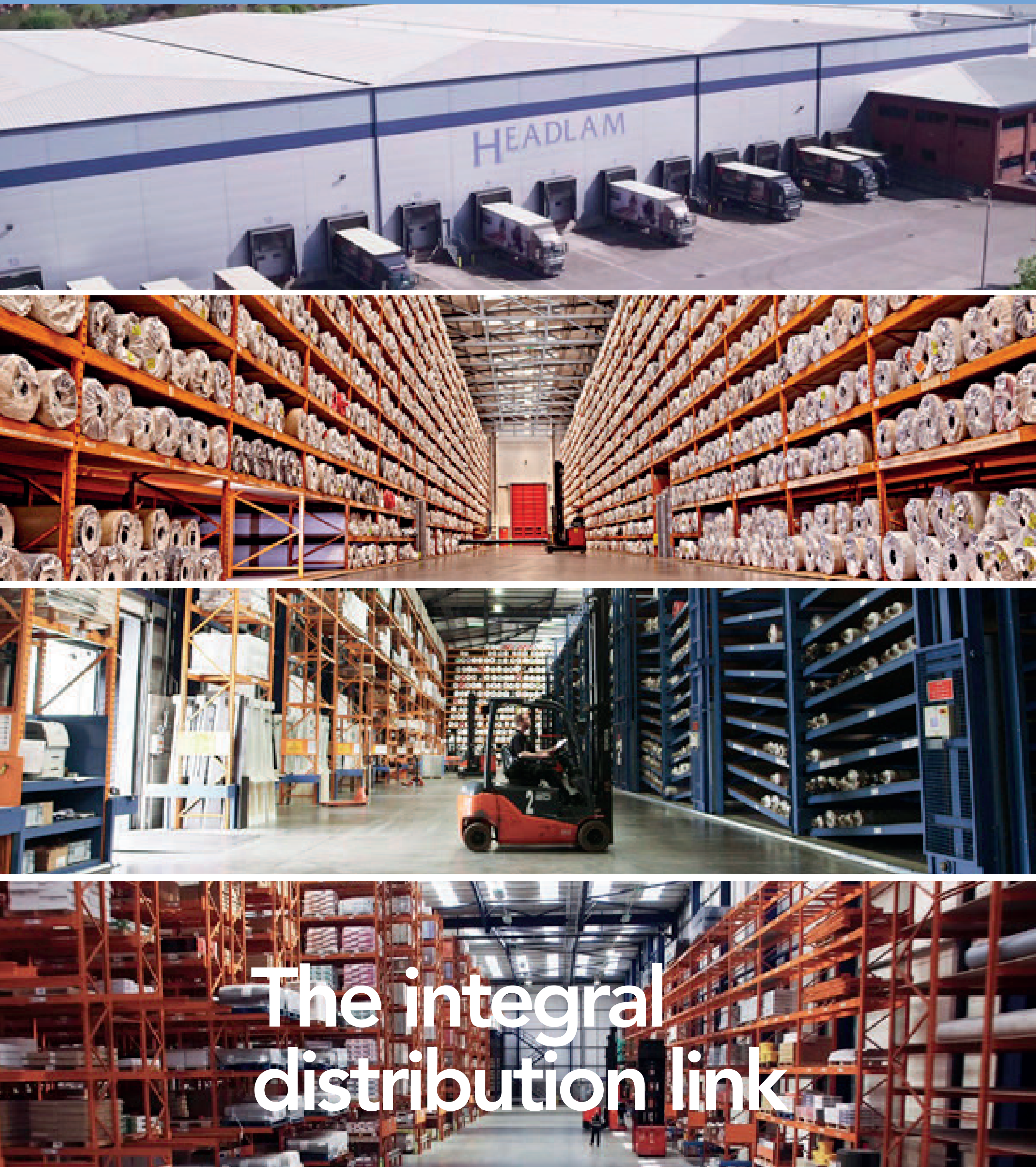
headlam group plc

Annual Report and Accounts
for the year ended 31 December 2016



The integral distribution link

www.headlam.com
Stock code: LSE: HEAD

Europe's largest distributor of floorcoverings

About Us

Headlam Group plc is Europe's largest distributor of floorcoverings, having grown significantly via organic growth and acquisition since 1992.

Headlam Group plc ('Headlam' or 'the Company') is Europe's largest distributor of floorcoverings, having grown significantly via organic growth and acquisition since 1992.

Headlam provides the distribution link between suppliers and customers of floorcoverings, providing suppliers with the greatest coverage and customer penetration for their products across the UK and Continental Europe, and customers with the broadest range of products supported by next day delivery.

The Company is engaged with suppliers across 16 countries whose products cover a significant proportion of the floorcoverings market (including carpet, residential vinyl, wood, laminate, luxury vinyl tile, underlay and commercial flooring). The Company's customers are within the residential and commercial sectors and comprise principally independent retailers and flooring contractors.

The Company currently comprises 60 wholly owned businesses in the UK and Continental Europe, each operating under its own trade brand and utilising its individual sales team which achieves a greater reach into the customer base.

Each of the businesses is supported by the Company's centralised and financial resources and extensive distribution network across the UK and Continental Europe that comprises four distribution hubs, 18 distribution centres, 55 service centres and a corporate showroom.

Via organic growth and acquisitions, Headlam continues to gain market share and cement its market leading position with revenue in 2016 growing by 6.0% to £693.6 million. The increased revenue led to an improved operating performance as a result of operational gearing and leveraging the well-invested distribution network, with underlying profit* before tax increasing 12.6% to £40.1 million.

2017 marks Headlam's 25th year as a distributor of floorcoverings and it is the Company's intention to continue building on its relationship with suppliers and customers to deliver long-term shareholder value.

Investment Case

- Market leading position with significant scale and market penetration through breadth of product
- Consistent outperformance of the growth in the UK floorcoverings market which has shown, and continues to show, steady growth†
- Well-invested and extensive distribution network providing a significant barrier to entry
- Operational gearing from increasing revenue and leveraging the distribution network
- Ongoing operating efficiency strategies to increase further operating margin and profitability
- Strong balance sheet and cash flow, with net cash position of £52.6 million at 31 December 2016
- Progressive ordinary dividend policy, with potential for additional special dividend payments

* Before non-recurring items

† Source: AMA Research Ltd – Floorcoverings Market Report UK 2016-2020 Analysis

Visit us online at
www.headlam.com

Welcome to the 2016 Annual Report

Business Model

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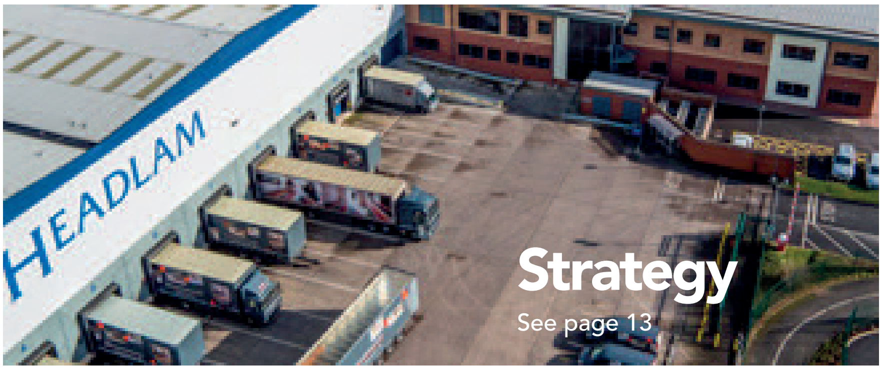

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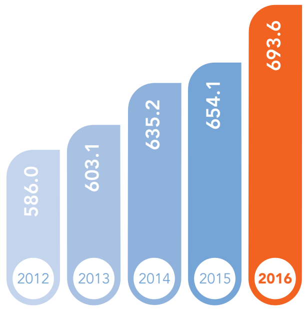
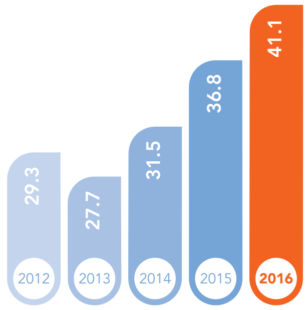
2016 Highlights

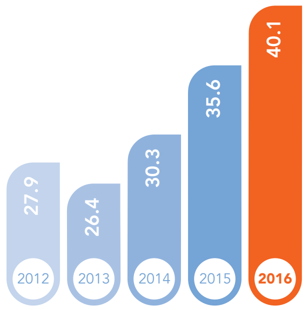
Financial Highlights



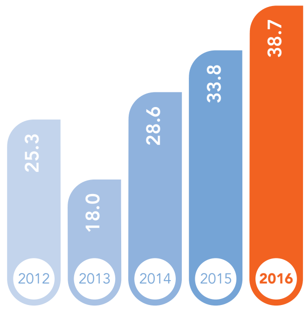
Revenue £million



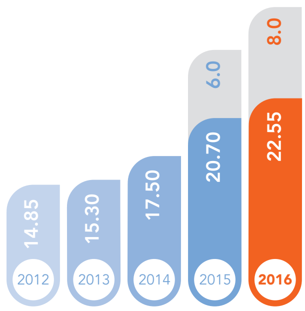
Underlying* Operating Profit £million



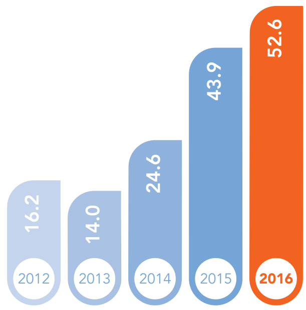
Underlying* Profit Before Tax £million



Basic Underlying* Earnings Per Share pence



Total Dividends Declared and Proposed in respect of 2016 pence†



Net Cash Position £million

Revenue £million

£693.6m +6.0%

2015: £654.1m

Underlying* Operating Profit £million

£41.1m +11.7%

2015: £36.8m

Underlying* Profit Before Tax £million

£40.1m +12.6%

2015: £35.6m

(Statutory Profit Before Tax £38.2m +7.3%
2015: £35.6m)

Basic Underlying* Earnings Per Share pence

38.7p +14.5%

2015: 33.8p

Total Dividends Declared and Proposed in respect of 2016 pence†

30.55p +14.4%

2015: 26.7p

Net Cash Position £million

£52.6m +19.8%

2015: £43.9m

Operational Highlights

- Improved operating performance as a consequence of increased revenue and leveraging of the extensive distribution network, with underlying* operating margin of 5.9% (2015: 5.6% (after adjusting for one-off benefit))
- No discernible impact on trading following the EU referendum in June 2016, and able to implement price increases to mitigate cost inflation due to a weakening of Sterling
- Continued expansion of the distribution network with seven service centres opened in 2016, and one post the year end, bringing the total number of service centres to 55

* Before non-recurring items

† A special dividend of 6.0 pence and 8.0 pence was declared in respect of the financial years 2015 and 2016 respectively in addition to the total ordinary dividend

Company Overview

2017 marks Headlam's 25th anniversary within floorcoverings distribution, and since 1992 the Company has grown via organic growth and acquisition to become Europe's largest distributor of floorcoverings employing over 2,300 people across the UK and Continental Europe.

Company Businesses

The Company currently comprises 60 wholly owned businesses in the UK and Continental Europe (France, Switzerland and the Netherlands)†. The UK and Continental Europe accounted for 86.8% and 13.2% respectively of the Company's total revenue of £693.6 million in 2016.

Each business operates under its own trade brand and utilises its own sales team to allow greater penetration into the Company's customer base, and is supported by the Company's centralised and financial resources and extensive distribution network. The Company's scale also allows the businesses to benefit from greater access to suppliers of floorcovering products and provides purchasing economies of scale. The Company's customers are within the residential and commercial sectors and comprise principally independent retailers and flooring contractors with whom the Company's businesses typically have long-standing relationships. The residential sector accounted for 67.5% of total revenue in 2016.

The Company's businesses operate in five market segments which collectively are aimed at maximising the Company's penetration of the floorcoverings market:

MARKET SEGMENT	CUSTOMER SECTOR	Number of Company businesses
Regional multi-product	Residential & Commercial	28
National multi-product	Residential & Commercial	5
Regional commercial	Commercial	10
Residential specialist	Residential (medium and premium brands)	15
Commercial specialist	Commercial (including the education, healthcare and leisure sectors)	2

† A Directory of the Company's businesses is given on the inside back cover of this Annual Report

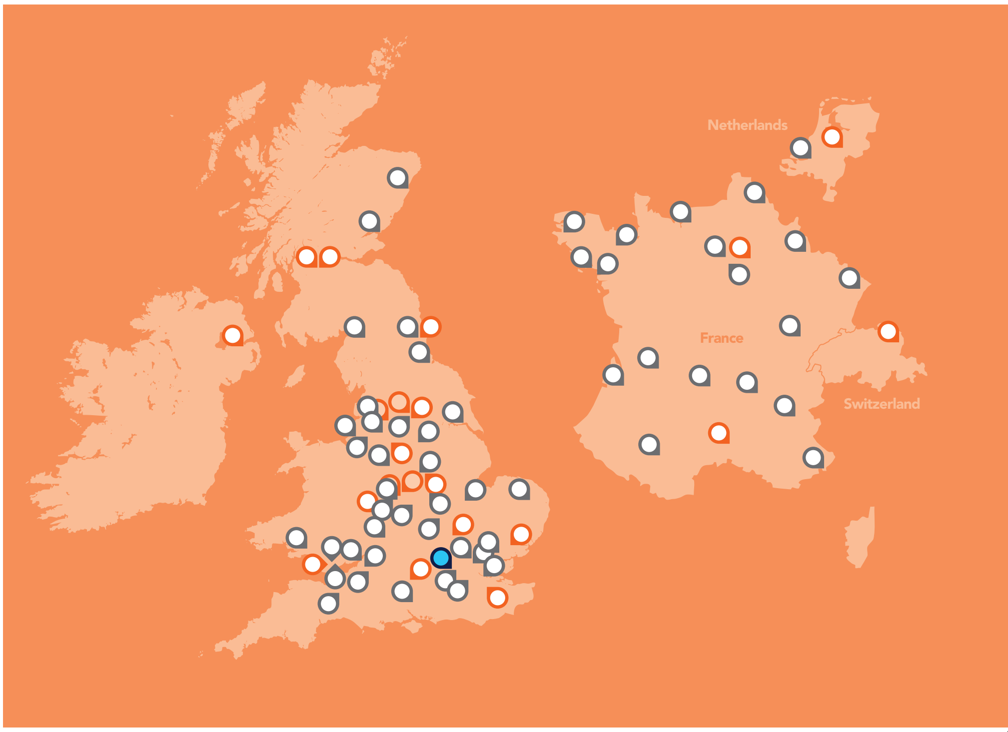
Company Overview

Distribution Network

The Company has established an extensive distribution network over the last 25 years with significant capital expenditure on property, plant and equipment, totalling for example £71.3 million over the last ten years. The Company is able to facilitate next day delivery to customers, and the UK network currently comprises four national distribution hubs, 14 regional distribution centres, 36 service centres, and a corporate showroom in London. In Continental Europe, there are a further four distribution centres and 19 service centres.

The Company's network currently has warehouse capacity of approximately 65 million cubic feet (58 million in the UK and 7 million in Continental Europe).

A total of 5,586,829 customer orders were processed in 2016 (5,117,288 in the UK and 469,541 in Continental Europe). Orders are received and inputted by each business's individual sales team, and processed utilising IT systems which allow the product to be located in the warehouse, selected, cut if appropriate, and sorted for next day delivery. The Company owns 30 cutting tables and operates a fleet of 297 forklift trucks and 381 commercial vehicles. Commercial vehicles are fitted with a tracking system that monitors performance and each driver has an iPhone-based delivery app providing real-time delivery schedules, arrival estimates, and subsequently generates electronic proof of delivery and invoices.



NETWORK	NO.	APPROX. AVERAGE SIZE (cubic feet)
Distribution Hub	4	6,900,000
Distribution Centre	18	1,800,000
Service Centre	55	90,000
Corporate Showroom	1	N/A

The total number of UK service centres has grown from 22 to 36 in the last five years with the intention to open more to support growth. Service centres are a relatively low-cost way of expanding the network and increasing engagement with customers, particularly in the commercial sector, while offering customers even more immediate access to products through collection.

In addition, the corporate showroom in Clerkenwell, London was established in 2015 to target the specified commercial flooring market. Clerkenwell is a well-established design hub with a number of architectural practices in the area, and the dedicated sales team are targeting projects ranging in size from 100m^2 to 10,000m^2.

There continues to be ample opportunity to enhance and more effectively and efficiently utilise parts of the distribution network to support growth and increase profitability. Certain businesses have grown to an extent whereby they would benefit from larger premises. One such example is Faithfulls Floorcoverings which is proposed to move into a newly built dedicated regional distribution centre in Ipswich in 2018.

Continued revenue growth allows the Company to build on its relationship with suppliers and leverage its extensive distribution network, and thereby return increasing levels of profitability through operational gearing.

* Based on a width of 4.25m

Company Overview

Suppliers

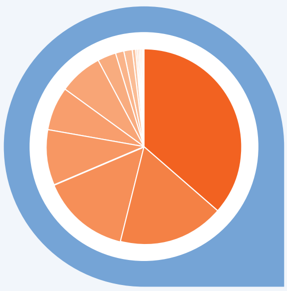
The Company sources an extensive range of floorcovering products including carpet, residential vinyl, wood, laminate, luxury vinyl tile, underlay and commercial flooring from suppliers across 16 countries covering a wide price range. In 2016, the Company purchased from 107 significant suppliers.

In 2016, 77.56% of products for the commercial sector were purchased from suppliers in the UK, whereas the UK only accounted for 14.61% in the residential sector.*

Suppliers benefit by gaining via the Company the greatest coverage and customer penetration for their products across the UK and Continental Europe. The Company also works in conjunction with the suppliers to tailor their product lines, launch new products and increase awareness of their products amongst customers primarily through point of sale ('POS') materials and positioning POS displays in the customer's premises.

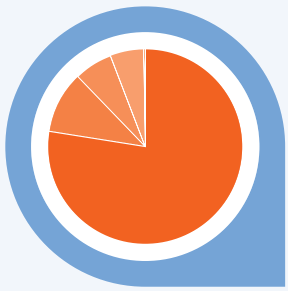
Through increasing revenues, the Company and its businesses are able to benefit from purchasing economies of scale with suppliers.

Residential sector purchases by country*



Belgium	36.41%	Egypt	1.20%
Netherlands	17.65%	Croatia	0.62%
UK	14.61%	Austria	0.37%
Germany	9.28%	Korea	0.31%
Turkey	7.32%	Portugal	0.31%
France	7.20%	Estonia	0.31%
China	3.00%	Italy	0.02%
Denmark	1.39%		

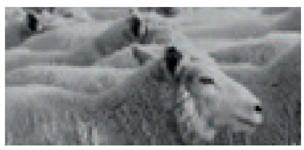
Commercial sector purchases by country*



UK	77.56%
Netherlands	10.25%
France	6.59%
Belgium	5.37%
Korea	0.19%
Hungary	0.04%

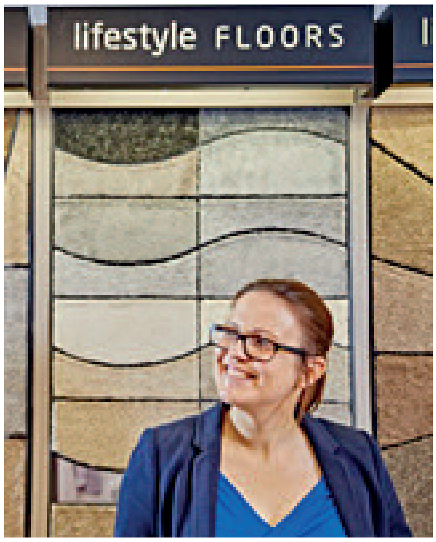
* Based on actual purchase prices from suppliers

BEST WOOL CARPETS
THE NETHERLANDS



'Best Wool Carpets in Best in the Netherlands has been designing, manufacturing and distributing beautiful woollen carpets and rugs since 1982. Genuine and honest natural products for people who appreciate quality, following trends in interior design and also creating trends ourselves. We have many years of experience as a reliable development and production partner. We always think along with our partners. Since 2003 we have worked with Headlam to both of our satisfaction. Headlam's distribution capabilities provide us with an extremely important route to market and access to the broadest customer base for our products in the UK. We currently supply Headlam with over 30 products and have seen the volume of our products supplied to Headlam increase by 50% over the last five years.'

YVAR MONASCH, MANAGING DIRECTOR



Customers

The Company had a total of 66,960 active customer accounts across the residential and commercial sectors in 2016. The residential and commercial sector accounted for 67.5% and 32.5% respectively of the Company's revenue in 2016, with this split remaining broadly similar over the last few years. Customers in the residential sector comprise principally independent retailers who are estimated to have approximately 60% share of the UK floorcoverings market.

The Company's businesses typically have well-established relationships with the customers, which are supported by frequent customer visits by the individual businesses sales teams. Sales visits were made to 52,840 customers in the UK in 2016, with an emphasis on also targeting new customers. The Company provides frequent training programmes to senior managers, sales managers and representatives within the businesses, and a CRM app enhances their interaction with customers.

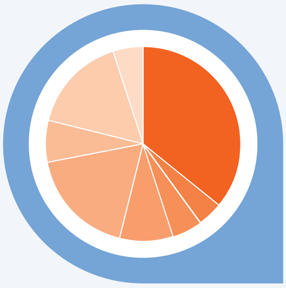
The Company offers its customers an extensive range of products covering a broad price spectrum supported by next day delivery. The product range is reviewed and altered as necessary to reflect customer orders and end consumer's tastes. The Company helps its customers to anticipate new trends and alerts them to new product lines reflecting these trends.

Carpet continues to account for the largest proportion of the Company's UK sales, 36% in 2016, although this has decreased from 41% in 2010 as there has been an increasing move towards hard floor alternatives such as wood, laminate and luxury vinyl tiles in recent years.

CARPETBARN
POOLE, FERNDOWN, EASTLEIGH AND FAREHAM

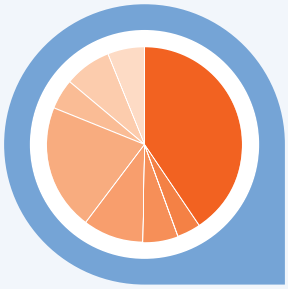
'We are a family-run, independent business currently operating out of four retail premises in the South of England with over 35 years of experience in the industry. We pride ourselves on our outstanding floorcovering knowledge and our passion and expertise are what set us apart, with unrivalled customer service and a product range that is second to none. We have been a customer of Headlam since it was established 25 years ago and Headlam is one of our main suppliers. They have undoubtedly helped support the growth of our business by providing us with the largest selection of floorcoverings, guaranteed next day delivery and good customer service. We get regular visits from many companies in the Headlam Group and it has always been a good mutually beneficial relationship.'

UK revenue by product in 2016



Carpet	36%
Underlay	4%
Carpet tiles	5%
Residential vinyl	9%
Commercial flooring	18%
Adhesive	7%
Wood & Laminates	16%
Miscellaneous	5%

UK revenue by product in 2010



Carpet	41%
Underlay	4%
Carpet tiles	5%
Residential vinyl	10%
Commercial flooring	21%
Adhesive	5%
Wood & Laminates	8%
Miscellaneous	6%

Company Overview

Employees

The Company employed 2,069 people across the UK and 315 in Continental Europe as at 31 December 2016, and a considerable number of the Company's managers have decades of experience within the floorcoverings and distribution industries. The Company has made considerable investment in people over the years, with emphasis on training and career progression, and has a proven track-record of cultivating homegrown talent.

In addition, it is the Company's intention to pursue recruitment initiatives over the coming years.

Financial Performance & Dividends

As a consequence of previous substantial capital expenditure, the Company is able to generate significant cash flow and also benefit from operational gearing as additional revenue is introduced into the network, as evidenced by the improvement in underlying operating margin to 5.9% in 2016 from 4.9% in 2010. It is the Company's intention to focus on improving levels of operating profit and margin through increasing revenue and also ongoing operating efficiency strategies. Any improvement in profit and basic earnings per share has a direct correlation with the total ordinary dividend payable to shareholders. Since 2014 the Company has utilised a cover ratio of 1.63 between total ordinary dividend and basic earnings per share. In addition, the Company has in place a policy which allows the return of surplus cash to shareholders via special dividends when circumstances permit.

Special dividends were declared in respect of the 2015 and 2016 financial years.

TONY HENDERSON
WAREHOUSE & DISTRIBUTION MANAGER
HEADLAM GATESHEAD

25 YEARS

"I joined John Hadfields & Sons at Tyne Tunnel Trading Estate in 1976 after leaving school. When I started I swept the warehouse floors, and helped other members of staff pick the next day's orders until I took charge of the warehouse floor in 1979.

One of the sales reps was retiring and I was asked if I would like to take over his patch, so from 1983 until 1988 I covered all of Cumbria, south Scotland and up to Berwick on the North East coast.

Then I took the role of Display Merchandiser for Hickson when Hadfields was bought by them, this lasted until 1992 when Headlam acquired the flooring division from Hickson and I was offered the Distribution Manager position for Headlam Newcastle. This position I have looked after for the last 25 years, something I have never been happier doing.

In the time I have worked under the Headlam banner there have been many changes, not only to the flooring environment but also within Headlam itself. All for the better I may add, the outlay of funds for technology and the ongoing Health, Safety and Environment ('HSE') making everyone's job easier and more secure.

We have many long-term employees at our depot here in Gateshead and I work as a hands-on manager, working from both within my office and on the warehouse floor helping other members of staff when things get busy.

Our depot is not as big as some at Headlam, but we are proud of the business we get and take from our competitors. We are not the cheapest, but we give the best service which is why our customers support us. Our Commercial Director and his sales team have doubled our turnover since we moved to Gateshead, this again is down to the service we give from managers to operatives and drivers.

Our depot is mainly commercial flooring based, holding approximately 3,500 rolls / cut lengths and two full aisles of screed and adhesives. Our trade counter business has progressed from a steady flow to manic every morning, also opening an extra hour on a Saturday morning to accommodate fitters who need gear. Some customers who call in will be sons, and sometimes daughters, of customers I used to call on when I was on the road, and our depot is not unlike that either as we have nephews, cousins and sons working from the same families here.

The flooring trade has been kind to me and I have enjoyed working within it, but more so since joining Headlam as I feel secure in the role I undertake and enjoy the company of the people I work with."

The Marketplace

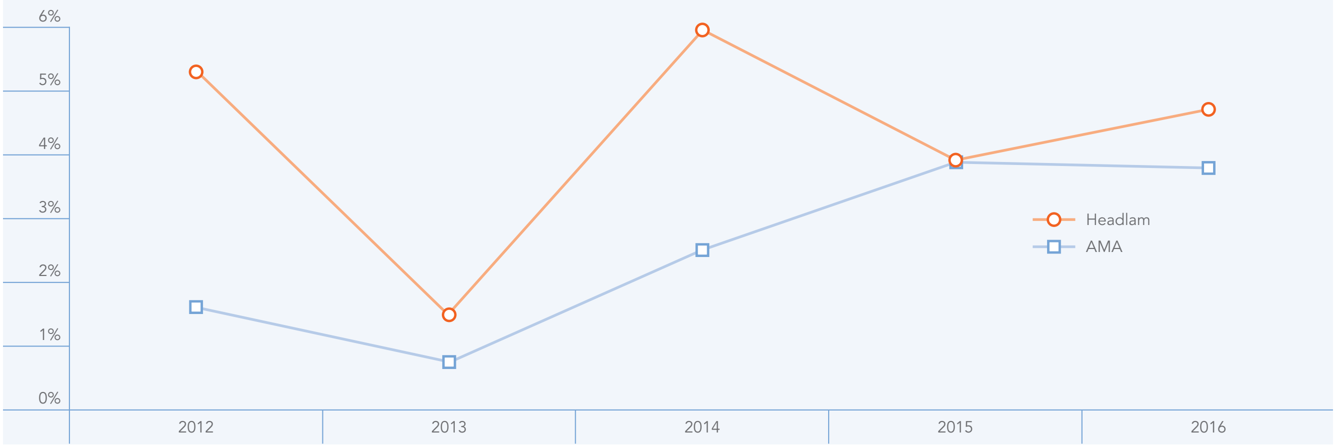
The UK and Continental European floorcoverings market is characterised as being mature due to it being heavily reliant on replacement and refurbishment. As such its performance is seen as being linked to consumer and business confidence, and the overall health of the economy. The most widely recognised and comprehensive data on the market is published approximately every two years by the specialist publisher AMA Research ('AMA') with the last report* forecasting growth of 3.8% in 2016 in the UK. The Company has consistently exceeded the growth in the market as it benefits from its relationships with customers and suppliers and its scale. Estimates up to 2020 forecast continued steady growth with a total UK market value, expressed by reference to manufacturer's selling price, moving from £1.94 billion in 2016 to £2.17 billion in 2020, an increase of 11.9%. The UK economy experienced an unprecedented downturn in 2008 affecting almost all industries and AMA's research showed the UK floorcoverings market fell by almost 21% between 2007 and 2011. The market has rebounded and there has been steady growth since 2012, with the 2016 forecast showing the market to be only approximately 11% below 2007 levels.

