contribution of Assets between an Investor and its Associate or Joint Venture";* |
| Annual Improvements to IFRSs 2014-2016 Cycle | Amendments to IFRS 1 *"First-time Adoption of International Financial Reporting Standards and IFRS 28 Investments in Associates and Joint Ventures";* |
| Annual Improvements to IFRSs 2015-2017 Cycle | Amendments to IFRS 3 *"Business Combinations, IFRS 11 Joint arrangements, IAS 12 Income tax and IAS 23 borrowing costs";* |
| IFRIC 22 | *"Foreign Currency Transactions and Advanced Consideration"; and* |
| IFRIC 23 | *"Uncertainty over Income Tax Treatments".* |

## 1 Accounting policies *continued*

### Significant accounting policies *continued*

### New and revised IFRSs in issue but not yet effective *continued*

The Directors do not expect that the adoption of the Standards listed above will have a material impact on the Financial Statements of the Group in future periods, except as noted below:

#### IFRS 15 "Revenue from Contracts with Customers"

IFRS 15, *"Revenue from Contracts with Customers"* supersedes IAS 18, *"Revenue"*, and establishes a principles-based approach to revenue recognition and measurement based on the concept of recognising revenue when performance obligations are satisfied. An assessment of the impact of IFRS 15 has been completed and revenue recognition under IFRS 15 is expected to be consistent with the current practice for the Group's revenue.

#### IFRS 16 "Leases"

IFRS 16, which has not yet been endorsed by the EU, introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. IFRS 16 will supersede the current lease guidance including IAS 17 *"Leases"* and the related interpretations when it becomes effective for accounting periods beginning on or after 1 January 2019. The Group currently expects to adopt IFRS 16 for the year ending 31 December 2019. No decision has been made about whether to use any of the transitional options in IFRS 16.

IFRS 16 distinguishes leases and service contracts on the basis of whether an identified asset is controlled by a customer. Distinctions of operating leases (off balance sheet) and finance leases (on balance sheet) are removed for lessee accounting, and are replaced by a model where a right-of-use asset and a corresponding liability have to be recognised for all leases by lessees (i.e. all on balance sheet) except for short-term leases and leases of low value assets. In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease. Furthermore, extensive disclosures are required by IFRS 16.

The right-of-use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the lease payments that are not paid at that date. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, amongst others. Furthermore, the classification of cash flows will also be affected because operating lease payments under IAS 17 are presented as operating cash flows; whereas under the IFRS 16 model, the lease payments will be split into a principal and an interest portion which will be presented as financing and operating cash flows respectively.

The Group has established a working group to assess the impact of the new standard. Work performed includes assessing the accounting impacts of the change, the process of collecting the required data from across the business and the necessary changes to systems and processes. From work performed to date, it is expected implementation of the new standard will have a significant impact on the consolidated results of the Group. On adoption, lease agreements will give rise to both a right of use asset and a lease liability for future lease payables. Depreciation of the right of use asset will be recognised in the Statement of Profit or Loss on a straight-line basis, with interest recognised on the lease liability. This will result in a change to the profile of the net charge taken to the Statement of Profit or Loss over the life of the lease. These charges will replace the lease costs currently charged to the Statement of Profit or Loss.

The Directors are currently assessing the potential impact. It is not practicable to provide a reasonable estimate of the financial effect until the Directors complete the review.

As at 31 December 2017, the Group has non-cancellable operating lease commitments of £65.2 million. IAS 17 does not require the recognition of any right-of-use asset or liability for future payments for these leases; instead, certain information is disclosed as operating lease commitments in Note 25.

#### IFRS 9 "Financial Instruments"

"The Group will apply IFRS 9 from 1 January 2018. The Group has elected not to restate comparatives on initial application of IFRS 9. The full impact of adopting IFRS 9 on the Group's Consolidated Financial Statements will depend on the financial instruments that the Group has during 2018 as well as on economic conditions and judgements made as at the year end. The Group has performed a preliminary assessment of the potential impact of adopting IFRS 9 based on the financial instruments and hedging relationships as at the date of initial application of IFRS 9 (1 January 2018).

*Classification and measurement*

With respect to the classification and measurement of financial assets, the number of categories of financial assets under IFRS 9 has been reduced compared to IAS 39. Under IFRS 9 the classification of financial assets is based both on the business model within which the asset is held and the contractual cash flow characteristics of the asset. There are 3 principal classification categories for financial assets that are debt instruments: (i) amortised cost, (ii) fair value through other comprehensive income ("FVTOCI") and (iii) fair value through profit or loss ("FVTPL"). Equity investments in scope of IFRS 9 are measured at fair value with gains and losses recognised in profit or loss unless an irrevocable election is made to recognise gains or losses in other comprehensive income. Under IFRS 9, derivatives embedded in financial assets are not bifurcated but instead the whole hybrid contract is assessed for classification.

Under IFRS 9, financial assets can be designated as at FVTPL to mitigate an accounting mismatch.

In respect to classification and measurement of financial liabilities, changes in the fair value of a financial liability designated as at FVTPL due to credit risk are presented in other comprehensive income unless such presentation would create or enlarge an accounting mismatch in profit or loss.

Based on the Group's preliminary assessment, the change in the classification and measurement of listed redeemable notes will not have a material impact on the Group Financial Statements.

## 1 Accounting policies *continued*
### Significant accounting policies *continued*
### IFRS 9 "Financial Instruments" *continued*
*Impairment*

The impairment model under IFRS 9 reflects "expected" credit losses, as opposed to only "incurred" credit losses under IAS 39. Under the impairment approach in IFRS 9, it is not necessary for a credit event to have occurred before credit losses are recognised. Instead, an entity always accounts for expected credit losses and changes in those expected credit losses. The amount of expected credit losses should be updated at each reporting date.

The new impairment model will apply to the Group's financial assets that are debt instruments measured at amortised costs or FVTOCI as well as the Group's finance lease receivables, contract assets and issued financial guarantee contracts.

The Group expects to apply the simplified approach to recognise lifetime expected credit losses for its trade receivables, finance lease receivables and contracts assets as required or permitted by IFRS 9. The Group's preliminary assessment is that the loss allowance for these assets as at 1 January 2018 is not significantly different to that under IAS 39.

*Hedge accounting*

On initial application of IFRS 9, an entity may choose, as its accounting policy, to continue to apply the hedge accounting requirements of IAS 39 instead of the hedge accounting requirements of IFRS 9. The Group has elected to apply the IFRS 9 hedge accounting requirements because they align more closely with the Group's risk management policies.

An assessment of the Group's hedging relationships under IAS 39 has been performed and it has been determined that the relationships will qualify as continuing hedging relationships under IFRS 9.

**(a) Statement of compliance**

The Group Consolidated Financial Statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the European Union ("adopted IFRSs"). The Parent Company has elected to prepare its Financial Statements in accordance with FRS 101 and these are presented on pages 112 to 119.

**(b) Basis of preparation**

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 2 to 23. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are also set out in the Strategic Report. In addition, Note 16 includes the Group's policies and procedures for managing its capital; its financial risk management objectives; details of its financial instruments; and its exposures to credit risk and liquidity risk.

Details of the Group's funding position are set out in Note 16 and are subject to normal covenant arrangements. The Group's on-demand overdraft facility is reviewed on an annual basis and the current arrangements were renewed and signed on 1 August 2017. In the opinion of the Directors there are sufficient unutilised facilities held which mature after 12 months. The Group's performance is dependent on economic and market conditions, the outlook for which is difficult to predict. Based on current expectations, the Group's cash forecasts continue to meet half-year and year-end bank covenants and there is adequate headroom which is not dependent on facility renewals. The Directors believe that the Group is well placed to manage its business risks successfully. Accordingly, they continue to adopt the going concern basis in preparing the Consolidated Financial Statements.

The Consolidated Financial Statements are prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments and liabilities for cash-settled share-based payments.

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

The Consolidated Financial Statements are presented in Sterling, rounded to the nearest thousand. Sterling is the currency of the primary economic environment in which the Group operates.

The preparation of Financial Statements in conformity with adopted IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. These are set out in Note 28 on page 111. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

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

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

## 1 Accounting policies *continued*

**Significant accounting policies** *continued*

**(c) Basis of consolidation**

*(i) Subsidiaries*

Subsidiaries (which are set out in detail in Note 32 on pages 116 and 117) are entities controlled by the Company. Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to 1 or more of the 3 elements of control listed above. When the Company has less than a majority of the voting rights of an investee, it considers that it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally. The Company considers all relevant facts and circumstances in assessing whether or not the Company's voting rights in an investee are sufficient to give it power, including:

- the size of the Company's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Company, other vote holders or other parties;
- rights arising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Company has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders' meetings.

Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company loses control of the subsidiary. Specifically, the results of subsidiaries acquired or disposed of during the year are included in the Consolidated Income Statement from the date the Company gains control until the date when the Company ceases to control the subsidiary.

*(ii) Associates (equity-accounted investees)*

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20 and 50 per cent of the voting power of another entity. Associates are accounted for using the equity method (equity-accounted investees) and are recognised initially at cost. The Group's investment includes goodwill identified on acquisition, net of any accumulated impairment losses. The Consolidated Financial Statements include the Group's share of the income and expenses and equity movements of equity-accounted investees, after adjustment to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an equity-accounted investee, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the investee.

*(iii) Transactions eliminated on consolidation*

Intra-group balances, and any unrealised gains and losses or income and expenses arising from intra-group transactions, are eliminated in preparing the Consolidated Financial Statements.

*(iv) Non-controlling interests*

Non-controlling interests in subsidiaries are identified separately from the Group's equity therein. Those interests of non-controlling shareholders that are present ownership interests, entitling their holders to a proportionate share of net assets, are initially measured at the non-controlling interests' proportionate share of the acquiree's identifiable net assets. Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at the initial recognition plus the non-controlling interests' share of subsequent changes in equity. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interests having a deficit balance.

**(d) Foreign currency transactions**

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

For the purposes of presenting Consolidated Financial Statements, the assets and liabilities of the Group's foreign operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used.

**(e) Derivative financial instruments**

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

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

## 1 Accounting policies *continued*

**Significant accounting policies** *continued*

**(f) Hedging**

*(i) Cash flow hedges*

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

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

*(ii) Economic hedges*

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

**(g) Property, plant and equipment**

*(i) Owned assets*

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

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

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

*(ii) Leased assets*

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

*(iii) Subsequent costs*

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

*(iv) Depreciation*

Depreciation is charged to the Consolidated Income Statement on a straight line basis over the estimated useful lives of each part of an item of property, plant and equipment. Depreciation on quarries is based on estimated rates of extraction. This is based on a comparison between the volume of relevant material extracted in any given period and the volume of relevant material available for extraction. Depreciation on leased assets is charged over the shorter of the lease term and their useful economic life. Freehold land is not depreciated. The rates are as follows:

| | | |
|---|---|---|
| Freehold and long leasehold buildings | – | 2.5 per cent to 5 per cent per annum |
| Short leasehold property | – | over the period of the lease |
| Fixed plant and equipment | – | 3.3 per cent to 25 per cent per annum |
| Mobile plant and vehicles | – | 14 per cent to 30 per cent per annum |
| Quarries | – | based on rates of extraction |

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

Site preparation costs associated with the development of new stone reserves are capitalised. These costs would include:

- costs of clearing the site (including internal and outsourced labour in relation to site workers);
- professional fees (including fees relating to obtaining planning consent);
- purchase, installation and assembly of any necessary extraction equipment; and
- costs of testing whether the extraction process is functioning properly (net of any sales of test products).

## 1 Accounting policies *continued*

**Significant accounting policies** *continued*

**(g) Property, plant and equipment** *continued*

*(iv) Depreciation continued*

Depreciation commences when commercial extraction commences and is based on the rate of extraction.

In accordance with IAS 37, provision is made for quarry restoration where a legal or constructive obligation exists, it is probable that an outflow of economic benefits will occur and the financial cost of restoration work can be reliably measured. The lives of quarries are almost always long and it is difficult to estimate the length with any precision. The majority of quarry restoration work is undertaken while extracting minerals from new areas (backfilling) and therefore work can be completed without additional cost. As a result of the particular characteristics of the Group's quarries, the IAS 37 criteria have not been met to date based on the assets so far acquired and, therefore, no provisions have been recognised.

**(h) Intangible assets**

*(i) Goodwill*

All business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group.

For acquisitions on or after 1 January 2004, the Group measures goodwill at the acquisition date as:

- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- the fair value of the existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in the Consolidated Income Statement.

Costs relating to the acquisition, other than those associated with the issue of debt or equity securities, are expensed as incurred.

Any contingent consideration payable is recognised at fair value at the acquisition date. If the contingent consideration is classified as equity, it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes to the fair value of the contingent consideration are recognised in profit or loss.

On a transaction-by-transaction basis, the Group elects to measure non-controlling interests either at their fair value or at their proportionate interest in the recognised amount of the identifiable net assets of the acquiree at the acquisition date.

In respect of business acquisitions that have occurred since 1 January 2004, goodwill represents the difference between the cost of the acquisition and the fair value of the net identifiable assets and contingent liabilities acquired. The classification and accounting treatment of business combinations that occurred prior to 1 January 2017 were not adjusted in preparing the Group's opening IFRS balance sheet at 1 January 2017.

In respect of acquisitions prior to 1 January 2004, goodwill is included on the basis of its deemed cost, which represents the amount recorded under the Group's previous accounting framework. The classification and accounting treatment of business combinations that occurred prior to 1 January 2004 were not adjusted in preparing the Group's opening IFRS balance sheet at 1 January 2004.

Goodwill is subsequently stated at cost less any accumulated impairment losses. Goodwill is allocated to cash generating units and is tested annually for impairment (see accounting policy (m)). In respect of equity-accounted investees, the carrying amount of goodwill is included in the carrying amount of the investment in the investee.

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

*(ii) Research and development*

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

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

*(iii) Other intangible assets*

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

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

*(iv) Subsequent expenditure*

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

## 1 Accounting policies *continued*
### Significant accounting policies *continued*
#### (h) Intangible assets *continued*
*(v) Amortisation*

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

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

#### (i) Trade and other receivables
Trade and other receivables are stated at their nominal amount (discounted if material) less impairment losses (see accounting policy (m)).

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

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

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

#### (l) Assets classified as held for sale
Assets classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. Assets are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and expected to be completed within 1 year from the date of classification, and the asset is available for immediate sale in its present condition.

#### (m) Impairment
*(i) Impairment review*

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

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

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

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

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

*(ii) Reversals of impairments*

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

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

#### (n) Share capital
*(i) Share capital*

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

## 1 Accounting policies *continued*

### Significant accounting policies *continued*

**(n) Share capital** *continued*

*(ii) Dividends*

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

**(o) Interest-bearing borrowings**

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

**(p) Pension schemes**

*(i) Defined benefit schemes*

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

If the calculation results in a surplus, the resulting asset is measured at the present value of any economic benefits available in the form of refunds from the plan, or reductions in future contributions to the plan. The present value of these economic benefits is discounted by reference to market yields at the balance sheet date on high quality corporate bonds.

When the benefits of the scheme are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the Income Statement in the period of the scheme amendment.

Actuarial gains and losses that arise in calculating the Group's obligation in respect of a plan are recognised immediately within the Consolidated Statement of Comprehensive Income.

*(ii) Defined contribution schemes*

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

**(q) Share-based payment transactions**

The Group enters into equity settled share-based payment transactions with its employees. In particular, annual awards are made to employees under the Company's Management Incentive Plan ("MIP").

The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. Where appropriate, the fair value of the options granted is measured using the Black-Scholes option valuation model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

Current tax relief is available as shares vest based on the value at the date of vesting. A deferred tax asset is recognised at grant date based on the number of shares expected to be issued, at the value at which they are expected to be issued, proportioned in line with the vesting period.

**(r) Own shares held by the Employee Benefit Trust**

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

**(s) Provisions**

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

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

**(t) Trade and other payables**

Trade and other payables are stated at the nominal amount (discounted if material).

**(u) Revenue**

Revenue from the sale of goods is recognised in the Consolidated Income Statement upon the despatch of goods, when the significant risks and rewards of ownership of the goods have been transferred to the buyer. Revenue represents the invoiced value of sales to customers less returns, allowances, rebates and value added tax.

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

# Notes to the Consolidated Financial Statements *continued*

## 1 Accounting policies *continued*

**Significant accounting policies** *continued*

**(v) Expenses**

*(i) Operating lease payments*

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

*(ii) Finance lease payments*

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

*(iii) Financial expenses*

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

**(w) Income tax**

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

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

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

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

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

**(x) Segment reporting**

IFRS 8 *"Operating Segments"* requires operating segments to be identified on the basis of discrete financial information about components of the Group that are regularly reviewed by the Group's Chief Operating Decision Maker ("CODM") to allocate resources to the segments and to assess their performance. As far as Marshalls is concerned, the CODM is regarded as being the Executive Directors. The Directors have concluded that the Group's Landscape Products business is a single reportable segment, which includes the UK operations of the Marshalls Landscape Products hard landscaping business, servicing both the UK Domestic and the Public Sector and Commercial end markets. Following its acquisition, the CPM business has been included within the Landscape Products operating segment. Financial information for Landscape Products is now reported to the Group's CODM for the assessment of segment performance and to facilitate resource allocation.

**(y) Alternative performance measures**

The Group uses alternative performance measures ("APMs") which are not defined or specified under IFRS. The Group believes that these APMs, which are not considered to be a substitute for IFRS measures, provide additional helpful information. APMs are consistent with how business performance is planned, reported and assessed internally by management and the Board and provide more meaningful comparative information. In relation to the year ended 31 December 2017 certain APMs are required as a consequence of the acquisition of CPM on 19 October 2017 in order to ensure comparability with the prior year period.

*Like-for-like revenue growth*

Management uses like-for-like revenue growth as it provides a consistent measure of the percentage increase / decrease in revenue year on year, excluding the effect of acquisitions.

| | **2017 £'000** | 2016 £'000 | Increase % |
|---|---|---|---|
| Reported revenue | **430,194** | 396,922 | 8% |
| CPM post-acquisition revenue | **(9,017)** | – | |
| Like-for-like revenue | **421,177** | 396,922 | 6% |

*EBITA and EBITDA*

EBITA represents earnings before interest, tax and the amortisation of intangibles. This is a component of the ROCE calculation. EBITDA is calculated by adding back depreciation to EBITA.

## 1 Accounting policies *continued*

**Significant accounting policies** *continued*

**(y) Alternative performance measures** *continued*

*EBITA and EBITDA continued*

| | 2017 £'000 | 2016 £'000 | Increase % |
|---|---|---|---|
| EBITDA | **67,895** | 60,794 | 12% |
| Depreciation | **(13,314)** | (12,146) | |
| EBITA | **54,581** | 48,648 | |
| Amortisation of intangible assets | **(1,142)** | (1,009) | |
| Operating profit | **53,439** | 47,639 | 12% |

*ROCE*

Reported ROCE is defined as EBITA divided by shareholders funds plus cash / net debt.

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| EBITA | **54,581** | 48,648 |
| Shareholders funds | **237,627** | 217,121 |
| Net debt / (cash) | **24,297** | (5,413) |
| | **261,924** | 211,708 |
| Reported ROCE | **20.8%** | 23.0% |

ROCE on a like-for-like basis (excluding the impact of CPM) includes adjustments to report the calculation on a basis that eliminates the impact of the acquisition of CPM. This ensures comparability with the prior year period.

| | 2017 £'000 | 2016 £'000 | Increase % |
|---|---|---|---|
| Reported EBITA | **54,581** | 48,648 | |
| CPM post acquisition EBIT | **(749)** | – | |
| CPM amortisation of intangibles assets | **132** | – | |
| Acquisition costs | **837** | – | |
| Adjusted EBITA | **54,801** | 48,648 | |
| Shareholders funds | **237,627** | 217,121 | |
| Net debt / (cash) | **24,297** | (5,413) | |
| | **261,924** | 211,708 | |
| Impact on net debt arising from the acquisition of CPM | **(41,227)** | – | |
| As adjusted | **220,697** | 211,708 | |
| ROCE on a like-for-like basis (excluding the impact of CPM) | **24.8%** | 23.0% | 8% |

## 2 Segmental analysis

**Segment revenues and results**

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| | **Landscape Products £'000** | **Other £'000** | **Total £'000** | Landscape Products £'000 | Other £'000 | Total £'000 |
| Total revenue | **339,655** | **94,622** | **434,277** | 311,100[1] | 89,070[1] | 400,170 |
| Inter-segment revenue | **(226)** | **(3,857)** | **(4,083)** | (89) | (3,159) | (3,248) |
| External revenue | **339,429** | **90,765** | **430,194** | 311,011[1] | 85,911[1] | 396,922 |
| Segment operating profit | **56,104** | **1,873** | **57,977** | 50,441[1] | 3,157[1] | 53,598 |
| Unallocated administration costs | | | **(4,538)** | | | (5,959) |
| Operating profit | | | **53,439** | | | 47,639 |
| Finance charges (net) | | | **(1,388)** | | | (1,593) |
| Profit before tax | | | **52,051** | | | 46,046 |
| Taxation | | | **(9,925)** | | | (8,539) |
| Profit after tax | | | **42,126** | | | 37,507 |

1 The 2017 Half Year Report disclosed the results of the Landscape Products segment on a basis consistent with reporting to the CODM. In line with the Group's emerging strategy, in the second half of the year, the reporting to the CODM reverted to the 2016 structure with the Natural Stone Paving business reported as part of the Landscape Products segment.

## 2 Segmental analysis *continued*

### Segment revenues and results *continued*

The Group has 2 customers who each contributed more than 10 per cent of total revenue in the current and prior year.

The Landscape Products reportable segment operates a national manufacturing plan that is structured around a series of production units throughout the UK, in conjunction with a single logistics and distribution operation. A national planning process supports sales to both of the key end markets, namely the UK Domestic and Public Sector and Commercial end markets and the operating assets produce and deliver a range of broadly similar products that are sold into each of these end markets. Within the Landscape Products operating segment the focus is on one integrated production, logistics and distribution network supporting both end markets. Following the acquisition, the CPM business has been included within the landscape products operating segment.

Included in "Other" are the Group's Street Furniture, Mineral Products, Premier Mortars and International operations, which do not currently meet the IFRS 8 reporting requirements.

The accounting policies of the Landscape Products operating segment are the same as the Group's accounting policies. Segment profit represents the profit earned without allocation of certain central administration costs that are not capable of allocation. Centrally administered overhead costs that relate directly to the reportable segment are included within the segment's results.

### Segment assets

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Fixed assets and inventory: | | |
| Landscape Products | **182,391** | 157,786[1] |
| Other | **64,561** | 57,922[1] |
| Total segment fixed assets and inventory | **246,952** | 215,708 |
| Unallocated assets | **168,494** | 117,370 |
| Consolidated total assets | **415,446** | 333,078 |

1 The 2017 Half Year Report disclosed the results of the Landscape Products segment on a basis consistent with reporting to the CODM. In line with the Group's emerging strategy, in the second half of the year, the reporting to the CODM reverted to the 2016 structure with the Natural Stone Paving business reported as part of the Landscape Products segment.

For the purpose of monitoring segment performance and allocating resources between segments, the Group's CODM monitors the tangible fixed assets and inventory. Assets used jointly by reportable segments are not allocated to individual reportable segments.

### Other segment information

| | Depreciation and amortisation | | Fixed asset additions | |
|---|---|---|---|---|
| | **2017 £'000** | 2016 £'000 | **2017 £'000** | 2016 £'000 |
| Landscape Products | **10,878** | 9,462[1] | **17,041** | 9,131[1] |
| Other | **3,578** | 3,693[1] | **5,445** | 3,883[1] |
| | **14,456** | 13,155 | **22,486** | 13,014 |

1 The 2017 Half Year Report disclosed the results of the Landscape Products segment on a basis consistent with reporting to the CODM. In line with the Group's emerging strategy, in the second half of the year, the reporting to the CODM reverted to the 2016 structure with the Natural Stone Paving business reported as part of the Landscape Products segment.

### Geographical destination of revenue

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| United Kingdom | **407,215** | 377,659 |
| Rest of the World | **22,979** | 19,263 |
| | **430,194** | 396,922 |

The Group's revenue is subject to seasonal fluctuations resulting from demand from customers. In particular, demand is higher in the summer months. The Group manages the seasonal impact through the use of a seasonal working capital facility.

## 3 Net operating costs

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Raw materials and consumables | **151,343** | 142,011 |
| Changes in inventories of finished goods and work in progress | **7,231** | 2,591 |
| Personnel costs (Note 4) | **100,811** | 98,128 |
| Depreciation | **13,314** | 12,146 |
| Amortisation of intangible assets | **1,142** | 1,009 |
| Own work capitalised | **(1,919)** | (1,381) |
| Other operating costs | **106,569** | 97,069 |
| Operational restructuring costs | **1,217** | 476 |
| Acquisition costs | **837** | – |
| Operating costs | **380,545** | 352,049 |
| Other operating income | **(2,842)** | (2,157) |
| Net gain on asset and property disposals | **(948)** | (609) |
| **Net operating costs** | **376,755** | 349,283 |

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Net operating costs include: | | |
| Auditor's remuneration (see below) | **211** | 163 |
| Leasing costs | **11,465** | 10,151 |
| Hire of plant and machinery | **4,651** | 4,943 |
| Research and development costs | **3,876** | 3,364 |

In respect of the year under review, Deloitte LLP carried out work in relation to:

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Audit of Marshalls plc | **25** | 20 |
| Audit of financial statements of subsidiaries of the Company | **166** | 123 |
| Half-yearly review of Marshalls plc | **20** | 20 |
| | **211** | 163 |

## 4 Personnel costs

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Personnel costs (including amounts charged in the year in relation to Directors): | | |
| Wages and salaries | **80,811** | 79,605 |
| Social security costs | **9,617** | 9,361 |
| Share-based payments | **3,883** | 3,750 |
| Contributions to defined contribution pension scheme | **6,500** | 5,412 |
| Included within net operating costs (Note 3) | **100,811** | 98,128 |
| Personnel costs relating to restructuring (Note 3) | **1,217** | 476 |
| **Total personnel costs** | **102,028** | 98,604 |

# Notes to the Consolidated Financial Statements *continued*

## 4 Personnel costs *continued*

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Remuneration of Directors: | | |
| Salary | **712** | 699 |
| Other benefits | **39** | 39 |
| MIP Element A bonus | **535** | 844 |
| MIP Element B bonus | **356** | 339 |
| Amounts receivable under the MIP at the end of the first cycle | **2,024** | – |
| Amounts receivable under the 2005 LTIP | **–** | 956 |
| Salary supplement in lieu of pension | **142** | 139 |
| Non-Executive Directors' fees and fixed allowances | **299** | 310 |
| | **4,107** | 3,326 |

The aggregate of emoluments and amounts receivable under the MIP of the highest paid Director was £2,383,000 (2016: £1,913,000), including a salary supplement in lieu of pension of £86,000 (2016: £84,000).

There are no Directors to whom retirement benefits are accruing in respect of qualifying services. As set out in the Annual Remuneration Report on page 60, the Executive Directors receive a salary supplement in lieu of pension equal to their contractual entitlement of 20 per cent of basic salary.

Further details of Directors' remuneration, share options, long-term incentive plans and Directors' pension entitlements are disclosed in the Annual Remuneration Report on pages 50 to 63.

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

| | 2017 Number | 2016 Number |
|---|---|---|
| Continuing operations | **2,307** | 2,253 |

## 5 Financial expenses and income

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| **(a) Financial expenses** | | |
| Net interest expense on defined benefit pension scheme | **377** | 445 |
| Interest expense on bank loans, overdrafts and loan notes | **1,005** | 1,143 |
| Finance lease interest expense | **6** | 6 |
| | **1,388** | 1,594 |
| **(b) Financial income** | | |
| Interest receivable and similar income | **–** | 1 |

Net interest expense on the defined benefit pension scheme is disclosed net of Company recharges.

## 6 Income tax expense

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| **Current tax expense** | | |
| Current year | **11,554** | 10,611 |
| Adjustments for prior years | **(732)** | (921) |
| | **10,822** | 9,690 |
| **Deferred taxation expense** | | |
| Origination and reversal of temporary differences: | | |
| Current year | **(797)** | (1,098) |
| Adjustments for prior years | **(100)** | (53) |
| **Total tax expense** | **9,925** | 8,539 |

## 6 Income tax expense *continued*

| | 2017 % | 2017 £'000 | 2016 % | 2016 £'000 |
|---|---|---|---|---|
| **Reconciliation of effective tax rate** | | | | |
| Profit before tax | **100.0** | **52,051** | 100.0 | 46,046 |
| Tax using domestic corporation tax rate | **19.3** | **10,020** | 20.0 | 9,209 |
| Impact of capital allowances in excess of depreciation | **0.3** | **184** | 0.4 | 173 |
| Short-term timing differences | **1.2** | **630** | 1.0 | 480 |
| Adjustment to tax charge in prior year | **(1.4)** | **(732)** | (2.0) | (921) |
| Expenses not deductible for tax purposes | **1.4** | **720** | 1.6 | 749 |
| Corporation tax charge for the year | **20.8** | **10,822** | 21.0 | 9,690 |
| Impact of capital allowances in excess of depreciation | **(1.2)** | **(618)** | (1.0) | (443) |
| Short-term timing differences | **(0.2)** | **(103)** | (0.1) | (66) |
| Pension scheme movements | **(0.1)** | **(77)** | 0.3 | 127 |
| Other items | **1.0** | **532** | (0.9) | (397) |
| Adjustment to tax charge in prior year | **(0.2)** | **(100)** | (0.1) | (53) |
| Impact of the change in the rate of corporation tax on deferred taxation | **(1.0)** | **(531)** | (0.7) | (319) |
| Total tax charge for the year | **19.1** | **9,925** | 18.5 | 8,539 |

The net amount of deferred taxation (debited) / credited to the Consolidated Statement of Comprehensive Income in the year was £21,000 debit (2016: £798,000 debit).