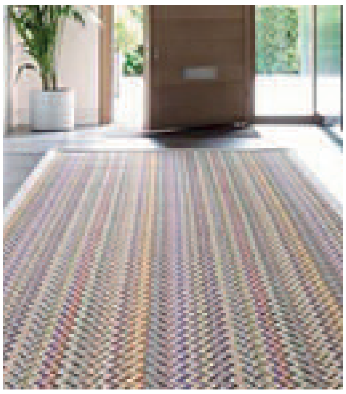
The Company's characteristics enable it to exceed the growth in the market as well as provide some insulation in the event of any downturn. These include:

- Market leading position and significant scale
- Substantial coverage of the floorcoverings market and breadth of product
- Breadth of supplier and customer base, with typically long-established relationships
- Approximately 67% of revenue from residential sector which is characterised by many smaller orders
- Well-invested extensive distribution network
- Operational gearing from increasing revenue and utilisation of the existing extensive network
- Ongoing operating efficiency strategies
- Strong cash flow and balance sheet, with a net cash position of £52.6 million as at 31 December 2016

* Source: AMA Research Ltd – Floorcoverings Market Report UK 2016-2020 Analysis

Headlam's UK like-for-like % revenue growth against AMA's UK floorcoverings market growth forecasts





The Marketplace

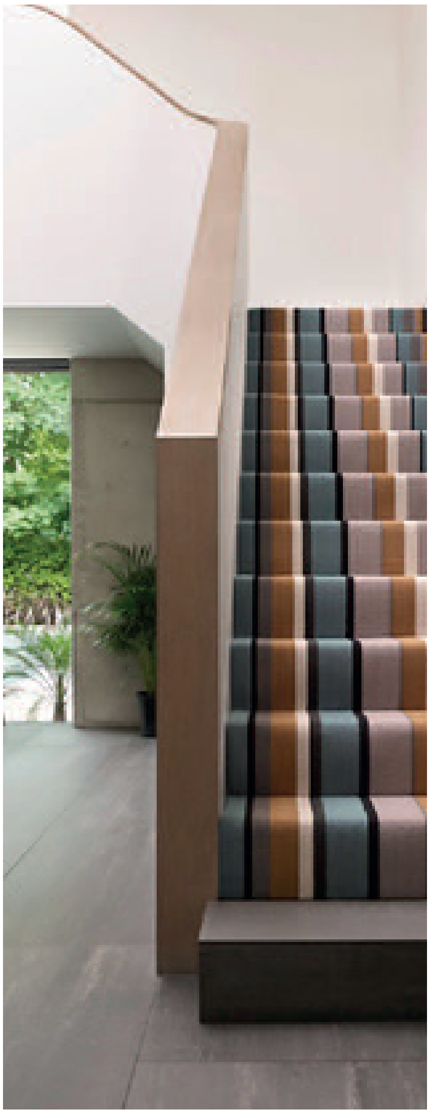
Suppliers of floorcoverings have become noticeably more global in recent years, and there is an increasing global supplier base wishing to bring their products to market and who need a distribution channel. This helps to support continued growth in the market and innovation in products, which in turn supports future growth. Recent years have seen a particular increase in suppliers from Turkey for example, and the percentage of carpet sales has decreased in favour of wood, laminate and luxury vinyl tile. The Company currently has well-established relationships with 107 significant suppliers and continues to increase its supplier base providing growth opportunities.

67.5% of the Company's revenue in 2016 was in the residential sector which typically generates higher margins than the commercial sector, and independent retailers are the Company's principal customer. Orders from independent retailers are typically smaller and more frequent in nature, reflecting the trend of the end consumer redecorating one room at a time. The average order size is around 4m by 5m, and qualitative data relating to the residential end consumer suggests that a room floor is changed approximately every ten years. In 2016, the Company's UK average order cut value for residential carpet and residential vinyl was £127.44 and £68.03 respectively. As such, the Company's financial performance isn't reliant on a few larger customers but many smaller ones. Housebuilders, which fall within the Company's residential sector revenue due to the utilisation of residential products, only accounted for approximately 4% of total Company revenue in 2016.

32.5% of the Company's revenue in 2016 was in the commercial sector (equivalent to £225.4 million), with 10,277 active accounts in this sector, again providing the Company with some protection from a downturn in any one customer or sub-sector.

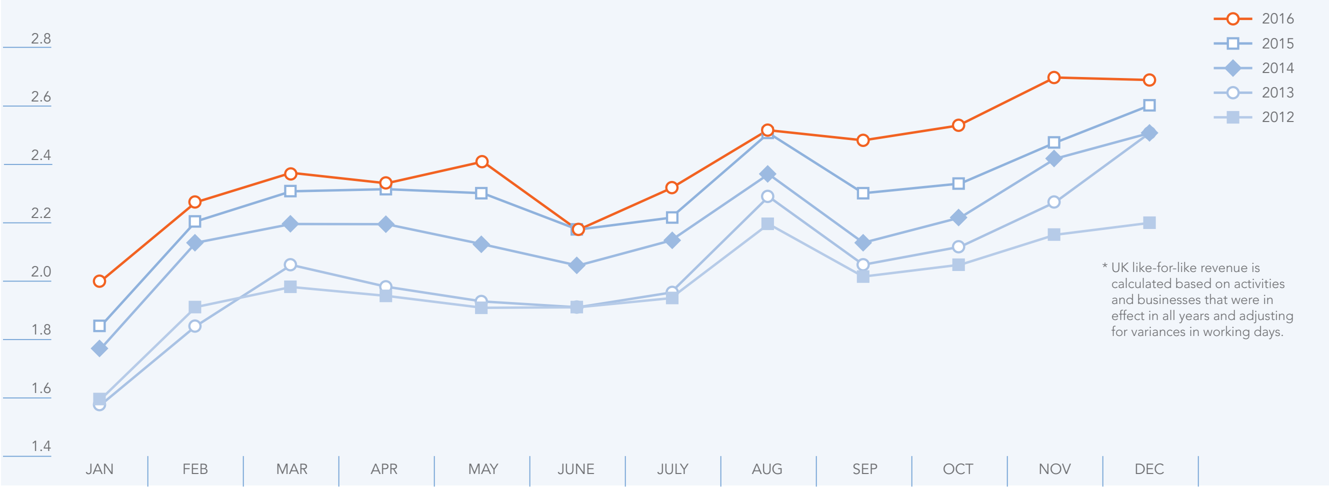
The Company experiences a high degree of consistency in customer order patterns throughout the year, with peak trading periods in August and the fourth quarter reflecting the refurbishment of educational institutions during the summer holidays and redecoration in residential accommodation in the run-up to the Christmas period respectively.

Floorcoverings have a natural shelf-life so whereas demand may be subject to cyclicality, the floorcoverings market remains a growth industry in the long-term being underpinned by fit-outs, replacement, refurbishment, fashion and innovation.



Headlam's 2016 UK Like-for-Like Daily Sales*

£million



EDUCATIONAL INSTITUTIONS' REFURBISHMENT

One of Headlam's traditional peak trading months in the UK is August, reflecting primarily the annual refurbishment of educational institutions in the summer months when the properties are empty. In 2016, the Company's UK revenue for August amounted to £56.2 million. One of the key components of educational institutional refurbishment is the renovation of university student accommodation, and in 2016 Headlam supplied floorcovering products to over 200 projects in this area, having been involved in the majority of these projects in previous years. Headlam often engages with the owner before subsequently dealing direct with the appointed subcontractor. The projects in 2016 ranged from small 500 m^2 areas to very large 10,000 m^2 buildings, and included the student accommodation at Loughborough University, Christchurch College Oxford, Warwick University, Sheffield University and Glasgow University among others. The projects utilised a broad range of floorcoverings including luxury vinyl tiles ('LVT'), sheet vinyl, carpet tiles and commercial broadloom carpet, with the majority of the flooring used being commercial products.

Business Model

'We are Europe's largest distributor of floorcoverings, linking together a global supplier base and an extensive customer base. Our scale gives our suppliers the broadest coverage with the greatest customer penetration for their products across the UK and Continental Europe, and our customers an unrivalled range of floorcoverings supported by next day delivery and a high level of customer service. Our business model has created value for reinvestment to continue growing our business and returns for our shareholders.'

Suppliers of floorcoverings → **Headlam** → **Customers of floorcoverings**

We apply our sources of competitive advantage…

- Market leading position
- Scale, with significant barriers to entry
- Extensive distribution network
- Well-known individual businesses
- Customer service proposition
- Employees with considerable expertise
- Long-established relationships
- Financial strength and centralised resources

…to our chosen market…

- We distribute floorcoverings from suppliers (manufacturers) in 16 countries to customers (predominately independent retailers and flooring contractors) with a total of 66,960 active accounts
- We have an extensive and well-invested distribution network with 65 million cubic feet of warehouse capacity and including 55 service centres
- We have grown organically and via acquisition, and operate under the brands of 60 individual businesses to maximise customer penetration
- We work in conjunction with suppliers to provide point of sale materials to customers and increase sales of their products
- We have dedicated individual sales teams and a high level of customer service to support customers

…generating value for our suppliers, customers and…

Suppliers

- Broadest coverage
- Greatest customer penetration
- Point of sale materials
- Effective route to market
- Innovation

Customers

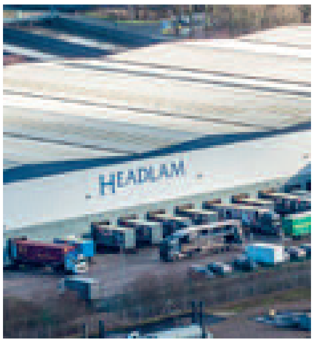
- Unrivalled range of floorcoverings
- Customer service
- Point of sale materials
- Next day delivery
- Innovation

…for our shareholders

- Outperformance of the growth in the market and increasing market share
- Increasing revenue and building on market leading position
- Operating leverage from increasing revenue
- Implementing strategies to enhance operating performance
- Ongoing investment in the business, organic growth and bolt-on acquisitions
- Financial strength
- Progressive ordinary dividend policy
- Special dividend policy to return surplus cash to shareholders

REINVESTMENT (ORGANIC AND ACQUISITIONS)

Strategy
'The integral distribution link'



- **Continuation** – Continue building on the existing business model

- **Scale** – Continue growing the scale of the business and build on market leading position through being the integral distribution link between suppliers and customers

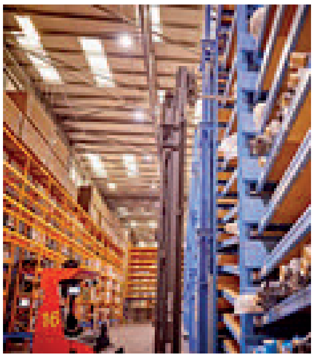
- **Outperformance** – Continue growing revenue in excess of the market growth as a consequence of scale and the value proposition to suppliers and customers

- **Suppliers** – Continue engaging with suppliers around the world to provide them with unique access to market for their products

- **Customers** – Continue enhancing the customer proposition through ongoing expansion of the product range, new customer service initiatives, and next day delivery

- **People** – Grow the expertise within the Company to support the continued growth of the business

- **Gross Margin** – Improve gross margin through increased unitisation of the Company's businesses' relationships with suppliers and customers



- **Operational Gearing** – Improve operational gearing through refinement and more effective and efficient utilisation of the network, as well as additional revenue

- **Dividends** – Continue progressive ordinary dividend policy with additional policy for returning surplus cash to shareholders via special dividends

Chairman's Statement

2016 was another successful year for Headlam, with total revenue and underlying profit before tax increasing by 6.0% and 12.6% to £693.6 million and £40.1 million respectively compared with 2015.

2016 was another successful year for Headlam, with total revenue and underlying profit before tax increasing by 6.0% and 12.6% to £693.6 million and £40.1 million respectively compared with 2015. We were able to significantly outperform the steady growth in the UK floorcoverings market and thereby gain market share, further cementing our market leading position in Europe. As a consequence of the increased revenue and leveraging of our extensive distribution network, we were also able to deliver an improved operating performance.

It was especially gratifying that we experienced no discernible impact on trading following the EU referendum in June 2016, and were able to implement price increases in August 2016 to mitigate cost inflation due to a weakening of Sterling.

The 2016 financial results and overall financial strength of the Company have allowed us to declare a further special dividend, which supplements the Company's progressive ordinary dividend policy. Therefore, dividends declared and proposed in respect of the 2016 financial year, which are a reflection of the cash generative nature of the business, total 30.55 pence, being a combination of a total ordinary dividend amounting to 22.55 pence per ordinary share (2015: 20.70 pence), an increase of 8.9% on 2015, and a special dividend of 8.0 pence per ordinary share (2015: 6.0 pence).

We would like to thank all our employees, without whom this success would not be possible, and again would like to express our appreciation to Tony Brewer who stepped down as Chief Executive during 2016 and was instrumental in building Headlam into the Company it is today. The Board was delighted that Steve Wilson moved from Finance Director to Chief Executive ensuring continuity and also providing the skillset for the future development of the business. We are advanced with our search for a Chief Financial Officer and are committed to securing someone of the calibre that Headlam deserves. We are also pleased to announce that Tony Judge, 52, who has worked at Headlam for more than 24 years, is to be appointed to the Board as Chief Operating Officer with effect from 31 March 2017. Tony has held a number of senior operational roles at the Company, most recently as the UK's Commercial Director. Tony has 35 years' experience in the floorcoverings industry and brings an abundance of knowledge and expertise to the role of Chief Operating Officer*.

The Board recognises the value derived from good corporate governance and the setting of high standards, not least in the confidence it brings to our shareholders, employees, suppliers and customers. The Board continues to encourage full participation and contributions from all its employees and promotes a culture of openness and transparency.

We are dedicated to building on our existing business model which has achieved the strong financial results evident to date, whilst beginning to implement plans to further improve the operating performance of the business going forward.

2017 marks our 25th year as a distributor of floorcoverings and we look forward to continue building on our success.

Dick Peters
Chairman
7 March 2017

*No further information is required to be disclosed pursuant to LR 9.6.13

Chief Executive's Review

Our strategic aim is to continue being the pre-eminent distribution link between suppliers and customers of floorcoverings.

Strategy

Our strategic aim is to continue being the pre-eminent distribution link between suppliers and customers of floorcoverings, providing suppliers with the greatest coverage and customer penetration for their products across the UK and Continental Europe, and customers with the broadest range of products supported by next day delivery. This is facilitated by our 60 wholly owned businesses across the UK and Continental Europe and extensive distribution network that comprises four distribution hubs, 18 distribution centres, 55 service centres and a corporate showroom. Each of the Company's distribution businesses operates under its own brand name and utilises its individual sales team, while being supported by the Company's centralised and financial resources, which allows greater reach into the customer base. The Company's customers are within the residential and commercial sectors and comprise principally independent retailers and flooring contractors with whom the Company's businesses typically have long-standing relationships.

Performance

The Company continued to experience better than anticipated trading throughout the year but particularly in the important fourth quarter which accounted for 26.0% of total revenue in 2016 (2015: 25.6%).

Total revenue for the year of £693.6 million was up 6.0% against 2015, approximately 4.5% in constant currency, with a strong performance from both the UK and Continental Europe operations. The second half of the year accounted for 52.6% of revenue (H2 2015: 52.1%) reflecting the traditional weighting of activity to the second half.

We experienced no discernible impact on trading following the EU referendum result in June 2016, and the Company was able to mitigate cost inflation due to a weakening of Sterling following the referendum by implementing price increases to our customers which mirrored those of our suppliers. The price increases were implemented in August 2016 on virtually all residential sector products sourced from Continental Europe. Purchases from suppliers in the Eurozone accounted for roughly 70% of the Company's residential sector purchases in 2016, and the price increases for those products averaged approximately 6%. The Company's average selling price across the majority of its UK products rose by approximately 1.6% in 2016.

Gross margin was 30.60% versus 30.39% in 2015 (after adjusting for a one-off benefit in 2015) due to product mix variance and rebate benefit. The Company achieved an improved operating performance, with underlying operating profit and underlying profit before tax increasing 11.7% and 12.6% to £41.1 million and £40.1 million respectively against 2015, reflecting utilisation of the existing network and operational gearing from increased revenue.

Chief Executive's Review

UK

The UK accounted for 86.8% of total revenue in 2016, a marginal change from the 88.0% in 2015. There were no acquisitions in 2016, and UK like-for-like growth was 4.7%, a significant outperformance of the 3.8% growth in the market (Source: AMA Research Ltd - Floorcoverings Market Report UK 2016-2020 Analysis) and the 3.9% like-for-like growth in 2015.

Continental Europe

During 2016, the Company's three businesses in the Netherlands were amalgamated into one trading name, Headlam BV, so that the Company now has a total of three Continental European businesses located in each of the Netherlands, France and Switzerland. Continental Europe revenue grew by 3.6% to £81.5 million in constant currency, strongly reversing the decline of 3.8% in 2015, and, following translation, accounted for 13.2% of total revenue in 2016 (2015: 12.0%).

Suppliers

We continue to engage with suppliers around the world to provide them with unique access to market for their products and are now engaged with 107 significant suppliers in 16 countries. Our suppliers' products cover a significant proportion of the floorcoverings market (including carpet, residential vinyl, wood, laminate, luxury vinyl tile, underlay and commercial flooring) and we continue to look to supplement product lines either by engaging with suppliers or via acquisition.

Customers

Our customers are within the residential and commercial sectors, and the revenue split between the two sectors has remained broadly similar over the past few years. In 2016 the residential sector accounted for 67.5% of total revenue (2015: 67.2%) and the commercial sector for 32.5% (2015: 32.8%). The residential sector revenue is principally comprised of sales to independent retailers, and as a consequence is characterised by many smaller orders. In the UK, the Company's average order cut value for residential carpet and residential vinyl in 2016 was £127.44 and £68.03 respectively.

Operational Gearing & Investments

One of the focuses for 2017 and beyond is the operational gearing of the business above and beyond that which comes from additional revenue and growing our market leading position. In relation to this we are looking at the refinement and more effective and efficient utilisation of our distribution network. Initiatives already undertaken at negligible cost include merging IT platforms and de-duplication of inventory in instances where two distribution centres are located in close proximity to each other, which has effectively created growth capacity. This can be replicated across other parts of the network in 2017 and 2018 and it is our intention to examine other straightforward initiatives as well as longer-term plans. No job losses are anticipated as part of these future initiatives and they will also improve service for customers.

We have re-examined the plans for our proposed purpose-built distribution centre in Ipswich for Faithfulls Floorcovering, one of our regional multi-product businesses which has experienced good growth and has outgrown its existing premises in nearby Hadleigh. Whilst we have received planning permission for

our initial proposed site we are now considering an alternative site also in the Ipswich area that will better suit our needs and is more in line with our strategy of making our network ultimately more efficient while creating growth capacity. This potential new site is in a purpose-built distribution park, offers a quicker build and operational timeline, and 33% more cubic capacity in the same footprint as the initial site. The anticipated total cost, including land cost and warehouse equipment, is slightly higher at £17 million compared with the approximate £15 million for the initial site, but it is hoped that, due to its simpler nature, the distribution centre can be operational during the first half of 2018. There is also scope in the future for the new Ipswich site to support other Company businesses in the area.

Customer service is of paramount importance to our business model and we continue to develop our low-cost service centre network allowing ease of customer collection and ordering. Seven new service centres were opened in strategic locations in 2016, six in the UK and one in the Netherlands, and a further one in the UK post the year end bringing the total to 55 across the Company. This service centre network has led to the number of customer collections in the UK increasing by 29,528 in 2016 to 953,428 (2015: 923,900) which has the added benefit of reducing distribution costs.

Acquisitions

We continue to pursue growth both organically and via bolt-on acquisitions to build on our market leading position, and assess acquisitions on a continual basis utilising strict criteria. While no acquisitions were completed during 2016, since the year end the Company has completed the acquisition of Mitchell Carpets Limited, a regional floorcovering distribution business based in Poole, Dorset. This has brought the total number of wholly owned businesses in the UK and Continental Europe to 60, and all our businesses benefit from being part of the Company through our continued financial and centralised support and purchasing economies of scale.

Ordinary & Special Dividends

With the existing capital expenditure plans largely aligned with previous guidance, coupled with the robust financial performance and strength of the business, we are pleased to be able to declare a further special dividend. The special dividend is our mechanism of returning surplus cash to Shareholders when it is not currently required due to our strong cash flow, cash balances and already well-invested extensive distribution network. Therefore, total dividends in respect to the 2016 financial year increased by 14.4% to 30.55 pence per ordinary share (2015: 26.70 pence). We shall continue to consider future special dividend payments in conjunction with potential acquisitions and future capital expenditure plans.

Current Trading

2017 to date has shown continued growth in both the UK and Continental Europe, and the Company continues to trade in line with the Board's expectations for the full year. UK like-for-like revenue growth was 0.23% and 2.10% in January and February 2017 respectively, with January and February 2016 being particularly strong comparators having recorded like-for-like growth of 9.18% of 3.33% respectively.

Continental Europe grew by 0.25% and 4.63% in January and February 2017 respectively in constant currency continuing the positive performance seen in 2016.

We implemented further price increases in January 2017 averaging approximately 3% across the majority of our residential sector products purchased from Continental Europe, again mirroring those of our suppliers and with no detrimental effect on trading to date. We will continue to monitor movements in currency and pricing and endeavour to implement price increases accordingly.

As stated above, a focus of 2017 is the network's effectiveness and efficiency, and also overheads so that incremental revenue has a greater impact on operating margin going forward, and we look forward to the year with confidence.

Steve Wilson
Chief Executive
7 March 2017

Finance Review

UK like-for-like revenue growth of 4.7% once more outperformed annual market growth, which was forecasted to be 3.8%.

Revenue

During the year, revenue increased by £39.5 million from £654.1 million to £693.6 million, an improvement of 6.0%.

The Company's UK like-for-like growth of 4.7% once more outperformed forecasted annual market growth (Source: AMA Research Ltd) with the like-for-like performance of 5.1% during the second half accelerating ahead of the first half performance of 3.4%. UK residential revenues accounted for 70.1% of total UK revenues in 2016 and achieved an annual like-for-like performance of 5.3% benefiting from the stronger showing during the second half of 5.8%, compared with the first half of 4.7% as markets strengthened during the course of the year.

Commercial revenues in the UK, representing 29.9% of total UK revenues in 2016, increased by 1.9% on a like-for-like basis with a second half of 3.4% versus 0.4% in the first half.

	£000	%	£000	%
Revenue for the year ended 31 December 2015				
UK	575,341	88.0		
Continental Europe	78,737	12.0		
			654,078	100.0
Items contributing to growth during the 12-month period to 31 December 2016				
Like-for-like UK organic growth	24,356	4.3		
Additional working day	2,290	0.4		
Acquisition	117	–		
			26,763	4.7
Growth in Continental Europe	2,798	3.6		
Translation effect	9,933	–		
			12,731	16.2
Total movement			39,494	6.0
Revenue for the year ended 31 December 2016				
UK	602,104	86.8		
Continental Europe	91,468	13.2		
			693,572	100.0

The revenue from the Continental European businesses improved during the year with the first half like-for-like improvement of 2.8% increasing to 4.3% during the second half giving rise to an annual increase of 3.6% in constant currency.

Both the Netherlands and France businesses contributed to the increase, with the Swiss business in line with its performance in 2015.

The weighting between combined residential and commercial revenue in Continental Europe showed a slight movement to commercial with 49.3% of revenue (2015: 48.8%).

Gross margin

Gross margin decreased marginally during the year from 30.7% in 2015 to 30.6%. However, the gross margin achieved during 2015 included a one-off benefit amounting to 31 basis points and totalling £2.0 million, which arose during 2015 because of the rapid appreciation of Sterling against the Euro during the first quarter of the year. After adjusting for this one-off benefit, underlying gross margin in 2016 improved 21 basis points against 2015, attributable to product mix variance of 9 basis points and a rebate benefit of 12 basis points.

Expenses

Combined distribution and administrative expenses increased by 5.9%, up by £9.7 million, from £163.7 million to £173.4 million. The percentage proportions of distribution and administration expenses of total expenses for 2016 remained largely unaltered compared with 2015, with 2016 being 73.8% and 26.2% respectively (2015: 73.3% and 26.7%).

	Total expenses		Distribution		Administration	
	£000	%	£000	%	£000	%
Expenses for 2015	163,733		120,070	73.3	43,663	26.7
Significant movements in 2016:						
People cost	5,596	78.4	4,444	79.2	1,152	75.7
Commercial vehicle expenses	801	11.2	801	14.3	–	–
Carriage costs	330	4.6	330	5.9	–	–
Packaging costs	251	3.5	251	4.5	–	–
Sampling investment	366	5.1	366	6.5	–	–
Bad debts	(723)	(10.1)	(723)	(12.9)	–	–
Depreciation	472	6.6	2	–	470	30.9
Ipswich	305	4.3	–	–	305	20.1
Occupancy	(232)	(3.2)	–	–	(232)	(15.2)
Share-based payments	139	1.9	–	–	139	9.1
Intangibles	(375)	(5.3)	–	–	(375)	(24.6)
Warehouse repairs	236	3.3	236	4.2	–	–
Discounts	496	7.0	–	–	496	32.6
Foreign exchange gains	(471)	(6.6)	–	–	(471)	(30.9)
Other	(57)	(0.7)	(95)	(1.7)	38	2.3
	7,134	100.0	5,612	100.0	1,522	100.0
Currency translation	2,492		2,300		192	
Expenses for 2016	173,359		127,982	73.8	45,377	26.2

The increase in people cost, £5.6 million (2015: increase of £3.0 million), was once more the largest component increase, being 78.4% of the gross expenses increase before currency translation. The increase was fuelled by the cost of living increase of 2.5% awarded to all UK employees, a modest increase in people numbers, incentive awards relating to annual performance targets, and non-recurring costs relating to personnel changes of £1.9 million.

Costs relating to the currency translation of the Continental European businesses amounted to £2.5 million, reflecting the degree to which Sterling depreciated against the Euro and Swiss Franc in 2016.

The remaining expenses movements were directly linked to the increase in revenue during 2016 compared with 2015.

Finance Review

Operating profit

The underlying operating profit for 2016 increased by 11.7% compared with 2015 and the underlying operating margin improved to 5.9%, up from 5.6% (after adjusting for the one-off benefit), reflecting the absolute gain in gross margin due to the volume benefits on the additional revenue, product mix variance and rebate benefit. The operating margin generated by the incremental year-on-year revenue improvement amounted to 10.9% compared with 28.2% in 2015 due to a substantial increase in overhead costs primarily related to people and the cost of living award.

	£000
Operating profit 2015	36,777
Gross margin improvement in 2016	
Volume benefit	11,986
Pricing benefit	2,008
Currency one-off benefit in 2015	(2,000)
	11,994
Expenses increase	
Distribution	(7,912)
Administration	213
Total increase	(7,699)
Underlying operating profit 2016	41,072
Drop through rate %	10.9
Operating margin %	5.9
Improvement %	11.7

Tax

The underlying effective tax rate for 2016 was 18.9% which is lower than the headline rate of corporation tax in the UK of 20%. The main reason for this difference is due to a release in provisions for uncertain tax positions following a reassessment of the level of tax risks in the Company. The anticipated effective underlying rate for 2017 is expected to be 19%.

The Company is committed to being fully compliant with the relevant tax laws and compliance obligations regarding the filing of tax returns, payment and collection of tax. The Company maintains an open relationship with HM Revenue & Customs and currently operates with a level of tax compliance risk that is rated as "low".

The Company does not undertake any form of artificial tax planning but does seek to maximise tax reliefs available, for example by making capital allowance claims on fixed asset expenditure.

Earnings and dividend

Ordinary dividends

The Board's ordinary dividend policy is aimed at improving dividends annually, such that the total of the interim and final dividends for any particular financial year increases in line with the basic earnings per ordinary share for that year.

When declaring the interim and recommending the final dividend, the Board considers the Company's cash resource, adequacy of distributable reserves and the expected cash requirements of the Company.

Basic underlying earnings per share for the year increased to 38.7 pence, representing an improvement of 14.5% on basic earnings of 33.8 pence for 2015. Total ordinary dividends declared and proposed in relation to 2016 have increased by 8.9% from 20.7 pence to 22.55 pence which represents a cover ratio of 1.63 based on basic earnings per share of 36.8 pence.

The Board believes that whilst there is a continuing underlying risk relating to potential volatility around future growth in European floorcovering markets and, as a consequence, a lack of predictability around future earnings, it is nonetheless of the view that the current dividend policy will continue during the medium term. Additionally, and subject to the nature and term of any adverse movement in earnings, financial strength, cash resource and the assessment of future trading, the Board has the option to allow a temporary fall in the cover ratio in order to maintain the dividend.

In implementing the policy, the Board ensures the parent company has sufficient distributable reserves available from which to make the distribution. Details of current year distributable reserves are shown in the retained earnings column in the Statement of Changes in Equity.

Dividend announcements, approvals and payments are typically expected to be as follows:

Dividend	Status and date Announced	Approval	Approximate payment date
Ordinary interim	Declared August	The Board August	January in the year following announcement
Ordinary final	Recommended March	AGM by Shareholders May	July

Special dividends

The Board gives consideration to the distribution of surplus capital by the use of special dividend payments. As first stated in the 2015 Annual Report, the circumstances that apply to any special dividend declaration are: firstly, the Company's forecast average net debt in the year in which the special dividend is paid should be approximately equal to or less than 0.5 of earnings before interest, tax, depreciation and amortisation; secondly, the cover ratio of the aggregated ordinary and special dividends when expressed in terms of dividend cover will not be less than one; and thirdly, the payment must be made from available distributable reserves. The Board believes this approach provides a flexible mechanism for managing the maintenance and expansion of the Company's asset base.

The Board has decided to declare a special dividend of 8.0 pence per ordinary share (2015: special dividend of 6.0 pence per ordinary share). The payment will be made on 24 April 2017 to Shareholders on the register at 31 March 2017.

Employee benefits

The liability attaching to employee benefits is as follows:

	2016 £000	2015 £000
Current liabilities	**2,169**	2,171
Non-current liabilities	**20,781**	16,843
Total	**22,950**	19,014

Whilst the liability relates to both the UK and Swiss defined benefit pension plans, its composition is dominated by the UK plan. The year-on-year increase in the deficit amounts to £3.9 million. This was mainly caused by the increase in the liabilities of the UK defined benefit pension plan resulting from the decrease in the discount rate assumption from 3.7% per annum to 2.7% per annum over the year. This decrease was a consequence of the significant fall over the year in UK corporate bond yields, which are used to derive this assumption.

Cash flow

Net cash flow from operating activities

During the year, net cash flow from operating activities decreased by £3.9 million from £36.5 million to £32.6 million. The elements contributing to the movement are shown in the table below.