The majority of the Group's profits are earned in the UK with the standard rate of corporation tax being 19.25 per cent for the year to 31 December 2017.

Capital allowances are tax reliefs provided in law for the expenditure the Group makes on fixed assets. The rates are determined by Parliament annually, and spread the tax relief due over a number of years. This contrasts with the accounting treatment for such spending, where the expenditure on fixed assets is treated as an investment with the cost then being spread over the anticipated useful life of the asset, and / or impaired if the value of such assets is considered to have reduced materially.

The different accounting treatment of fixed assets for tax and accounting purposes is one reason why the taxable income of the Group is not the same as its accounting profit. During the year ended 31 December 2017 the depreciation charge for the year exceeded the capital allowances due to the Group.

Short-term timing differences arise on items such as depreciation in stock and share-based payments because the treatment of such items is different for tax and accounting purposes. These differences usually reverse in the years following those in which they arise, as is reflected in the deferred tax charge in the Financial Statements.

Adjustments to tax charges arising in earlier years arise because the tax charge to be included in a set of accounts has to be estimated before those financial statements are finalised. Such charges therefore include some estimates that are checked and refined before the Group's corporation tax returns for the year are submitted to HM Revenue & Customs, which may reflect a different liability as a result.

Some expenses incurred may be entirely appropriate charges for inclusion in the Financial Statements but are not allowed as a deduction against taxable income when calculating the Group's tax liability for the same accounting period. Examples of such disallowable expenditure include business entertainment costs and some legal expenses.

As can be seen from the tax reconciliation, the process of adjustment that can give rise to current year adjustments to tax charges arising in previous periods can also give rise to revisions in prior year deferred tax estimates. This is why the current year adjustments to the current year charge for capital allowances and short-term timing differences are not exactly replicated in the deferred taxation charge for the year.

The Group's overseas operations comprise a manufacturing operation in Belgium and sales and administration offices in the USA, China and Dubai. The sales of these units, in total, were less than 5 per cent of the Group's turnover in the year ended 31 December 2017. In total, the trading profits were not material and no tax was due.

## 7 Earnings per share

Basic earnings per share of 21.52 pence (2016: 18.95 pence) per share is calculated by dividing the profit attributable to Ordinary Shareholders for the financial year, after adjusting for non-controlling interests, of £42,503,000 (2016: £37,350,000) by the weighted average number of shares in issue during the period of 197,518,109 (2016: 197,130,419).

## 7 Earnings per share *continued*

**Profit attributable to Ordinary Shareholders**

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Profit for the financial year | **42,126** | 37,507 |
| Loss / (profit) attributable to non-controlling interests | **377** | (157) |
| Profit attributable to Ordinary Shareholders | **42,503** | 37,350 |

**Weighted average number of Ordinary Shares**

| | 2017 Number | 2016 Number |
|---|---|---|
| Number of issued Ordinary Shares | **199,378,755** | 199,378,755 |
| Effect of shares transferred into employee benefit trust | **(1,860,646)** | (2,248,336) |
| Weighted average number of Ordinary Shares at end of the year | **197,518,109** | 197,130,419 |

Diluted earnings per share of 21.37 pence (2016: 18.61 pence) per share is calculated by dividing the profit for the financial year, after adjusting for non-controlling interests, of £42,503,000 (2016: £37,350,000) by the weighted average number of shares in issue during the period of 197,518,109 (2016: 197,130,419) plus potentially dilutive shares of 1,384,707 (2016: 3,561,243), which totals 198,902,816 (2016: 200,691,662).

**Weighted average number of Ordinary Shares (diluted)**

| | 2017 Number | 2016 Number |
|---|---|---|
| Weighted average number of Ordinary Shares | **197,518,109** | 197,130,419 |
| Potentially dilutive shares | **1,384,707** | 3,561,243 |
| Weighted average number of Ordinary Shares (diluted) | **198,902,816** | 200,691,662 |

## 8 Dividends

After the balance sheet date a final dividend of 6.80 pence (2016: 5.80 pence) per qualifying Ordinary Share was proposed by the Directors. In addition a supplementary dividend of 4.00 pence (2016: 3.00 pence) per qualifying Ordinary Share was proposed by the Directors. These dividends have not been provided for and there are no income tax consequences. The total dividends proposed in respect of the year are as follows:

| | Pence per qualifying share | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| 2017 supplementary | **4.00** | **7,904** | |
| 2017 final | **6.80** | **13,436** | |
| 2017 interim | **3.40** | **6,718** | |
| | **14.20** | **28,058** | |
| 2016 supplementary | 3.00 | | 5,927 |
| 2016 final | 5.80 | | 11,460 |
| 2016 interim | 2.90 | | 5,720 |
| | 11.70 | | 23,107 |

The following dividends were approved by the shareholders and recognised in the year:

| | Pence per qualifying share | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| 2017 interim | **3.40** | **6,718** | |
| 2016 supplementary | **3.00** | **5,927** | |
| 2016 final | **5.80** | **11,460** | |
| | **12.20** | **24,105** | |
| 2016 interim | 2.90 | | 5,720 |
| 2015 supplementary | 2.00 | | 3,945 |
| 2015 final | 4.75 | | 9,369 |
| | 9.65 | | 19,034 |

## 8 Dividends *continued*

The Board recommends a 2017 final dividend of 6.80 pence per qualifying Ordinary Share (amounting to £13,436,000), alongside a supplementary dividend of 4.00 pence per qualifying Ordinary Share (amounting to £7,904,000), to be paid on 29 June 2018 to shareholders registered at the close of business on 8 June 2018.

## 9 Property, plant and equipment

| | Land and buildings £'000 | Quarries £'000 | Plant, machinery and vehicles £'000 | Total £'000 |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 January 2016 | 84,392 | 22,951 | 313,434 | 420,777 |
| Exchange differences | 944 | – | 624 | 1,568 |
| Additions | 551 | 446 | 11,083 | 12,080 |
| Reclassified as held for sale | (1,910) | – | – | (1,910) |
| Disposals | (297) | – | (1,665) | (1,962) |
| **At 31 December 2016** | 83,680 | 23,397 | 323,476 | 430,553 |
| At 1 January 2017 | **83,680** | **23,397** | **323,476** | **430,553** |
| Exchange differences | **311** | **–** | **223** | **534** |
| Additions | **2,509** | **67** | **18,160** | **20,736** |
| Acquisition of subsidiary | **8,437** | **–** | **7,639** | **16,076** |
| Disposals | **(1,281)** | **–** | **(2,629)** | **(3,910)** |
| **At 31 December 2017** | **93,656** | **23,464** | **346,869** | **463,989** |
| **Depreciation and impairment losses** | | | | |
| At 1 January 2016 | 36,567 | 7,004 | 229,717 | 273,288 |
| Depreciation charge for the year | 1,814 | 531 | 9,801 | 12,146 |
| Reclassifications and transfers to assets held for sale | (1,286) | 288 | – | (998) |
| Exchange differences | 15 | – | 382 | 397 |
| Disposals | (94) | – | (1,181) | (1,275) |
| **At 31 December 2016** | 37,016 | 7,823 | 238,719 | 283,558 |
| At 1 January 2017 | **37,016** | **7,823** | **238,719** | **283,558** |
| Depreciation charge for the year | **1,829** | **583** | **10,902** | **13,314** |
| Exchange differences | **7** | **–** | **132** | **139** |
| Disposals | **(26)** | **–** | **(2,089)** | **(2,115)** |
| **At 31 December 2017** | **38,826** | **8,406** | **247,664** | **294,896** |
| **Net book value** | | | | |
| At 1 January 2016 | 47,825 | 15,947 | 83,717 | 147,489 |
| At 31 December 2016 | 46,664 | 15,574 | 84,757 | 146,995 |
| **At 31 December 2017** | **54,830** | **15,058** | **99,205** | **169,093** |

Mineral reserves and associated land have been separately disclosed under the heading of "Quarries".

Assets disclosed as held for sale as at 31 December 2016 have been disposed of in the year ended 31 December 2017.

The carrying amount of tangible fixed assets includes £402,000 (2016: £402,000) in respect of land assets held under finance leases. Group cost of land and buildings and plant and machinery includes £1,484,000 (2016: £nil) and £7,105,000 (2016: £999,000) respectively for assets in the course of construction.

# Notes to the Consolidated Financial Statements *continued*

## 9 Property, plant and equipment *continued*

### Capital commitments

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Capital expenditure that has been contracted for but for which no provision has been made in the Consolidated Financial Statements | **5,058** | 1,427 |

### Depreciation charge

The depreciation charge is recognised in the following line items in the Consolidated Income Statement:

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Net operating costs (Note 3) | **13,314** | 12,146 |

## 10 Intangible assets

| | Goodwill £'000 | Customer relationships £'000 | Supplier relationships £'000 | Patents, trademarks and know-how £'000 | Development costs £'000 | Software £'000 | Total £'000 |
|---|---|---|---|---|---|---|---|
| **Cost** | | | | | | | |
| At 1 January 2016 | 43,691 | 2,210 | 1,200 | 1,660 | 159 | 11,676 | 60,596 |
| Additions | – | – | – | – | – | 934 | 934 |
| **At 31 December 2016** | 43,691 | 2,210 | 1,200 | 1,660 | 159 | 12,610 | 61,530 |
| At 1 January 2017 | **43,691** | **2,210** | **1,200** | **1,660** | **159** | **12,610** | **61,530** |
| Additions | **–** | **–** | **–** | **–** | **–** | **1,750** | **1,750** |
| Recognised on acquisition of subsidiary | **25,145** | **6,704** | **429** | **100** | **–** | **–** | **32,378** |
| **At 31 December 2017** | **68,836** | **8,914** | **1,629** | **1,760** | **159** | **14,360** | **95,658** |
| **Amortisation and impairment losses** | | | | | | | |
| At 1 January 2016 | 8,912 | 2,210 | 728 | 1,366 | 93 | 7,119 | 20,428 |
| Amortisation for the year | – | – | 60 | 32 | 8 | 909 | 1,009 |
| **At 31 December 2016** | 8,912 | 2,210 | 788 | 1,398 | 101 | 8,028 | 21,437 |
| At 1 January 2017 | **8,912** | **2,210** | **788** | **1,398** | **101** | **8,028** | **21,437** |
| Amortisation for the year | **–** | **121** | **69** | **34** | **8** | **910** | **1,142** |
| **At 31 December 2017** | **8,912** | **2,331** | **857** | **1,432** | **109** | **8,938** | **22,579** |
| **Carrying amounts** | | | | | | | |
| At 1 January 2016 | 34,779 | – | 472 | 294 | 66 | 4,557 | 40,168 |
| At 31 December 2016 | 34,779 | – | 412 | 262 | 58 | 4,582 | 40,093 |
| **At 31 December 2017** | **59,924** | **6,583** | **772** | **328** | **50** | **5,422** | **73,079** |

All goodwill has arisen from business combinations. The carrying amount of goodwill is allocated across cash generating units ("CGUs") and these CGUs are independent sources of income streams and represent the lowest level within the Group at which the associated goodwill is monitored for management purposes. The Group tests goodwill annually for impairment, or more frequently if there are indications that goodwill might be impaired.

## 10 Intangible assets *continued*

The recoverable amounts of the CGUs are determined from value-in-use calculations and at both 31 December 2017 and 31 December 2016 the full amount of goodwill in the Group Balance Sheet related to the Landscape Products CGU. The goodwill arising on the acquisition of CPM is included within the landscape products CGU. These calculations use cash flow projections based on a combination of individual financial 5-year forecasts, containing assumptions for revenue growth and operational gearing, and appropriate long-term growth rates of 2.45 per cent. To prepare value-in-use calculations, the cash flow forecasts are discounted back to present value using an appropriate market-based discount rate. The pre-tax discount rate used to calculate the value in use was 9.8 per cent (2016: 9.5 per cent). The Directors have reviewed the recoverable amounts of the CGUs and do not consider that any reasonable change in the assumptions would give rise to the need for further impairment.

Included in software additions is £910,000 (2016: £819,000) of own work capitalised.

**Amortisation charge**

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

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Net operating costs (Note 3) | **1,142** | 1,009 |

## 11 Inventories

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Raw materials and consumables | **15,690** | 13,788 |
| Finished goods and goods for resale | **62,169** | 54,925 |
| | **77,859** | 68,713 |

Inventories stated at a net realisable value less than cost at 31 December 2017 amounted to £4,148,000 (2016: £7,848,000). The write down of inventories made during the year amounted to £1,477,000 (2016: £2,868,000). There were £73,000 reversals of inventory write-downs made in previous years in 2017 (2016: £nil).

## 12 Trade and other receivables

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Trade receivables | **47,925** | 42,133 |
| Other receivables | **15,839** | 3,003 |
| Prepayments and accrued income | **4,457** | 3,874 |
| | **68,221** | 49,010 |

Included within other receivables is a reimbursement asset of £12,000,000 which is held in escrow in relation to the acquisition of CPM Group Limited (Note 22).

**Ageing of trade receivables**

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Neither impaired nor past due | **21,363** | 23,687 |
| Not impaired but overdue by less than 30 days | **19,117** | 14,499 |
| Not impaired but overdue by between 30 and 60 days | **3,653** | 2,032 |
| Not impaired but overdue by more than 60 days | **3,792** | 1,915 |
| | **47,925** | 42,133 |

Receivables totalling £nil (2016: £208,000) were due after more than 1 year. All amounts disclosed above are considered recoverable and are disclosed net of an allowance for doubtful debts of £609,000 (2016: £804,000).

# Notes to the Consolidated Financial Statements *continued*

## 13 Cash and cash equivalents

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Bank balances | **19,833** | 20,661 |
| Cash in hand | **12** | 20 |
| Cash and cash equivalents in the Consolidated Cash Flow Statement | **19,845** | 20,681 |

## 14 Trade and other payables

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| **Current liabilities** | | |
| Trade payables | **52,180** | 36,605 |
| Taxation and social security | **10,449** | 9,217 |
| Other payables | **15,056** | 19,148 |
| Accruals | **19,867** | 14,676 |
| | **97,552** | 79,646 |

All trade payables are due in 6 months or less.