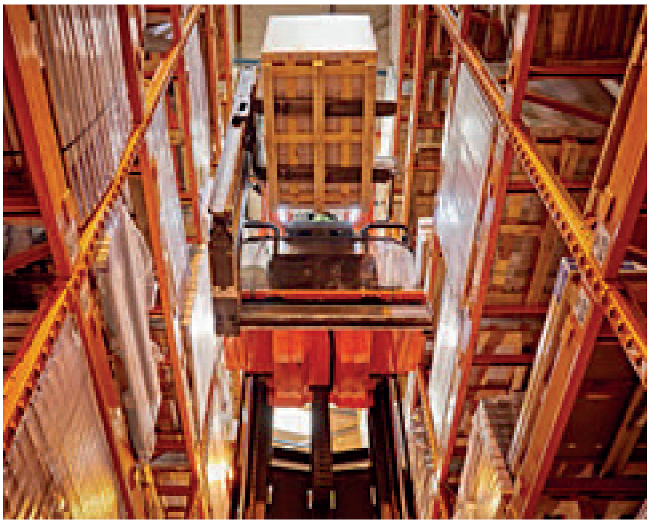
	£000
2015 net cash flow from operating activities	36,506
Operating profit	2,368
Depreciation and amortisation	97
Profit on asset disposals	16
Share-based payments	139
Working capital	(5,916)
Interest paid	135
Taxation	(1,458)
Lower pension contributions	754
2016 net cash flow from operating activities	32,641

As with previous years, two key contributors to the year-on-year movement were the operating profit increase of £2.4 million and the net working capital investment of £5.9 million. In addition, there was a significant increase in the tax payment during the year.

The working capital movement of £5.9 million is due to a cash inflow of £3.9 million reported in 2015 and the more normal working capital profile of 2016 giving a cash outflow of £2.0 million. The increase in inventory and receivables, £5.9 million and £6.5 million respectively, was driven by the revenue activity and supported by a £10.4 million rise in payables.

The increase in the tax payment is solely due to the timing of tax payments.

Finance Review



Cash flows from investing and financing activities

The table below summarises the cash flow movements arising from investing and financing activities during the year. The overall net cash outflow from the two activities was £38.0 million, with the two main factors being a reduction in debt through the repayment of borrowings and the additional dividend payment as a result of last year's maiden special dividend payment.

	£000
2015 cash flows from investing activity	(3,830)
2015 cash flows from financing activity	(16,467)
	(20,297)
Movement in investing activity:	
Net reduction in capital expenditure	17
Interest received	26
Acquisitions	1,977
	2,020
Movement in financing activity:	
Treasury share issues	(582)
Share purchase	(647)
Repayment of borrowings	(10,727)
Dividends paid	(7,809)
	(19,765)
Net movement	(17,745)
2016 cash flows from investing activity	(1,810)
2016 cash flows from financing activity	(36,232)
	(38,042)

Net debt

As detailed in the table below, Company net funds at the end of the year increased by £8.7 million, 19.8%, from £43.9 million to £52.6 million.

Company	At 1 January 2016 £000	Cash flows £000	Translation differences £000	**At 31 December 2016 £000**
Cash at bank and in hand	63,932	(5,397)	808	**59,343**
Bank overdraft	–	(4)	–	**(4)**
Debt due within one year	–	(215)	(9)	**(224)**
Debt due after one year	(20,000)	13,759	(252)	**(6,493)**
	43,932	8,143	547	**52,622**

Funding and going concern

The Company completed a refinancing of its UK banking facilities, which were due for renewal on 8 March 2017, on 14 December 2016. The Company has entered into two separate agreements with Barclays Bank PLC and HSBC Bank Plc that include both Sterling and Euro term facilities. The new banking arrangements, which run to 14 December 2021, increase the level of Sterling committed facilities from £40 million to £47.5 million, and have additional Euro facilities of €8.6 million. The Company also has short-term uncommitted facilities which amount to £25 million, and are renewable on an annual basis. In addition, the Company has existing facilities of £7.8 million in Continental Europe.

The Company maintains sufficient banking facilities to fund its operations and investments, and as at 31 December 2016 92.3% of the total facilities were undrawn as shown below.

	Drawn £000	Undrawn £000	Total facility £000
Less than one year	228	32,819	33,047
Over one year and less than five years	6,493	48,111	54,604
	6,721	80,930	87,651

Having reviewed the Company's resources and a range of likely outcomes, the Board believes there are reasonable grounds for stating that the Company has adequate resources to continue in operational existence for a period no shorter than 12 months from the date of this financial review and it is appropriate to adopt the going concern basis in preparing the Company's financial accounts.

Steve Wilson
Chief Executive
7 March 2017

Viability Statement

Provision C2.2 of the 2014 revision of the UK Corporate Governance Code requires the Board to assess the prospects of the Company over a period in excess of the 12 months required by the 'Going Concern' provision.

After analysing various options, a period of three years, to December 2019, was chosen for the purpose of the viability assessment, in line with the Company's rolling three-year strategic plan normally used to evaluate liquidity. This period also allows for modelling of capital investments planned during the time frame. Due to the current macroeconomic uncertainty in the UK and Continental Europe, the Board believed an assessment over a longer time period would incorporate a high degree of inherent uncertainty.

Reporting on the Company's viability requires the Board to consider those principal risks that could impair the solvency and liquidity of the Company. In order to determine those risks the Board considered the Company-wide principal risks:

- Market demand
- Competitor risk
- Technology
- People
- Employee benefits
- Legislation and regulation

In light of the Company's competitive position in its geographical markets, the Board considered it unlikely that any of the individual risks, other than market demand, would compromise the Company's viability.

With reference to market demand the Board considers that the key risk arises from periods of economic recession that create reduced consumer and business confidence leading to a reduction in consumer demand created through residential property refurbishment or moves and new residential housing development and a wide range of commercial refurbishment and building projects. A contraction in demand triggered by these events will inevitably cause a fall in demand for the Company's products. As a result, two alternative downside scenarios were modelled:

Scenario A – recessionary environment

Scenario A is modelled on the basis that there is a sustained recessionary environment in both the UK and Continental Europe throughout the period of the viability assessment, such that revenues decline whilst there remain ongoing inflationary cost pressures.

Scenario B – economic crisis

Scenario B is modelled on the basis that there is a similar economic and financial crisis to that observed during the second half of 2008 through to 2012. The Board has utilised its experience of the trading environment in that period. This scenario assumed there is significant double digit decline in revenues in the period of the viability assessment.

Consideration was also given to the plausibility of the occurrence of other individual events that in their own right could have a material impact on the Company's viability. None of these events was considered plausible.

The scenarios modelled are hypothetical and extremely severe for the purpose of creating outcomes that could have the ability to threaten the viability of the Company. However, based on the consolidated financial impact of the scenario analysis and associated mitigating actions that are either in place or could be implemented, the Board has been able to conclude that the Company will be able to operate within its existing bank covenants and maintain sufficient bank facilities to meet its funding needs over the three-year assessment period. In coming to this conclusion, it has been assumed that the Company's UK bank facilities, recently renewed on 14 December 2016, through to 31 December 2019, will continue in existence.

Confirmation of longer term viability

Based on the results from these scenarios, and having considered the available mitigating actions, the Board has a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to 31 December 2019. This longer-term assessment process supports the Board's statements on both viability and going concern.

Key Performance Indicators

The following measures are used to assess the Company's progress towards its medium-term strategic objectives.

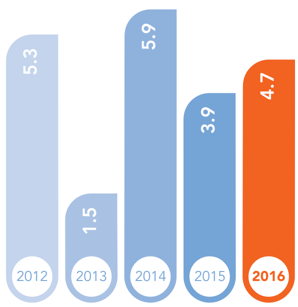
1 UK Like-For-Like Revenue Growth

MEASUREMENT

Like-for-like revenue growth measures changes in revenue in the current year compared with the previous year. The measure excludes the effects of acquisitions.

WHY THIS IS IMPORTANT

The Company's medium-term growth objective is to achieve an increase in like-for-like revenue which exceeds the growth in the UK floorcoverings market, thereby maintaining growth in market share.



UK Like-For-Like Revenue Growth % **4.7**
2015: 3.9

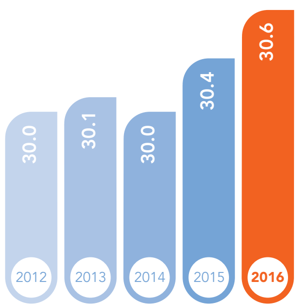
2 Underlying* Gross Profit Margin

MEASUREMENT

The ratio of gross profit to revenue.

WHY THIS IS IMPORTANT

Gross profit margin is a primary indicator of business performance and market competitiveness. A movement in gross margin generally reflects a change in the business product mix or market pricing or a combination of both.



Underlying Gross Profit Margin % **30.6**
2015: 30.4

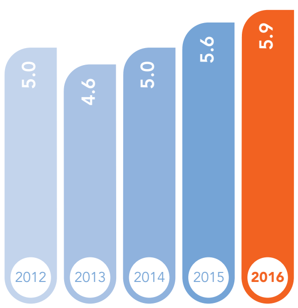
3 Underlying* Operating Profit Margin

MEASUREMENT

Underlying operating profit margin is determined by adding back finance income and expense and non-recurring items to profit before tax and then measuring as a percentage of revenue.

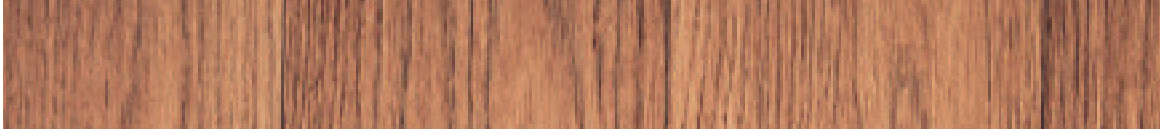
WHY THIS IS IMPORTANT

The majority of the Company's operating costs are fixed and therefore changes in operating profit margin provide a measure of operating efficiency and the effects of incremental profitability arising from an increase in revenue.



Underlying Operating Profit Margin % **5.9**
2015: 5.6

* The non-underlying items in 2016 relate to non-recurring people costs paid out during the year and the related tax on these costs. There were no non-underlying items in 2015 or 2014. The non-underlying items in 2013 relate to the impairment of intangible and tangible fixed assets, totalling £5.4 million. The underlying measures have been used to provide a better understanding of the business performance.



4 Underlying* Earnings Per Share ('EPS')

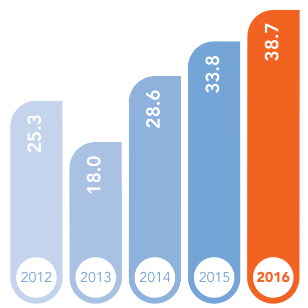
MEASUREMENT

Earnings per share ('EPS') is calculated by reference to post tax profit divided by the weighted average number of shares in issue during the year.

Underlying EPS is calculated by adjusting for non-recurring items.

WHY THIS IS IMPORTANT

EPS and EPS growth are widely used measures of company performance. EPS growth forms the basis of the Company's current ordinary dividend policy since the Board anticipates ordinary dividend growth to be broadly in line with the growth in EPS.



Underlying Earnings Per Share p

38.7

2015: 33.8

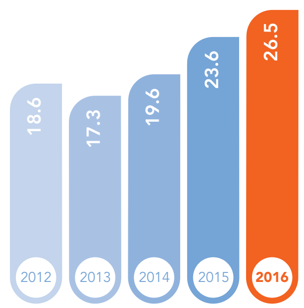
5 Return on Capital Employed

MEASUREMENT

Return on capital employed is derived from underlying operating profit divided by the simple average of the net assets after adjusting for cash and borrowings at the start and end of the year.

WHY THIS IS IMPORTANT

Return on capital employed provides an indication on whether the Company's activities are creating value for its shareholders.



Return on Capital Employed %

26.5

2015: 23.6

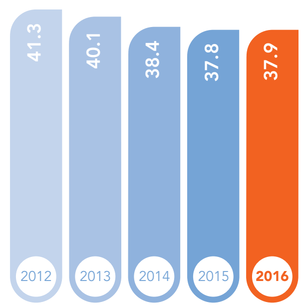
6 Credit Taken by UK Customers and Receivables Impairment Loss Percentage

MEASUREMENT

Credit taken is calculated by reference to trade receivables net of impairment provisions expressed as a proportion of current and prior months' revenue inclusive of VAT. The receivables impairment loss percentage is calculated by expressing the annual impairment loss as a percentage of revenue.

WHY THIS IS IMPORTANT

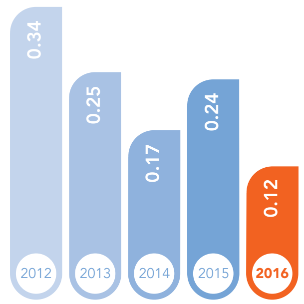
These two indicators provide a regular check on the financial health of independent retail customers.



UK Credit Taken days

37.9

2015: 37.8



Receivables Impairment Loss %

0.12

2015: 0.24

Managing our Risks

During the year the Board carried out a robust assessment of the financial risks facing the Company, including those that would threaten its business model, future performance, solvency or liquidity.

The Company's business, results and financial condition are influenced by a range of risks and uncertainties, a number of which remain beyond the control of the Board.

The Board reviews key risks and controls and, whilst the following highlights some of the key risks that have affected or could affect the Company, it is not an exhaustive analysis of the threats that may affect or influence the conduct of the business.

Area of risk	DESCRIPTION	POTENTIAL IMPACT	MITIGATION
Market demand	A significant proportion of the Company's revenue arises from trade with independent retailers and flooring contractors. The activity levels within this customer base are determined by consumer demand created through residential property refurbishment or moves, new residential housing developments and a wide range of commercial refurbishment and building projects.	Periods of economic recession that create reduced consumer confidence or contraction in the construction industry and changes in trends and preferences all have the potential to affect market activity and demand for products supplied by the Company. This risk has been a feature of the floorcovering markets since 2008 in the territories where the Company has traded.	Market activity is monitored daily in each individual business and collectively at Company level. This visibility allows prompt response to factors adversely affecting trading. Furthermore, since the Company's principal activities are supply and distribution, the Company has the ability to react quickly to market changes. In addition, the development of a range of regional, national and specialist businesses provides the Company with broad market penetration and the capability to manage the downside risk arising from a market contraction.
Competitor risk	The Company operates across four geographical markets, each of which has a number of similar trading characteristics. Within each market, the Company competes directly with a variety of regional and national distributors and manufacturers selling directly to its customer base and indirectly with multiple retail chains.	The emergence of a competitor with a strong business model could undermine the Company's growth objectives.	The Company seeks to sustain its competitive position by maintaining close relationships with its supplier and customer base. Substantial and continued investment in management and facilities, an extensive product offering, a knowledgeable selling resource, product availability, IT, efficient material handling and logistics enables the Company to continue to improve its market leading position.
Technology	The software platform is a vital component of the Company's operating strategy, underpinning the delivery of operational objectives and providing the framework for the maintenance of financial control.	Given its importance, any prolonged system failure has the potential to adversely affect business performance.	Each business has its own dedicated hardware and failure in one will not interrupt another. Furthermore, the Company operates well defined backup procedures and has contingency plans in place to enable swift recovery from a failure of this nature.

Area of risk	DESCRIPTION	POTENTIAL IMPACT	MITIGATION
People	The Company's ability to deliver continued success is very dependent upon its people.	An inadequate pool of suitably qualified and talented people can disrupt business development and undermine the Company's ability to deliver sustainable growth.	Recruitment, training and development are aimed at ensuring the Company has suitably skilled and qualified people to meet the current and future operational needs of its businesses. Furthermore, the Company is committed to creating opportunities for individuals to progress their careers.
Employee benefits	The costs associated with funding the Company's defined benefit plans continue to be affected by the volatility in investment returns, bond yields, inflation and an improving mortality trend.	The Company operates defined benefit plans in the UK and Switzerland. As at 31 December 2016, the UK plan deficit of £18.3 million represented 80% of the total Company deficit. An increase in the plan deficit could require the Company to increase the deficit reduction contributions.	The Company's most recent triennial valuation of the UK plan was assessed as at 31 March 2014. The trustees commissioned an annual update valuation as of 31 March 2016. As a result of the 2014 valuation, it was agreed to decrease the deficit reduction contribution during 2016 to £2.1 million rising to circa £2.2 million in 2017 due to an agreed 3.3% increase. This 3.3% increase will occur each subsequent 1 January, with a view to eliminating the shortfall by 30 April 2019. The next triennial valuation will take place at 31 March 2017. The reduction in the annual UK contribution has been agreed by the Company and trustee because the trustee is content with setting a deficit reduction programme over a longer time frame given the underlying financial strength of the Company.
Legislation and regulation	The Company's operations are regulated by a variety of laws and regulations, the principal ones relating to health and safety, the environment, employment, commerce, corporate, financial reporting and taxation.	Failure to comply could cause reputational harm and lead to serious civil or criminal proceedings, causing disruption to the Company's operations and leading to financial loss.	The Company manages its obligations through a framework of set policies and procedures and, where appropriate, engages the services of competent third–party advisers.

Corporate Responsibility

Corporate Responsibility

Headlam's strategic aim is to generate value for our shareholders. We are committed to managing the business in a socially responsible way, recognising that the proper management of such matters makes good business sense and can result in strategic, commercial and reputational benefits. We recognise that to be successful in achieving our strategy of sustainable profitable growth it is essential that we act responsibly in all our businesses and towards all people who are stakeholders in them. This includes our employees, customers, suppliers and communities in which we operate. We aim to consistently improve the social, environmental and economic issues within our control or influence throughout the business and our supply network.

The Company is committed to implementing the correct policies and procedures relating to the sustainability of the environment and to the successful delivery of an effective health and safety system, as well as ensuring that the people connected with the Company behave in the right way, complying with all local legal and regulatory requirements.

Policy

The Board, which is responsible for the Company's Corporate Social Responsibility ('CSR'), periodically reviews our policy towards CSR to ensure that it continues to meet the needs of the markets and communities in which we operate. In recognising the importance of CSR issues, we seek to encourage and facilitate positive management behaviour in alignment with the Company's business strategy. This includes the morale and welfare of our employees, the satisfaction of our customers and suppliers, and our impact on the environment.

Through the individual businesses and at a Company level, we consider social and environmental factors, managing relationships with shareholders and communicating with them through a variety of channels. These include the AGM, annual and interim reporting and announcements through a regulatory news service for matters relating to trading and the development of the business, all of which are available on our website at www.headlam.com. Additionally, in order to assist with their understanding of the business and to ensure that the Board is aware of their views and concerns, meetings are held with our institutional shareholders.

Equal opportunities

Our recruitment, training and development processes are designed to ensure that we have suitably skilled and qualified employees to meet the operational needs of the business. We recognise that successful businesses need to deliver a good service and product which can only be done by developing, supporting and maintaining the right staff to provide this. We are committed to developing the potential of our people, offering opportunities for employees to develop and grow and periodically reviewing succession planning processes. We also participate in work experience placement schemes. Employee turnover remains relatively low resulting in a stable employee base.

It is our policy that all employees should have access to employment opportunities, irrespective of age, gender, ethnic origin, religion or disability. As the Company has businesses in Continental Europe, these are appropriate for the local areas of operation. Consideration is given to applications for employment, having due regard to the particular aptitudes and abilities of the applicants and to our responsibilities under the Disability Discrimination Act. Where practicable, subject to the nature of our activities, employees who develop a disability during employment are given the opportunity to retrain for alternative employment within the Company.

Human rights

We are committed to treating our employees fairly and equitably, recognising individuals' basic human rights and an ethical approach to employees, suppliers and customers. The Company respects the human rights of those working for or with us, and of the people in the communities where we operate. We will not knowingly do business with companies, organisations or individuals that we believe are not working to at least basic human rights standards. Our businesses comply with applicable pay and working-time laws and other laws or regulations affecting the employment relationship and workplace.

We oppose the exploitation of workers and we will not tolerate forced labour, or labour which involves physical, verbal or psychological harassment or intimidation of any kind and we will not employ child labour in any of our operations. Nor will we permit the exploitation of, or

discrimination against, any vulnerable group. We support fair and reasonable rewards for workers, with pay reflecting local norms and meeting or exceeding any legal minimum wage levels.

The Board is committed to taking the necessary steps to ensure that slavery and human trafficking are not taking place in our businesses and seeks to gain transparency within our supply chain. We shall report further on these activities on our website shortly.

The Company is also committed to maintaining a safe and productive environment, free from harassment in which all individuals are treated with respect and dignity and we expect all our employees and individuals that work at our sites to follow our health and safety policies and procedures and be free from substance abuse at all times.

Communications

The continued success of our business relies on good relations and communications with employees and on the provision of a safe and environmentally sound workplace, which complies with applicable laws and regulations, providing an environment in which people can flourish and succeed. Our employees' wellbeing and professional development is a key element to recruiting and retaining high-performing individuals.

Our people seek to deliver their best for the business, which, combined with a fair and responsible way of doing business, generates a common ambition to add value. We expect employees to respect confidential information, Company time and assets, and believe in open and honest communication, fair treatment and equal opportunities, all of which support the fundamental principles of good governance.

We encourage the involvement and participation of employees in matters that affect their interests through formal and informal meetings, and value their communication with management, both senior and at the business unit. Employees continue to be informed on matters affecting them and on the various factors influencing the performance of the Company, including through the Company's website and intranet site. Eligible employees are able to benefit from the Company's performance through participation in share schemes, including a savings-related share option scheme which at the year end had 924 active savings accounts representing circa 900 employees participating.

Considering it important for our employees to make provision for their retirement, the Company offers opportunities for participation in the Headlam Group Staff Retirement Benefits Scheme, the Headlam Group Pension Plan and the Government auto-enrolment National Employee Savings Trust, also providing death in service benefits through the Headlam Group Life Assurance scheme.

Training

Employees are encouraged to take advantage of our training and development opportunities, which are an important part of our strategy for success. Training is delivered through internal resources, a significant proportion of which is on a one-to-one basis, and external providers. In 2017 we have continued the bespoke training programme for our managers and sales representatives.

We require our employees to act ethically and responsibly in accordance with the policies and procedures within our employment handbook, which covers our policies on ethics, bribery, fraud and whistleblowing. This includes a zero tolerance approach to discrimination, bullying and harassment. All our policies promote the principles of fairness and equal opportunities and if these are not followed, employees can use the whistleblowing hotline to report adverse behaviours.

Utilising the services of an external trainer, continuing professional competence training for commercial vehicle drivers was undertaken during the year with further training scheduled during 2017.

Our externally sourced driver training team continues to deliver the driver Certificate of Professional Competence ('CPC') to all of our commercial drivers to ensure that the statutory requirement of 35 hours' CPC training for every driver over a five year period is achieved, a total of 403 drivers each receiving seven hours' training in 2016. Training is facilitated using our distribution facilities, with course material in 2016 including loading and loading safely, lifting accessories, product handling, carpet winch, vehicle loading and load distribution and restraint. The 2017 training programme is following a similar approach to that in 2016 albeit with different subject matter, including driver responsibilities, defect reporting, drivers' hours rules and regulations, tachograph legislation and digital downloads, working time rules and regulations and first aid. We continue to offer the opportunity for class 2 driver training to drivers where changes in business need require a heavy goods vehicle to be used. Additionally, our Transport Managers

Corporate Responsibility

and Supervisors attended an Operator's Licence Awareness Training course and received refresher training on a broad range of transport related activities. Several employees completed their Managers Certificate of Professional Competence, something that we encourage and support our Transport Managers and Supervisors to strive towards.

Health and safety

The health and safety of employees and individuals likely to be affected by our business, including contractors, customers, staff and members of the public where appropriate, is treated with the utmost importance. We are committed to developing and maintaining a positive and effective health and safety culture. It is our policy to seek to ensure that the Company's operations are carried out at all times in compliance with the relevant health and safety guidance in the jurisdictions in which we operate.

Our health and safety policy, which is endorsed by the Board, is tailored to each of our business operations and the circumstances in which they operate. It is amended to reflect changes in procedures and processes and any modifications to our control and inspection procedures. The Board receives a detailed presentation on health and safety issues, covering each trading location, on an annual basis, with interim updates as considered necessary. These include comments on improvements following inspections of the UK businesses undertaken by our advisers. At least once a year, each of the UK businesses receives an updated bespoke comprehensive health and safety manual for use as a source of information, guidance and training together with a set of compliance documentation. These detailed presentations have also shown that sites continue to demonstrate a high level of health and safety management.

Each of the businesses occupying our distribution facilities has a Health and Safety Committee comprising representatives from the various business departments. These meet on a periodic basis and are co-ordinated by the on-site health and safety manager. Management teams are encouraged to create a supportive health and safety culture and recognise the value of employee participation.

The report to the Board includes our businesses in Continental Europe, which operate in accordance with the health and safety legislation and inspection practices in their respective countries. Inspections undertaken by our third-party adviser form the basis on which we determine our standards and are continually reviewed and improved. Additional inspections are undertaken where changes to operations have occurred or new premises occupied.

These are complemented by inspections of racking systems carried out by independent externally appointed assessors and, in the UK, risk inspections undertaken by our insurers at several of our businesses.

Health and safety is an important part of employee induction, at which time we ensure that all employees are aware of our policies and of the commitment that is expected of them towards their safety. Managers, to whom the day-to-day responsibility for health and safety is delegated and who are best placed to monitor and control safety, are guided and supported by our third-party advisers in risk assessment techniques. Job-specific training, including periodic refresher training, is supported by good practice guides which set out the important features associated with many aspects of the roles and duties undertaken by employees. Good practice guides are reviewed not less than annually to ensure they remain relevant to the business and include an awareness of impending changes in relevant legislation and other specialist subjects. They are also reviewed, as appropriate, following any accident or incident. The majority of the local business managers with responsibility for health and safety have completed the Institute of Occupational Safety and Health "Managing Safely" course, with refresher training planned this year.

Our businesses maintain good relationships with health and safety and environmental health regulators with positive and prompt responses to any findings or observations following compliance inspections. We have open and active reporting of any accidents and incidents. During the year we introduced near miss reporting, which has resulted in some improvements to our operating procedures. In 2016 there were 17 reportable incidents, compared to 15 in 2015, none of which had resulted in a serious injury or fatality. Whilst this is a small increase on prior year, the number of reports is fairly consistent from year to year. All reportable accidents are investigated and, in the minority of instances where improvement is required, changes are implemented in a timely manner. There were no prosecutions for breaches of health and safety or enforcement actions in the year. Whilst there were a few slips, trips and falls, there was no common cause or trend.

New commercial vehicles for delivery in 2017 will arrive with a fall arrest system installed in the rear of the vehicle. This, in conjunction with the body harness worn by the driver, is designed to prevent future falls by drivers unloading from the side or back of the vehicle.

Containment and inspection regimes in higher risk areas, such as fuel and lubrication stores, compressors and forklift truck battery charging areas, are kept under review. Fire risk protection continues to be improved, training and awareness increased and special containers are sited at least five metres from the main buildings for the storage of flammable products and combustible waste. Bespoke provision for such aspects of the business is incorporated within the design of the new distribution facilities.

Scheduled in the first half of 2017, an automated external defibrillator ('AED') is to be installed at each of our operating businesses, at which time selected employees will be trained in their usage. Recently, after placing the order but prior to installation, we experienced an employee having need of an AED whilst at work. This reinforces our view that their installation is a positive step towards employee wellbeing.

We will continue our efforts in promoting a safe and secure workplace in the forthcoming year, with continued focus on collation of data relating to near misses and the continuation of the external health and safety risk advice programme, the aim being to at least maintain, if not improve, standards.

Environmental

Product sourcing

As an importer of wood products from outside the EU, we have a procedure in place to comply with the requirements of the European Union Timber Regulations which came into force in March 2013. The procedure culminates in a documented trail confirming that the wood products are sourced from authorised and renewable supplies. As part of this procedure, we also make enquiries to ensure that the manufacturers we deal with do not use child labour or exploit children and treat their workforce fairly.

Utilities

We monitor our greenhouse gases on a consistent basis with the aim of improving our use of energy, water, recyclable and non-recyclable resources, ensuring long-term environmental and business sustainability and creating long-term value for shareholders and other stakeholders.

We recognise that our business can have a direct and indirect effect upon the environment. As a wholesale distributor of floorcoverings operating from distribution facilities in the UK, France, Switzerland and the Netherlands, we are not a significant consumer of water, electricity or gas. Electricity and gas supplies in the UK are purchased on a Company contract basis.

Water

Water consumption arises predominantly in respect of employee welfare and commercial vehicle washing. The majority of our water charges are in respect of water supplied and used. We encourage our drivers to keep the commercial vehicles clean and tidy. To assist them, we have a combination of jet wash machines and, at four of the distribution facilities from which a significant number of commercial vehicles operate, specialist truck washes. Each truck wash utilises 100% recycled water, helping with conservation, and environmentally friendly washing detergents.

We seek to reduce water consumption and charges by analysing invoices received in respect of water, through the installation of water meters and by reducing consumption through repair, renewal or installation of equipment to improve efficiency.

Our water consumption in 2016 was consistent with the 32,660 cubic metres consumed in each of the previous three years.

Electricity

Electricity consumption continues to be predominantly in respect of forklift truck battery charging, the operation of specialist cutting tables used to cut lengths from full and part rolls of broadloom products, associated mechanical handling and compressed air equipment, office and warehouse lighting and office equipment. Modern and energy efficient construction techniques and products are incorporated when we invest in new facilities or undertake refurbishment or repair works, which are more efficient, automatically switching off during periods of inactivity.

Photovoltaic panels, installed on the roof of the Coleshill facility in 2014, generate an estimated 46,000 kWh of electricity. Consideration will be given to further similar installations following a period of evaluation. Future construction projects will similarly incorporate intelligent lighting systems and, where practical, renewable energy solutions. We benefit from the improved information arising following the installation last year of automated meters. We continue to install more energy efficient LED units when undertaking lighting repairs and replacement.

The actual cost of electricity and gas in 2016 at 0.2% of revenue was consistent with the prior year.

Gas

Gas is consumed predominantly in respect of office heating and very limited localised radiant heating above work stations on the cutting tables located within the distribution centre. Future savings in the consumption of electricity and gas have been identified through the installation of sophisticated heating control systems either in new facilities or during refurbishment works. Consideration will be given to installing such control systems in other premises if considered viable.

Owing to the nature of our business and with our proactive approach when planning and developing new facilities, we believe that our activities generally have a low impact on the environment, with no environmental legal or compliance issues arising during the year.

Corporate Responsibility

Carbon reporting

We are required to report on all the measured emissions sources under The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013. Data has been collected in accordance with the Carbon Reduction Commitment Energy Efficiency Scheme. Conversion factors for electricity, gas and fuel are those published by the Carbon Trust and Defra in 2013.

Fuel type	2016 CO_2/ tonnes	2015 CO_2/ tonnes
Electricity	**4,111**	4,348
Gas	**1,052**	1,010
Commercial vehicle fuel	**19,597**	18,153
Car fuel	**4,780**	4,603
Total	**29,540**	28,114
Tonnes per £1 million revenue	**45**	43

The increase in respect of commercial vehicle fuel was a result of an increase in the number of deliveries made in the year as reflected in the uplift in revenue.

2016 electricity emissions decreased and gas consumption emissions increased, the gas in part due to slightly colder weather conditions in 2016 compared to 2015. Energy reduction projects carried out at our distribution facilities, which included installing more LED lighting in heavily trafficked areas such as the dispatch bays and voltage optimisation, resulted in a reduction in electricity emissions.

Commercial and motor vehicles are replaced respectively on a five and three-year basis, in doing so improving operational efficiencies and reducing operating costs and vehicle emissions. All of our commercial vehicles comply with Euro 5 emission standards which, when introduced, further reduced the levels of carbon monoxide, hydrocarbon, nitrogen oxide and particulate emissions. New commercial and motor vehicles delivered to us since October 2014 have been compliant with Euro 6 emission standards which were binding for the registration of new commercial and motor vehicles from September 2015. Euro 6 more than halves the amount of nitrogen oxides that a diesel car can emit with a cap of 80mg/km. We periodically review our fleet requirements to ensure the optimum design to maximise capacity and improve aerodynamics. Further usage of the Scottish Integrated Distribution system, which facilitates the consolidated distribution of Company products throughout Scotland through the use of trunker deliveries to a transhipment facility in Aberdeen, has further improved the efficiency of product delivery into northern Scotland. Following a period of evaluation, it is anticipated that other similar efficiency initiatives may be identified.

ESOS

The Energy Savings Opportunity Scheme ('ESOS') is a mandatory energy assessment scheme for large organisations in the UK, an assessment for which was carried out by an external assessor in late 2015. Due to the mix of energy, with the majority related to transport fuel, the assessment comprised an audit of the energy used by our transport activities, there being no requirement to audit the energy consumed in respect of buildings and industrial processes. The assessment identified a number of potential cost-effective energy saving measures, some of which have been implemented.

FORS

During the year, several of our businesses supplying goods into and around London sought and achieved bronze, accreditation with the Fleet Operator Recognition Scheme ('FORS'). FORS is a voluntary scheme that helps improve operators' performance in respect of all aspects of safety, fuel efficiency, economical operations and vehicle emissions. For vehicle operators, it confirms that they are meeting their legislative requirements, as well as helping to increase efficiency, reduce costs and secure work. Increasingly contractors insist upon a minimum of FORS bronze accreditation before accepting deliveries to premises in and around the London area, rejecting deliveries from non-accredited suppliers. As part of the accreditation process, additional signs and mirrors are fitted to vehicles in order to reduce cycling and motorcycling accidents. It is anticipated that the requirement for FORS accreditation will in time spread to other cities in the UK.

Waste

The waste arising from our operations is predominantly protective plastic packaging, cardboard poles and boxes and wooden pallets. The cardboard poles from the centre of full rolls, part rolls and cut lengths of carpet and vinyl delivered to our customers are subsequently collected from our customers' premises and re-used until no longer fit for purpose.

We continue to seek to increase the percentage that we recycle, baling plastics and cardboard, and stacking unwanted pallets for dispatch to specialist reprocessing agents, when it is economic to do so. This has significantly reduced the quantity of our waste going to landfill sites. Guidance on waste management is issued to the managers of the individual businesses to increase awareness of the need to control and reduce waste. Where possible, wrapping and packing materials are sourced from manufacturers using a high proportion of recycled materials.

Our approach to recycling is of environmental and financial benefit, with the bales of plastic and cardboard and the broken and unwanted wooden pallets either generating income or being collected for minimal charge.

We participate in initiatives to reduce the amount of waste going to landfill and increase that going into recycling both local to our businesses and on a national basis. In recent years a number of our businesses received recognition for our proactive approach.

According to Carpet Recycling UK, of which we are a member, 142,000 tonnes of carpet were recovered in 2016 for recycling or energy recovery, equivalent to a landfill diversion rate of 35%, a 14% increase on the 2015 diversion total of 125,000 tonnes. Energy recovery increased by 35% compared to 2015 as the use of carpets as a renewable fuel source in cement kilns continues to replace fossil fuels in this growing sector. A 50% increase in capacity for municipal energy-from-waste facilities over the past two years has also contributed to greater use of carpet waste in renewable electricity and energy generation.

We continue with initiatives to recover and recycle trimmings of carpet, vinyl and underlay arising during installation by our customers through the provision of on-site dedicated containers.

Within the UK, the Company complies with the Producer Obligations (Packaging Waste) Regulations 2007 (as amended) in compliance with the European Union Directive. The Company provides evidence to VALPACK, an organisation that provides confirmation to the UK government that the Company is continuing to meet UK recycling and recovery standards set by Defra.

Community

Whilst the Company does not support a specific charity or community, it is committed to encouraging charitable organisations local to our operating businesses and to engaging with the local communities. We value our relationship with the local stakeholders, supporting them financially and through the donation of products for specific projects.

In addition, the Company matches the charitable donations made by employees through the Pennies from Heaven payroll giving scheme. It also allows employees paid time off work to undertake charitable duties.

GOVERNANCE

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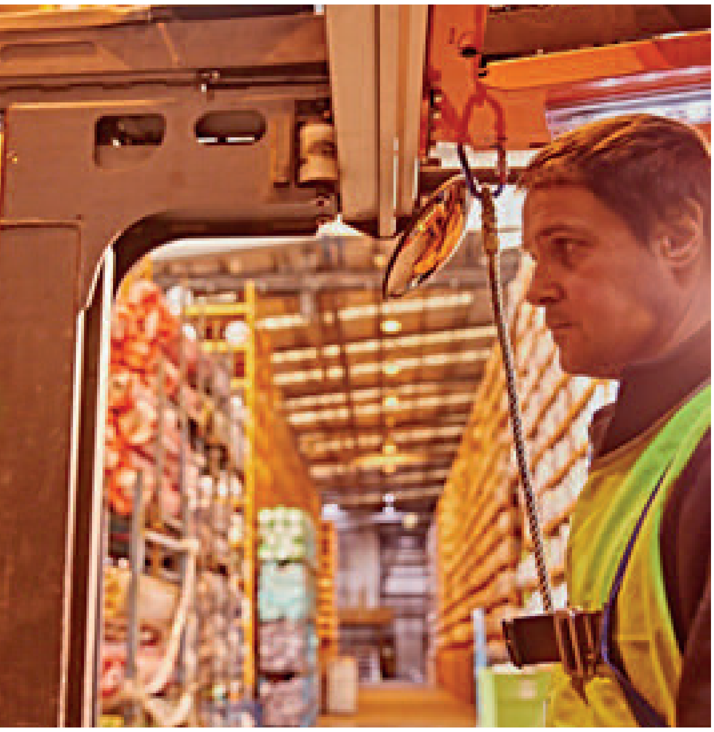


Chairman's Introduction to Governance

Our approach and commitment to corporate governance is essential to the delivery of our strategic priorities, support of sustainable growth and protection of shareholder value.

We set out on the following pages our approach and commitment to corporate governance which we consider to be essential to the delivery of our strategic priorities, support of sustainable growth and protection of shareholder value. We seek by way of this report to explain how, through the membership and work of the Board and its Committees, the approach to ensuring Board members have an appropriate understanding of the business and how the Board considers its effectiveness, your Company is directed and controlled. The report also explains the executive direction and control and our corporate governance structures and procedures which continue to change in response to changes in the rules that are in place at any point in time to ensure that they continue to be robust.

The 2014 UK Corporate Governance Code (the 'Code'), which sets out guidance in the form of principles and provisions on how companies should be directed and controlled to follow good governance practice, has applied throughout the year and I am pleased to confirm that the Board considers it has complied, as applicable, with the main principles of the Code. The Code is available on the Financial Reporting Council's website (www.frc.org.uk).

Together with the reports from each of the Nominations, Remuneration and Audit Committees, this report provides an overview of our key governance activities and practices during the period.

We consider that our Board has the diversity and mix of skills, experience, independence and knowledge required in order for the Company to be able to discharge its responsibilities successfully. Our Board evaluation this year was through an internal review process, further details of which are included on page 41. The Board is focused on the need to review and continue to develop its effectiveness, in order to support the Company in its ambitions. Profiles of each Director, together with information on their experience relevant to the Company, are set out on pages 36 to 37.

The Nominations Committee considered changes to the composition of the Board following the resignation of Tony Brewer on 14 September 2016. Steve Wilson, Group Finance Director, was appointed his successor as Chief Executive and Tony Judge, Commercial Director, will be appointed to the Board as Chief Operating Officer with effect from 31 March 2017. We are advanced with our search for a Chief Financial Officer. In addition we plan to recruit a further Non-Executive Director.

Further details on the Board's composition are given on pages 36 and 37.

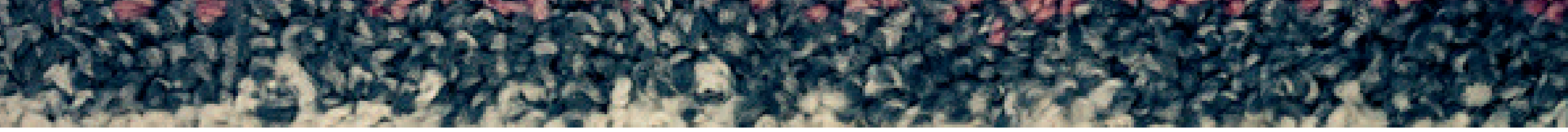
The basis on which the Company generates and preserves value over the longer term and the strategy for delivering the objectives of the Company are to be found in the Strategic Report on pages 2 to 33.

During the year, the Remuneration Committee has focused on the review of the remuneration policy, last put to Shareholders at the 2014 AGM. The Committee believes that the majority of the current remuneration framework continues to be effective in supporting the delivery of our strategic objectives; however, changes are recommended to the policy in respect of long-term share awards to ensure it is aligned with best practice and provides sufficient flexibility to support succession planning and potential changes to business needs over the coming three years. The revised policy is discussed in detail in the Remuneration Committee's Report on pages 52 to 62 and will be presented to Shareholders at the 2017 AGM.

The Audit Committee has focused on the development of the audit strategy and internal controls following the appointment of PwC as successor to KPMG after conducting a full tender of the external audit.

Further details are provided in the Audit Committee Report on pages 44 to 49.

Dick Peters
Chairman
7 March 2017



Board of Directors & Senior Management Team

R W Peters

Non-Executive Chairman

Dick was appointed Chairman of Headlam Group plc on 1 September 2013 following the resignation of Graham Waldron, having been appointed a Non-Executive Director in December 2005. Prior to his appointment as Chairman he had been the Chairman of the Audit Committee. He is a Director and Chairman of Headlam Pension Trustees Limited, the corporate trustee for the defined benefit and defined contribution pension schemes.

Dick was formerly Senior Partner for the East Midlands practice of Deloitte & Touche in Nottingham, and is a fellow of the Institute of Chartered Accountants. He has considerable experience of auditing large companies, both UK and overseas, transactional support and project management activities.

Committees – Audit, Nominations, Remuneration

S G Wilson

Chief Executive

Steve was appointed Chief Executive on 14 September 2016, having up to that date been the Group Finance Director, a position he had held since joining the business in December 1991.

Steve is a Non-Executive Director of Conviviality Plc, a UK wholesaler and distributor of alcohol and impulse products with a listing on the London Stock Exchange, and, until his retirement from their board on 22 September 2010, was the Non-Executive Chairman of Synergy Health plc, which delivers outsourced services to healthcare providers. He is a fellow of the Institute of Chartered Accountants.

Committees – Nominations

A K Eastgate

Senior Independent Director

Andrew was appointed a Non-Executive Director in May 2010 at which time he was appointed a member of the Audit, Remuneration and Nominations Committees. He is the Chairman of the Remuneration and Nominations Committees and Senior Independent Director. Andrew is a solicitor and was formerly a Partner in Pinsents, including being head of Pinsents' corporate practice in Birmingham.

Andrew has broad experience of advising quoted companies, particularly in connection with transactions and compliance issues, and is Chairman of Epwin Group Plc, the AIM listed manufacturer of low maintenance building products. He is also an experienced commercial mediator.

Committees – Audit, Nominations (Chairman), Remuneration (Chairman)

Changes to the Board

On 14 September 2016, Tony Brewer resigned from the Board after serving over 25 years as a Director, having been appointed an Executive Director in June 1991, becoming Managing Director of the Floorcoverings Division in January 1992, and appointed Group Chief Executive in November 2000.

Steve Wilson was appointed Chief Executive on 14 September 2016 and a recruitment process is in place to appoint a successor as Chief Financial Officer.

Tony Judge was appointed Chief Operating Officer on 14 September 2016. With effect from 31 March 2017 he will be appointed as a Director of Headlam Group plc. In accordance with the Articles of Association, Tony will retire from the Board at the first AGM following his appointment and stand for election. The Directors consider his appointment as a Director of the Company to be in the best interests of the Company and recommend shareholders to vote in favour of the resolution, as they intend to do in respect of their own shareholdings.

P J Lawrence
Non-Executive Director

Philip was appointed a Non-Executive Director in June 2015 at which time he was appointed a member of the Remuneration and Nominations Committees and Chairman of the Audit Committee. Philip is the Chief Executive of the Coal Authority, which on behalf of the Department of Business Energy and Industrial Strategy manages the effects of past coal mining, including subsidence damage claims, mine water pollution and other mining legacy issues. Prior to this, he held significant roles with Marconi plc and Deloitte & Touche. He is an Associate of the Institute of Chartered Accountants.

Committees – Audit (Chairman), Nominations, Remuneration

Senior Executive Management

G M Duggan
Company Secretary

Geoff was appointed Company Secretary in April 1998. He is a fellow of the Institute of Chartered Secretaries and Administrators and a fellow of the Chartered Institute of Management Accountants. He is additionally a Director of the corporate pension trustee.

D A Price
Commercial Director, selected UK Operations

On 14 September 2016, Darryl took operational responsibility for all UK businesses with the exception of Tamworth Mercado, National Carpets, Headlam Scotland and MCD Scotland.

Darryl joined the Company in February 1994 as Sales Office Manager at Thatcham before progressing to Operations Director at Thatcham and, from January 2003 to November 2015, was the Commercial Director responsible for the businesses in Coleshill. In November 2015 he was appointed to the Senior Executive Management at which time he took operational responsibility for 12 of the Company's UK businesses.

Darryl has 22 years' experience in the floorcoverings industry.

A R Judge
Chief Operating Officer

Tony Judge was appointed Chief Operating Officer on 14 September 2016, and with effect from 31 March 2017 he will be appointed to the Board of Directors of Headlam Group plc.

Tony joined the Company in May 1992 as the Managing Director of Florco, becoming the Commercial Director for the European businesses in 2000-2001, and in 2001 the Commercial Director of the Coleshill businesses. In 2005, in addition to Coleshill, he was appointed Managing Director of the Tamworth businesses and took operational responsibility for the Thatcham and Stockport businesses in 2012 and Gildersome in 2015. In September 2016, his role expanded to include responsibility for all operational matters.

Tony has 35 years' experience in the floorcoverings industry.

Corporate Governance Report

Our Governance framework helps the Group in the delivery of its strategic objectives and ensures that its obligations to its shareholders and others are understood and met.

The Board is collectively responsible to shareholders for the proper management and success of the Group. The Directors bring strong judgement to the Board's deliberations and the size, diversity and balance of skills and experience of the Board is considered appropriate for the requirements of the business.

The Board operates within a set of prudent and effective controls which sets the Group's values and standards, roles and responsibilities, accountabilities and the assessment and management of risk. Our governance framework helps the Group in the delivery of its strategic objectives and ensures that its obligations to its shareholders and others are understood and met.

The Board is the Group's principal decision making body. The schedule of matters reserved for the Board, which was last reviewed on 6 April 2016, is available on our website, www.headlam.com. It includes matters relating to strategy, capital expenditure, acquisitions and disposals and risk management.

The Board reviews the key activities of the business, receiving papers and presentations from Executives and senior management generally a week in advance of the meeting. The Company Secretary is responsible to the Board in respect of Board procedures and is available to individual Directors. In conjunction with the Chairman, the Company Secretary ensures that information distributed to the Board is sufficient, clear and accurate, circulated in a timely manner, and is appropriate to enable the Board to discharge its duties. All Directors are equally accountable for the proper stewardship of the Group's affairs. However, the Non-Executive Directors have a particular responsibility to ensure that the strategies proposed by the Executive Directors are fully discussed and critically examined.

The above, enables the Directors to promote the success of the Group for the benefit of its shareholders as a whole, while having regard to, among other matters, the interests of employees, the fostering of business relationships with customers, suppliers and others, and the impact of the Group's operations on the communities and environment in which the business operates.

Certain roles and responsibilities have been delegated by the Board to its principal Committees. Each Committee Chairman reports to the Board on decisions and actions taken. The terms of reference for each Committee are reviewed periodically to ensure they remain fit for purpose and comply with the provisions of the Code.

As at 31 December 2016 the Board comprised Dick Peters, Chairman, one Executive Director, Steve Wilson, Chief Executive, and two independent Non-Executive Directors, Andrew Eastgate and Philip Lawrence. Steve Wilson, formerly the Group Finance Director, had been appointed as Chief Executive on 14 September 2016 following the resignation of Tony Brewer.

The Board is supported in its role by the Audit, Nominations and Remuneration Committees, all of which have written terms of reference, the details of which are set out in the relevant Committee report.

The Directors' roles and membership of the Committees are as set out on pages 36 and 37 in the Directors' biographies.

The biographies also document each Director's significant other commitments and any changes to these commitments that occurred during the year.

Directors' attendance during the year at Board meetings is set out on page 40, and meetings of the Audit, Nominations and Remuneration Committees is given in the relevant Committee report.

The Board considers that it may be beneficial for the Executive Directors to hold an external Directorship to broaden their experience and normally this would be limited to one company. With effect from 31 January 2014, Steve Wilson was appointed a Non-Executive Director of Conviviality Plc.

The Board considers the balance achieved between Executive and Non-Executive Directors during the year, subject to the recruitment of a Chief Financial Officer to succeed Steve Wilson, was appropriate and effective for the control and direction of the business.

The roles and responsibilities of the Chairman and Chief Executive are clearly divided and periodically reviewed by the Board. Whilst collectively they are responsible for the leadership of the Group, the Chairman's primary responsibility is for leading the Board and ensuring its effectiveness. This includes ensuring the other Directors make an effective contribution and, through the Company Secretary, that the Directors receive accurate and timely information. The Chief Executive is responsible for implementing strategy, running the businesses in accordance with the powers delegated by the Board, objectives and policies agreed by the Board, for ongoing communication with shareholders and for the executive management of the Group.

The Senior Independent Director's role includes being a 'sounding board' for and intermediary to the Chairman, leading the assessment of the Chairman's performance and being available to shareholders. The role of other Non-Executive Directors includes challenge and contribution to Group strategy, periodically meeting with the Chairman without the Executive Directors present, questioning the delivery of strategic objectives and monitoring operational and financial performance.

The Chairman communicates frequently with the Non-Executive and Executive Directors, and the Non-Executive Directors have the opportunity to meet with and discuss any issues or concerns with the Chairman at any time throughout the year.

Matters that are not specifically reserved for the Board and its Committees under their terms of reference or for shareholders in general meeting are delegated to the Chief Executive.

Through the Nominations Committee, the Board ensures that plans are in place for the succession of the Executive and Non-Executive Directors.

The Directors bring strong judgement to the Board's deliberations and the size, diversity and balance of skills and experience of the Board are considered appropriate for the requirements of the business. The Board believes that all three Non-Executive Directors are independent of management and free from any business or other relationship that could materially interfere with the exercise of independent and objective judgement. In making this determination the Board has considered whether each Director is independent in character and judgement and whether there are relationships or circumstances which are likely to, or could, affect the Director's judgement. Andrew Eastgate, who served as the Senior Independent Director throughout the year is available to shareholders if they have concerns which are not resolved through the normal channels of the Chairman, Chief Executive or Chief Financial Officer, or for which such contact is inappropriate. The Non-Executive Directors do not participate in any bonus, share option or pension scheme of the Group. They are initially appointed for a three-year term and, subject to review and re-election, can serve up to a maximum of three such terms.

In order to fulfil their duties, procedures are in place for Directors to seek both independent advice and the advice and services of the Company Secretary, who is responsible for advising the Board, through the Chairman, on all governance matters.

The Non-Executive Directors periodically meet without the Chairman present, and also meet with the Chairman without management present.

Election and re-election of Directors

All Directors are subject to election by shareholders at the first AGM following their appointment by the Board. Under the Articles of Association of the Group, each of the Directors is required to retire by rotation at least once every three years. Details of the Directors retiring and seeking election or re-election at the forthcoming AGM are given to shareholders in the Notice of AGM.

The Board is of the opinion, supported by the Nominations Committee, that each Director retiring continues to make an effective and valuable contribution and demonstrates commitment to their role.

Whistleblowing Policy

We have a Whistleblowing Policy, the purpose of which is to ensure that our people feel secure when raising any concerns they may have without any adverse effect on their career and development.

Diversity Policy

It is our policy to recruit the best people and to invest in our people. Responsibility for diversity and equality is a matter for the Board, it being essential that we consider diversity in our decision-making process.

Corporate Governance Report

Table showing gender diversity

	Directors	Senior managers	Other employees	Total employees
Male	4	290	1,685	1,979
Female	–	33	372	405
Number of employees at 31 December 2016	4	323	2,057	2,384

Board meetings and attendance

The Board met ten times in the year, one more than the usual nine times a year, at times that ensure the latest operating information is available for review and sufficient focus can be given to matters under consideration. During the year there is ample opportunity for the Chairman to meet with the Non-Executive Directors without the Executive Directors being present, should this be deemed appropriate. In addition, Directors have contact between meetings and, on occasions, visit trading locations in order to maintain contact with the Group's business. A record of Directors' attendance at Board meetings held during the year is set out below and Committee meeting attendance is given in the relevant Committee report.

Steve Wilson	10/10
Dick Peters	10/10
Andrew Eastgate	10/10
Philip Lawrence	10/10
Tony Brewer*	7/7*

*Resigned 14 September 2016

In addition to the ten principal Board meetings held during 2016, there were two meetings which approved the 2016 Interim Report and 2015 Annual Report and Accounts and one exclusively held to consider strategic issues. The meetings approving the 2016 Interim Report and 2015 Annual Report and Accounts are constituted by a Committee of the Board formed for that sole purpose comprising the Group Chief Executive and Group Finance Director, having considered the views of the whole Board beforehand.

Directors' interests and indemnity arrangements

At no time during the year did any Director hold a material interest in any contract of significance with the Group or any of its subsidiary undertakings, other than a third-party indemnity provision between each Director and the Group, and service contracts between each Executive Director and the Group. The Group has purchased and maintained throughout the year Directors' and Officers' liability insurance in respect of itself and its Directors. The Directors also have the benefit of the indemnity provision contained in the Group's Articles of Association. This provision extends to include the Directors of Headlam Group Pension Trustees Limited, a corporate trustee of the Group's occupational pension schemes, in respect of liabilities that may attach to them in their capacity as Directors of that corporate trustee. These provisions were in force throughout the year and are currently in force. Details of Directors' remuneration, service contracts and interests in the shares of the Group are set out in the Directors' Remuneration Report.

Directors' conflicts of interest

Procedures are maintained by the Board whereby potential conflicts of interests are reviewed regularly. These procedures have been designed so the Board may be reasonably assured that any potential situation where a Director may have a direct or indirect interest which may conflict, or may possibly conflict, with the interests of the Group are identified and, where appropriate, dealt with in accordance with the Companies Act 2006 and the Group's Articles of Association. The Board has not had to deal with any conflict during the period.

Induction and training

When joining the Board, induction programmes are tailored for each individual Director. A comprehensive information pack is compiled which includes background information about the Group, Directors' duties and responsibilities, Board meeting procedures, internal Group policies, structure charts, matters reserved for the Board and Committee terms of reference. It also includes an explanation of the Group's financing structure, relevant statutory and regulatory guidance notes, including the UK Corporate Governance Code and the Group's share dealing policy. With the appointment of Tony Judge as Chief Operating Officer and the forthcoming appointment of a new Chief Financial Officer, specific internal and external training programmes are being developed.

An induction programme will include site visits and meetings with relevant colleagues and advisers.

A briefing on the general Group strategy, including visits to Group businesses, is provided by the Chief Executive. Training and development in the year took various forms, including visits to Group businesses and attendance at courses run by professional bodies on various commercial and regulatory matters. Directors receive regular updates appropriate to the business throughout the year aimed at developing and refreshing their knowledge and capabilities. All Directors are considered to be suitably qualified, trained and experienced so as to be able to participate fully in the work of the Board. To assist with the independent conduct of their function and, if required, in connection with their duties, a process is in place for the Non-Executive Directors to obtain professional advice at the Group's expense.

Training and development

The Chairman takes responsibility for ensuring that Directors continually update their skills, knowledge and familiarity with the Group. Where identified, training needs are incorporated into the Board's agenda. The Group provides the resources to meet development requirements for individual Directors as and when required and it will continue to review development initiatives for Directors.

For example, two of the Non-Executive Directors attended external technical seminars run by professional advisers and guidance was provided on the new market abuse regulations and other new regulations.

The Non-Executive Directors are encouraged to further their knowledge of the Group by spending time with the Executive Directors and other senior managers on visits to our distribution facilities. Non-Executive Directors are also encouraged to engage with our people across the business to further enhance their understanding of the business.

Directors holding significant commitments outside of the Group are required to disclose them prior to appointment and on an ongoing basis where there are any changes. Actual and potential conflicts of interest are regularly reviewed. Under the Articles of Association, the Board has authority to authorise potential conflicts of interest and to impose any limits or conditions it sees fit. All of the Directors are required to allocate sufficient time to the Group to discharge their responsibilities effectively. As part of the annual evaluation process, this is reviewed by the Chairman.

Performance evaluation 2016

The Code recommends that an evaluation of the effectiveness of the Board and its Committees is conducted annually and that this process is externally facilitated at least every third year.

During the year, an evaluation of the Board's effectiveness, including the effectiveness of the Board Committees, was undertaken internally. The review was broadly based, focusing on the key drivers of effectiveness and comprised meetings with each member of the Board and other senior Executives together with a review of Board and Committee meeting packs. The individual meetings considered matters such as the balance and composition of the Board, the extent of independent challenge and oversight provided by the Non-Executive Directors. Also included was consideration of how the Board perceived it had performed and risk management and succession planning. In respect of the Committees, the evaluation considered the performance of the respective Committees throughout the year, whether agendas covered their remit and the appropriateness of that remit.

The evaluation concluded that the Board and its Committees continued to operate effectively, meeting the requirements and spirit of the Code.

The Nominations Committee has access to the performance evaluation process and the Chairman has confirmed that Andrew Eastgate, who is standing for re-election at this year's AGM, together with Tony Judge, who is standing for election at this year's AGM, and will be appointed to the Board on 31 March 2017, have been performing effectively and have demonstrated commitment to their roles. The Board will continue to review its performance and that of its Committees and individual Directors on an annual basis and for 2017 the process will include external evaluation.

Fair, balanced and understandable assessment

In accordance with the Code's requirement that the Board should consider whether the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable, reviews are undertaken by the finance team as part of the year end process. The Board receives drafts of the Annual Report and Accounts to allow sufficient time to review and provide an opportunity for challenge and discussion, ahead of approving the final documents. In addition, the external Auditor reviews the consistency between the narrative reporting and financial disclosures.

Corporate Governance Report

Communication with shareholders

The Group places considerable importance on communication with shareholders. Engagement with our shareholders is essential to ensure a greater understanding of, and confidence in, the development and implementation of the medium and longer-term strategy of the Group. When reporting to shareholders, the Board aims to present a balanced and understandable assessment of the Group's financial position and prospects, reporting twice a year, when its half year and full year results are announced and respectively an Interim and Annual Report is issued to shareholders. Additionally as necessary, the Group issues a trading update in advance of the interim and final results announcements. Further information regarding business developments is available to investors on the Group's website: www.headlam.com.

The Group has an ongoing programme of dialogue and meetings between the Executive Directors and institutional investors, fund managers and analysts which cover strategy, trading and market conditions. Contact with the major shareholders is principally maintained by the Chief Executive and Director of Communications. A number of these meetings were held at certain of our distribution centres with the aim of providing them with increased exposure to our operations and management. The Chairman ensures that the views of shareholders are communicated to the Board as a whole. Buchanan continue in their role of financial public relations and investor relations adviser with the objective of improving communication with shareholders.

The Chairman and Chief Executive have met with the Group's brokers during the year to ensure they are aware of the current views of major shareholders and of any material issues they may have. These reports include summaries on the market's reaction to results announcements and the subsequent meetings between management and investors. External brokers' reports on the Group are circulated to all Directors. The Senior Independent Director and the other Non-Executive Directors are invited to attend presentations to analysts and institutional shareholders, in particular the final and interim results presentations, the Chairman attending meetings with the representatives of the largest shareholders in the year. This ensures that shareholders' views and any issues of concern are heard by the Board.

The investor section of the Group's website is available to all shareholders and provides share price information, results presentations and announcements, financial calendars and general information on the business. The Annual Report and Accounts is a key communication tool providing a comprehensive review of the business, details of our governance arrangements and annual results.

All shareholders have the opportunity to communicate directly with the Board at the AGM. shareholders are able to ask questions during the meeting, followed by an opportunity to meet with the Directors of the business on an informal basis. The senior management team also attend the AGM and meet with shareholders before and after the meeting. All of the Directors attend and the Chairman of the Board and each Committee are available to answer shareholder questions during the formal business of the meeting. The voting on all resolutions at the AGM is conducted on a show of hands unless a poll is requested. The Group will release the results of voting, including proxy votes on each resolution, on its website on the next business day at www.headlam.com/investors and announce them through a regulatory news service. Details of the 2017 AGM are set out in the Notice of Annual General Meeting on pages 142 to 154.