## 15 Loans

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| **Current liabilities** | | |
| Finance lease liabilities | **35** | 34 |
| **Non-current liabilities** | | |
| Bank loans | **43,883** | 14,975 |
| Finance lease liabilities | **224** | 259 |
| | **44,107** | 15,234 |

**Bank loans**

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

**Finance lease liabilities**

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| | **Minimum lease payments £'000** | **Interest £'000** | **Principal £'000** | Minimum lease payments £'000 | Interest £'000 | Principal £'000 |
| Less than 1 year | **40** | **5** | **35** | 40 | 6 | 34 |
| 1 to 2 years | **40** | **4** | **36** | 40 | 5 | 35 |
| 2 to 5 years | **120** | **10** | **110** | 120 | 11 | 109 |
| In more than 5 years | **80** | **2** | **78** | 120 | 5 | 115 |
| | **280** | **21** | **259** | 320 | 27 | 293 |

## 16 Financial instruments

The Group holds and uses financial instruments to finance its operations and to manage its interest rate, liquidity and currency risks. The Group primarily finances its operations using share capital, retained profits and borrowings. The Group's bank loans are non-equity funding instruments, further details of which are set out on page 100.

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

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and pricing risk. The Board reviews and agrees the policies for managing each of these risks and they have remained unchanged since 2016.

### Capital management

The Group defines the capital that it manages as its total equity and net debt balances. The Group manages its capital structure in light of current economic conditions and its strategic objectives to ensure that it is able to continue as a going concern whilst maximising the return to stakeholders through the optimisation of debt and equity balances.

The Group manages its medium-term bank debt to ensure continuity of funding and the policy is to arrange funding ahead of requirements and to maintain sufficient undrawn committed facilities. A key objective is to ensure compliance with the covenants set out in the Group's bank facility agreements.

From time to time the Group purchases its own shares on the market; the timing of these purchases depends on market prices. Primarily the shares are intended to be used for issuing shares under the Group's incentive schemes. Buy and sell decisions are made on a specific transaction basis by the Board.

There has been no change in the objectives, policies or processes with regard to capital management during the years ended 31 December 2017 and 31 December 2016.

### Financial risks

The Group has exposure to a number of financial risks through the conduct of its operations. Risk management is governed by the Group's operational policies, guidelines and authorisation procedures, which are outlined in the Strategic Report on pages 2 to 33. The key financial risks resulting from financial instruments are liquidity risk, interest rate risk, credit risk, foreign currency risk and pricing risk.

In managing interest rate and currency risks the Group aims to reduce the impact of short-term fluctuations on the Group's earnings. Over the longer term, however, permanent changes in foreign exchange and interest rates would have an impact on consolidated earnings. For instance, a weakening of Pound Sterling on the foreign currency market would increase the cost of certain raw materials, whereas a strengthening would have the opposite effect.

### (a) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Board is responsible for ensuring that the Group has sufficient liquidity to meet its financial liabilities as they fall due and does so by monitoring cash flow forecasts and budgets. Cash resources are largely and normally generated through operations and short-term flexibility is achieved by bank facilities. Bank debt is raised centrally and the Group aims to maintain a balance between flexibility and continuity of funding by having a range of maturities on its borrowings. Details of the Group borrowing facilities are provided on page 101.

### (b) Interest rate risk

The Group's policy is to review regularly the terms of its available short-term borrowing facilities and to assess individually and manage each long-term borrowing commitment accordingly. The Group borrows principally at floating rates of interest and, where appropriate, uses interest rate swaps to generate the desired interest rate profile, thereby managing the Group's exposure to interest rate fluctuations.

Approximately 60 to 70 per cent of core debt is covered by interest rate swaps of varying maturities, which reflects the maturity date of the related loans and medium-term requirements, in accordance with Group policy. The Group classifies its interest rate swaps as cash flow hedges and states them at fair value. The fair value of interest rate swaps is a £14,000 asset (2016: £49,000 liability) and is adjusted against the hedging reserve on an ongoing basis.

The period that the swaps cover is matched against the debt maturity in order to fix the impact on the Income Statement. During the year £23,000 (2016: £nil) has been recognised in other comprehensive income for the year with £43,000 (2016: £75,000) being reclassified from equity to the Income Statement. The interest rate swaps have been fully effective in the period.

With the addition of the fuel hedges (Note 16(e)) and forward contracts this gives a total of £146,000 credit (2016: £1,123,000 credit) recognised in other comprehensive income for the year with £385,000 debit (2016: £1,681,000 credit) being reclassified from equity to the Income Statement.

## 16 Financial instruments *continued*

**Financial risks** *continued*

**(b) Interest rate risk** *continued*

*Sensitivity analysis*

A change of 100 basis points in interest rates at the balance sheet date would have decreased equity and profit by the amounts shown below. The sensitivity analysis has been undertaken before the effect of tax. The sensitivity analysis of the Group's exposure to interest rate risk has been determined based on the change taking place at the beginning of the financial year and held constant throughout the reporting period.

This analysis assumes that all other variables, in particular foreign currency rates, remain constant and considers the effect of financial instruments with variable interest rates, financial instruments at fair value through profit or loss or available for sale with fixed interest rates and the fixed rate element of interest rate swaps. The analysis was performed on the same basis for 2016.

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Increase of 100 basis points | **(211)** | (185) |
| Decrease of 100 basis points | **211** | 185 |

**(c) Credit risk**

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all customers requiring credit over a certain amount and, where appropriate, credit insurance cover is obtained. This provides excellent intelligence to minimise the number and value of bad debts and ultimately provides compensation if bad debts are incurred. An ageing of trade receivables is shown in Note 12 on page 95.

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

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

**(d) Foreign currency risk**

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

The Group's policy is to cover all significant foreign currency commitments in respect of trade receivables and trade payables by using forward foreign currency contracts. All the forward exchange contracts have maturities of less than 1 year after the balance sheet date. Where necessary, the forward exchange contracts are rolled over at maturity.

The Group classifies its forward exchange contracts as cash flow hedges and states them at fair value. The fair value of forward exchange contracts is £42,000 asset (2016: £30,000 asset) and is adjusted against the hedging reserve on an ongoing basis. At 31 December 2017 all outstanding forward exchange contracts had a maturity date within 6 months.

The foreign currency profile of monetary items was:

| | **2017** | | | | | 2016 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Sterling £'000** | **Euro £'000** | **US Dollar £'000** | **AED £'000** | **Total £'000** | Sterling £'000 | Euro £'000 | US Dollar £'000 | AED £'000 | Total £'000 |
| Cash and cash equivalents | **17,830** | **912** | **1,006** | **97** | **19,845** | 16,733 | 2,373 | 1,510 | 65 | 20,681 |
| Trade receivables | **46,530** | **1,035** | **360** | **–** | **47,925** | 38,804 | 2,972 | 357 | – | 42,133 |
| Secured bank loans | **(28,251)** | **(15,632)** | **–** | **–** | **(43,883)** | – | (14,975) | – | – | (14,975) |
| Trade payables | **(42,943)** | **(8,328)** | **(909)** | **–** | **(52,180)** | (28,333) | (8,014) | (258) | – | (36,605) |
| Derivative financial instruments | **405** | **42** | **–** | **–** | **447** | 627 | 37 | (7) | – | 657 |
| Balance sheet exposure | **(6,429)** | **(21,971)** | **457** | **97** | **(27,846)** | 27,831 | (17,607) | 1,602 | 65 | 11,891 |

A 10 per cent strengthening and weakening of the following currencies against the Pound Sterling at 31 December 2017 would have increased / (decreased) equity and profit or loss by the amounts shown below. This calculation assumes that the change occurred at the balance sheet date and had been applied to risk exposures existing at that date.

## 16 Financial instruments *continued*

**Financial risks** *continued*

**(d) Foreign currency risk** *continued*

This analysis assumes that all other variables, in particular other exchange rates and interest rates, remain constant. The analysis was performed on the same basis for 2016:

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| 10 per cent strengthening of £ against € | **1,953** | 1,565 |
| 10 per cent weakening of £ against € | **(1,598)** | (1,280) |
| 10 per cent strengthening of £ against $ | **(41)** | (142) |
| 10 per cent weakening of £ against $ | **33** | 117 |
| 10 per cent strengthening of £ against Dhs | **(9)** | (6) |
| 10 per cent weakening of £ against Dhs | **7** | 9 |

**(e) Pricing risks**

Where appropriate the Group uses hedging instruments to mitigate the risks of significant forward price rises of fuel in relation to expected consumption. The current hedges held are in place until 31 December 2017. The Group classifies its fuel hedges as cash flow hedges and states them at fair value. The fair value of the fuel hedges is £391,000 asset (2016: £676,000 asset) and is adjusted against the hedging reserve on an ongoing basis. The period that the fuel hedges cover is matched against future expected purchases in order to fix the impact on the Income Statement. During the year £123,000 (2016: £1,123,000) has been recognised in other comprehensive income, with £428,000 (2016: £1,606,000) being reclassified from equity to the Income Statement. The fuel hedges have been fully effective in the period.

**(f) Other risks**

Further information about the Group's strategic and financial risks is contained in the Strategic Report on pages 2 to 33.

*Effective interest rates and maturity of liabilities*

At 31 December 2017 there were £259,000 (2016: £293,000) of Group borrowings on a fixed rate. Interest rate swaps have been taken out with the intention to fix the interest on approximately 60 to 70 per cent of the Group's core debt. The interest rate profile of the financial liabilities was:

| | Fixed or variable rate | Effective interest rate % | Total £'000 | 6 months or less £'000 | 6 – 12 months £'000 | 1 – 2 years £'000 | 2 – 5 years £'000 | More than 5 years £'000 |
|---|---|---|---|---|---|---|---|---|
| **31 December 2017** | | | | | | | | |
| Cash and cash equivalents (Note 13) | Variable | **1.97** | **(19,845)** | **(19,845)** | **–** | **–** | **–** | **–** |
| Bank loans | Variable | **1.97** | **43,883** | **–** | **14,500** | **24,239** | **5,144** | **–** |
| Finance lease liabilities | Fixed | **10.0** | **259** | **–** | **35** | **36** | **110** | **78** |
| | | | **24,297** | **(19,845)** | **14,535** | **24,275** | **5,254** | **78** |

| | Fixed or variable rate | Effective interest rate % | Total £'000 | 6 months or less £'000 | 6 – 12 months £'000 | 1 – 2 years £'000 | 2 – 5 years £'000 | More than 5 years £'000 |
|---|---|---|---|---|---|---|---|---|
| **31 December 2016** | | | | | | | | |
| Cash and cash equivalents (Note 13) | Variable | 1.50 | (20,681) | (20,681) | – | – | – | – |
| Bank loans | Variable | 1.50 | 14,975 | – | – | 10,048 | 4,927 | – |
| Finance lease liabilities | Fixed | 10.0 | 293 | – | 34 | 35 | 109 | 115 |
| | | | (5,413) | (20,681) | 34 | 10,083 | 5,036 | 115 |

## 16 Financial instruments *continued*

**Financial risks** *continued*

**(f) Other risks** *continued*

***Effective interest rates and maturity of liabilities continued***

At 31 December the undiscounted outstanding contractual payments (including interest) of financial liabilities were as follows:

| | Fixed or variable rate | Carrying value £'000 | Total £'000 | 6 months or less £'000 | 6 – 12 months £'000 | 1 – 2 years £'000 | 2 – 5 years £'000 | More than 5 years £'000 |
|---|---|---|---|---|---|---|---|---|
| **31 December 2017** | | | | | | | | |
| Bank loans | Variable | **43,883** | **44,519** | **244** | **14,665** | **24,427** | **5,183** | **–** |
| Trade payables | Variable | **52,180** | **52,180** | **52,180** | **–** | **–** | **–** | **–** |
| Finance lease liabilities | Fixed | **259** | **280** | **3** | **37** | **40** | **120** | **80** |
| Derivative financial assets | Fixed | **(447)** | **(391)** | **(236)** | **(155)** | **–** | **–** | **–** |
| | | **95,875** | **96,588** | **52,191** | **14,547** | **24,467** | **5,303** | **80** |

| | Fixed or variable rate | Carrying value £'000 | Total £'000 | 6 months or less £'000 | 6 – 12 months £'000 | 1 – 2 years £'000 | 2 – 5 years £'000 | More than 5 years £'000 |
|---|---|---|---|---|---|---|---|---|
| **31 December 2016** | | | | | | | | |
| Bank loans | Variable | 14,975 | 15,182 | 43 | 43 | 10,108 | 4,988 | – |
| Trade payables | Variable | 36,605 | 36,605 | 36,605 | – | – | – | – |
| Finance lease liabilities | Fixed | 293 | 320 | 3 | 37 | 40 | 120 | 120 |
| Derivative financial assets | Fixed | (657) | (624) | (416) | (208) | – | – | – |
| | | 51,216 | 51,483 | 36,235 | (128) | 10,148 | 5,108 | 120 |

**Borrowing facilities**

The total bank borrowing facilities at 31 December 2017 amounted to £115.0 million (2016: £95.0 million), of which £71.1 million (2016: £80.0 million) remained unutilised. There are additional seasonal bank working capital facilities of £10.0 million available between 1 February and 31 August each year. The undrawn facilities available at 31 December 2017, in respect of which all conditions precedent had been met, were as follows:

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Committed: | | |
| Expiring in more than 2 years but not more than 5 years | **50,617** | 65,025 |
| Expiring in 1 year or less | **5,500** | – |
| Uncommitted: | | |
| Expiring in 1 year or less | **15,000** | 15,000 |
| | **71,117** | 80,025 |

On 17 August 2017, the Group renewed its short-term working capital facilities of £25.0 million. On 16 October 2017 the Group took out an additional committed facility of £20.0 million with a 2022 maturity date. The committed facilities are all revolving credit facilities with interest charged at variable rates based on LIBOR. The Group's bank facilities continue to be aligned with the current strategy to ensure that headroom against available facilities remains at appropriate levels.

## 16 Financial instruments *continued*

### Borrowing facilities *continued*

The maturity profile of borrowing facilities is structured to provide balanced, committed and phased medium-term debt. The current facilities are set out as follows:

| | Facility £'000 | Cumulative facility £'000 |
|---|---|---|
| **Committed facilities** | | |
| Q3: 2022 | 20,000 | 20,000 |
| Q3: 2021 | 20,000 | 40,000 |
| Q3: 2020 | 20,000 | 60,000 |
| Q3: 2019 | 20,000 | 80,000 |
| Q3: 2018 | 20,000 | 100,000 |
| **On-demand facilities** | | |
| Available all year | 15,000 | 115,000 |
| Seasonal (February to August inclusive) | 10,000 | 125,000 |

### Fair values of financial assets and financial liabilities

A comparison by category of the book values and fair values of the financial assets and liabilities of the Group at 31 December 2017 is shown below:

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Book amount £'000** | **Fair value £'000** | Book amount £'000 | Fair value £'000 |
| Trade and other receivables | **62,787** | **62,787** | 46,033 | 46,033 |
| Cash and cash equivalents | **19,845** | **19,845** | 20,681 | 20,681 |
| Bank loans | **(43,883)** | **(42,836)** | (14,975) | (14,192) |
| Finance lease liabilities | **(259)** | **(280)** | (293) | (320) |
| Trade and other payables | **(95,777)** | **(95,777)** | (70,939) | (70,939) |
| Interest rate swaps, forward contracts and fuel hedges | **447** | **447** | 657 | 657 |
| Financial instrument assets and liabilities – net | **(56,840)** | | (18,836) | |
| Non-financial instrument assets and liabilities – net | **294,467** | | 235,957 | |
| | **237,627** | | 217,121 | |

### Estimation of fair values

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

*(a) Derivatives*

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

*(b) Interest-bearing loans and borrowings*

Fair value is calculated based on the expected future principal and interest cash flows discounted at the market rate of interest at the balance sheet date.