Board Committees

The Board has established Audit, Nominations and Remuneration Committees to oversee and debate important issues of policy and assist in attending to its responsibilities, with terms of reference that each comply with the provisions of the Code and are available on written request from the Company Secretary at the registered office or on the Group's website.

Audit Committee

Information on the activities of the Audit Committee is given in the Audit Committee Report on pages 44 to 49 which should be read in conjunction with this report.

Remuneration Committee

The Directors' Remuneration Report is set out on pages 50 to 69. Our Remuneration Committee has reviewed the Remuneration Policy during the year and a revised policy will be subject to a binding vote by shareholders at the 2017 AGM. The report also includes the Annual Report on Remuneration which is subject to an advisory vote at the 2017 AGM.

Nominations Committee

Information on the activities of the Nominations Committee is given in the Nominations Committee Report on pages 70 to 71 which should be read in conjunction with this report.

The Group's risk management processes seek to ensure sustainable development throughout the conduct of its business in a way which:

- satisfies its customers;
- maintains proper relationships with suppliers and contractors;
- provides a safe and healthy workplace;
- develops environmentally aware processes;
- minimises the cost and consumption of increasingly scarce resources; and
- maintains a positive relationship with the communities in which it operates.

The systems are designed to meet the Group's particular needs and to manage rather than eliminate risks, by their nature, providing reasonable and not absolute assurance against material misstatement or loss. The measures taken, including physical controls, segregation of duties and reviews by management, are considered by the Board to provide sufficient and objective assurance.

The Board maintained its process of hierarchical reporting and review during the year in order to evaluate the effectiveness of the Group's systems of financial and non-financial controls. A comprehensive series of operating and financial control procedures applying to all businesses has been developed and the Group finance team performs monthly reviews to verify that the businesses are complying with the prescribed operating and financial control procedures. Additionally, the Board reviews risk management arrangements and the Audit Committee receives reports from the external Auditor on matters identified in the course of its statutory audit work. These procedures provide a documented and auditable trail of accountability, the results of which are periodically reviewed for completeness and accuracy.

These procedures allow for successive assurances to be given at increasingly higher levels of management through to the Board. Planned corrective actions are monitored for timely completion. The Board has not identified any failings or weaknesses, or been advised of any, which it has determined to be significant during the course of its review of the system of internal control. There were in addition no changes in the Group's internal controls or financial reporting that have materially affected, or are reasonably likely to affect, the Group's systems of internal control.

A comprehensive planning system includes detailed reviews at all business and formal reviews and approval of annual plans by the Board. Actual performance is measured on a monthly basis against plan and prior year, including a detailed explanation of significant variances. Revenue, gross margin and cash flow are reported on a daily basis against plan and prior year. The control procedures operated by the Group are designed to ensure complete and accurate accounting for financial transactions and to limit the potential exposure to fraud. Guidelines for capital expenditure and investment appraisal include annual plans, detailed appraisal and review procedures, authority levels and due diligence requirements when businesses are acquired and the acquisition or disposal of a business requiring formal Board approval. These detailed reviews are an important aspect of management reporting in the identification of new and emerging risks.

An ongoing process of risk management and internal control in accordance with the Code has been in place for the financial year under review and up to the date of this report, the careful management of risk considered to be a key activity in delivering business opportunities.

The ethos of the Group, delegation of responsibility and other control procedures together with accounting policies and procedures are communicated through the Group and employment handbook, supported by the Group's anti-bribery policy. The integrity and competence of personnel is assessed during the recruitment process and monitored throughout employment.

The Group promotes a high standard of health and safety management at all levels supported by training programmes at operating businesses. Group health and safety rules are monitored and audited to promote a high level of awareness and commitment, with individual businesses assessed on a periodic basis. Remedial solutions are implemented where necessary, action plans and progress being monitored and reported.

Audit Committee Report

The Committee has continued its focus on the integrity of financial reporting and internal controls throughout the year...and are able to confirm they have carried out a robust assessment of the principal risks facing the Group.

As Chairman of the Audit Committee ('Committee') I am pleased to present the Audit Committee's Report for the year ended 31 December 2016.

The Committee is composed wholly of the Chairman and independent Non-Executive Directors. Each of the Committee members contributes their considerable business and financial experience to the reports, statements and matters considered, challenged and debated by the Committee to effectively assess the external audit of the Company and the internal control and risk management systems. The Board considers that both Dick Peters and I meet the requirements of the UK Corporate Governance Code ('Code') as having recent and relevant financial experience.

The Committee has continued its focus on the integrity of financial reporting and internal controls throughout the year, particularly the process by which the Directors are able to confirm 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. The Committee continues to monitor changes in regulation, particularly relating to operational health and safety matters, and reviews the potential impact on the Group's financial reporting and control processes. To ensure that it remains appropriate and provides a robust assessment of the principal risks, the Committee has reviewed the risk management framework and the assurance process.

The robust assessment is supported by the Group's accounting team which undertakes reviews of each business, similar to those that might be undertaken by a formal internal audit function. The Committee has reviewed the proposed internal controls and the detailed audit plan for the next 12 months which help the business achieve its strategic objectives by improving the effectiveness of risk management, control and governance processes.

As previously disclosed, PricewaterhouseCoopers ('PwC') were appointed last year following a formal tender to which KPMG LLP, given the length of their tenure, were not invited to participate. The Committee has welcomed the fresh pair of eyes and believes that PwC have to date provided an effective audit service and recommends their reappointment to shareholders at the forthcoming AGM.

The Report describes the work of the Committee, its responsibilities and key tasks as well as its major areas of activity and key considerations for the financial year.

Philip Lawrence
Chairman of the Audit Committee
7 March 2017

Audit Committee

The members of the Committee and its Chairman are as follows:

	From	To
Philip Lawrence (Chairman)	1 June 2015	To date
Dick Peters	10 March 2006	To date
Andrew Eastgate	17 May 2010	To date

Committee meetings

The Committee has an agenda linked to events in the Group's financial calendar, normally meeting at least twice a year before the final and interim results announcements. The Committee met three times in the year, the three members attending all meetings, during which it discharged its responsibilities as set out in the terms of reference and schedule of business for the year. Whilst only members of the Committee are entitled to be present at meetings, the external Auditor, Chief Executive and Chief Financial Officer may attend by invitation. The Committee has authority to investigate any matters within its terms of reference, access resources, call for information and obtain external professional advice at the cost of the Group. The full terms of reference of the Committee, which were reviewed during the year, can be found in the governance section of the Group's website, www.headlam.com.

Role of the Committee

The Committee is responsible for monitoring and reviewing:

- the effectiveness of the Group's systems of internal control and risk management and control over financial reporting;
- updates from Executive Directors and senior executive management on key financial control matters;
- the consistency of and any changes to the Group's accounting policies, the application of appropriate accounting standards and methods used to account for significant or unusual transactions;
- the integrity of the interim and annual financial statements, including a review of the significant financial reporting judgements contained therein;
- the effectiveness of the external audit process;
- the external Auditor's plan for the audit of the Group's accounts, confirmation of the external Auditor's objectivity and independence and of the individuals carrying out the audit, approval of the proposed audit fee, approving the audit terms of engagement, the Company's relationship with the external Auditor and management's response to any major external audit recommendations;
- reports from management and the external Auditor on the Group's systems of internal control, including a summary of and commentary on the business risks and internal control processes, and reporting to the Board on the results of this review;
- the appointment, reappointment or dismissal of the external Auditor;
- Non-audit services and fees;
- the application of the Board's policy on Non-audit work performed by the Group's external Auditor together with the Non-audit fees payable to the external Auditor;
- the appropriateness of an internal audit function;
- the Group's overall approach to securing compliance with laws, regulations and governance; and
- the Group's systems for detecting fraud, preventing bribery and allowing employees to raise concerns in a safe and confidential manner.

Key activities of the Committee during the year

In addition to matters relating specifically to its terms of reference, agendas incorporate matters arising and topical items on which the Committee has chosen to focus.

Audit Committee Report

The work of the Committee during the year is summarised in the table below.

Internal controls and risk	External auditor	Accounting
Considered reports from management and the external Auditor on their assessment of the control environment.	Considered and approved the audit approach and scope of the audit work to be undertaken by the external Auditor and the fees for the same.	Reviewed the half year and annual financial statements and the significant financial reporting judgements including the planning for the new lease accounting standard (effective 2019).
Assessed the effectiveness of the Group's internal control environment and the need for an internal audit function.	Reviewed reports on Audit findings.	Considered the liquidity risk and the basis for preparing the Group half yearly and full year accounts on a going concern basis and reviewed the related disclosures in the annual report and accounts.
Reviewed the main corporate risks and the outcomes from testing the systems and processes for managing and mitigating those risks, satisfying itself that the risk management framework provides sufficient assurances.	Considered the independence of the external Auditor and their effectiveness.	Reviewed reporting disclosures in relation to internal controls, risk management, principal risks and uncertainties and the work of the Committee.
Reviewed matters reported in accordance with the whistleblowing policy which allows employees to raise concerns in a safe and confidential manner.		Reviewed and considered whether the annual report and accounts is balanced, fair and understandable, and provides information necessary for shareholders to assess the Group's performance, business model and strategy. Drafting a viability statement that assesses the prospects of the Group over an appropriate period. The Committee considered that the Group's existing three year financial planning view makes that time period the most appropriate.

Significant issues considered by the Committee

After discussion with both management and the external Auditor, the Committee determined that the key risks of misstatement of the Group's financial statements, related to:

- impairment of goodwill;
- complex supplier arrangements; and
- inventory valuation.

These issues were discussed with management during the year and with the external Auditor at the time the Committee reviewed and agreed the external Auditor's Group audit plan and also at the conclusion of the audit of the financial statements.

Impairment of goodwill

As more fully explained in note 1 to the financial statements, the Group's principal non-financial assets are grouped into cash generating units ('CGUs') for the purpose of assessing the recoverable amount.

The Group's CGUs represent individual operating businesses, either in the UK or in Continental Europe. As set out in note 11 to the financial statements, all CGUs to which goodwill is allocated, in accordance with the requirements of IFRS, are tested for impairment on an annual basis.

This year, the impairment reviews for the CGUs to which goodwill is allocated did not result in an impairment loss.

In performing their impairment tests, management determined the recoverable amount of each CGU and compared this to the carrying amount. Management reported to the Committee the results of their impairment assessment, noting to the Committee that future cash flows for each CGU had been estimated based on the most up-to-date business forecasts or actual financial results and discounted using discount rates that reflected current market assessments of the time value of money and risks specific to the assets. Management highlighted to the Committee how they arrived at the key assumptions to estimate future cash flows for the CGUs, specifically future growth rates and discount rates.

Management also brought to the attention of the Committee the sensitivity analysis to be disclosed in note 11 to the financial statements with regard to the recoverable amount of the CGUs' goodwill.

The Committee interrogated management's key assumptions to understand their impact on the CGUs' recoverable amounts. The Committee was satisfied that the significant assumptions used for determining the recoverable amount of CGUs to which goodwill is allocated had been appropriately scrutinised and challenged and were sufficiently robust.

Complex supplier arrangements

The Group has a significant number of rebate agreements with suppliers. These agreements can contain multiple terms or tiered arrangements based on the volume of goods purchased and significant amounts remain outstanding at the year end.

The Committee reviewed management's calculation of amounts expected to be received. Management explained the process of recalculating the amounts expected to be received and confirming these balances with suppliers. The Committee challenged the assumptions used by management and reviewed the level of cash receipts or credit notes received after the year end. The Committee is satisfied that the amounts recognised have been appropriately scrutinised and that the assumptions upon which the calculation were based are sufficiently robust.

Audit Committee Report

Inventory valuation

As set out in the statement of financial position, inventory amounts to £126.0 million and represents the Group's second largest asset class. Inventory is held across a broad and diverse product range which is subject to a risk that changes in consumer tastes and demand result in some inventory lines becoming slow-moving or obsolete, such that the recoverable amount is less than the carrying value.

The Committee discussed the Group's management of its inventory position and calculation of net cost and gave careful consideration to the gross carrying value and related provisions. Management explained to the Committee that the process of determining the appropriate valuation of inventory entailed close monitoring of inventory levels, review of relevant supplier rebates or overheads which should be absorbed into the cost of inventory, review of the ageing profile and consideration of inventory sold for less than its carrying value. These three measures are reported to senior management on a monthly basis by individual businesses. Management use this information to determine the provisions to be made against inventory.

The Committee reviewed the valuation basis and challenged management's assumptions. The Committee was satisfied that the significant assumptions used for determining the valuation of inventory had been appropriately scrutinised and challenged and were sufficiently robust.

Other matters considered by the Committee

Valuation of employee benefit liabilities

In the UK, the Group operates a defined benefit pension plan, further details of which are set out in note 20 to the financial statements. At 31 December 2016, the scheme had assets of £109.7 million and liabilities, measured on an IAS 19 basis, of £128.0 million, with a net deficit of £18.3 million.

As set out in note 1 to the financial statements, the plan liabilities are calculated by estimating the amount of benefit that employees have earned for their service in current and future periods. This estimation requires making certain assumptions, notably in relation to inflation rates, mortality rates and the discount rate to apply to determine present value. The selection of these assumptions is subjective and small changes in these assumptions can materially impact the net IAS 19 deficit reported in the statement of financial position. The assumptions adopted by management are set out in note 20 to the financial statements.

In selecting the assumptions, management took advice from the Group's external actuary and considered the appropriateness of this advice in light of the specific circumstances of the UK plan. Management highlighted to the Committee how they arrived at the key assumptions.

The Committee reviewed management's assumptions and were satisfied that they had been appropriately scrutinised and challenged and were robust. They also reviewed the sensitivity analysis set out in note 20 to the financial statements and consider it to be appropriate.

The Committee considered the views and procedures of the external Auditor, which entailed a benchmarking of management's assumptions with the external Auditor's expectations.

Misstatements

Management reported to the Committee that they were not aware of any material misstatements or immaterial misstatements made intentionally to achieve a particular presentation. The external Auditor reported to the Committee the misstatements that they had found in the course of their work and no material amounts remain unadjusted. The Committee confirmed that it was satisfied that the external Auditor had fulfilled their responsibilities with diligence and professional scepticism.

After reviewing the presentations and reports from management and consulting, where necessary, with the external Auditor, the Committee was satisfied that the financial statements appropriately addressed the critical judgements and key estimates, both in respect to the amounts reported and the disclosures. The Committee was also satisfied that the significant assumptions used for determining the value of assets and liabilities had been appropriately scrutinised and challenged and were sufficiently robust.

The Committee has welcomed the fresh pair of eyes which has resulted in a restatement of the comparative balance sheet as explained in note 1.

Internal audit

In accordance with the Code, the Committee has undertaken an assessment of the need for a Group internal audit function. The Committee considers that the Group's accounting team, control systems and associated procedures are adequate for the business and therefore does not currently propose to introduce a formal Group internal audit function. The Committee will continue to keep the matter under review.

External audit

The Committee reviews annually the appointment and performance of the external Auditor and considers their independence and objectivity taking into account all appropriate guidelines. Following a review of PwC's performance and independence in 2016, including compliance with rules on Non-audit services, the Committee was satisfied with the external Auditor's effectiveness and independence.

The Committee assessed the ongoing effectiveness of the external Auditor and audit process on the basis of meetings with Executive Directors. In reviewing the independence of the external Auditor, the Committee considered a number of factors which included the standing, experience and tenure of the external audit partner, the nature and level of services provided by the external Auditor and confirmation from the external Auditor that it had complied with relevant regulatory requirements.

The Committee has the specific task of keeping the nature and extent of Non-audit services provided by the external Auditor under review in order to ensure that objectivity and independence are maintained. The external Auditor has processes in place to ensure independence is maintained when providing Non-audit services and has written to the Committee confirming that, in its opinion, they remain independent within the meaning of the regulation on this matter and their professional standards.

In addition, the fees and objectivity of the external Auditor were considered by the Committee. The Committee recognises that there are occasions when it is advantageous to use the external Auditor to undertake non-audit services, where they are best placed to do so. The policy states that non-audit fees paid to the external Auditor should not exceed 70% of the audit fee. The Chairman of the Committee is required to authorise Non-audit work above a pre-agreed threshold. A breakdown of audit and Non-audit fees is provided in note 3 to the financial statements.

The Committee has independent access to the external Auditor and the external Auditor has direct access to the Chairman of the Committee outside formal Committee meetings. At each meeting there is an opportunity for the external Auditor to discuss matters with the Committee without executive management being present.

Summary

The Committee has concluded as a result of its work during the year that it has acted in accordance with its terms of reference and fulfilled its responsibilities. The Committee Chairman will be available at the AGM to answer any questions on the work of the Committee.

Directors' Remuneration Report

THE CHAIRMAN'S ANNUAL STATEMENT

We have reviewed our binding remuneration policy this year which is to be put to shareholders at the 2017 AGM. The Committee is proposing changes which simplify the structure whilst continuing to link reward to the long-term performance of the business.

On behalf of the Board, I am pleased to present the Directors' Remuneration Report for 2016, which includes this statement, the Directors' remuneration policy which is intended to take effect from 25 May 2017 and the Annual Report on Remuneration for the year ended 31 December 2016. Our previous policy was adopted in 2014 and, as we are required to put the policy to shareholders every three years, resolutions to approve the updated Directors' remuneration policy, and the Annual Report on Remuneration, will be put to shareholders at the forthcoming Annual General Meeting. In addition, we are seeking approval for the adoption of a new long-term incentive plan and a deferred bonus plan.

Remuneration policy

The Committee has undertaken a detailed review in light of recent changes at Executive Director level and feedback from investors and voting bodies, and is proposing some changes with the aim of creating a framework which is simpler than the current structure and which encourages long-term focus on sustained business improvement. Our objective has been to create a competitive reward package which is appropriate for a business of Headlam's current size but with flexibility to change as the business grows. We are proposing to:

- Remove our bonus matching share plan (the 'Co-Investment Plan' or 'CIP') so that no further awards will be made.
- Introduce a new performance share plan ('PSP') with a maximum award proposed for 2017 of 80% of salary. The PSP also has a two year holding period and will therefore, in line with best practice, constitute a five year plan from grant to vesting.
- Introduce deferral into the annual bonus so that one-third of any amount earned is deferred into shares for two years. This deferral element is delivered under the terms of Deferred Bonus Plan ('DBP').
- Currently there is no pension provision in the 2014 policy and whilst there is no intention to provide a pension to the Chief Executive or the newly announced Chief Operating Officer, for future external hires a maximum pension contribution (or cash allowance in lieu of pension) of up to 15% of salary has been provided for in the new policy.
- Clarify our shareholding guidelines, which require that Executive Directors hold at least 2 × salary in Group shares.

Detailed terms of both the PSP and the DBP are summarised on page 60.

The key terms of the PSP are as follows:

Maximum	A current maximum award of 80% of salary. The policy includes provisions to allow for a greater award to be made in future (but no more than 100%) if the Committee considers this appropriate but this would only be done together with a review of the applicable performance targets.
Holding period	To balance the overall long-term nature of the package, and in line with best practice, a two year post-vesting holding period has been included. Awards will not be released to participants until the end of the holding period.
Performance metrics	We are adopting the same metrics in place for the CIP which are 80% based on Adjusted EPS growth and 20% based on relative Total Shareholder Return against the FTSE Small Cap index. Further details of the targets are provided on page 55.
Threshold vesting	25% of the PSP award vests for threshold vesting where previously this was 30% under the CIP.
Dividend equivalents	Dividend equivalents will be earned over the holding period but not over the performance period.

Business performance and incentive out-turn for 2016

The business performed strongly during the year with a growth in revenues and improvement in our margins which resulted in reported 2016 underlying profit before tax of £40.1 million, an improvement on 2015 of 12.6%. Bonus earned, based on profit before tax (after non-underlying items) of £38.2 million, was 77% of maximum.

The CIP award granted on 1 April 2014 was subject to an EPS growth target for the three financial years ended 31 December 2016 and relative TSR measured against the FTSE Small Cap Index. Due to strong EPS performance and share price performance over the period, the CIP will vest at 98.6% and details are provided on page 65 of the report.

In September Tony Brewer resigned and Steve Wilson, formerly Group Finance Director, was appointed as our new Chief Executive. Steve's salary was increased to £475,000 with effect from 1 January 2017 to reflect his new role and positioned at a level which reflected his experience and responsibilities whilst also being set at a level below that of the outgoing Group Chief Executive, Tony Brewer (£557,600).

The exit arrangements for Tony Brewer are set out in detail on page 66. Under the terms of his contract and as disclosed in our 2014 remuneration policy, Tony was contractually entitled to a bonus equal to the average bonus over the two financial years prior to his departure. Tony's long-term incentive awards under the CIP have all been prorated for time served and will vest at the usual time. Shareholders should note that under new service contracts agreed this year for all new Executive Directors, including Steve Wilson, there is no contractual right to a bonus on departure and this change is reflected in the new policy.

Following a review of Non-Executive Director and Chairman fees, these were structured to increase the base fee from £36,000 to £40,000 whilst reducing the fees for chairing a committee from £7,000 to £5,000 as the Board felt this was a more appropriate balance to reflect time and responsibilities. Fees for the Senior Independent Director are £10,000. In addition, the Chairman's fee was increased to £110,000 on the basis that it had fallen markedly behind competitive practice and was not an appropriate reflection of the time and experience brought to the Board by the Chairman.

Reward for 2017

No changes are proposed to the annual bonus for 2017, other than the introduction of the deferred element under the new policy.

Subject to shareholder approval, the first award under the PSP will be made following the AGM. The award for the Executive Directors will be 80% of salary. The EPS target required for maximum vesting has been set at 8% annual growth which is above current consensus forecasts and above the internal business plan and at a level which the Committee considers to be appropriate given the level of stretch within the forecast numbers. The Committee is satisfied that the EPS target range appropriately reflects business risks and uncertainties and fully encompasses management's expected positive variance over the next three years. Further details are provided on page 55.

We announced that the Board will be strengthened by the addition of Tony Judge as our Chief Operating Officer, with effect from 31 March 2017. Tony's salary has been set at £425,000 to reflect the extension of his existing responsibilities and the scope of this new role.

Conclusion

We believe that the combination of a holding period on the new PSP and newly introduced deferral into shares under the annual bonus, together with the shareholding guidelines, aligns Executive Director interests with shareholders and create a satisfactory long-term framework for our business. We also believe that the introduction of a more appropriate long-term incentive which rewards fairly to all participants, based on a combination of internal and external performance measures which shareholders have supported in the past, will help to support a culture change within our business focused on fairness, rewarding appropriately and longevity of decision making.

We remain committed to a responsible approach to executive pay as I trust that this Remuneration Report demonstrates.

A. K. Eastgate

Andrew Eastgate
Chairman of the Remuneration Committee
7 March 2017

DIRECTORS' REMUNERATION POLICY

Key principles

Headlam's remuneration package for Executive Directors has been designed based on the following key principles:

- To appropriately align executive reward with the Group's strategic goals and the delivery of value to shareholders;
- To promote appropriately the long-term success of the Group, through the rigorous application of stretching and transparent performance conditions; and
- To have a competitive mix of base salary and short and long-term incentives, with an appropriate proportion of the package determined by stretching targets linked to the Group's performance.

Policy table for Executive Directors

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance measures
Base salary	To provide a competitive base salary for the market in which the Group operates to attract and retain Executives of a suitable calibre.	Salaries are usually reviewed annually taking into account: ■ pay and conditions elsewhere in the Group; ■ overall performance; ■ individual performance and experience; ■ competitive salary levels and market forces.	While there is no maximum salary, increases will normally be in line with the typical range of salary increases awarded (in percentage of salary terms) to the wider workforce. Larger salary increases may be awarded to take account of individual circumstances, such as, but not limited to: ■ where an Executive Director has been promoted or has had a change in scope or responsibility; ■ an individual's development or performance in role (e.g. to align a newly appointed Executive Director's salary with the market over time); ■ where there has been a change in market practice; or ■ where there has been a change in the size and/or complexity of the business. Increases may be implemented over such time period as the Committee deems appropriate.	Although there are no formal performance conditions, any increase in base salary is only implemented after careful consideration of individual contribution and performance.

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance measures
Benefits	To provide broadly market competitive benefits as part of the total remuneration package.	Executive Directors receive benefits in line with market practice, and these include life assurance, private medical insurance, company car or car allowance and, where relevant, relocation expenses. Other benefits may be provided based on individual circumstances.	Whilst the Committee has not set an absolute maximum on the level of benefits Executive Directors may receive, the value of benefits is set at a level that the Committee considers appropriate against the market and provides a sufficient level of benefits based on individual circumstances.	Not applicable.
Retirement benefits	New appointments may be entitled to an appropriate level of retirement benefit (or cash allowance equivalent).	The current Chief Executive does not receive pension benefits. For new appointments the Group may offer participation in a defined contribution pension plan or may permit Executive Directors to take a cash supplement instead of contributions to a pension plan.	Up to 15% of base salary.	Not applicable.
Save as You Earn Scheme	Participation in the Save as You Earn share option scheme ('SAYE') promotes a sense of ownership and aligns interests with the Group.	The SAYE is an HMRC tax qualifying monthly savings scheme facilitating the purchase of shares at a discount by eligible employees. All qualifying employees are entitled to participate on the same basis.	SAYE contributions and the level of discount are as permitted in accordance with the relevant tax legislation from time to time.	Not applicable.

Directors' Remuneration Report

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance measures
Annual bonus	Rewards performance against targets which support the strategic direction of the Group. Bonus deferral provides a retention element through share ownership and direct alignment with shareholders' interests.	Awards are based on performance (typically measured over a year) against key financial targets and/or the delivery of strategic/individual objectives. Pay-out levels are determined by the Committee after the year end based on performance against those targets. The Committee has discretion to amend the pay-out should any formulaic output not reflect the Committee's assessment of overall business performance. Executive Directors are required to defer one-third of any bonus award into shares for a two-year period. The Committee may decide to pay the whole of the bonus earned in cash where the amount to be deferred would, in the opinion of the Committee, be so small as to make deferral administratively burdensome. Deferred shares will typically take the form of nil-cost share options but may be structured as an alternative form of share award. Executive Directors may also be offered the opportunity to defer voluntarily up to 100% of any annual bonus award earned into shares for a two-year period. Deferred bonus awards may be granted on the basis that the participant shall be entitled to an additional benefit (in cash or shares) in respect of dividends paid over the deferral period, calculated on such basis as the Committee shall determine. The vesting of the deferred shares is not subject to the satisfaction of any additional performance conditions. However, the Committee has the right to apply malus and/or clawback as set out below this table.	Maximum annual bonus opportunity is 125% of base salary.	Targets are set annually reflecting the Group's strategy and aligned with key financial, strategic and/or individual targets. At least 75% of the annual bonus is assessed against key financial performance metrics of the business and the balance may be based on non-financial strategic/personal objectives. **Financial metrics** Up to 10% of salary is paid at threshold performance. This increases to up to 60% of the maximum potential for this element of the bonus for on-target performance and all of the maximum potential will be paid for maximum performance. **Non-financial strategic or individual metrics** Vesting of the non-financial strategic or individual metrics will apply on a scale between 0% and 100% based on the Committee's assessment of the extent to which a non-financial performance metric has been met.

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance measures
Performance Share Plan ('PSP')	To incentivise Executive Directors, and to deliver genuine performance-related pay, with a clear line of sight for Executives and direct alignment with shareholders' interests.	The first PSP awards will be granted in respect of 2017. Awards will be in the form of nil-cost share options, conditional shares or other such form as has the same economic effect. Awards will be granted with vesting dependent on the achievement of performance conditions set by the Committee, normally over at least a three year performance period. Awards will usually be subject to a two year holding period following the end of the performance period, and shares will typically not be released to participants until the end of any such holding period. Awards under the PSP may be granted on the basis that the participant shall be entitled to an additional benefit (in cash or shares) in respect of dividends paid over the holding period. This amount shall be calculated on such basis as the Committee determines. The Committee has the right to apply malus and/or clawback as set out below this table.	The normal maximum award is 100% of salary in respect of a financial year. For awards in respect of 2017 the maximum will be 80% of salary. The normal maximum award limit will only be exceeded in exceptional circumstances such as on the recruitment of an Executive Director and is subject to an overall limit of 200% of salary in respect of a financial year.	Performance measures are selected that reflect underlying business performance. Performance metrics and their weighting where there is more than one metric are reviewed annually to maintain appropriateness and relevance. For awards in respect of 2017 80% will be subject to EPS performance and 20% subject to TSR performance. Awards will vest between 25% and 100% for performance between 'threshold' performance (the minimum level of performance that results in any level of vesting) and 'maximum' performance.

Directors' Remuneration Report

Malus and clawback

Prior to the vesting of an annual bonus or PSP award, the Committee may operate 'malus' to cancel the award.

For up to two years following the payment of an annual bonus award, the Committee may operate 'clawback' to require the repayment of any cash amount paid or may cancel any deferred bonus award. For up to two years after the vesting of a PSP award, the Committee may operate 'clawback' to cancel the award during the holding period (or require repayment of the award if it has been released prior to the end of the holding period). The circumstances in which malus and clawback may be operated are as follows.

- The Executive's gross negligence, fraud, dishonesty or other misconduct causing or contributing to the Group or any Group business having to restate all or a portion of its financial statements to a material degree;
- The Executive's conduct being such that it would entitle (or, where the Employment has terminated prior to the date on which the Board becomes aware of such act or omission, would have entitled) the Group to terminate the Employment summarily;
- A material error having occurred in determining whether any corporate or personal performance conditions relating to the bonus or PSP award have been met (or any other material error having occurred in calculating the sum that was awarded as a bonus or the size of the PSP award); or
- Such other exceptional circumstances which, in the Remuneration Committee's absolute discretion, justify such reimbursement being imposed.

Non-Executive Directors

Purpose and link to strategy	Approach of the Company
Non-Executive Directors' fees are set at a level that reflects market conditions and is sufficient to attract individuals with appropriate knowledge and experience.	Fees are normally reviewed annually. Fees paid to Non-Executive Directors for their services are approved by the Board. Fees may include a basic fee and additional fees for further responsibilities (for example, chairmanship of Board committees or holding the office of Senior Independent Director). Fees are based on the level of fees paid to Non-Executive Directors serving on the board of similar-sized UK listed companies and the time commitment and contribution expected for the role. Overall fees paid to Non-Executive Directors will remain within the limits set by the Group's Articles of Association, from time to time. Non-Executive Directors cannot participate in any of the Group's share schemes or annual bonus. Non-Executive Directors may be eligible to receive benefits such as the use of secretarial support, travel costs or other benefits that may be appropriate.