*(c) Finance lease liabilities*

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

*(d) Trade and other receivables / payables*

For receivables / payables with a remaining life of less than 1 year, the notional amount is deemed to reflect the fair value. All other receivables / payables are discounted to determine the fair value.

## 16 Financial instruments *continued*

**Borrowing facilities** *continued*

**Estimation of fair values** *continued*

*(e) Fair value hierarchy*

The table below analyses financial instruments, measured at fair value, into a fair value hierarchy based on the valuation techniques used to determine fair value.

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

| | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 |
|---|---|---|---|---|
| **31 December 2017** | | | | |
| Derivative financial assets | **–** | **447** | **–** | **447** |
| **31 December 2016** | | | | |
| Derivative financial assets | – | 657 | – | 657 |

## 17 Employee benefits

The Company sponsors a funded defined benefit pension scheme in the UK ("the Scheme"). The Scheme is administered within a trust which is legally separate from the Company. The Trustee Board is appointed by both the Company and the Scheme's membership and acts in the interest of the Scheme and all relevant stakeholders, including the members and the Company. The Trustee is also responsible for the investment of the Scheme's assets.

The defined benefit section of the Scheme provides pension and lump sums to members on retirement and to dependants on death. The defined benefit section closed to future accrual of benefits on 30 June 2006 with the active members becoming entitled to a deferred pension. Members no longer pay contributions to the defined benefit section. Company contributions to the defined benefit section after this date are used to fund any deficit in the Scheme and the expenses associated with administering the Scheme, as determined by regular actuarial valuations.

The Trustee is required to use prudent assumptions to value the liabilities and costs of the Scheme whereas the accounting assumptions must be best estimates.

The defined benefit section of the Scheme poses a number of risks to the Company, for example longevity risk, investment risk, interest rate risk, inflation risk and salary risk. The Trustee is aware of these risks and uses various techniques to control them. The Trustee has a number of internal control policies, including a risk register, which are in place to manage and monitor the various risks it faces. The Trustee's investment strategy incorporates the use of liability-driven investments ("LDIs") to minimise sensitivity of the actuarial funding position to movements in interest rates and inflation rates.

The defined benefit section of the Scheme is subject to regular actuarial valuations, which are usually carried out every 3 years. The next actuarial valuation is expected to be carried out with an effective date of 5 April 2018. These actuarial valuations are carried out in accordance with the requirements of the Pensions Act 2004 and so include deliberate margins for prudence. This contrasts with these accounting disclosures which are determined using best estimate assumptions.

A formal actuarial valuation was carried out as at 5 April 2015. The results of that valuation have been projected to 31 December 2017 by a qualified independent actuary. The figures in the following disclosure were measured using the projected unit method.

The amounts recognised in the Consolidated Balance Sheet were as follows:

| | **2017 £'000** | 2016 £'000 | 2015 £'000 |
|---|---|---|---|
| Present value of Scheme liabilities | **(350,554)** | (355,793) | (298,812) |
| Fair value of Scheme assets | **354,681** | 360,069 | 302,239 |
| Net amount recognised at year end (before any adjustments for deferred tax) | **4,127** | 4,276 | 3,427 |

## 17 Employee benefits *continued*

The current and past service costs, settlements and curtailments, together with the net interest expense for the year, are included in the employee benefits expense in the Statement of Comprehensive Income. Remeasurements of the net defined benefit surplus are included in other comprehensive income.

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Net interest expense recognised in the Consolidated Income Statement | **477** | 545 |
| Remeasurements of the net liability: | | |
| Return on scheme assets (excluding amount included in interest expense) | **(2,819)** | (59,837) |
| Loss arising from changes in financial assumptions | **10,158** | 62,332 |
| Gain arising from changes in demographic assumptions | **(7,667)** | – |
| Experience gain | **–** | (3,889) |
| Credit recorded in other comprehensive income | **(328)** | (1,394) |
| Total defined benefit charge / (credit) | **149** | (849) |

The principal actuarial assumptions used were:

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Liability discount rate | **2.50%** | 2.65% |
| Inflation assumption – RPI | **3.15%** | 3.20% |
| Inflation assumption – CPI | **2.15%** | 2.20% |
| Rate of increase in salaries | **n/a** | n/a |
| Revaluation of deferred pensions | **2.15%** | 2.20% |
| Increases for pensions in payment: | | |
| CPI pension increases (maximum 5% p.a.) | **2.15%** | 2.20% |
| CPI pension increases (maximum 5% p.a., minimum 3% p.a.) | **3.20%** | 3.10% |
| CPI pension increases (maximum 3% p.a.) | **1.95%** | 2.10% |
| Proportion of employees opting for early retirement | **0%** | 0% |
| Proportion of employees commuting pension for cash | **50.0%** | 50.0% |
| Mortality assumption – before retirement | **Same as post retirement** | Same as post retirement |
| Mortality assumption – after retirement (males) | **S2PMA tables** | S2PMA tables |
| Loading | **105%** | 105% |
| Projection basis | **Year of birth** | Year of birth |
| | **CMI_2016 1.0%** | CMI_2015 1.0% |
| Mortality assumption – after retirement (females) | **S2PFA tables** | S2PFA tables |
| Loading | **105%** | 105% |
| Projection basis | **Year of birth** | Year of birth |
| | **CMI_2016 1.0%** | CMI_2015 1.0% |
| Future expected lifetime of current pensioner at age 65: | | |
| Male aged 65 at year end | **86.2** | 86.5 |
| Female aged 65 at year end | **88.0** | 88.5 |
| Future expected lifetime of future pensioner at age 65: | | |
| Male aged 45 at year end | **87.2** | 87.8 |
| Female aged 45 at year end | **89.2** | 89.8 |

## 17 Employee benefits *continued*

**Changes in the present value of assets over the year**

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Fair value of assets at start of the year | **360,069** | 302,239 |
| Interest income | **9,313** | 10,943 |
| Return on assets (excluding amount included in net interest expense) | **2,819** | 59,837 |
| Benefits paid | **(16,937)** | (12,291) |
| Administration expenses | **(583)** | (659) |
| Fair value of assets at end of the year | **354,681** | 360,069 |
| Actual return on assets over the year | **12,132** | 70,922 |

**Changes in the present value of liabilities over the year**

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Liabilities at start of the year | **355,793** | 298,812 |
| Interest cost | **9,207** | 10,829 |
| Remeasurement losses / (gains): | | |
| Actuarial losses arising from changes in financial assumptions | **10,158** | 62,332 |
| Actuarial gains arising from changes in demographic assumptions | **(7,667)** | – |
| Other experience gains | **–** | (3,889) |
| Benefits paid | **(16,937)** | (12,291) |
| Liabilities at end of the year | **350,554** | 355,793 |

**The split of the Scheme's liabilities by category of membership is as follows:**

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| Deferred pensioners | **193,464** | 195,742 |
| Pensioners in payment | **157,090** | 160,051 |
| | **350,554** | 355,793 |
| Average duration of the Scheme's liabilities at the end of the year (in years) | **18** | 18 |

**The major categories of Scheme assets are as follows:**

| | 2017 £'000 | 2016 £'000 |
|---|---|---|
| **Return-seeking assets** | | |
| UK equities | **42,464** | 37,333 |
| Overseas equities | **20,015** | 17,348 |
| Other equity type investments | **41,784** | 39,739 |
| Total return-seeking assets | **104,263** | 94,420 |
| **Other** | | |
| Insured pensioners | **819** | 1,251 |
| Cash | **575** | 7,165 |
| Liability-driven investments | **249,024** | 257,233 |
| Total matching assets | **250,418** | 265,649 |
| Total market value of assets | **354,681** | 360,069 |

The return-seeking assets and LDI assets have quoted prices in active markets. The valuation of the insured pensions has been taken as the value of the corresponding liabilities assessed using the assumptions set out above.

The Scheme has no investments in the Company or in property occupied by the Company.

The Company expects to pay no contributions to the defined benefit section of the Scheme during the year ended 31 December 2018.

## 17 Employee benefits *continued*

### Sensitivity of the liability value to changes in the principal assumptions

If the discount rate were 0.1 per cent higher (lower), the defined benefit section Scheme liabilities would decrease by approximately £6.6 million (increase by £6.9 million) if all the other assumptions remained unchanged.

If the inflation assumption were 0.1 per cent higher (lower), the Scheme liabilities would increase by £2.7 million (decrease by £2.7 million). In this calculation all assumptions related to the inflation assumption have been appropriately adjusted, that is salary, the deferred pension and pension in payment increases. The other assumptions remain unchanged.

If life expectancies were to increase (decrease) by 1 year, the Scheme liabilities would increase by £15.8 million (decrease by £15.6 million) if all the other assumptions remained unchanged.

### Share-based payments

### Marshalls plc 2005 Long Term Incentive Plan ("LTIP")

The LTIP was replaced in 2014 by the Management Incentive Plan ("MIP") and accordingly no further share-based payment awards were made during the year ended 31 December 2017 under the LTIP. The remaining LTIP awards made in respect of the 2014 scheme year were subject to the achievement of a 3-year performance target. The awards vested on 15 March 2017. Details of the performance criteria applicable to 2014 LTIP awards were set out in the Remuneration Report in the 2016 Annual Report.

| | **Weighted average share price at date of grant (pence per share) 2017** | **Number of options 2017** | Weighted average share price at date of grant (pence per share) 2016 | Number of options 2016 |
|---|---|---|---|---|
| Outstanding at 1 January | **172** | **693,479** | 141 | 1,647,146 |
| Lapsed | **172** | **(51,051)** | 180 | (27,108) |
| Exercised | **172** | **(642,428)** | 139 | (926,559) |
| Outstanding at 31 December | **–** | **–** | 172 | 693,479 |

The Company's share price at 31 December 2017 was 454.90 pence.

### Management Incentive Plan ("MIP")

Share-based payment awards have been made during the year in accordance with the rules of the MIP. Full details of the performance criteria and the basis of operation of the MIP are set out in the Annual Remuneration Report on pages 50 to 53.

Equity settled awards are settled by physical delivery of shares. The following equity settled awards have been granted:

| | Number of instruments | £'000 | Date of grant | Vesting period |
|---|---|---|---|---|
| Equity settled awards granted to Directors of Marshalls plc | 318,631 | 820 | 11 April 2014 | 4 years |
| Equity settled awards granted to other employees | 347,801 | 929 | 11 April 2014 | 4 years |
| Equity settled awards granted to Directors of Marshalls plc | 276,140 | 983 | 10 March 2015 | 3 years |
| Equity settled awards granted to other employees | 350,577 | 1,250 | 10 March 2015 | 3 years |
| Equity settled awards granted to Directors of Marshalls plc | 417,093 | 1,476 | 11 March 2016 | 2 years |
| Equity settled awards granted to other employees | 557,129 | 1,985 | 11 March 2016 | 2 years |
| Equity settled awards granted to Directors of Marshalls plc | 283,385 | 1,247 | 15 March 2017 | 4 years |
| Equity settled awards granted to other employees | 380,310 | 1,674 | 15 March 2017 | 4 years |
| | 2,931,066 | 10,364 | | |

Analysis of closing balance (deferred into shares):

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **£'000** | **Shares** | £'000 | Shares |
| Equity settled awards granted to Directors of Marshalls plc | **4,526** | **1,295,249** | 3,144 | 1,074,635 |
| Equity settled awards granted to other employees | **5,838** | **1,635,817** | 3,990 | 1,364,249 |
| | **10,364** | **2,931,066** | 7,134 | 2,438,884 |

## 17 Employee benefits *continued*

### Share-based payments *continued*

### Management Incentive Plan ("MIP") *continued*

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Value £'000** | **Number of options** | Value £'000 | Number of options |
| Outstanding at 1 January | **7,134** | **2,438,884** | 5,504 | 1,693,639 |
| Granted | **2,921** | **663,695** | 2,757 | 942,785 |
| Change in value of notional shares | **1,145** | **19,286** | (106) | 222,456 |
| Element released | **(836)** | **(190,799)** | (1,021) | (419,996) |
| Outstanding at 31 December | **10,364** | **2,931,066** | 7,134 | 2,438,884 |

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

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Awards granted and total expense recognised as employee costs | **5,218** | 3,428 |

Further details in relation to the Directors are set out in the Annual Remuneration Report on pages 50 to 63. Included in the total expense of £5,218,000 (2016: £3,428,000) is an amount of £1,804,000 (2016: £525,000) which is expected to be settled as interim cash payments under the terms of the scheme and which has been included within wages and salaries in Note 3 and accruals in Note 14.

### Employee Bonus Share Plan

A Bonus Share Plan was approved by shareholders in May 2015 under which a number of senior management employees were granted performance related bonuses with an element of this bonus being in the form of shares. The bonus performance criteria are the same as those applicable to the MIP awards and are in relation to the years ended 31 December 2017 and 31 December 2016. The bonus shares take the form of nil-cost options to acquire shares at the end of a 3-year vesting period from the date of grant, and vesting is conditional on continued employment at the end of the vesting period. Awards are made to participants following publication of the Group's year-end results. Awards outstanding at 31 December 2017 were over 328,267 shares (31 December 2016: 55,587). The total expenses recognised for the year arising from share-based payments were £169,000 (2016: £116,000).

### All-employee Sharesave ("SAYE") scheme

On 5 October 2015 options were granted over 1,000,000 shares to employees who had subscribed to the SAYE scheme. The option price is 291 pence, a discount of 20 per cent to the market price on the date of grant. The option is exercisable by relevant employees after a period of 3 years. The total expense recognised for the year arising from share-based payments was £300,000 (2016: £300,000).

### Employee profit sharing scheme

At 31 December 2017 the scheme held 42,328 (2016: 42,328) Ordinary Shares in the Company.

## 18 Provisions

| | Legal and regulatory provisions £'000 |
|---|---|
| At 1 January 2017 | – |
| On acquisition of subsidiary undertaking | 11,840 |
| **At 31 December 2017** | **11,840** |

Provisions have been made for the estimated cost of settlement of certain legal and regulatory matters relating to the CPM Group Limited business acquired during the year, reflecting the Directors' estimate of the likely outflow from settlement of these matters. These provisions are expected to be settled within the next 2 years. As explained in Note 12, the Group has a right of access to the cash paid into an escrow account at the date of acquisition to be used to settle these matters to the extent that a liability crystallises.

## 19 Deferred taxation

### Recognised deferred taxation assets and liabilities

| | Assets | | Liabilities | |
|---|---|---|---|---|
| | **2017 £'000** | 2016 £'000 | **2017 £'000** | 2016 £'000 |
| Property, plant and equipment | **–** | – | **(10,545)** | (10,838) |
| Intangible assets | **–** | – | **(1,351)** | (265) |
| Inventories | **–** | – | **(368)** | (377) |
| Employee benefits | **–** | – | **(702)** | (727) |
| Equity settled share-based payments | **2,775** | 1,821 | **–** | – |
| Other items | **–** | – | **(2,020)** | (1,448) |
| Tax assets / (liabilities) | **2,775** | 1,821 | **(14,986)** | (13,655) |

The March 2016 Budget announced that the UK corporation tax rate will reduce to 17 per cent by 2020. The reduction in the rate to 17 per cent (effective April 2020) was substantively enacted at the balance sheet date. This will reduce the Group's future current tax charge accordingly. The deferred taxation liability at 31 December 2017 has been calculated based on the rate at which the deferred tax is expected to unwind in the future using rates enacted at the balance sheet date.

The deferred taxation liability of £702,000 (2016: £727,000) in relation to employee benefits is in respect of the net surplus for the defined benefit obligations of £4,127,000 (2016: £4,276,000 net surplus) (Note 17) calculated at 17 per cent (2016: 17 per cent).

Deferred tax assets on capital losses and overseas trading losses have not been recognised due to uncertainty around the future use of the losses.

### Movement in temporary differences

### Year ended 31 December 2017

| | 1 January 2017 £'000 | Recognised in income £'000 | Recognised in other comprehensive income £'000 | Recognised in statement of changes in equity £'000 | On acquisition of subsidiary undertaking £'000 | **31 December 2017 £'000** |
|---|---|---|---|---|---|---|
| Property, plant and equipment | (10,838) | 718 | – | – | (425) | **(10,545)** |
| Intangible assets | (265) | 25 | – | – | (1,111) | **(1,351)** |
| Inventories | (377) | 9 | – | – | – | **(368)** |
| Employee benefits | (727) | 81 | (56) | – | – | **(702)** |
| Equity settled share-based payments | 1,821 | 69 | – | 885 | – | **2,775** |
| Other items | (1,448) | (5) | 35 | – | (602) | **(2,020)** |
| | (11,834) | 897 | (21) | 885 | (2,138) | **(12,211)** |

### Year ended 31 December 2016

| | 1 January 2016 £'000 | Recognised in income £'000 | Recognised in other comprehensive income £'000 | Recognised in statement of changes in equity £'000 | 31 December 2016 £'000 |
|---|---|---|---|---|---|
| Property, plant and equipment | (11,334) | 496 | – | – | (10,838) |
| Intangible assets | (283) | 18 | – | – | (265) |
| Inventories | (427) | 50 | – | – | (377) |
| Employee benefits | (617) | 127 | (237) | – | (727) |
| Equity settled share-based payments | 1,316 | 383 | – | 122 | 1,821 |
| Other items | (964) | 77 | (561) | – | (1,448) |
| | (12,309) | 1,151 | (798) | 122 | (11,834) |

Deferred taxation liabilities represent sums that might become payable as tax in future years as a result of transactions that have occurred in the current year. The explanation as to why such liabilities may arise is included in the notes to the tax reconciliation (Note 6).

The deferred tax balances on short-term timing differences are expected to reverse within 1 to 3 years.

Based on the current investment programme of the Group and assuming that current rates of capital allowances on fixed asset expenditure continue into the future, there is little prospect of any significant part of the deferred taxation liability of the Company becoming payable over the next 3 years. It is not realistic to make any projection after a 3-year period.

## 19 Deferred taxation *continued*

### Movement in temporary differences *continued*

The deferred tax liabilities disclosed in the year ended 31 December 2017 include the deferred tax relating to the Group's pension scheme assets. Deferred tax assets on capital losses and overseas trading losses have not been recognised due to uncertainty around the future use of the losses.

## 20 Capital and reserves

### Called-up share capital

| | Issued and paid up | |
|---|---|---|
| | **2017 £'000** | 2016 £'000 |
| **At 1 January and at 31 December** | **49,845** | 49,845 |
| Number of 25 pence Ordinary Shares | **199,378,755** | 199,378,755 |

### Consolidation reserve

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

### Hedging reserve

This represents the gains and losses arising on derivatives used for cash flow hedging, principally from the Group's interest rate swaps, energy price contracts and forward exchange contracts.

### Dividends

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

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| 6.80 pence final dividend (2016: 5.80 pence) per Ordinary Share | **13,436** | 11,460 |
| 4.00 pence supplementary dividend (2016: 3.00 pence) per Ordinary Share | **7,904** | 5,927 |
| | **21,340** | 17,387 |

## 21 Non-controlling interests

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| At 1 January | **1,465** | 1,139 |
| Share of (loss) / profit for the year | **(377)** | 157 |
| Foreign currency transaction differences | **371** | 169 |
| **At 31 December** | **1,459** | 1,465 |

## 22 Acquisition of subsidiary

On 19 October 2017, Marshalls Mono Limited acquired 100 per cent of the issued share capital of CPM Group Limited, a precast concrete manufacturer which specialises in underground water management solutions. The acquisition is in line with the Group's 2020 Strategy. CPM Group Limited operates within the UK and is registered in England and Wales.

The amounts recognised in respect of the identifiable assets acquired and liabilities assumed are as set out in the table below:

| | **Provisional fair values acquired £'000** |
|---|---|
| Land and buildings | **8,437** |
| Plant, machinery and vehicles | **7,639** |
| Identifiable intangible assets | **7,233** |
| Inventories | **4,580** |
| Trade and other receivables | **12,334** |
| Cash and cash equivalents | **(2,955)** |
| Trade and other payables | **(16,931)** |
| Provisions | **(11,840)** |
| Borrowings | **(3,407)** |
| Corporation tax | **(1,825)** |
| Deferred tax | **(2,138)** |
| Total identifiable assets | **1,127** |
| Goodwill | **25,145** |
| Initial cash consideration | **26,272** |
| Monies paid into escrow | **12,000** |
| Total cash payments in connection with the acquisition | **38,272** |
| **Analysis of amounts paid in connection with the acquisition** | |
| Total cash payments | **38,272** |
| Net borrowings acquired | **2,955** |
| Total cash outflow in connection with the acquisition | **41,227** |

Initial cash consideration paid to the vendors was £26,272,000 and, in addition, a further £12,000,000 was paid into an escrow account in relation to certain ongoing legal and regulatory matters identified during the course of due diligence carried out prior to concluding the acquisition. Provisions of £11,840,000 have been recorded at the date of acquisition, for the estimated liabilities arising from concluding these ongoing matters (see Note 18). The Group has a right of reimbursement of amounts held in an escrow account to the extent that any liability crystallises in respect of these ongoing legal and regulatory matters to enable the Group to settle these liabilities, up to the full value of the £12,000,000 held in escrow and consequently a reimbursement asset of £12,000,000 has been recognised within other debtors. To the extent that any liabilities arising from these ongoing legal and regulatory matters are resolved at a lower amount than the escrow balances, the excess balance remaining in escrow is payable to the vendors as additional consideration.

Due to their contractual dates, the fair value of the receivables (shown above) approximate to the gross contractual amounts receivable. The amount of gross contractual receivables not expected to be recovered is immaterial.

The goodwill arising from the acquisition represents the opportunity to grow by utilising the capabilities and technical expertise of the acquired workforce and by developing synergistic opportunities.

The goodwill arising from the acquisition is not expected to be deductible for income tax purposes.

Transaction costs incurred on acquisition were £837,000, and these have been fully expensed in the period (Note 3).

CPM Group Limited contributed revenue of £9,017,000 and profit of £749,000 to the Group's profit for the period between the date of acquisition and the balance sheet date.

If the acquisition of CPM Group Limited had been completed on the first day of the financial year, Group revenue for the period would have been £485,532,000 and Group profit before tax would have been £56,255,000.

# Notes to the Consolidated Financial Statements *continued*

## 23 Analysis of net debt

| | 1 January 2017 £'000 | Cash flow £'000 | On acquisition of subsidiary undertaking £'000 | Other changes £'000 | **31 December 2017 £'000** |
|---|---|---|---|---|---|
| Cash at bank and in hand | 20,681 | 1,925 | (2,955) | 194 | **19,845** |
| Debt due after 1 year | (14,975) | (25,413) | (2,847) | (648) | **(43,883)** |
| Finance leases | (293) | 594 | (560) | – | **(259)** |
| | 5,413 | (22,894) | (6,362) | (454) | **(24,297)** |

**Reconciliation of net cash flow to movement in net debt**

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Net increase / (decrease) in cash equivalents | **1,925** | (4,680) |
| Cash (inflow) / outflow from decrease in debt and lease financing | **(24,819)** | 23,831 |
| On acquisition of subsidiary undertaking | **(6,362)** | – |
| Effect of exchange rate fluctuations | **(454)** | (2,276) |
| **Movement in net debt in the year** | **(29,710)** | 16,875 |
| **Net debt at 1 January** | **5,413** | (11,462) |
| **Net debt at 31 December** | **(24,297)** | 5,413 |

## 24 Changes in liabilities arising from financing activities

The table below details changes in the Group's liabilities arising from financing activities, including both cash and non-cash changes. Liabilities arising from financing activities are those for which cash flows were, or future cash flows will be, classified in the Group's Consolidated Cash Flow Statement as cash flows from financing activities.

| | | | Non-cash changes | | |
|---|---|---|---|---|---|
| | 1 January 2017 | Financing cash flows (i) | Acquisition of subsidiary (Note 22) | Other changes (ii) | **31 December 2017** |
| Bank loans (Note 15) | (14,975) | (25,413) | (2,847) | (648) | **(43,883)** |
| Finance lease liabilities (Note 15) | (293) | 594 | (560) | – | **(259)** |
| Interest rate swaps fair value hedging or economically hedging financing liabilities (Note 16) | 657 | (385) | – | 175 | **447** |
| Total liabilities from financing activities | (14,611) | (25,204) | (3,407) | (473) | **(43,695)** |

(i) The cash flows from bank loans, loans from related parties and other borrowings make up the net amount of proceeds from borrowings and repayments of borrowings in the cash flow statement.

(ii) Exchange adjustments.

## 25 Operating leases

The Group had non-cancellable total minimum lease payments to be paid in respect of operating leases on property, plant, machinery and vehicles as follows:

| **31 December 2017** | Total £'000 | 6 months or less £'000 | 6 – 12 months £'000 | 1 – 2 years £'000 | 2 – 5 years £'000 | More than 5 years £'000 |
|---|---|---|---|---|---|---|
| Expiring: | | | | | | |
| Within 1 year | **1,758** | **1,173** | **585** | **–** | **–** | **–** |
| Between 1 and 5 years | **30,995** | **4,950** | **4,922** | **9,137** | **11,984** | **2** |
| In more than 5 years | **32,463** | **1,158** | **1,152** | **2,234** | **6,927** | **20,992** |
| | **65,216** | **7,281** | **6,659** | **11,371** | **18,911** | **20,994** |

## 25 Operating leases *continued*

| 31 December 2016 | Total £'000 | 6 months or less £'000 | 6 – 12 months £'000 | 1 – 2 years £'000 | 2 – 5 years £'000 | More than 5 years £'000 |
|---|---|---|---|---|---|---|
| Expiring: | | | | | | |
| Within 1 year | 1,185 | 1,021 | 164 | – | – | – |
| Between 1 and 5 years | 33,973 | 5,577 | 5,549 | 9,704 | 13,140 | 3 |
| In more than 5 years | 35,838 | 1,203 | 1,197 | 2,471 | 8,759 | 22,208 |
| | 70,996 | 7,801 | 6,910 | 12,175 | 21,899 | 22,211 |

The total minimum lease payments under non-cancellable operating leases (above) comprise property of £30,236,000 (2016: £27,606,000) and plant, machinery and vehicles of £34,980,000 (2016: £43,390,000).

Certain leased properties have been sublet by the Group. Sublease payments of £306,020 (2016: £200,020) are expected to be received during the following financial year. An amount of £345,446 (2016: £246,186) was recognised as income in the Consolidated Income Statement within net operating costs in respect of subleases.

## 26 Contingencies

Royal Bank of Scotland plc has issued, on behalf of Marshalls plc, the following irrevocable letters of credit relating to the Group's cap on self insurance for employer's liability and vehicle insurance:

| Beneficiary | Amount | Period | Purpose |
|---|---|---|---|
| M S Amlin Limited | £675,000 | 23 Dec 2011 to 30 Oct 2018 | Employer's liability |
| Aviva Insurance Limited | £350,000 | 19 Mar 2014 to 30 Oct 2018 | Vehicle insurance |
| M S Amlin Limited | £350,000 | 30 Oct 2016 to 30 Oct 2018 | Vehicle insurance |

FINANCIAL STATEMENTS

## 27 Related parties

### Identity of related parties

The Group has a related party relationship with its Directors.

### Transactions with key management personnel

Other than the Directors, there are no senior managers in the Group who are relevant for establishing that Marshalls plc has the appropriate expertise and experience for the management of its business.

Directors of the Company and their immediate relatives control 0.1804 per cent (2016: 0.0881 per cent) of the voting shares of the Company.

In addition to their salaries and pension allowances, the Group also provides non-cash benefits to Directors. Further details in relation to Directors are disclosed in the Annual Remuneration Report on pages 50 to 63.

## 28 Accounting estimates and judgements

Management discussed with the Audit Committee the development, selection and disclosure of the Group's critical accounting policies and estimates and the application of these policies and estimates. The accounting policies are set out in Note 1 on pages 78 to 87. As stated in the accounting policies, revenue is disclosed net of rebates. Whilst the Directors do not regard the determination of accruals for rebates as a key area of estimation uncertainty, the estimation of appropriate accruals for rebates requires commercial assessment. Note 11 contains details of the Group's inventory. Whilst not considered by the Directors to be a key source of estimation uncertainty, the carrying value of the Group's finished goods inventory has been reviewed using commercial judgement with regard to the assessment of the appropriate level of provisioning against inventory obsolescence and for net realisable value. The Directors consider the following to be the only key source of estimation uncertainty.

- Note 17 contains information about the principal actuarial assumptions used in the determination of defined benefit pension obligations. These key assumptions include discount rates, the expected return on net assets, inflation rates and mortality rates and have been determined following advice received from an independent qualified actuary. Sensitivity analysis is disclosed in Note 17 on page 105.