Explanation of performance measures chosen

Performance measures are selected that are aligned with the performance of the Group and the interests of shareholders. Stretching performance targets are set each year for the annual bonus and PSP awards. When setting these performance targets, the Committee will take into account a number of different reference points, which may include the Group's business plans and strategy and the economic environment. Full vesting will only occur for what the Committee considers to be stretching performance.

For 2017, 100% of the annual bonus award will be based on Profit Before Tax, a key financial measure recognised by all colleagues throughout the business and directly linked to our strategy of focusing on profitability and growth. It is used as a KPI by the senior management team and is a key part of bonus schemes throughout the business.

Long-term performance measures provide a robust and transparent basis on which to measure the Group's performance over the longer term and provide further alignment with the business strategy. PSP awards granted in respect of 2017 will be based on Earnings Per Share and relative Total Shareholder Return ('TSR'). EPS is currently the critical KPI for the Group, supporting its focus on profitability and growth. TSR is aligned with the Group's focus on creating value for our shareholders.

The awards granted under the PSP will be subject to a further underpin in accordance with which the level of vesting may be reduced if the Committee does not consider it reflective of the overall financial performance of the Group over the performance period.

The Committee retains the ability to adjust or set different performance measures or targets if events occur (such as a change in strategy, a material acquisition and/or a divestment of a Group business or a change in prevailing market conditions) which cause the Committee to determine that the measures are no longer appropriate and that amendment is required so that they achieve their original purpose.

Operation of share plans

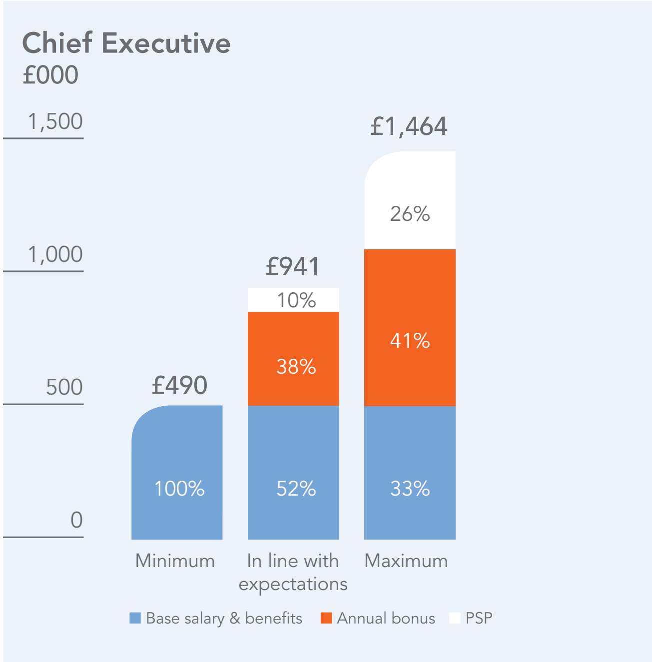
The Committee retains the discretion to operate the Group's share plans in accordance with their terms, including the ability to adjust awards and options in the event of a variation of share capital, demerger, delisting, special dividend or other event that may affect the Group's share price, and to settle awards in cash.

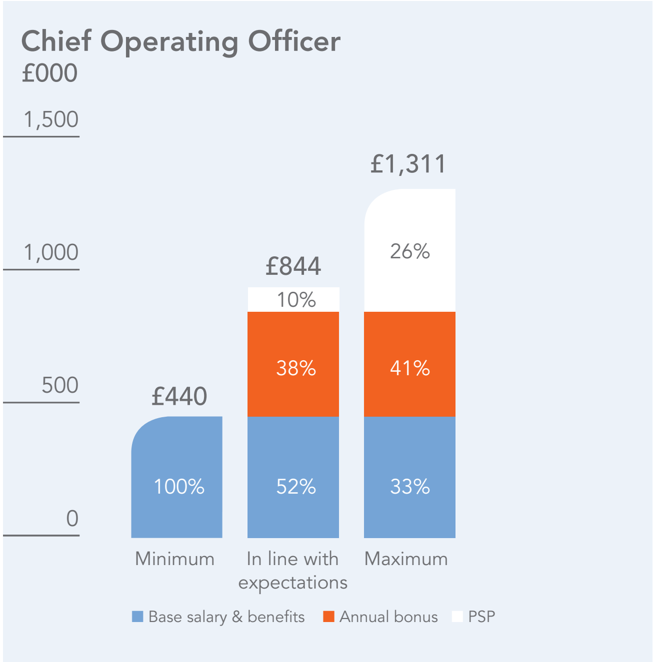
Policy for the remuneration of employees more generally

The Remuneration Policy applied to the Executive Directors is similar to the policy for the wider senior management team in that a significant element of remuneration is dependent on Group performance. The key principles of the remuneration philosophy are applied consistently across the Group below this level, taking into account seniority and market practice.

Illustrations of application of remuneration policy

The chart below sets out for the Chief Executive and Chief Operating Officer an illustration of the application for 2017 of the remuneration policy set out above. The chart shows the split of remuneration between fixed pay, annual bonus (including any amount deferred) and PSP on the basis of minimum remuneration, remuneration receivable for performance in line with the Group's expectations and maximum remuneration (not allowing for any share price appreciation).





In illustrating the potential reward, the following assumptions have been made.

	Fixed pay	Annual bonus (including any amount deferred)	PSP
Minimum performance	Fixed elements of remuneration only – base salary (being the salary as at 1 January 2017, or date of appointment in the case of Tony Judge and benefits as disclosed in the single figure table on page 62 for the year ended 31 December 2016*)	No annual bonus award.	No vesting.
Performance in line with expectations		75% of salary awarded for achieving target performance.	25% of maximum award vesting (equivalent to 20% of salary) for achieving target performance.
Maximum performance		125% of salary awarded for achieving maximum performance.	100% of maximum award vesting (equivalent to 80% of salary) for achieving maximum performance.

* As Tony Judge was not a Director during 2016, for the purposes of these scenario charts his benefits figure has been assumed to be the same as for Steve Wilson

Recruitment remuneration

The policy aims to facilitate the appointment of individuals of sufficient calibre to lead the business and execute the Group's strategy effectively for the benefit of shareholders. When appointing a new Executive Director, the Committee seeks to ensure that arrangements are in the best interests of the Group and not to pay more than is appropriate.

The Committee will take into consideration a number of relevant factors, which may include the calibre of the individual, the candidate's existing remuneration package, and the specific circumstances of the individual including the jurisdiction from which the candidate was recruited.

When hiring a new Executive Director, the Committee will typically align the remuneration package with the above policy. The Committee may include other elements of pay which it considers are appropriate; however, this discretion is capped and is subject to the principles and the limits referred to below.

- Base salary will be set at a level appropriate to the role and the experience of the Executive Director being appointed. This may include agreement on future increases up to a market rate, in line with increased experience and/or responsibilities, subject to good performance, where it is considered appropriate.
- Retirement and other benefits will be provided in line with the above policy.
- The Committee will not offer non-performance related incentive payments (for example a 'guaranteed sign-on bonus').
- Others elements may be included in the following circumstances:
  - an interim appointment being made to fill an Executive Director role on a short-term basis;
  - if exceptional circumstances require that the Chairman or a Non-Executive Director takes on an executive function on a short-term basis;
  - if an Executive Director is recruited at a time in the year when it would be inappropriate to provide a bonus or long-term incentive award for that year as there would not be sufficient time to assess performance. Subject to the limit on variable remuneration set out below, the quantum in respect of the months employed during the year may be transferred to the subsequent year so that reward is provided on a fair and appropriate basis;
  - if the Executive Director will be required to relocate in order to take up the position, it is the Group's policy to allow reasonable relocation, travel and subsistence payments. Any such payments will be at the discretion of the Committee.
- The Committee may also alter the performance measures, performance period, vesting period, deferral period and holding period of the annual bonus or PSP, if the Committee determines that the circumstances of the recruitment merit such alteration. The rationale will be clearly explained in the following Directors' Remuneration Report.
- The maximum level of variable remuneration which may be granted (excluding 'buyout' awards as referred to below) is 325% of salary.

Any share awards referred to in this section will be granted as far as possible under the Group's existing share plans. If necessary, and subject to the limits referred to above, recruitment awards may be granted outside of these plans as permitted under the Listing Rules which allow for the grant of awards to facilitate, in unusual circumstances, the recruitment of an Executive Director.

The Committee may make payments or awards in respect of hiring an employee to 'buyout' remuneration arrangements forfeited on leaving a previous employer. In doing so, the Committee will take account of relevant factors including any performance conditions attached to the forfeited arrangements and the time over which they would have vested. The Committee will generally seek to structure buyout awards or payments on a like-for-like basis to the remuneration arrangements forfeited. Any such payments or awards are limited to the expected value of the forfeited awards. Where considered appropriate, such special recruitment awards will be liable to forfeiture or 'malus' and/or 'clawback' on early departure.

Where a position is filled internally, any ongoing remuneration obligations or outstanding variable pay elements shall be allowed to continue according to the original terms.

Fees payable to a newly appointed Chairman or Non-Executive Director will be in line with the fee policy in place at the time of appointment.

Service contracts

Executive Directors' service contracts are on a rolling basis and may be terminated on 12 months' notice by the Group or the Executive. Service contracts for new Executive Directors will generally be limited to 12 months' notice by the Group. A new service agreement was entered into by Steve Wilson on 3 March 2017, which may be terminated by either party on 12 months' notice.

All Non-Executive Directors have fixed-term agreements with the Group which may be terminated by the giving of one month's notice. The agreements last for an initial period of three years and may then be extended for additional periods of three years, subject to re-election by shareholders at the relevant AGM.

Details of the Non-Executive Directors' appointment dates are set out below:

Non-Executive Director	Date of appointment	Expiry of current term
Dick Peters	10 March 2006	9 March 2018
Andrew Eastgate	17 May 2010	16 May 2017*
Philip Lawrence	1 June 2015	31 May 2018

* Mr Eastgate is proposed for re-election at the 2017 AGM.

Payments for loss of office

The principles on which the determination of payments for loss of office will be approached are set out below:

	Policy
Payment in lieu of notice	The Group has discretion to make a payment in lieu of notice. Such a payment would include base salary and, at the election of the Committee, compensation for benefits and pension contributions (if applicable) for the unexpired period of notice.

Directors' Remuneration Report

	Policy
Annual bonus	This will be at the discretion of the Committee on an individual basis and the decision as to whether or not to award an annual bonus award in full or in part will be dependent on a number of factors, including the circumstances of the individual's departure and their contribution to the business during the annual bonus period in question. Any annual bonus award amounts paid will normally be prorated for time in service during the annual bonus period and will, subject to performance, be paid at the usual time (although the Committee retains discretion to pay the annual bonus award earlier in appropriate circumstances). Any bonus earned for the year of departure and, if relevant, for the prior year may be paid wholly in cash at the discretion of the Committee.
Deferred bonus awards	The extent to which any unvested deferred bonus award will vest will be determined in accordance with the rules of the DBP. If a participant ceases employment for any reason (other than summary dismissal, in which case his award will lapse), his award will ordinarily continue until the normal vesting date. The Committee retains discretion to release awards when the participant leaves. Awards (in the form of nil cost options) which have vested and been released but remain unexercised at the date of cessation may be exercised, for such period as the Committee determines, if a participant leaves for any reason (other than summary dismissal).
PSP	The extent to which any unvested award will vest will be determined in accordance with the rules of the PSP. Unvested awards will normally lapse on cessation of employment. However, if a participant leaves due to death, ill health, injury, disability, the sale of his employer or any other reason at the discretion of the Committee, the Committee shall determine whether the award will be released at cessation or on the normal release date or at some other time (such as following the end of the performance period). In any case, the extent of vesting will be determined by the Committee taking into account the extent to which the performance condition is satisfied and, unless the Committee determines otherwise, the period of time elapsed from the date of grant to the date of cessation relative to the performance period. Awards may then be exercised during such period as the Committee determines. If a participant leaves for any reason (other than summary dismissal) after an award has vested but before it has been released (i.e. during a 'holding period'), his award will ordinarily continue until the normal release date when it will be released to the extent it vested. The Committee retains discretion to release awards when the participant leaves. Awards (in the form of nil cost options) which have vested and been released but remain unexercised at the date of cessation may be exercised, for such period as the Committee determines, if a participant leaves for any reason (other than summary dismissal).
Change of control	The extent to which unvested awards under the DBP and PSP will vest will be determined in accordance with the rules of the relevant plan. Awards under the DBP will vest in full in the event of a takeover, merger or other relevant corporate event. Unvested awards under the PSP will vest early on a takeover, merger or other relevant corporate event. The Committee will determine the level of vesting taking into account the extent to which the performance condition is satisfied and, unless the Committee determines otherwise, the period of time elapsed from the date of grant to the date of the relevant corporate event relative to the performance period. Awards under the PSP which have vested but not been released (i.e. awards which are subject to a holding period) will be released, to the extent vested.

	Policy
Mitigation	If an Executive Director's employment is terminated any compensation payment will be calculated in accordance with normal legal principles including the application of mitigation to the extent appropriate to the circumstances of the termination.
Other payments	Payments may be made either in the event of a loss of office or a change of control under the Save as You Earn Scheme, which is governed by its rules and the legislation relating to such tax-qualifying plans. There is no discretionary treatment for leavers or on a change of control under this scheme. In appropriate circumstances, payments may also be made in respect of accrued holiday, outplacement and legal fees and other benefits that may be considered appropriate taking into account the circumstances of the termination. The Committee reserves the right to make additional exit payments where such payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of settlement or compromise of any claim arising in connection with the termination of a Director's office or employment.

Where a buy-out award is made under the Listing Rules then the leaver provisions would be determined at the time of the award.

Where the Committee retains discretion it will be used to provide flexibility in certain situations, taking into account the particular circumstances of the Director's departure and performance.

There is no entitlement to any compensation in the event of Non-Executive Directors' fixed-term agreements not being renewed or the agreement terminating earlier.

Existing contractual arrangements

The Committee retains discretion to make any remuneration payment or payment for loss of office outside the policy in this report (including exercising any discretions available to it in connection with any such payment):

- where the terms of the payment were agreed before the policy came into effect (including the satisfaction of options granted under the CIP), provided in the case of any payment whose terms were agreed after the previous Directors' Remuneration Policy was approved at the Group's 2014 AGM and before the policy in this report became effective, the remuneration payment or payment for loss of office was permitted under that former policy;
- where the terms of the payment were agreed at a time when the relevant individual was not a Director of the Group and, in the opinion of the Committee, the payment was not in consideration of the individual becoming a Director of the Group.

External appointments

The Board believes that experiences of other companies' practices and challenges is valuable both for the personal development of its Executive Directors and for the Group. It is therefore the Group's policy to allow each Executive Director to accept one non-executive directorship of another company, provided that there is no conflict of interest, although the Board retains the discretion to vary this policy. Fees received by Executive Directors in respect of external non-executive appointments are retained by the individual Director. Details of such appointments are included in the Annual Report on Remuneration.

Directors' Remuneration Report

Consideration of employment conditions elsewhere in the Group

The Committee considers the general basic salary increase, remuneration arrangements and employment conditions for the broader employee population when determining remuneration policy for the Executive Directors.

Shareholder views

The Committee is committed to an ongoing dialogue with shareholders and welcomes feedback on Executive and Non-Executive Directors' remuneration. The Committee will seek to engage directly with major shareholders and their representative bodies should any material changes be made to the Policy and has consulted with major shareholders in relation to the new Policy and the new PSP.

Shareholding guidelines

In order to further align the Executive Directors' long-term interests with those of shareholders, the Group operates share ownership guidelines. The guidelines provide that the Executive Directors are required to build up and maintain (as relevant) a shareholding in the Group equivalent in value to 200% of annual salary. Until the guideline has been reached Executive Directors are required to retain half of the net number of vested shares from the CIP, PSP and DBP. Vested shares which are subject to a holding period under the PSP and shares which are subject to DBP awards will count towards the limit (on a net of assumed tax basis).

ANNUAL REPORT ON REMUNERATION

Certain information provided in this part of the Directors' Remuneration Report is subject to audit. This is annotated as audited. Any information not annotated as audited is unaudited.

Single total figure of remuneration for each Director

The table below reports the total remuneration receivable in respect of qualifying services by each of the Executive Directors for the years 2016 and 2015.

Executive Directors' remuneration as a single figure – 2016 (audited)

Executive Directors	Base salary and fees 2016 £000	Non-salary benefits 2016 £000	Annual performance bonus 2016 £000	Share-based incentive schemes 2016 £000	Pension related benefits 2016 £000	Termination payment 2016 £000	Total 2016 £000
Tony Brewer (i)	393	16	0	255	–	1,143	1,807
Steve Wilson (ii)	403	15	386	204	–	–	1,008
	796	31	386	459	–	1,143	2,815

Executive Directors' remuneration as a single figure – 2015 (audited)

Executive Directors	Base salary and fees 2015 £000	Non-salary benefits 2015 £000	Annual performance bonus 2015 £000	Share-based incentive schemes 2015 £000	Pension related benefits 2015 £000	Total 2015 £000
Tony Brewer	544	39	592	–	–	1,175
Steve Wilson	393	36	428	–	–	857
	937	75	1,020	–	–	2,032

(i) Tony Brewer resigned as a Director on 14 September 2016. Further details of the termination payment are provided on page 66.
(ii) Steve Wilson was appointed as Chief Executive on 14 September 2016 although his salary was not increased until 1 January 2017.

The table below reports the total remuneration receivable in respect of qualifying services by each of the Non-Executive Directors for the years 2016 and 2015.

Non-Executive Directors' remuneration as a single figure – 2016 (audited)

Non-Executive Directors	Base salary and fees 2016 £000	Non-salary benefits 2016 £000	Annual performance bonus 2016 £000	Share-based incentive schemes 2016 £000	Pension related benefits 2016 £000	Total 2016 £000
Andrew Eastgate	55	–	–	–	–	55
Philip Lawrence (iii)	45	–	–	–	–	45
Dick Peters	110	–	–	–	–	110
	210	–	–	–	–	210

Non-Executive Directors' remuneration as a single figure – 2015 (audited)

Non-Executive Directors	Base salary and fees 2015 £000	Non-salary benefits 2015 £000	Annual performance bonus 2015 £000	Share-based incentive schemes 2015 £000	Pension related benefits 2015 £000	Total 2015 £000
Andrew Eastgate	43	–	–	–	–	43
Philip Lawrence (iii)	25	–	–	–	–	25
Dick Peters	64	–	–	–	–	64
	132	–	–	–	–	132

(iii) Philip Lawrence was appointed as a Director on 1 June 2015. Fees in respect of Philip Lawrence are paid to the Coal Authority, which releases him to perform his duties as a Non-Executive Director.

External appointments

Steve Wilson was appointed a Non-Executive Director of Conviviality Plc on 31 January 2014. He received fees of £40,000 per annum during 2015 and 2016.

Individual elements of remuneration

The figures in the single figure table are derived from the following:

Base salary and fees	The amount of salary/fees received in the financial period (up to the date of resignation as a Director in the case of Tony Brewer for 2016).
Non-salary benefits	The taxable value of benefits received in the financial period (up to the date of resignation as a Director in the case of Tony Brewer for 2016). These are car benefit, car fuel benefit, private medical insurance and other benefits deemed to be an employment benefit.
Annual performance bonus	The amount of performance related bonus received in respect of the financial period.
Pension related benefits	There was no provision.
Share-based incentive schemes	The value of Co-Investment Plan ('CIP') awards that vest in respect of the financial period and the value of Save-As-You-Earn ('SAYE') options granted in the financial period.

Directors' Remuneration Report

Base salaries and fees

For 2016, the Committee determined that it was appropriate for the Executive Directors to receive a cost of living increase to their base salary in line with the 2.5% average salary increase across the Group.

	2016 £000	2015 £000	Increase %
Tony Brewer	**557**	544	2.5%
Steve Wilson	**403**	393	2.5%

Following a benchmarking review in 2015, Non-Executive Director fees were restructured taking into account the time and responsibilities required of the roles and market positioning. The Chairman's fee was increased to £110,000, recognising that his fee had fallen markedly behind competitive practice and was not an appropriate reflection of the time and experience brought to the Board.

	2016 £000	2015 £000	Increase %
Chairman fee	**110**	64	72%
Base fee	**40**	36	11%
Additional fee for – Chairmanship of the Remuneration Committee	**5**	7	(29%)
– Chairmanship of the Audit Committee	**5**	7	(29%)
– Senior Independent Director	**10**	–	–

Annual performance bonus

For 2016, the Executive Directors were awarded a maximum annual bonus opportunity equal to 125% of salary. The bonus was assessed against a Group Profit Before Tax (after non-underlying items) performance metric.

The following table sets out the bonus earned by Steve Wilson for 2016 and how this reflects performance for the year.

Performance metric	Proportion of bonus determined by metric	Threshold performance	Target performance	Maximum performance	Actual performance	Bonus earned (% max)
Group Profit Before Tax	100%	£32.6m	£36.0m	£42.3m	£38.2m	76.8%

Headlam Group Co-investment Plan 2008 (the 'CIP')

CIP awards vesting during the financial period

CIP awards were granted to Executive Directors on 1 April 2014 subject to EPS and relative TSR performance metrics over the three year period ended 31 December 2016.

Matching	EPS growth (80% of award)	TSR relative to the constituents of the FTSE SmallCap Index (20% of award)
No match	Less than RPI + 3% p.a.	Below median
0.6:1	RPI + 3% p.a.	Median
2:1	RPI + 6% p.a.	Upper quartile

Straight-line matching between points.

Details of the vesting outcome are set out below:

	Number of awards granted	Maximum potential value at grant (% of salary)	Performance outcome	Level of award vesting (% of maximum)	Total value of vesting[i]
Tony Brewer(ii)					
Proportion of award subject to EPS	47,378	42.9%	EPS growth of 16% p.a	90.2%	£206,712
Proportion of award subject to relative TSR	11,844	10.7%	Between median and upper quartile	83.8%	£48,038
Steve Wilson					
Proportion of award subject to EPS	34,222	42.9%	EPS growth of 16% p.a	100%	£165,634
Proportion of award subject to relative TSR	8,556	10.7%	Between median and upper quartile	92.9%	38,468

(i) A share price of 484p was used to estimate the total value of vesting which is based on the average share price over the last quarter of the financial period.
(ii) Tony Brewer was permitted to retain his CIP awards under the terms of the plan rules. The total value of his CIP awards at vesting has been reduced to take into account his time served as a Director during the vesting period.

CIP awards granted during the financial period

CIP awards were granted to Executive Directors on 6 May 2016 subject to EPS and relative TSR performance metrics.

	Number of awards granted	Maximum potential value at grant (% of salary)	Face value at grant(i) (£'000)	Award vesting at threshold (% of maximum)	Performance period
Tony Brewer	56,603	49.6%	£269,996	30%	3 years commencing on 1 January 2016
Steve Wilson	40,886	49.6%	£195,026	30%	3 years commencing on 1 January 2016

(i) The share price used to determine the face value at grant was 477p, the mid-market closing share price on the grant date.

Matching	EPS growth (80% of award)	TSR relative to the constituents of the FTSE SmallCap Index (20% of award)
No match	Less than RPI + 3% p.a.	Below median
0.6:1	RPI + 3% p.a.	Median
2:1	RPI + 6% p.a.	Upper quartile

Straight-line matching between points.

Dilution

The Committee supports the IA guidelines regarding dilution and regularly monitors compliance with these requirements. The share plan rules limit the number of newly issued shares which can be granted in a ten-year period to 10% of the issued share capital under all employee share plans and 5% under the discretionary share plans.

As at the date of this report, the Group's usage of shares against the limits detailed above in respect of the all employee schemes was 2% of the issued share capital and in respect of grants under discretionary plans was 0% of issued capital. It is the Committee's intention that options exercised under the SAYE scheme will be satisfied by shares held in treasury. With regard to the CIP, the Committee will instigate market purchases of shares, through a trust, taking account of the likelihood of performance targets being met and also potential lapsing of awards because of leavers.

Further information on share-based payments is set out note 21 to the financial statements.

Pension related benefits

No Executive Director received any pension benefit during the financial period.

Payments to past Directors

No payments were made to past Directors during the financial period.

Payments for loss of office

Tony Brewer resigned as a Director on 14 September 2016. Under the terms of his employment contract and in accordance with the 2014 remuneration policy, Tony Brewer received a payment in lieu of notice of £564,378 in respect of his 12 month notice period (consisting of £557,600 in lieu of basic salary and £6,778 in lieu of private healthcare, death in service and telephone benefits), together with a payment of £573,000 being the average annual bonus earned over the two financial periods prior to his resignation as a Director. The Group also made a payment of £5,978 in respect of Tony Brewer's legal costs. The total payment for loss of office is included in the table showing Executive Directors' remuneration as a single figure - 2016, on page 62.

Tony Brewer was permitted to retain his CIP awards under the terms of the plan rules and the 2014 policy and these will vest pro-rated for time served at normal vesting date subject to the outcome of the relevant performance metrics. The estimated vesting outcome of his 2014 CIP awards is described on page 64. Details of the vesting outcome of his 2015 and 2016 CIP awards will be provided in the Annual Report on Remuneration for the year of vesting.

Statement of Directors' shareholding and share interests (audited)

In order to align their interests with the Group's shareholders, the Committee is keen to encourage Executive Directors to increase their shareholdings in the Group. The Executive Directors are required to have a beneficial, including family, interest in the shares of the Group equivalent in value to two times annual base salary. Executive Directors are required to retain half of the net of tax vested shares under all of the Group's share plans until the guideline is met.

Steve Wilson as at 31 December 2016 held shares in excess of the shareholding guideline (based on the Group's closing mid-market share price on 31 December 2016).

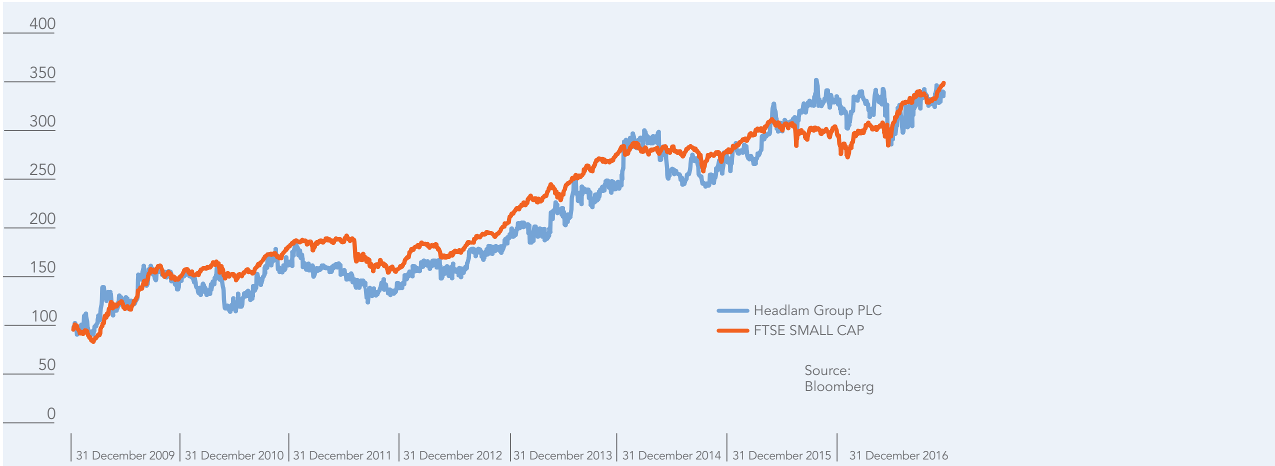
The interests of Directors and their connected persons in the Group's ordinary shares as at 31 December 2016 (or, if earlier, the date on which the Director resigned from the Board) were as set out below. So far as the Group is aware there have been no changes to those interests between 31 December 2016 and the date of signing of these financial statements.

	Type	Grant date	Option price	Share price at grant	Owned outright	Unvested and subject to performance conditions	Unvested and not subject to performance conditions	Vesting date	Total as at 31 December 2016(i)
Tony Brewer(ii)	Shares	–	–	–	613,214	–	–	–	613,214
	2016 CIP	6 May 2016	Nil	477p	–	56,603	–	May 2019	56,603
	2015 CIP	1 May 2015	Nil	466p	–	61,085	–	May 2018	61,085
	2014 CIP	1 April 2014	Nil	492p	–	59,222	–	April 2017	59,222
	2014 SAYE	8 May 2014	381p	476p	–	–	7,874	–	7,874
Steve Wilson	Shares	–	–	–	572,065	–	–	–	572,065
	2016 CIP	6 May 2016	Nil	477p	–	40,886	–	May 2019	40,886
	2015 CIP	1 May 2015	Nil	466p	–	44,124	–	May 2018	44,124
	2014 CIP	1 April 2014	Nil	492p	–	42,778	–	April 2017	42,778
	2014 SAYE	8 May 2014	381p	476p	–	–	7,874	July 2019	7,874
Andrew Eastgate	Shares	–	–	–	1,000	–	–	–	1,000
Philip Lawrence	Shares	–	–	–	0	–	–	–	0
Dick Peters	Shares	–	–	–	5,000	–	–	–	5,000

(i) Or, if earlier, the date of resignation from the Board.
(ii) Tony Brewer was permitted to retain his CIP awards under the terms of the plan rules. The total value of his CIP awards at vesting will be reduced to take into account his time served as a Director during the vesting period. Tony Brewer's SAYE awards lapsed on his resignation as a Director.

The graph below shows the value at 31 December 2016 of £100 invested in the Company on 1 January 2009 compared to the value of £100 invested in the FTSE SmallCap Index, making the assumption that dividends are reinvested to purchase additional equity.

The FTSE SmallCap Index has been selected as a comparator due to the Group being a constituent member within the Household Goods & Home Construction sector. This allows comparison of the Group's performance against the performance of the index as a whole.