The critical accounting judgements applied in the preparation of the Financial Statements are:

- Note 2 contains information about the assumptions and judgements made relating to the identification of operating segments for the Group as defined in IFRS 8 *"Operating Segments"*; and
- Note 22 contains information relating to the acquisition of CPM Group Limited. Judgement was applied in determining the fair value adjustments.

# Parent Company Statement of Changes in Equity

**for the year ended 31 December 2017**

| | Share capital £'000 | Share premium account £'000 | Own shares £'000 | Capital redemption reserve £'000 | Equity reserve £'000 | Retained earnings £'000 | Total equity £'000 |
|---|---|---|---|---|---|---|---|
| **Current year** | | | | | | | |
| At 1 January 2017 | **49,845** | **22,695** | **(3,622)** | **75,394** | **5,377** | **118,079** | **267,768** |
| **Total comprehensive loss for the year** | | | | | | | |
| **Loss for the financial year** | **–** | **–** | **–** | **–** | **–** | **(7,755)** | **(7,755)** |
| **Total comprehensive loss for the year** | **–** | **–** | **–** | **–** | **–** | **(7,755)** | **(7,755)** |
| **Transactions with owners, recorded directly in equity** | | | | | | | |
| **Contributions by and distributions to owners** | | | | | | | |
| Share-based payments | **–** | **–** | **–** | **–** | **2,278** | **1,603** | **3,881** |
| Deferred tax on share-based payments | **–** | **–** | **–** | **–** | **365** | **–** | **365** |
| Dividends to equity shareholders | **–** | **–** | **–** | **–** | **–** | **(24,107)** | **(24,107)** |
| Purchase of own shares | **–** | **–** | **(1,210)** | **–** | **–** | **–** | **(1,210)** |
| Disposal of own shares | **–** | **–** | **2,473** | **–** | **–** | **(2,473)** | **–** |
| **Total contributions by and distributions to owners** | **–** | **–** | **1,263** | **–** | **2,643** | **(24,977)** | **(21,071)** |
| **Total transactions with owners of the Company** | **–** | **–** | **1,263** | **–** | **2,643** | **(32,732)** | **(28,826)** |
| **At 31 December 2017** | **49,845** | **22,695** | **(2,359)** | **75,394** | **8,020** | **85,347** | **238,942** |

There were no items of other comprehensive income / (expense) in the year other than the loss for the financial year recorded above.

| | Share capital £'000 | Share premium account £'000 | Own shares £'000 | Capital redemption reserve £'000 | Equity reserve £'000 | Retained earnings £'000 | Total equity £'000 |
|---|---|---|---|---|---|---|---|
| **Prior year** | | | | | | | |
| At 1 January 2016 | 49,845 | 22,695 | (5,529) | 75,394 | 4,122 | 144,836 | 291,363 |
| **Total comprehensive loss for the year** | | | | | | | |
| **Loss for the financial year** | – | – | – | – | – | (6,030) | (6,030) |
| **Total comprehensive loss for the year** | – | – | – | – | – | (6,030) | (6,030) |
| **Transactions with owners, recorded directly in equity** | | | | | | | |
| **Contributions by and distributions to owners** | | | | | | | |
| Share-based payments | – | – | – | – | 1,195 | 1,389 | 2,584 |
| Deferred tax on share-based payments | – | – | – | – | 60 | – | 60 |
| Dividends to equity shareholders | – | – | – | – | – | (19,034) | (19,034) |
| Purchase of own shares | – | – | (1,175) | – | – | – | (1,175) |
| Disposal of own shares | – | – | 3,082 | – | – | (3,082) | – |
| **Total contributions by and distributions to owners** | – | – | 1,907 | – | 1,255 | (20,727) | (17,565) |
| **Total transactions with owners of the Company** | – | – | 1,907 | – | 1,255 | (26,757) | (23,595) |
| **At 31 December 2016** | 49,845 | 22,695 | (3,622) | 75,394 | 5,377 | 118,079 | 267,768 |

There were no items of other comprehensive income / (expense) in the year other than the loss for the financial year recorded above.

# Company Balance Sheet
**at 31 December 2017**

| | Notes | 2017 £'000 | 2016 £'000 |
|---|---|---|---|
| **Fixed assets** | | | |
| Investments | 32 | **345,785** | 343,507 |
| Deferred taxation assets | 33 | **1,492** | 1,010 |
| | | **347,277** | 344,517 |
| **Current assets** | | | |
| Debtors | 34 | **1,602** | 1,257 |
| **Current liabilities** | | | |
| Creditors | 35 | **(109,937)** | (78,006) |
| **Net current liabilities** | | **(108,335)** | (76,749) |
| **Net assets** | | **238,942** | 267,768 |
| **Capital and reserves** | | | |
| Called-up share capital | 36 | **49,845** | 49,845 |
| Share premium account | | **22,695** | 22,695 |
| Own shares | | **(2,359)** | (3,622) |
| Capital redemption reserve | | **75,394** | 75,394 |
| Equity reserve | | **8,020** | 5,377 |
| Profit and loss account | | **85,347** | 118,079 |
| **Equity shareholders' funds** | | **238,942** | 267,768 |

The Company reported a loss for the financial year ended 31 December 2017 of £7,755,000 (2016: £6,030,000).

Approved at a Directors' meeting on 14 March 2018.

On behalf of the Board:

**Martyn Coffey**
**Chief Executive**

**Jack Clarke**
**Finance Director**

The Notes on pages 114 to 119 form part of these Company Financial Statements.

# Notes to the Company Financial Statements

## 29 Accounting policies

The following paragraphs summarise the main accounting policies of the Company, which have been applied consistently in dealing with items which are considered material in relation to the Company's Financial Statements. The Company is exempt from the requirement to give its own disclosures as the entity forms part of the Consolidated Financial Statements of Marshalls plc, which has included disclosures under IFRS 7 *"Financial Instruments: Disclosures".*

**(a) Authorisation of Financial Statements and Statement of Compliance with FRS 101**

The Parent Company Financial Statements of Marshalls plc for the year ended 31 December 2017 were authorised for issue by the Board of Directors on 14 March 2018. Marshalls plc is a public limited company that is incorporated, domiciled and has its registered office in England and Wales. The Company's Ordinary Shares are publicly traded on the London Stock Exchange and the Company is not under the control of any single shareholder.

These Financial Statements were prepared in accordance with Financial Reporting Standard 101 *"Reduced Disclosure Framework"* ("FRS 101").

No profit and loss account is presented by the Company as permitted by Section 408 of the Companies Act 2006.

**(b) Basis of preparation**

The Company has adopted FRS 101 from the UK Generally Accepted Accounting Practice for all periods presented.

The accounting policies which follow set out those policies which apply in preparing the Financial Statements for the year ended 31 December 2017.

In these Financial Statements, the Company has applied the exemptions available under FRS 101 in respect of the following disclosures:

- the requirements of paragraphs 45(b) and 46 – 52 of IFRS 2 "*Share-based Payments";*
- the requirement of IFRS 7 "*Financial Instruments: Disclosures";*
- the requirement of paragraphs 91 – 99 of IFRS 13 *"Fair Value Measurement"*;
- the requirement in paragraph 38 of IAS 1 *"Presentation of Financial Statements"* to present comparative information in respect of: paragraph 79(a)(iv) of IAS 1;
- the requirements of paragraphs 10(d), 10(f), 16, 39(c), 40A, 40B, 40C, 40D, 111 and 134 – 136 of IAS 1 *"Presentation of Financial Statements"*;
- the requirements of IAS 7 *"Statement of Cash Flows"*;
- the requirements of paragraphs 30 and 31 of IAS 8 *"Accounting Policies, Changes in Accounting Estimates and Errors"*;
- the requirements of paragraph 17 of IAS 24 *"Related Party Disclosures"*;
- the requirements in IAS 24 *"Related Party Disclosures"* to disclose related party transactions entered into between 2 or more members of a group, provided that any subsidiary which is a party to the transaction is wholly owned by such a member; and
- the requirements of paragraphs 134(d) – 134(f) and 135(c) – 135(e) of IAS 36 *"Impairment of Assets".*

The Company also intends to take advantage of these exemptions in the Financial Statements to be issued in the following year. Objections may be served in the Company by shareholders holding in aggregate 5 per cent or more of the total allocated shares in the Company. Where required, additional disclosures are given in the Consolidated Financial Statements.

**(c) Investments**

Fixed asset investments in subsidiaries and associates are shown at cost less provision for impairment. The Directors consider annually whether a provision against the value of investments on an individual basis is required.

**(d) Share capital**

**(i) Share capital**

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

**(ii) Dividends**

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

**(e) Pension schemes**

**(i) Defined benefit scheme**

The Company participates in a Group-wide pension scheme providing benefits based on final pensionable pay. The defined benefit section of the scheme was closed to future service accrual in July 2006.

The assets of the scheme are held separately from those of the Company. The defined benefit cost and contributions payable are borne by Marshalls Group Limited and, therefore, the defined benefit surplus or deficit is recorded in Marshalls Group Limited. Full details are provided in Note 17 on pages 103 to 106.

**(ii) Defined contribution scheme**

Obligations for contributions to defined contribution schemes are recognised as an expense as incurred.

## 29 Accounting policies *continued*

### (f) Share-based payment transactions

The Company enters into equity settled share-based payment transactions with its employees. In particular, annual awards are made to employees under the Company's Management Incentive Plan ("MIP") and the Employee Bonus Share Plan ("BSP").

These schemes allow employees to acquire shares in Marshalls plc. The fair value of options granted is recognised as an employee expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. Where appropriate, the fair value of the options granted is measured using the Black-Scholes option valuation model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

Current tax relief is available as shares vest based on the value at the date of vesting. A deferred tax asset is recognised at grant date based on the number of shares expected to be issued, at the value at which they are expected to be issued, proportioned in line with the vesting period.

### (g) Own shares held by the Employee Benefit Trust

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

### (h) Trade and other payables

Trade and other payables are stated at nominal amount (discounted if material).

### (i) Income tax

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

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

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

## 30 Operating costs

The audit fee for the Company was £25,000 (2016: £20,000). This is in respect of the audit of the Financial Statements. Fees paid to the Company's auditor for services other than the statutory audit of the Company are not disclosed in the Notes to the Company Financial Statements since the consolidated accounts of the Group are required to disclose non-audit fees on a consolidated basis.

Details of Directors' remuneration, share options, long-term incentive plans and Directors' pension entitlements are disclosed on pages 50 to 63 of the Annual Remuneration Report.

The average monthly number of employees of Marshalls plc (including Executive Directors) in the year ended 31 December 2017 was 178 (2016: 95). The personnel costs for the majority of these employees are borne by Marshalls Group Limited. The personnel costs charged to Marshalls plc in the year were £5,090,000 (2016: £4,071,000) in relation to 19 employees (2016: 17), including the Directors.

## 31 Ordinary dividends: equity shares

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Pence per share** | **£'000** | Pence per share | £'000 |
| 2016 final: paid 30 June 2017 | **5.80** | **11,460** | 4.75 | 9,369 |
| 2016 supplementary: paid 30 June 2017 | **3.00** | **5,927** | 2.00 | 3,945 |
| 2016 interim: paid 6 December 2017 | **3.40** | **6,718** | 2.90 | 5,720 |
| | **12.20** | **24,105** | 9.65 | 19,034 |

# Notes to the Company Financial Statements *continued*

## 31 Ordinary dividends: equity shares *continued*

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

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| 2017 final: 6.80 pence (2016: 5.80 pence) per Ordinary Share | **13,436** | 11,460 |
| 2017 supplementary: 4.00 pence (2016: 3.00 pence) per Ordinary Share | **7,904** | 5,927 |
| | **21,340** | 17,387 |

## 32 Investments

| | £'000 |
|---|---|
| At 1 January 2017 | 343,507 |
| Additions | 2,278 |
| **At 31 December 2017** | **345,785** |

Investments comprise shares in the subsidiary undertaking, Marshalls Group Limited. The Directors have considered the carrying value of the Company's investments and are satisfied that no provision is required.

The increase in the year of £2,278,000 represents adjustments to the number of shares expected to vest in respect of share-based payment awards granted to employees of Marshalls Group Limited.

Pursuant to Sections 409 and 410(2) of the Companies Act 2006, the principal subsidiary undertakings of Marshalls plc at 31 December 2017 are set out below.

| Subsidiaries | Principal activities | Class of share | % ownership |
|---|---|---|---|
| Alton Glasshouses Limited | Non-trading | Ordinary | 100 |
| Bollards Direct Limited | Non-trading | Ordinary | 100 |
| Capability Brown Garden Centres Limited | Non-trading | Ordinary | 100 |
| Capability Brown Landscaping Limited | Non-trading | Ordinary | 100 |
| Classical Flagstones Limited | Non-trading | Ordinary | 100 |
| CPM Group Limited | Landscape products manufacturer | Ordinary | 100 |
| Dalestone Concrete Products Limited | Non-trading | Ordinary | 100 |
| Locharbriggs Sandstone Limited | Non-trading | Ordinary | 100 |
| Lloyds Quarries Limited | Non-trading | Ordinary | 100 |
| Marshalls Building Materials Limited | Non-trading | Ordinary | 100 |
| Marshalls Building Products Limited | Property management | Ordinary | 100 |
| Marshalls Concrete Products Limited | Non-trading | Ordinary | 100 |
| Marshalls Directors Limited | Non-trading | Ordinary | 100 |
| Marshalls Dormant No. 30 Limited | Non-trading | Ordinary | 100 |
| Marshalls Dormant No. 31 Limited | Non-trading | Ordinary | 100 |
| Marshalls EBT Limited[1] | Non-trading | Ordinary | 100 |
| Marshalls Estates Limited | Non-trading | Ordinary | 100 |
| Marshalls Group Limited[1] | Intermediate holding company | Ordinary | 100 |
| Marshalls Landscape Products Limited | Non-trading | Ordinary | 100 |
| Marshalls Landscape Products FZE | Landscape products supplier | Ordinary | 100 |
| Marshalls Landscape Products (North America) Inc. | Landscape products supplier | Ordinary | 100 |
| Marshalls Mono Limited | Landscape products manufacturer and supplier and quarry owner supplying a wide variety of paving, street furniture and natural stone products | Ordinary | 100 |
| Marshalls Natural Stone Limited | Non-trading | Ordinary | 100 |
| Marshalls NV | Landscape products manufacturer and supplier | Ordinary | 66.7 |
| Marshalls Profit Sharing Scheme Limited | Non-trading | Ordinary | 100 |
| Marshalls Properties Limited | Property management | Ordinary | 100 |
| Marshalls Register Limited | Non-trading | Ordinary | 100 |
| Marshalls Stone Products Limited | Non-trading | Ordinary | 100 |