CEO remuneration table

The table below sets out the remuneration of the Chief Executive for the previous eight financial periods. Tony Brewer resigned as a Director on 14 September 2016. The 2016 figures in the table below reflect his remuneration earned from the start of 2016 until the date of his resignation as a Director.

Period		Chief Executive single figure of total remuneration £000	Annual bonus (% of maximum opportunity)	Long-term incentive vesting rates against maximum opportunity %
2016	Steve Wilson	1,011*	76.8	98.6
	Tony Brewer	667**	n/a	88.9
2015	Tony Brewer	1,175	87.1	n/a
2014	Tony Brewer	1,134	81.4	n/a
2013	Tony Brewer	927	42.7	n/a
2012	Tony Brewer	1,347	65.5	n/a
2011	Tony Brewer	1,095	66.5	n/a
2010	Tony Brewer	1,179	64.7	n/a
2009	Tony Brewer	1,027	77.0	n/a

* This remuneration is for the full year.

** This remuneration is for a part year and does not include a termination payment.

Percentage change in Chief Executive remuneration

The table below shows the percentage change in the Chief Executive's remuneration and the Group's employees as a whole between the financial periods 2016 and 2015.

Percentage increase/(decrease) in remuneration in 2016 compared with 2015	CEO*	Total employees
Salary and fees	2.5%	11.5%
All taxable benefits	(58.0)%	–
Annual bonuses	(9.6)%	(25.0)%

* The Chief Executive remuneration is based on Steve Wilson for both 2016 and 2015 to enable a clearer comparison.

Directors' Remuneration Report

Relative importance of spend on pay

The table below shows the overall expenditure on dividends and on pay as a whole across the Group along with the percentage change between each.

	2016 £000	2015 £000	% change
Dividends	22,464	14,655	53.3
Overall expenditure on pay	96,772	90,704	6.7

Statement of implementation of remuneration policy in 2017

As described in the Chairman's introduction, the committee has undertaken a detailed review of executive remuneration policy in light of recent changes at Executive Director level and feedback from shareholders and voting bodies. Details of how we will operate our remuneration policy in 2017 is provided below (subject to shareholder approval of the remuneration policy).

Base salaries and fees

The salary for Steve Wilson on his promotion to Chief Executive has been set at £475,000 which is significantly below the salary of his predecessor (£557,600 at the time Tony Brewer resigned as a Director). Steve Wilson previously received a salary of £402,520 for his role as Group Finance Director. On appointment as Chief Operating Officer on 31 March 2017, Tony Judge's salary will be £425,000.

	2017 £000	2016 £000	Increase %
Steve Wilson	475	403	17
Tony Judge	425	n/a	n/a

There are no increases to Non-Executive Director or Chairman fees for 2017.

Annual bonus

Maximum annual bonus opportunity for 2017 will remain at 125% of salary. The bonus will be subject to Profit Before Tax performance. The Committee considers that the Profit Before Tax performance targets are commercially sensitive. The targets will be fully disclosed in the 2017 Annual Report on Remuneration on the same basis as the 2016 targets are disclosed on page 64.

In line with best practice, one-third of any amount earned will be deferred into shares which vest two years after the date on which the annual bonus pay-out is determined.

PSP

The committee intends to grant the first awards under the Headlam 2017 Performance Share Plan ('PSP') in 2017. Awards will be granted in the form of nil cost options at the level of 80% of salary and will be subject to EPS and relative TSR performance metrics.

Vesting (% of maximum)	EPS growth (80% of award)	TSR relative to the constituents of the FTSE SmallCap Index (20% of award)
0%	Less than 5% p.a.	Below median
25%	5% p.a.	Median
100%	8% p.a.	Upper quartile

Straight-line vesting between points.

To balance the overall long-term nature of the package, in line with best practice, awards will be subject to a two year holding period following the date of vesting.

Consideration by the Directors of matters relating to Directors' remuneration

The Board has approved the terms of reference delegating certain responsibilities to the Committee. The terms of reference are reviewed periodically, most recently in April 2016, and are available on the Group's website www.headlam.com.

The Committee comprises the three Non-Executive Directors. By invitation, the Executive Directors may attend meetings. No one attending a Committee meeting may participate in discussions relating to their own terms and conditions of service or remuneration.

The Committee met four times during the year and has responsibility for:

- Selecting the framework and policy for Executive Directors' remuneration and determining the remuneration packages for the Executive Directors and Chairman.
- Monitoring the level and structure of remuneration for senior executive management.
- Approving the design and operation of the Group's short-term and long-term incentive arrangements. This includes agreeing the targets that are applied to awards made to Executive Directors and senior executive management.
- Administering Group share plans as required.

Date	Key agenda items
2 March 2016	Approval of 2015 Directors' Remuneration Report Approval of 2015 annual bonus outcome. Review performance to date against targets for 2014 and 2015 CIP awards Agree performance metrics and targets for 2016 annual bonus 2016 salary reviews for Executive Directors
22 April 2016	Consideration of AGM voting outcome in respect of the annual report on remuneration
6 May 2016	Approval of proposed grant of 2016 CIP award and performance metrics
23 November 2016	Approval of new service agreement for existing and newly appointed Executive Directors Consideration of the 2017 remuneration policy and design

Deloitte LLP were appointed as advisers to the Committee in October 2016. Deloitte's fees in respect of advice to the Committee during the period were £16,200 and were charged on a time and disbursements basis or fixed fee depending on the nature of the advice. Deloitte also provided advice to the Group during the period in relation to share plans and tax matters. Deloitte is a founder member of the Remuneration Consultants Group and as such voluntarily operates under its Code of Conduct in relation to executive remuneration in the UK. The Committee is satisfied that all advice received was objective and independent.

Statement of Shareholders' votes

The following table sets out the results of the advisory vote on the 2015 Annual Report on remuneration at the Group's 2016 AGM and binding vote on the remuneration policy at the Group's 2014 AGM.

	For %	Against %	Withheld %
2015 annual report on remuneration	72.6%	24.8%	2.6%
2014 remuneration policy	88.9%	8.8%	2.3%

Approval

This report has been approved by the Board of Directors and signed on its behalf by

A K. Eastgate

Andrew Eastgate
Chairman of the Remuneration Committee
7 March 2017

Nominations Committee Report

The principal purpose of the Nominations Committee (the 'Committee') is to monitor the balance of skills, knowledge, experience and diversity on the Board and recommend any changes to the composition of the Board giving full consideration to succession planning and the leadership needs of the Group. The Committee has focused on ensuring that your Board has strong and responsible leadership together with knowledge and experience, which are critical to creating long-term shareholder value and business success. The Committee also makes recommendations to the Board on the composition and chairmanship of the Audit and Remuneration Committees.

Composition

The Committee comprises all three Non-Executive Directors, Dick Peters, Philip Lawrence and myself, together with the Chief Executive, Steve Wilson. The Committee is chaired by me other than when it is dealing with matters in relation to me.

Responsibilities

- Ensure the Board and its Committees have the right balance of skills, knowledge and experience.
- To plan for the orderly succession of Directors to the Board and other senior managers. To identify and nominate suitable candidates for Executive and Non-Executive Director vacancies having regard to, amongst other factors, the benefits of diversity, including gender diversity.

Attendees

- Other Executive Directors, senior management and external advisers may be invited to attend meetings.

Key activities during the reporting year

- Ensuring that succession planning is aligned with the ongoing leadership requirements of the business.
- Refreshment of Committees and appointment of Steve Wilson in succession to Tony Brewer.
- Engaging with search agency and provision of brief for recruitment of new Chief Financial Officer.
- Reviewing the contribution and tenure of each Director before recommending for election / re-election by shareholders.
- Considering future succession planning for the executive team and how best to support executive development needs. Appointment of Tony Judge as Chief Operating Officer and appointment of additional executive roles in human relations, communications and logistics and compliance.

Advice

The Committee has access to such information and advice, both from within the Group and externally, at the cost of the Group, as it deems necessary. This may include the appointment of external executive search consultants, where appropriate. No Director is involved in any decisions regarding their own reappointment or re-election.

Membership and attendance at meetings held in 2016

The Committee meets when required and met four times in the year, the table below identifying members in attendance.

Members	Meetings attended	Eligible to attend
Dick Peters	4	(4)
Philip Lawrence	4	(4)
Andrew Eastgate	4	(4)
Steve Wilson [1]	2	(2)
Tony Brewer [2]	1	(1)

1 Steve Wilson joined the Committee on 14 September 2016

2 Tony Brewer stepped down from the Committee on 14 September 2016

Only members of the Committee are entitled to be present at meetings but other Directors and advisers may be invited by the Committee to attend. The Board has agreed the procedures to be followed by the Committee in making appointments to the various positions on the Board and as Company Secretary.

Performance evaluation and succession

Ahead of this year's internal evaluation process, the Committee met to consider the most effective method for the review of the Board, its committees and the individual contribution of each Director.

After frequent and prolonged discussions regarding the future strategic direction of the business, the Committee concluded that it would be necessary to make changes in the executive team to achieve changes that the Board had determined necessary to strategic direction. On 14 September 2016 Tony Brewer was succeeded as Chief Executive by the Group Finance Director Steve Wilson and Tony Judge was appointed Chief Operating Officer, and will be appointed a Director of Headlam Group plc on 31 March 2017. Darryl Price took on additional responsibilities with oversight responsibility for the majority of the UK businesses. Further details are set out in Directors' biographies on pages 36 and 37.

Keith Yates retired from the executive management at the end of 2016 at which time he was succeeded as Managing Director of Mercado by James Kellett and Adrian Laffey, respectively responsible for contract and residential aspects of the Mercado business.

2016 focus

Board succession planning continued to be a key focus for the Committee with more than 50% of its time spent discussing various matters in relation to succession during the year. The Committee is very aware of its responsibilities in relation to Board and senior management succession plans with a view to ensuring that unforeseen changes are managed effectively and efficiently, without disruption to the Group's strategy or day-to-day operations.

Re-election and evaluation

As part of its role, the Committee considered the time required from each Non-Executive Director, their effectiveness and the experience brought to the Board. New Directors are appointed by the Board and, in accordance with the Company's articles of association, they must be elected at the next AGM to continue in office. Existing Directors retire by rotation in accordance with article 89 of the articles of association, which requires them to retire from office and, if eligible for reappointment, stand again at the third AGM after which they were appointed or last reappointed.

Items discussed by the Committee during the year to enable it to discharge its duties in accordance with its terms of reference included proposals to elect Tony Judge and re-elect Andrew Eastgate under the retirement by rotation provisions.

Having regard to the personal effectiveness and commitment assessed as part of the evaluation of the Board, through the completion of an internally prepared questionnaire, the performance of each continuing Board member was considered to be effective and therefore shareholders are recommended to vote in favour of resolutions 3 and 4 at the 2017 AGM.

Terms of reference

Full terms of reference of the Committee can be found in the governance section of the Group's website. In accordance with our terms of reference, the Committee has also considered its own effectiveness during the year. This allows the Committee to formally review the way we work and whether our strategy for discharging our duties remains appropriate. The Committee is satisfied that it continues to perform its duties in accordance with its terms of reference.

Diversity policy

Our approach to diversity is unchanged. We continue to take note of the guidance provided and to make appointments on the basis of merit. However, we recognise the benefit that greater diversity can bring and take into account such factors when considering any particular appointment. Currently there are no female Board members and no specific numeric target has been set.

The Committee, in conjunction with the Board, receives updates from the Chief Executive on succession and development planning for senior positions within the Group.

Changes to Directors' commitments are reported to the Committee as they arise and are considered on their individual merits. Appointments to the Committee are made by the Board.

After review, the Committee was satisfied that it continues to perform its duties in accordance with its terms of reference.

A K. Eastgate

Andrew Eastgate
Chairman of the Nominations Committee
7 March 2017

Other Statutory Disclosures

The Directors present their report, together with the audited financial statements, for the year ended 31 December 2016. This report, which has been prepared solely for the Group's shareholders, contains additional information which the Directors are required by law and regulation to include within the annual report and accounts.

In conjunction with the information from the Chairman's Statement on page 14 to the Statement of Directors' Responsibilities on page 78 this section constitutes the Directors' Report in accordance with the Companies Act 2006.

Principal activities

The principal activities of the Group are wholly aligned to the sales, marketing, supply and distribution of floorcoverings and certain other ancillary products. The principal activity of the Group is that of a holding company and its subsidiaries are listed on page 140. Further details of the Group's activities and future plans are set out in the Strategic Report on pages 2 to 33.

Headlam Group plc is a company incorporated and domiciled in the UK. The address of the registered office is PO Box 1, Gorsey Lane, Coleshill, Birmingham, B46 1LW.

Strategic Report and Future Developments

The Group is required by the Companies Act to include a Strategic Report in this document. The information that fulfils the requirements of the strategic report can be found on the inside front cover to page 33, which are incorporated in this report by reference.

Corporate Governance Statement

The Corporate Governance Statement as required by the Financial Conduct Authority's Disclosure and Transparency Rules (DTR) 7.2.1 is set out on page 38 and is incorporated into this report by reference.

Acquisitions and post balance sheet events

There were no acquisitions in 2016. Details of those made in 2015 and post the balance sheet date are given in note 24.

Results and ordinary dividends

The results for the year and financial position at 31 December 2016 are shown in the Consolidated Income Statement on page 86 and Statements of Financial Position on page 88.

An interim ordinary dividend of 6.70p per share (2015: 6.00p) was paid on 3 January 2017 to shareholders on the register at the close of business on 2 December 2016. The Directors propose a final ordinary dividend of 15.85p per ordinary share (2015: 14.70p), to be paid on 3 July 2017 to shareholders on the register of members at the close of business on 2 June 2017, the associated ex dividend date being 1 June 2017.

This would bring the total ordinary dividend for the year to 22.55p per ordinary share (2015: 20.70p). The payment of the final ordinary dividend is subject to shareholder approval at the Annual General Meeting ('AGM').

Special dividend

A special dividend has been declared of 8.0 pence per ordinary share (2015: special dividend of 6.0 pence per ordinary share). The payment will be made on 24 April 2017 to shareholders on the register at 31 March 2017.

Share capital

As at 31 December 2016, the issued share capital of the Group comprised a single class of ordinary shares of 5p each.

The Group's ordinary shares are listed on the Main Market of the London Stock Exchange. No shares were issued during the year, there were no additions to treasury shares and the reduction in treasury shares related to transfers in connection with the SAYE and executive share option schemes.

Details of the Group's share capital are set out in note 22 to the financial statements, which should be treated as forming part of this report.

Subject to the provisions of the articles and the Companies Acts, shares may be issued with such rights or restrictions as the Group may by ordinary resolution determine or, if the Group has not so determined, as the Directors may decide. There are, however, no restrictions on the transfer of securities in the Group, except that certain restrictions may from time to time be imposed by law or regulation, for example, insider trading laws, and pursuant to the Listing Rules of the Financial Conduct Authority (the 'Listing Rules'), whereby certain employees require the approval of the Group to deal in the Group's shares.

On a show of hands at a general meeting of the Group every holder of ordinary shares present in person and entitled to vote shall have one vote, and on a poll every member present in person or by proxy and entitled to vote shall have one vote for every ordinary share held. The Notice of AGM specifies deadlines for exercising voting rights and appointing a proxy or proxies to vote in relation to resolutions to be passed at the AGM. All proxy votes are counted and the numbers for, against or withheld in relation to each resolution are announced at the AGM and published on the Group's website after the meeting. The holders of ordinary shares are entitled to receive the Group's Annual Report and Accounts, to attend and speak at general meetings of the Group, to appoint proxies and to exercise voting rights. The Group is not aware of any agreements between holders of securities that may result in restrictions on voting rights. Further shareholder information is available on pages 142 to 157.

Subject to certain limits, at the AGM on 20 May 2016, the Directors were granted general authority to allot shares in the Group together with an authority to allot shares in the Group in connection with a rights issue and in respect of cash without first offering them to existing shareholders. Whilst no shares have been allotted by the Group during the year, the Directors will be seeking to renew these authorities to allot unissued shares and to disapply statutory pre-emption rights at the forthcoming AGM. Further details are set out in the Notice of AGM.

At the AGM on 20 May 2016, the Group was given the authority to purchase shares in the Group up to 10% of the issued share capital. Whilst no shares have been purchased under the buyback authority by the Group during the year, the Directors will be seeking to renew this authority for the Group to purchase its ordinary shares at the forthcoming AGM.

Further details are set out in the Notice of AGM.

Directors

Biographies of Directors currently serving on the Board are set out on pages 36 and 37.

Changes to the Board during the period are set out in the Corporate Governance Report on page 38. Details of Directors' service contracts are set out in the Directors' Remuneration Report on page 59.

The Directors shall be not less than three and not more than eight in number, although the Group may by ordinary resolution vary these numbers. Directors may be appointed by the Group by ordinary resolution or by the Board, a Director appointed by the Board holding office only until the next AGM of the Group after their appointment, at which they are then eligible to stand for election.

Tony Judge who retires at the first AGM following his appointment on 31 March 2017 and Andrew Eastgate who retires by rotation, and being eligible, offer themselves for election and re-election respectively at the forthcoming AGM.

The Group does not seek to comply with the provision in the UK Corporate Governance Code (the 'Code') which requires the annual re-election of all Directors. The Group may by ordinary resolution, but subject to special notice, remove any Director before the expiry of the Director's period of office. The office of a Director shall be vacated if certain circumstances arise, as set out in the articles. With regard to the appointment and replacement of Directors, the Group is governed by its Articles of Association, the Code, the Companies Act 2006 and related legislation. The articles may be amended by special resolution of the shareholders. The powers of the Directors are further described in the Corporate Governance Report on page 39.

Other Statutory Disclosures

The table below shows the dates of appointment and the most recent re-election dates for Directors.

	Date of appointment	Date of original letter of appointment	Effective date of current letter of appointment	Next due for re-election
Executive Directors				
Tony Brewer [1]	June 1991	n/a	n/a	n/a
Steve Wilson	December 1991	n/a	3 March 2017	May 2018
Non-Executive Directors				
Dick Peters	10 March 2006	1 December 2005	10 March 2015	9 March 2018
Andrew Eastgate	17 May 2010	27 April 2010	17 May 2014	16 May 2017
Philip Lawrence	1 June 2015	18 June 2015	1 June 2015	20 May 2018

(1) Resigned 14 September 2016

Directors' and officers' indemnity insurance

The Group maintains Directors' and Officers' liability insurance in respect of legal action that might be brought against its Directors and Officers. In accordance with the Group's Articles of Association and to the extent permitted by law, the Group has indemnified each of its Directors and other Officers of the Group against certain liabilities that may be incurred as a result of their position within the Group. These indemnities were in place for the whole of the period ended 31 December 2016 and as at the date of the report. There are no indemnities in place for the benefit of the Auditor.

Directors' conflict of interests

No Director had, at any time during the period under review, any interests in any contract with the Group or any of its subsidiaries, a position which was unchanged at 7 March 2017, other than their service contracts.

Directors' interests

The interests of the persons, including the interests of any connected persons who were Directors at the end of the year, in the share capital of the Group, and their interests under share option and incentive schemes, are shown on page 66.

Change of control

The Group has entered into certain agreements that may take effect, alter or terminate upon a change of control of the Group following a takeover bid. The significant agreements in this respect are the Group's bank facility and certain of its employee share schemes. The Group's term loan facilities include a provision such that, in the event of a change of control, the lender may cancel all or any part of the facility and/or declare that all amounts outstanding under the facility are immediately due and payable by the Group. Outstanding options granted under the SAYE scheme may be exercised within a period of six months from a change of control of the Group following a takeover taking place.

Matching share awards granted under the 2008 CIP may, proportionate to the performance period, vest within a period of six months from a change of control of the Group. At the end of such period, awards will lapse and cease to be exercisable to the extent not exercised.

Details regarding Directors' service agreements are included within the Directors' Remuneration Report.

Management of conflicts of interest

The Group's Articles of Association include provisions relevant to the activity of the Board and its Committees. These provisions include requirements for disclosure and approval by the Board of potential conflicts of interest. It is the Board's view that they operated effectively during 2016. Each Director has a duty to avoid a situation in which they have or may have a direct or indirect interest that conflicts or possibly may conflict with the interests of the Group. This duty is in addition to the duty that they owe to the Group to disclose to the Board any interest in any transaction or arrangement under consideration by the Group. If any Director becomes aware of any situation which may give rise to a conflict of interest, that Director informs the rest of the Board and the Board is then permitted to decide to authorise such conflict, the matter being recorded in the relevant Board minutes.

Substantial interests in voting rights

Notifications of the following voting interests in the Group's ordinary share capital had been received by the Group (in accordance with Chapter 5 of the DTR). The information shown below was correct at the time of disclosure. However, the date received may not have been within the current financial reporting period and the percentages shown (as provided at the time of disclosure) have not been recalculated based on the issued share capital at the period end. It should also be noted that these holdings may have changed since the Group was notified; however, notification of any change is not required until the next notifiable threshold is crossed.

No further notifications have been received by the Group between 31 December 2016 and 28 February 2017 (being the latest practical date prior to the date of this report).

Ordinary shares of 5p each

	26 February 2016 aggregate voting rights	%	28 February 2017 aggregate voting rights	%	Indirect/direct
Franklin Templeton Institutional LLC	15,066,975	18.02	14,565,712	17.22	indirect
FIL Limited	5,857,660	6.93	0	n/a	n/a
BlackRock Inc	4,449,038	5.29	4,449,038	5.29	indirect
Heronbridge Investment Mgmnt LLP	4,209,552	5.04	4,209,552	5.04	direct
JO Hambro Capital Mgmnt Limited	4,190,972	5.01	4,190,972	5.01	direct
Ruffer LLP	4,270,594	5.00	4,270,594	5.00	direct
Rathbone Brothers plc	4,070,078	4.87	4,070,078	4.87	indirect
Tweedy, Browne Company LLC	3,567,409	4.24	3,567,409	4.24	direct

As far as the Group is aware, there are no persons with substantial holdings in the Group other than those noted above.

Rights under employees' share schemes

As at 31 December 2016, Kleinwort Hambros, as trustee of the Headlam Group Employee Trust Company Limited ('Trust') which acts as the trustee of the Headlam Group Co-investment Plan 2008 ('CIP') and the Headlam Group Performance Share Plan 2008 ('PSP'), which was approved by shareholders on 20 June 2008, held 375,941 shares, approximately 0.4% of the issued share capital of the Group, on trust for the benefit of the Directors and certain senior managers of the Group. Kleinwort Hambros waives the dividends payable in respect of these shares.

As at the same date, the Headlam Group Employee Trust Company Limited held 100,088 shares, approximately 0.1% of the issued share capital of the Group, which may be used to fulfil the exercise of SAYE options, the dividend payable in respect of these shares similarly being waived.

Securities carrying special rights

There are no requirements for prior approval of any transfers and no person holds securities in the Group carrying special rights with regard to control of the Group.

Employees

The Group recognises the value of its employees and seeks to create an energetic, dynamic and responsive environment in which to work. The Group maintains a policy of employing the best candidates available in every position, regardless of gender, ethnic group or background, and is committed to fair and equal treatment. It places considerable importance on communications with employees which take place at many levels through the organisation and by a variety of means on both a formal and informal level.

Reward is linked to business plans and targets, thereby giving employees the opportunity to share in the financial success of the Group. In keeping with the structure of the business, this policy is applied locally and, as a result, staff of all levels regularly benefit from achieving local targets.

Where existing employees become disabled, it is the Group's policy, wherever practicable, to provide continuing employment under normal terms and conditions and to provide training, career development and promotion wherever

Other Statutory Disclosures

appropriate, and the Group gives full and fair consideration to applications for employment from disabled persons. Further details of arrangements relating to employees are described in the report on Corporate Responsibility on pages 28 to 33, and the average number of employees and their remuneration are shown in note 4 to the financial statements.

The Group has communicated an internally operated whistleblowing policy and procedure to employees. The policy enables them to report any concerns on matters affecting the Group or their employment without fear of recrimination, and reduces the risk of malpractice taking place and remaining unreported. In addition, the Group does not tolerate matters of discrimination or harassment and bullying, and policies and procedures are in place for reporting and dealing with these matters.

Employees are encouraged to own shares in the Group and the Group operates an HMRC Approved Savings Related Share Option Scheme ('SAYE'). Those employees who choose to take up the option to purchase shares in the Group may enter into a savings arrangement for either a three or five year period, with the option price determined by reference to the share price at the date of grant. On exercise the shares are purchased by the employee free of income tax and national insurance although capital gains tax rules apply.

The Group considers that diversity, including gender diversity, is essential to good business and measures are in place to ensure all appointments are made on merit. Currently there are no female Directors out of a total of four Board members.

Without seeking to set a specific goal for female representation on the Board, the Group is committed to maintaining diversity, including gender diversity, appropriate to and reflecting the nature and strategic aims of the Group. This similarly applies to women in leadership positions in the Group.

As at 31 December 2016 we had 2,384 employees of which 17.3% are female. The significant majority of our employees work regular full time hours with a minority working flexible hours.

Modern slavery statement

We support the aims of the Modern Slavery Act and will publish our disclosure on our website shortly.

Environmental policy and mandatory greenhouse gas emissions reporting

Our environmental policy is included within our report on Corporate Responsibility. The Board recognises that a responsible approach at the heart of the business is key to sustainable growth and a good reputation.

Information on energy consumption, water usage and waste is included within the report on Corporate Responsibility.

Disclosure of information to Auditor

So far as each Director is aware, there is no audit information relevant to the preparation of the Auditor's report of which the Auditor is unaware and each Director has taken all the steps that they ought to have taken as Directors to make themselves aware of any relevant audit information and to establish that the Auditor is aware of that information.

Directors' and Auditor's Responsibilities

A statement by the Directors on their responsibilities in respect of the annual report and the financial statements is given on page 78 and a statement by the Auditor on their responsibilities is given on page 85.

Political donations and expenditure

The Group's policy is not to make any donations for political purposes in the UK or to donate to EU political parties or incur EU political expenditure. Accordingly, neither the Group nor its subsidiaries made any political donations or incurred political expenditure in the financial period under review (2014: £nil).

Charitable contributions

Charitable donations made during the year in support of charitable causes in the local communities in which the Group operates, nationally and those of interest to employees amounted to £20,180 (2015: £11,321). In addition, employees participated in a variety of fundraising activities and supported charities local to their businesses. Further details are reported in our report on Corporate Responsibility.

Amendment of articles

The Group's articles may only be amended by a special resolution at a general meeting of shareholders.

Financial instruments

The disclosures required in relation to the use of financial instruments by the Group together with details of our treasury policy and management are set out in note 23 to the financial statements on pages 129 to 136.

Going concern

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. The financial position of the Group is described on page 22. In addition, note 23 to the financial statements on pages 129 to 136 includes the Group's objectives, policies and processes for managing its exposures to interest rate risk, foreign currency risk, counterparty risk, credit risk and liquidity risk. Details of the Group's financial instruments and hedging activities are also provided in note 23.

The Board has a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, the financial statements set out on pages 86 to 141 have been prepared on the going concern basis.

Auditor

PricewaterhouseCoopers LLP have indicated their willingness to continue as Auditor and their reappointment has been approved by the Audit Committee. Resolutions to reappoint them and to authorise the Directors to determine their remuneration will be proposed at the 2017 AGM.

AGM

This year's AGM will be held at the Group's distribution facility in Coleshill on Thursday, 25 May 2017 at 10.00 am. The notice convening this meeting is set out within this Annual Report and Accounts on page 143, along with explanatory notes regarding the resolutions that will be proposed at the meeting on pages 146 to 151.

The Annual Report and Accounts, which includes the notice convening the meeting will, during April, also be available at wwwheadlam.com.

This report was approved by the Board and signed on its behalf by

Geoff Duggan
Company Secretary
7 March 2017

Company registration number: 460129

Statement of Directors' Responsibilities

IN RESPECT OF THE FINANCIAL STATEMENTS

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have prepared the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Parent Company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. 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 the profit or loss of the Group and Parent Company for that period. In preparing the financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable IFRSs as adopted by the European Union have been followed for the Group financial statements and IFRSs as adopted by the European Union have been followed for the Company financial statements, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and Parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Parent Company and enable them to ensure that the financial statements and the Directors' Remuneration Report comply with the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

The Directors are also responsible for safeguarding the assets of the Group and Parent Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the Group and Parent Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

The Directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for Shareholders to assess the Group and Parent Company's performance, business model and strategy.

Each of the Directors, whose names and functions are listed in the Annual Report and Accounts, confirm that, to the best of their knowledge:

- the Parent Company financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Company;
- the Group financial statements, which have been prepared in accordance with IFRSs as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit of the Group; and
- the Strategic Report includes a fair review of the development and performance of the business and the position of the Group and Parent Company, together with a description of the principal risks and uncertainties that it faces.

In the case of each Director in office at the date the Directors' Report is approved:

- so far as the Director is aware, there is no relevant audit information of which the Group and Parent Company's auditor is unaware; and
- they have taken all the steps that they ought to have taken as a Director in order to make themselves aware of any relevant audit information and to establish that the Group and Parent Company's Auditor is aware of that information.

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Independent Auditors' Report

TO THE MEMBERS OF HEADLAM GROUP PLC

Report on the financial statements

Our opinion

In our opinion:

- Headlam Group plc's Group financial statements and parent company financial statements (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 2016 and of the Group's profit and the Group's and the parent company's cash flows 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 IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; 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.

What we have audited

The financial statements, included within the Annual Report and Accounts (the 'Annual Report'), comprise:

- the Group and Company Statements of Financial Position as at 31 December 2016;
- the Consolidated Income Statement and Consolidated Statement of Comprehensive Income for the year then ended;
- the Group and Company Cash Flow Statements for the year then ended;
- the Group and Company Statements of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is IFRSs as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006, and applicable law.

Our audit approach

Overview

Overall Group materiality: £1.91 million which represents 5% of profit before tax.

The Group financial statements are a consolidation of a number of reporting companies comprising the Group's operating businesses, centralised functions and non-trading Group companies.

- We performed full scope audits on the financial information of three UK reporting companies: HFD Limited, MCD Group Limited and Headlam Group plc (the Company) due to their size and risk characteristics. These UK reporting companies comprise 87% of consolidated revenue and 99% of consolidated operating profit.
- In addition, limited scope audit procedures were performed on two further reporting companies, one in France and one in Switzerland, for Group reporting purposes.