## 32 Investments *continued*

| Subsidiaries | Principal activities | Class of share | % ownership |
|---|---|---|---|
| Marshalls Street Furniture Limited | Non-trading | Ordinary | 100 |
| Ollerton Limited | Non-trading | Ordinary | 100 |
| Panablok (UK) Limited | Non-trading | Ordinary | 100 |
| Paver Systems (Carluke) Limited | Non-trading | Ordinary | 100 |
| Paver Systems Limited | Non-trading | Ordinary | 100 |
| Premier Mortars Limited | Non-trading | Ordinary | 100 |
| Quarryfill Limited | Non-trading | Ordinary | 100 |
| Rhino Protec Limited | Non-trading | Ordinary | 100 |
| Robinson Associates Stone Consultants Limited | Non-trading | Ordinary | 100 |
| Robinsons Greenhouses Limited | Non-trading | Ordinary | 100 |
| Rockrite Limited | Non-trading | Ordinary | 100 |
| S Marshall & Sons Limited | Non-trading | Ordinary | 100 |
| Scenic Blue Limited | Non-trading | Ordinary | 100 |
| Scenic Blue Landscape Franchise Limited | Non-trading | Ordinary | 100 |
| Scenic Blue (UK) Limited | Non-trading | Ordinary | 100 |
| Stancliffe Stone Company Limited | Non-trading | Ordinary | 100 |
| Stoke Hall Quarry Limited[1] | Non-trading | Ordinary | 100 |
| Stone Shippers Limited | Non-trading | Ordinary | 100 |
| Stonemarket (Concrete) Limited | Non-trading | Ordinary | 100 |
| Stonemarket Limited | Non-trading | Ordinary | 100 |
| The Great British Bollard Company Limited | Non-trading | Ordinary | 100 |
| The Stancliffe Group Limited | Non-trading | Ordinary | 100 |
| The Yorkshire Brick Co. Limited | Non-trading | Ordinary | 100 |
| Town & Country Paving Limited | Non-trading | Ordinary | 100 |
| Urban Engineering Limited | Non-trading | Ordinary | 100 |
| Woodhouse Group Limited | Non-trading | Ordinary | 100 |
| Woodhouse UK Limited | Non-trading | Ordinary | 100 |
| Xiamen Marshalls Import Export Company Limited | Sourcing and distribution of natural stone products | Ordinary | 100 |

1 Held by Marshalls plc. All others held by subsidiary undertakings.

Marshalls NV is largely dependent on the continued support of Marshalls Mono Limited, which has indicated that it intends to continue providing this support for the foreseeable future.

With the exception of Marshalls NV, Xiamen Marshalls Import Export Company Limited, Marshalls Landscape Products (North America) Inc. and Marshalls Landscape Products FZE, all the companies operate within the United Kingdom and are registered in England and Wales at the following address: Landscape House, Premier Way, Lowfields Business Park, Elland, HX5 9HT. Marshalls NV is registered in Belgium. Xiamen Marshalls Import Export Company Limited is registered in China, Marshalls Landscape Products (North America) Inc. is registered in the USA and Marshalls Landscape Products FZE is registered in Dubai. The reflective registered offices are:

Paver Systems Limited and Paver Systems (Carluke) Limited
Roadmeetings, Carluke, Lanarkshire, ML8 4QG

Locharbriggs Sandstone Limited
Locharbriggs, Dumfries, Dumfriesshire, DG1 1QS

Marshalls Landscape Products FZE
TPOFCB00WS58, Jebel Ali, Dubai, United Arab Emirates

Marshalls Landscape Products (North America) Inc.
1209 Orange Street, Wilmington, County of New Castle, Delaware 19801, USA

Marshalls NV
Nieuwstraat 4, 2840 Rumst, Belgium

Xiamen Marshalls Import Export Company Ltd.
12 A4, Xiangyu Building, No. 22 4th Xiangxing Road, Xiangyu Free Trade Zone, Xiamen, China

# Notes to the Company Financial Statements *continued*

## 33 Deferred taxation

### Recognised deferred taxation assets and liabilities

| | Assets | | Liabilities | |
|---|---|---|---|---|
| | **2017 £'000** | 2016 £'000 | **2017 £'000** | 2016 £'000 |
| Equity settled share-based payments | **1,492** | 1,010 | **–** | – |

### Movement in temporary differences

| | 1 January 2017 £'000 | Recognised in income £'000 | Recognised in other comprehensive income £'000 | **31 December 2017 £'000** |
|---|---|---|---|---|
| Equity settled share-based payments | 1,010 | 117 | 365 | **1,492** |

## 34 Debtors

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Corporation tax | **1,602** | 1,257 |

No debtors were due after more than 1 year.

## 35 Creditors

| | **2017 £'000** | 2016 £'000 |
|---|---|---|
| Amounts owed to subsidiary undertakings | **109,937** | 78,006 |

## 36 Capital and reserves

### Called-up share capital

As at 31 December 2017, the issued and fully paid up share capital was as follows:

| | Issued and paid up | | | |
|---|---|---|---|---|
| | **2017 Number** | **2017 nominal value £'000** | 2016 Number | 2016 nominal value £'000 |
| **At 31 December** | **199,378,755** | **49,845** | 199,378,755 | 49,845 |

### Equity reserve

The equity reserve represents the number of shares expected to vest in respect of share-based payment awards granted to employees of the Company.

## 37 Capital and leasing commitments

The Company had no capital or leasing commitments at 31 December 2017 or 31 December 2016.

## 38 Bank facilities

The Group's banking arrangements are in respect of Marshalls plc, Marshalls Group Limited and Marshalls Mono Limited with each company being nominated borrowers. The operational banking activities of the Group are undertaken by Marshalls Group Limited and the Group's bank debt is largely included in Marshalls Group Limited's balance sheet.

## 39 Contingent liabilities

Royal Bank of Scotland plc has issued, on behalf of Marshalls plc, the following irrevocable letters of credit relating to the Group's cap on self insurance for employer's liability and vehicle insurance:

| Beneficiary | Amount | Period | Purpose |
|---|---|---|---|
| M S Amlin Limited | £675,000 | 23 Dec 2011 to 30 Oct 2018 | Employer's liability |
| Aviva Insurance Limited | £350,000 | 19 Mar 2014 to 30 Oct 2018 | Vehicle insurance |
| M S Amlin Limited | £350,000 | 30 Oct 2016 to 30 Oct 2018 | Vehicle insurance |

## 40 Pension scheme

The Company is the sponsoring employer of the Marshalls plc Pension Scheme (the "Scheme") which has both a defined benefit and a defined contribution section. The assets of the Scheme are held in separately managed funds which are independent of the Group's finances.

Full details of the Scheme are provided in Note 17. The Company is unable to identify its share of the Scheme assets and liabilities on a consistent and reasonable basis.

The latest funding valuation of the defined benefit section of the Scheme was carried out as at 5 April 2015 and was updated for the purposes of the 31 December 2017 Financial Statements by a qualified independent actuary.

## 41 Accounting estimates and judgements

The preparation of the Financial Statements requires management to make judgements, estimates and assumptions. Although these judgements and estimates are based on management's best knowledge, actual results ultimately may differ from these estimates.

The key sources of estimation uncertainty that have a significant risk of causing material adjustments to the carrying value of assets and liabilities within the next financial year are disclosed below.

Note 17 contains information about the principal actuarial assumptions used in the determination of defined benefit pension obligations. These key assumptions include discount rates, the expected return on net assets, inflation rates and mortality rates and have been determined following advice received from an independent qualified actuary. Sensitivity analysis is disclosed in Note 17 on page 105.

Note 33 contains details of the Company's deferred taxation. Liabilities recognised are determined by reference to the likelihood of settlement and the likelihood that assets are received is based on assumptions of future actions.

## 42 Related parties

Related party relationships exist with other members of the Group. All operating costs are borne by Marshalls Group Limited and are recharged to Marshalls plc in respect of specifically attributable costs. All related party transactions were made on terms equivalent to those that prevail in arm's length transactions.

# Financial History – Consolidated Group

| | Year ended 31 December 2013[1] £'000 | Year ended 31 December 2014[1] £'000 | Year ended 31 December 2015 £'000 | Year ended 31 December 2016 £'000 | **Year ended 31 December 2017 £'000** |
|---|---|---|---|---|---|
| **Consolidated Income Statement** | | | | | |
| Revenue | 307,390 | 358,516 | 386,204 | 396,922 | **430,194** |
| Net operating costs | (291,300) | (333,211) | (348,752) | (349,283) | **(376,755)** |
| Operating profit | 16,090 | 25,305 | 37,452 | 47,639 | **53,439** |
| Financial income and expenses (net) | (3,064) | (2,884) | (2,174) | (1,593) | **(1,388)** |
| Profit before tax | 13,026 | 22,421 | 35,278 | 46,046 | **52,051** |
| Income tax expense | (67) | (4,198) | (7,387) | (8,539) | **(9,925)** |
| Profit for the financial year before post-tax profit of discontinued operations | 12,959 | 18,223 | 27,891 | 37,507 | **42,126** |
| Post-tax profit of discontinued operations | 503 | – | – | – | **–** |
| Profit for the financial year | 13,462 | 18,223 | 27,891 | 37,507 | **42,126** |
| Profit for the year attributable to: | | | | | |
| Equity shareholders of the Parent | 14,096 | 19,857 | 28,149 | 37,350 | **42,503** |
| Non-controlling interests | (634) | (1,634) | (258) | 157 | **(377)** |
| | 13,462 | 18,223 | 27,891 | 37,507 | **42,126** |
| EBITA[2] | 17,028 | 26,536 | 38,774 | 48,648 | **54,581** |
| EBITDA[2] | 30,227 | 38,518 | 51,828 | 60,794 | **67,895** |
| Earnings per share (pence): | | | | | |
| Basic (continuing operations) | 6.94 | 10.13 | 14.32 | 18.95 | **21.52** |
| Basic (total operations) | 7.20 | 10.13 | 14.32 | 18.95 | **21.52** |
| Dividends per share (pence) – IFRS | 5.25 | 5.50 | 6.25 | 9.65 | **12.20** |
| Dividend cover (times) – IFRS (continuing) | 1.3 | 1.8 | 2.3 | 2.0 | **1.80** |
| Dividends per share (pence) – traditional | 5.25 | 6.00 | 7.00 | 8.70 | **10.20** |
| Dividends per share (pence) – supplementary | – | – | 2.00 | 3.00 | **4.00** |
| Dividend cover (times) – traditional (continuing) | 1.3 | 1.7 | 1.6 | 1.6 | **1.5** |
| Year-end share price (pence) | 176.25 | 234.0 | 325.0 | 292.5 | **454.9** |
| Tax rate (%) | 0.5 | 18.7 | 20.9 | 18.5 | **19.1** |

1 The comparatives have been restated in respect of discontinued operations.

2 EBITA is defined as earnings before interest, tax and amortisation of intangibles. EBITDA is defined as earnings before interest, tax and amortisation of intangibles and depreciation.

| | 2013 £'000 | 2014 £'000 | 2015 £'000 | 2016 £'000 | **2017 £'000** |
|---|---|---|---|---|---|
| **Consolidated Balance Sheet** | | | | | |
| Non-current assets | 198,082 | 195,951 | 192,815 | 193,393 | **249,074** |
| Current assets | 120,832 | 132,593 | 137,017 | 139,685 | **166,372** |
| Total assets | 318,914 | 328,544 | 329,832 | 333,078 | **415,446** |
| Current liabilities | (74,137) | (80,969) | (87,071) | (87,068) | **(106,886)** |
| Non-current liabilities | (69,345) | (65,681) | (50,043) | (28,889) | **(70,933)** |
| Net assets | 175,432 | 181,894 | 192,718 | 217,121 | **237,627** |
| Net borrowings | (35,569) | (30,480) | (11,462) | 5,413 | **(24,297)** |
| Gearing ratio | 20.3% | 16.8% | 6.0% | (2.5%) | **10.2%** |

# Shareholder Information

## Shareholder analysis at 31 December 2017

| Size of shareholding | Number of shareholders | % | Number of Ordinary Shares | % |
|---|---|---|---|---|
| 1 to 500 | 1,881 | 45.20 | 272,227 | 0.14 |
| 501 to 1,000 | 497 | 11.94 | 373,235 | 0.19 |
| 1,001 to 2,500 | 621 | 14.93 | 1,052,733 | 0.53 |
| 2,501 to 5,000 | 416 | 10.00 | 1,473,397 | 0.74 |
| 5,001 to 10,000 | 252 | 6.06 | 1,754,658 | 0.88 |
| 10,001 to 25,000 | 156 | 3.75 | 2,486,355 | 1.25 |
| 25,001 to 100,000 | 152 | 3.65 | 7,885,799 | 3.95 |
| 100,001 to 250,000 | 68 | 1.63 | 10,579,728 | 5.30 |
| 250,001 to 500,000 | 36 | 0.87 | 12,784,570 | 6.41 |
| 500,001 and above | 82 | 1.97 | 160,716,053 | 80.61 |
| | 4,161 | 100.00 | 199,378,755 | 100.00 |

## Financial calendar

| | | |
|---|---|---|
| Preliminary announcement of results for the year ended 31 December 2017 | Announced | 14 March 2018 |
| Annual General Meeting | | 9 May 2018 |
| Final dividend for the year ended 31 December 2017 | Payable | 29 June 2018 |
| Half-yearly results for the year ending 31 December 2018 | Announcement | 16 August 2018 |
| Half-yearly dividend for the year ending 31 December 2018 | Payable | 5 December 2018 |
| Results for the year ending 31 December 2018 | Announcement | Early March 2019 |

## Advisers

**Stockbrokers**
Peel Hunt
Numis Securities Limited

**Auditor**
Deloitte LLP

**Legal advisers**
Herbert Smith Freehills LLP
Eversheds LLP
Pinsent Masons LLP

**Financial advisers**
N M Rothschild & Sons Limited

**Bankers**
Royal Bank of Scotland plc
Lloyds TSB Bank plc
HSBC Bank plc

## Registrars

Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol BS99 6ZZ

Shareholders' enquiries should be addressed to the Registrars at the above address (tel: 0870 707 1134)

## Registered office

Landscape House
Premier Way
Lowfields Business Park, Elland
Halifax HX5 9HT
West Yorkshire

Telephone: 01422 312000

Website: www.marshalls.co.uk

Registered in England and Wales: No. 5100353

CERTIFIED CARBON NEUTRAL® publication
CarbonNeutral.com

FSC® www.fsc.org
MIX
Paper from responsible sources
FSC® C001785

The Group's commitment to environmental issues is reflected in this Annual Report which has been printed on Symbol Freelife Satin which is a mixed source FSC® certified and ECF (Elemental Chlorine Free) material. This is a certified CarbonNeutral® publication. Printed in the UK by Park Communications, using their environmental printing technology; vegetable inks were used throughout. Both the manufacturing mill and the printer are registered to the Environmental Management System ISO14001 and are Forest Stewardship Council® (FSC) chain-of-custody certified.

Marshalls

Marshalls plc, Landscape House,
Premier Way, Lowfields Business Park,
Elland HX5 9HT