Our assessment of the risk of material misstatement also informed our views on the areas of particular audit focus for our work, which are:

- Absorption of overhead costs and supplier arrangements within the valuation of inventory; and
- Complex supplier arrangements.

The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ('ISAs (UK & Ireland)').

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as 'areas of focus' in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

Area of focus	How our audit addressed the area of focus
Absorption of overhead costs and supplier arrangements within the valuation of inventory Refer to the Audit Committee Report on page 48, the use of estimates and judgements in the Accounting Policies on page 93 and the inventory note on page 113. Consistent with other supply and distribution companies, inventory represents a significant asset on the Group's Statement of Financial Position and is carried at the lower of cost and net realisable value. We identified the absorption of rebates and overheads within inventory as an area of focus because they can have a significant impact on the determination of inventory cost. Management's assessment of cost includes an element of subjectivity in identifying those overheads which should be absorbed into inventory cost and estimation in determining the absorption of supplier rebate arrangements.	We re-performed management's calculation and agreed inputs back to underlying financial records. We checked that the nature of the rebates and costs being absorbed are those incurred in bringing inventory to its present location and condition. For those costs whose nature means absorption is more subjective in nature, such as those that could be considered storage costs, we performed a sensitivity to check that these did not have a material impact on the absorption calculation. No material inconsistencies or exceptions were noted. In addition, as part of the re-performance of management's absorption calculation, we checked that supplier rebate arrangements were appropriately incorporated based on the proportion of rebates receivable in the year that relate to the year-end inventory balance. Details of the other audit procedures performed over rebates are further outlined within the Complex Supplier Arrangements section below. No material inconsistencies or exceptions were noted.
Complex supplier arrangements Refer to the Audit Committee Report on page 47 and the use of estimates and judgements in the Accounting Policies on page 93. The Group has a significant number of rebate agreements with suppliers. These agreements can contain multiple terms or tiered arrangements based on the volume of goods purchased. Consequently, the calculation of these rebates can be complex and requires accurate inputs and calculations to be made. The majority of agreements are coterminous with the financial year, meaning that, although the calculation of the rebate does not rely on estimates of future purchases, there are significant amounts of rebates receivable subject to recovery at the year-end.	We tested a sample of rebate balances by recalculating the amount due based on the supporting purchase agreements and testing the calculation inputs back to underlying financial records. Where recalculation of the balance was complex due to the tiered arrangements, we confirmed the balance with the counterparty. All confirmations requested were received and no material inconsistencies or exceptions were noted. For those balances subject to testing, we agreed all post year end settlements back to evidence of cash receipt or credit notes received, to provide comfort over the recoverability of the balances. In addition, in order to assess management's ability to accurately calculate rebate receivable balances, we compared cash receipts received during the year against. No material inconsistencies or exceptions were noted.

Independent Auditors' Report

TO THE MEMBERS OF HEADLAM GROUP PLC

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the geographic structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

The Group operates as a supplier and distributor of floorcovering products and has two operating segments: the UK and Continental Europe. The Group financial statements are a consolidation of a number of reporting companies, comprising the Group's operating businesses, centralised functions and non-trading Group companies.

In establishing the overall approach to the Group audit, we identified three UK reporting companies which, in our view, required an audit of their complete financial information both due to their size and risk characteristics: HFD Limited, MCD Group Limited and Headlam Group plc (the Company). These reporting companies were audited by the Group engagement team. In addition, we conducted a limited scope audit over two insignificant reporting companies, one in France and one in Switzerland, conducted by PwC network firms in their respective countries as component auditors.

In addition to the written instructions issued to the component auditors, the Group audit team were in contact with them at each stage of the audit. The Group team discussed in detail with the component auditors the planned audit approach for the work performed including the areas of focus that were relevant to their work, were in attendance at local audit closing meetings and discussed and evaluated the detailed findings from this work.

The work at these five companies, together with additional procedures performed at the Group level, including analytical procedures and specific testing of the consolidation, gave us the evidence we needed for our opinion on the Group financial statements as a whole.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole.

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

Overall Group materiality	£1.91 million
How we determined it	5% of profit before tax.
Rationale for benchmark applied	We believe that profit before tax is the primary measure used by the Shareholders in assessing the performance of the Group, and is a generally accepted auditing benchmark.
Component materiality	For each component in our audit scope, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £112,000 and £1,692,000.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £65,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Going concern

Under the Listing Rules we are required to review the Directors' statement, set out on page 22, in relation to going concern. We have nothing to report having performed our review.

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to the Directors' statement about whether they considered it appropriate to adopt the going concern basis in preparing the financial statements. We have nothing material to add or to draw attention to.

As noted in the Directors' statement, the Directors have concluded that it is appropriate to adopt the going concern basis in preparing the financial statements. The going concern basis presumes that the Group and parent company have adequate resources to remain in operation, and that the Directors intend them to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the Directors' use of the going concern basis is appropriate. However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the Group's and parent company's ability to continue as a going concern.

Other required reporting

Consistency of other information and compliance with applicable requirements

Companies Act 2006 reporting

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 addition, in light of the knowledge and understanding of the Group, the parent company and their environment obtained in the course of the audit, we are required to report if we have identified any material misstatements in the Strategic Report and the Directors' Report. We have nothing to report in this respect.

ISAs (UK & Ireland) reporting

Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:

■ information in the Annual Report is: — materially inconsistent with the information in the audited financial statements; or — apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Group and parent company acquired in the course of performing our audit; or — otherwise misleading.	We have no exceptions to report.
■ the statement given by the Directors on page 78, in accordance with provision C.1.1 of the UK Corporate Governance Code (the 'Code'), that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the Group's and parent company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and parent company acquired in the course of performing our audit.	We have no exceptions to report.
■ the section of the Annual Report on page 44, as required by provision C.3.8 of the Code, describing the work of the Audit Committee, does not appropriately address matters communicated by us to the Audit Committee.	We have no exceptions to report.

Independent Auditors' Report

TO THE MEMBERS OF HEADLAM GROUP PLC

The Directors' assessment of the prospects of the Group and of the principal risks that would threaten the solvency or liquidity of the Group

Under ISAs (UK & Ireland) we are required to report to you if we have anything material to add or to draw attention to in relation to:

■ the Directors' confirmation on page 26 of the Annual Report, in accordance with provision C.2.1 of the Code, 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.	We have nothing material to add or to draw attention to.
■ the disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.	We have nothing material to add or to draw attention to.
■ the Directors' explanation on page 23 of the Annual Report, in accordance with provision C.2.2 of the Code, 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 have nothing material to add or to draw attention to.

Under the Listing Rules we are required to review the Directors' statement that they have carried out a robust assessment of the principal risks facing the Group and the Directors' statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the Code; and considering whether the statements are consistent with the knowledge acquired by us in the course of performing our audit. We have nothing to report having performed our review.

Adequacy of accounting records and information and explanations received

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 and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Directors' Remuneration Report – Companies Act 2006 opinion

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

Other Companies Act 2006 reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of Directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Corporate governance statement

Under the Listing Rules we are required to review the part of the Corporate Governance Statement relating to ten further provisions of the Code. We have nothing to report having performed our review.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 78, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the parent company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of financial statements involves

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Group's and the parent company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the Directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report. With respect to the Strategic Report and Directors' Report, we consider whether those reports include the disclosures required by applicable legal requirements.

Mark Smith (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Birmingham
7 March 2017

Consolidated Income Statement

FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	Underlying 2016 £000	Non-underlying 2016 £000	Total 2016 £000	2015 £000
Revenue	2	693,572	–	693,572	654,078
Cost of sales		(481,068)	–	(481,068)	(453,568)
Gross profit		212,504	–	212,504	200,510
Distribution costs		(127,982)	–	(127,982)	(120,070)
Administrative expenses	3	(43,450)	(1,927)	(45,377)	(43,663)
Operating profit	2	41,072	(1,927)	39,145	36,777
Finance income	6	756	–	756	738
Finance expenses	6	(1,722)	–	(1,722)	(1,891)
Net finance costs		(966)	–	(966)	(1,153)
Profit before tax	3	40,106	(1,927)	38,179	35,624
Taxation	7	(7,601)	385	(7,216)	(7,213)
Profit for the year attributable to the equity Shareholders		32,505	(1,542)	30,963	28,411
Dividend paid per share	22			26.70p	17.50p
Earnings per share					
Basic	9	38.7p		36.8p	33.8p
Diluted	9	38.5p		36.6p	33.7p

All Group operations during the financial years were continuing operations.

Consolidated Statement of Comprehensive Income

FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	2016 £000	2015 £000
Profit for the year attributable to the equity Shareholders		**30,963**	28,411
Other comprehensive income:			
Items that will never be reclassified to profit or loss			
Remeasurement of defined benefit plans	20	**(4,336)**	1,292
Related tax		**961**	(231)
Impact of change in UK tax rates on deferred tax		**(183)**	(323)
		(3,558)	738
Items that are or may be reclassified to profit or loss			
Foreign exchange translation differences arising on translation of overseas operations		**1,707**	6
Effective portion of changes in fair value of cash flow hedges		**572**	(556)
Transfers to profit or loss on cash flow hedges		**175**	172
Related tax		**(148)**	66
Impact of change in UK tax rates on deferred tax		**(3)**	(8)
		2,303	(320)
Other comprehensive (expense)/income for the year		**(1,255)**	418
Total comprehensive income attributable to the equity Shareholders for the year		**29,708**	28,829

Statements of Financial Position

AT 31 DECEMBER 2016

	Note	Group 2016 £000	Group Restated* 2015 £000	Group Restated* 2014 £000	Company 2016 £000	Company Restated* 2015 £000	Company Restated* 2014 £000
Assets							
Non-current assets							
Property, plant and equipment	10	**102,934**	104,677	106,875	**36**	109	101
Investment properties	10	**–**	–	–	**84,835**	86,529	88,056
Intangible assets	11	**10,388**	10,388	10,013	**–**	–	–
Investments in subsidiary undertakings	12	**–**	–	–	**90,707**	89,806	88,985
Deferred tax assets	13	**1,138**	629	515	**–**	–	–
		114,460	115,694	117,403	**175,578**	176,444	177,142
Current assets							
Inventories	14	**126,037**	118,165	115,591	**–**	–	–
Trade and other receivables	15	**128,934**	120,300	118,962	**17,351**	20,185	15,334
Cash and cash equivalents	16	**59,343**	63,932	47,589	**28,171**	33,001	14,237
		314,314	302,397	282,142	**45,522**	53,186	29,571
Total assets		**428,774**	418,091	399,545	**221,100**	229,630	206,713
Liabilities							
Current liabilities							
Bank overdraft	16	**(4)**	–	–	**–**	–	–
Other interest-bearing loans and borrowings	17	**(224)**	–	(204)	**–**	–	–
Trade and other payables	18	**(183,304)**	(171,375)	(165,240)	**(38,143)**	(38,051)	(37,672)
Employee benefits	20	**(2,169)**	(2,171)	(2,933)	**(2,169)**	(2,171)	(2,933)
Income tax payable	8	**(6,824)**	(6,974)	(6,073)	**(2,147)**	(2,691)	(2,892)
		(192,525)	(180,520)	(174,450)	**(42,459)**	(42,913)	(43,497)
Non-current liabilities							
Other interest-bearing loans and borrowings	17	**(6,493)**	(20,000)	(22,818)	**–**	(20,000)	(20,000)
Provisions	19	**(1,531)**	(1,087)	(787)	**–**	–	–
Deferred tax liabilities	13	**(4,077)**	(4,533)	(3,931)	**(3,239)**	(3,615)	(3,036)
Employee benefits	20	**(20,781)**	(16,843)	(18,803)	**(16,113)**	(13,993)	(16,457)
		(32,882)	(42,463)	(46,339)	**(19,352)**	(37,608)	(39,493)
Total liabilities		**(225,407)**	(222,983)	(220,789)	**(61,811)**	(80,521)	(82,990)
Net assets		**203,367**	195,108	178,756	**159,289**	149,109	123,723
Equity attributable to equity holders of the parent							
Share capital	22	**4,268**	4,268	4,268	**4,268**	4,268	4,268
Share premium		**53,512**	53,512	53,512	**53,512**	53,512	53,512
Other reserves	22	**2,272**	(275)	(1,721)	**15,714**	14,874	13,434
Retained earnings		**143,315**	137,603	122,697	**85,795**	76,455	52,509
Total equity		**203,367**	195,108	178,756	**159,289**	149,109	123,723

* See note 1.

The notes on pages 92 to 141 are an integral part of these consolidated financial statements.

The Company is taking advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement, however the profit for the year attributable to the equity Shareholders is £34,008,000.

These financial statements were approved by the Board of Directors on 7 March 2017 and were signed on its behalf by

Steve Wilson
Director

Company Number: 460129

Statement of Changes in Equity – Group

FOR THE YEAR ENDED 31 DECEMBER 2016

	Share capital £000	Share premium £000	Capital redemption reserve £000	Translation reserve £000	Cash flow hedging reserve £000	Treasury reserve £000	Restated* Retained earnings £000	Restated* Total equity £000
Balance at 1 January 2015	4,268	53,512	88	5,423	(132)	(7,100)	126,018	182,077
Restatement	–	–	–	–	–	–	(3,321)	(3,321)
Restated balance at 1 January 2015	4,268	53,512	88	5,423	(132)	(7,100)	122,697	178,756
Profit for the year attributable to the equity Shareholders	–	–	–	–	–	–	28,411	28,411
Other comprehensive income/ (expense)	–	–	–	6	(384)	–	796	418
Total comprehensive income/ (expense) for the year	–	–	–	6	(384)	–	29,207	28,829
Transactions with equity Shareholders, recorded directly in equity								
Share-based payments	–	–	–	–	–	–	1,100	1,100
Share options exercised by employees	–	–	–	–	–	1,824	(819)	1,005
Current tax on share options	–	–	–	–	–	–	95	95
Deferred tax on share options	–	–	–	–	–	–	(22)	(22)
Dividends to equity holders	–	–	–	–	–	–	(14,655)	(14,655)
Total contributions by and distributions to equity Shareholders	–	–	–	–	–	1,824	(14,301)	(12,477)
Balance at 31 December 2015	4,268	53,512	88	5,429	(516)	(5,276)	137,603	195,108
Balance at 1 January 2016	**4,268**	**53,512**	**88**	**5,429**	**(516)**	**(5,276)**	**137,603**	**195,108**
Profit for the year attributable to the equity Shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**30,963**	**30,963**
Other comprehensive income	**–**	**–**	**–**	**1,707**	**747**	**–**	**(3,709)**	**(1,255)**
Total comprehensive income/ (expense) for the year	**–**	**–**	**–**	**1,707**	**747**	**–**	**27,254**	**29,708**
Transactions with equity Shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**1,239**	**1,239**
Share options exercised by employees	**–**	**–**	**–**	**–**	**–**	**740**	**(317)**	**423**
Consideration for purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(647)**	**–**	**(647)**
Current tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**21**	**21**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**(21)**	**(21)**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(22,464)**	**(22,464)**
Total contributions by and distributions to equity Shareholders	**–**	**–**	**–**	**–**	**–**	**93**	**(21,542)**	**(21,449)**
Balance at 31 December 2016	**4,268**	**53,512**	**88**	**7,136**	**231**	**(5,183)**	**143,315**	**203,367**

* See note 1.

Statement of Changes in Equity – Company

FOR THE YEAR ENDED 31 DECEMBER 2016

	Share capital £000	Share premium £000	Capital redemption reserve £000	Special reserve £000	Cash flow hedging reserve £000	Treasury reserve £000	Restated* Retained earnings £000	Restated* Total equity £000
Balance at 1 January 2015	4,268	53,512	88	20,578	(132)	(7,100)	57,247	128,461
Restatement	–	–	–	–	–	–	(4,738)	(4,738)
Restated balance at 1 January 2015	4,268	53,512	88	20,578	(132)	(7,100)	52,509	123,723
Profit for the year attributable to the equity Shareholders	–	–	–	–	–	–	37,560	37,560
Other comprehensive income	–	–	–	–	(384)	–	814	430
Total comprehensive income/ (expense) for the year	–	–	–	–	(384)	–	38,374	37,990
Transactions with equity Shareholders, recorded directly in equity								
Share-based payments	–	–	–	–	–	–	1,040	1,040
Share options exercised by employees	–	–	–	–	–	1,824	(819)	1,005
Deferred tax on share options	–	–	–	–	–	–	6	6
Dividends to equity holders	–	–	–	–	–	–	(14,655)	(14,655)
Total contributions by and distributions to equity Shareholders	–	–	–	–	–	1,824	(14,428)	(12,604)
Balance at 31 December 2015	4,268	53,512	88	20,578	(516)	(5,276)	76,455	149,109
Balance at 1 January 2016	**4,268**	**53,512**	**88**	**20,578**	**(516)**	**(5,276)**	**76,455**	**149,109**
Profit for the year attributable to the equity Shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**34,008**	**34,008**
Other comprehensive income	**–**	**–**	**–**	**–**	**747**	**–**	**(3,128)**	**(2,381)**
Total comprehensive income/ (expense) for the year	**–**	**–**	**–**	**–**	**747**	**–**	**30,880**	**31,627**
Transactions with equity Shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**1,239**	**1,239**
Share options exercised by employees	**–**	**–**	**–**	**–**	**–**	**740**	**(317)**	**423**
Consideration for purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(647)**	**–**	**(647)**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**2**	**2**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(22,464)**	**(22,464)**
Total contributions by and distributions to equity Shareholders	**–**	**–**	**–**	**–**	**–**	**93**	**(21,540)**	**(21,447)**
Balance at 31 December 2016	**4,268**	**53,512**	**88**	**20,578**	**231**	**(5,183)**	**85,795**	**159,289**

* See note 1.

Cash Flow Statements

FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	Group 2016 £000	Group 2015 £000	Company 2016 £000	Company 2015 £000
Cash flows from operating activities					
Profit before tax for the year		**38,179**	35,624	**2,210**	1,635
Adjustments for:					
Depreciation, amortisation and impairment		**5,276**	5,179	**1,718**	1,734
Finance income	6	**(756)**	(738)	**(763)**	(655)
Finance expense	6	**1,722**	1,891	**1,178**	1,404
(Profit)/loss on sale of property, plant and equipment		**(15)**	(31)	**5**	(14)
Share-based payments	21	**1,239**	1,100	**338**	279
Operating cash flows before changes in working capital and other payables		**45,645**	43,025	**4,686**	4,383
Change in inventories		**(5,895)**	(1,827)	**–**	–
Change in trade and other receivables		**(6,467)**	(1,524)	**(782)**	4
Change in trade and other payables		**10,365**	7,270	**5,062**	(4,302)
Cash generated from the operations		**43,648**	46,944	**8,966**	85
Interest paid		**(1,133)**	(1,268)	**(565)**	(766)
Tax paid		**(7,703)**	(6,245)	**(339)**	(118)
Additional contributions to defined benefit plan	20	**(2,171)**	(2,925)	**(2,171)**	(2,925)
Net cash flow from operating activities		**32,641**	36,506	**5,891**	(3,724)
Cash flows from investing activities					
Proceeds from sale of property, plant and equipment		**401**	277	**327**	85
Interest received		**752**	726	**400**	393
Dividends received		**–**	–	**31,522**	35,947
Acquisition of subsidiaries, net of cash acquired	24	**–**	(1,977)	**–**	–
Acquisition of property, plant and equipment	10	**(2,963)**	(2,856)	**(282)**	(287)
Net cash flow from investing activities		**(1,810)**	(3,830)	**31,967**	36,138
Cash flows from financing activities					
Proceeds from the issue of treasury shares		**423**	1,005	**423**	1,005
Payment to acquire own shares		**(647)**	–	**(647)**	–
Repayment of borrowings		**(20,000)**	(2,817)	**(20,000)**	–
Drawdown of loans		**6,456**	–	**–**	–
Dividends paid	22	**(22,464)**	(14,655)	**(22,464)**	(14,655)
Net cash flow from financing activities		**(36,232)**	(16,467)	**(42,688)**	(13,650)
Net (decrease)/increase in cash and cash equivalents		**(5,401)**	16,209	**(4,830)**	18,764
Cash and cash equivalents at 1 January		**63,932**	47,589	**33,001**	14,237
Effect of exchange rate fluctuations on cash held		**808**	134	**–**	–
Cash and cash equivalents at 31 December	16	**59,339**	63,932	**28,171**	33,001

The Company's profit before tax excludes dividends received from subsidiaries.

Notes to the Financial Statements

1 Accounting policies

Reporting entity

Headlam Group plc (the 'Company') is a company incorporated and domiciled in the UK. The address of its registered office is PO Box 1, Gorsey Lane, Coleshill, Birmingham, B46 1LW.

Statement of compliance

Both the Company's and the Group's financial statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU ('adopted IFRSs'). On publishing the Company's financial statements here together with the Group financial statements, the Company is taking advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements.

The Company and Group financial statements were authorised for issuance on 7 March 2017.

Basis of preparation

The principal accounting policies applied in the preparation of the financial statements of the Company and the financial statements of the Group are set out below. These policies have been applied consistently to all years presented, unless otherwise stated.

Judgements made by the Directors, in the application of these accounting policies that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year, are discussed below.

The comparative balance sheet has been restated in order to: align certain accounting policies of overseas companies; better reflect the net value of certain inventory product lines; reassess deferred tax in relation to property; and to reclassify certain balances in order to present them in a consistent manner with the current year.

The net impact of these changes has been to change the Statement of Financial Position as follows:

	£000
Property, plant and equipment	3,414
Deferred tax	(6,142)
Inventory	(978)
Trade and other receivables	146
Trade and other payables	1,326
Provisions	(1,087)
Brought forward reserves	3,321

The comparative balance sheet of the Company has also been restated to reclassify land and buildings to reflect their nature as investment properties and to present them in a consistent manner with the current year.

(a) Measurement convention

These financial statements are presented in pounds sterling, which is the Company's functional currency. All financial information presented in pounds sterling has been rounded to the nearest thousand.

The Company and Group financial statements are prepared on the historical cost basis with the exception of derivative financial instruments and pension scheme assets and liabilities, both of which are stated at fair value. Non-current assets held for sale are stated at the lower of previous carrying amount and fair value less costs to sell.

The financial statements have been prepared on a going concern basis. In determining the appropriate basis of preparation of the financial statements the Directors are required to consider whether the Group can continue in operational existence for a period no shorter than 12 months from the date of approval of the annual report.

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Chairman's Statement on page 14 and Chief Executive's Review on pages 15 to 17.

The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Finance Review on pages 18 to 22. In addition, note 23 to the financial statements includes the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

1 Accounting policies continued

The Group meets its day-to-day working capital requirements through its banking facilities. As highlighted in note 17 to the Financial Statements, the Group completed a refinancing of its existing facilities, which were due for renewal on 8 March 2017, on 14 December 2016. The Group has entered into two separate agreements with Barclays Bank PLC and HSBC Bank Plc and include both Sterling and Euro term facilities. The Group's new banking arrangements, which run to 14 December 2021, increase the level of Sterling committed facilities from £40 million to £47.5 million, and have additional Euro facilities of €8.6 million. The Group also has short term uncommitted facilities which have been reduced by £10 million, to £25 million, and are renewable on an annual basis.

The Directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for a period no shorter than 12 months from the date of approval of the annual report. Thus they continue to adopt the going concern basis of accounting in preparing the annual financial statements.

b) Use of accounting estimates and judgements

The preparation of financial statements in conformity with adopted IFRSs requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting year. Although these estimates are based on management's best knowledge of the amount, events or actions, actual results ultimately may differ from those estimates.

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

The key sources of estimation uncertainty at the Statement of Financial Position date that may give rise to a material adjustment to the carrying value of assets and liabilities within the next financial year are as follows:

Goodwill impairment

The outcome of the Group's annual impairment test for goodwill is dependent on the forecast cash flows of each cash-generating unit together with key management assumptions, which are subject to inherent estimation and uncertainty, including the discount rate and future profit growth. No impairment resulted from the annual impairment test for 2016 and 2015 in the UK or in Continental Europe.

Taxation

Provision is made for any uncertain tax positions that the Group may be exposed to at the Statement of Financial Position date.

Deferred tax assets are recognised at the Statement of Financial Position date based on the assumption that there is a high expectation that the asset will be realised in due course. This assumption is dependent on the Group's ability to generate sufficient future taxable profits.

Inventory

Inventories are valued at the lower of cost and net realisable value. Cost is the invoiced cost of materials less any supplier discounts received and overheads incurred in bringing inventory to its present condition and location. This includes management's best estimates of overheads to be absorbed into the cost of inventory and discounts likely to be received from suppliers.

Provision is calculated based on the ageing profile and consideration of inventory sold for less than its carrying value.

Notes to the Financial Statements

1 Accounting policies continued

Employee benefits

The deficit relating to the Group's defined benefit plans is assessed annually in accordance with IAS 19 and after taking independent actuarial advice. The principal assumptions are set out in note 20. The amount of the deficit is dependent on plan asset and liability values and the actuarial assumptions used to determine the deficit.

The assumptions include asset growth rates, pension and salary increases, price inflation, discount rate used to measure actuarial liabilities and mortality rates.

(c) Impact of newly adopted accounting standards

There have been no significant changes in accounting policies or any material impact on the Group financial statements arising from the adoption of new accounting standards and interpretations in 2016.

(d) IFRS not yet applied

The following standards and interpretations, which were not effective as at 31 December 2016 and have not been early adopted by the Group, will be adopted in future accounting periods:

- International Financial Reporting Standard (IFRS) 15 'Revenue from contracts with customers' (effective 1 January 2018).
- International Financial Reporting Standard (IFRS) 9 'Financial instruments' (effective 1 January 2018).
- International Financial Reporting Standard (IFRS) 16 'Leases' (effective 1 January 2019).
- Clarification of Acceptable Methods of Depreciation and Amortisation – Amendments to IAS 16 and IAS 38.
- Equity Method in Separate Financial Statements – Amendments to IAS 27.
- Disclosure Initiative – Amendments to IAS 1.
- Annual Improvements to IFRSs – 2012-2014 Cycle.

With the exception of IFRS 15 and IFRS 16, none of the standards above are expected to have a material impact on the Group. The Group is assessing the impact of the new standards.

Basis of consolidation

The Group financial statements consolidate those of the Company and its subsidiaries which together are referred to as the 'Group'. The Company's financial statements present information about the Company as a separate entity and not about its Group.

Subsidiaries are entities controlled by the Group. Control exists when the Group has power over an entity, is exposed or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. In assessing control, potential voting rights that are currently exercisable or convertible are taken into account.

The financial statements of subsidiaries are included in the Group's financial statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group.

Inter-company transactions, balances and unrealised gains and losses on transactions between Group companies are eliminated in the Group's financial statements.

Foreign currency

Foreign currency transactions

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the Statement of Financial Position date are translated at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the 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.

1 Accounting policies continued

Financial statements of foreign operations

The assets and liabilities of foreign subsidiaries are translated at foreign exchange rates ruling at the Statement of Financial Position date.

The revenues, expenses and cash flows of foreign subsidiaries are translated at an average rate for the period where this rate approximates to the foreign exchange rates ruling at the dates of the transactions.

Exchange differences arising from this translation of foreign subsidiaries are taken directly to the translation reserve and reflected as a movement in the statement of comprehensive income.

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

Foreign currency exposure

Note 23 contains information about the foreign currency exposure of the Group and risks in relation to foreign exchange movements.

Derivative financial instruments

The Group holds derivative financial instruments to hedge its foreign currency and its interest rate risk exposures. Derivatives are recognised initially at fair value; attributable transaction costs are recognised in the income statement when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for as described below. The fair value of interest rate swaps is based on third-party valuations. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

The fair value of forward exchange contracts is their market price at the Statement of Financial Position date, being the present value of the forward price. The gain or loss on remeasurement to fair value of forward exchange contracts is recognised immediately in the income statement.

The fair value of diesel fuel price swaps is based on third party valuations. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract.

Cash flow hedges

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised directly in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in the income statement. If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases the amount recognised in equity is transferred to the income statement in the same period that the hedged item affects profit or loss.

The Group enters into forward diesel swaps in order to hedge exposures to commodity price risk. Cash flow hedging is applied in respect of these instruments in order to reduce volatility in the income statement.

The Group held interest rate swaps to manage the risk of movements in interest rates. Cash flow hedging is applied to reduce volatility in the income statement. Existing interest rate swaps expired during the financial year and were not renewed.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and any other costs directly attributable to bringing the asset to a working condition for its intended use. Self-constructed assets begin to be depreciated from the date they become available for use.

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.

Notes to the Financial Statements

1 Accounting policies continued

Depreciation is charged to the income statement on a straight-line basis in order to depreciate assets to their residual value over their useful economic lives. The annual rates applicable are:

Freehold and long leasehold properties	– 2%
Short leasehold properties	– period of lease
Motor vehicles	– 25%
Office and computer equipment	– 10%–33.3%
Warehouse and production equipment	– 10%–20%

Land is not depreciated.

The residual balances are reviewed annually.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognised in the income statement.

Investment properties

Investment properties are stated at cost less accumulated depreciation and impairment losses.

Depreciation is charged to the income statement on a straight-line basis in order to depreciate assets to their residual value over their useful economic lives. The annual rate applicable is:

Freehold and long leasehold properties	– 2%

The residual balances are reviewed annually.

Goodwill and other intangible assets

Goodwill

All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries. 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 identifiable assets, liabilities and contingent liabilities acquired.

Following the requirements of IFRS 3 revised, transaction costs associated with acquisitions and movements in contingent consideration are recognised in the income statement.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is not amortised but tested annually for impairment, or more frequently when there is an indicator that the unit may be impaired.

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 UK GAAP which was broadly comparable save that only separable intangibles were recognised and goodwill was amortised. This is in accordance with IFRS 1.

Other intangibles

Other intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and impairment losses. Intangible assets recognised as a result of a business combination are stated at fair value at the date of acquisition less cumulative amortisation and impairment losses.

Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. Amortisation on customer lists is charged to administrative expenses in the income statement.

Intangible assets with an indefinite useful life and goodwill are systematically tested for impairment at each Statement of Financial Position date. Other intangible assets are amortised from the date they are available for use. The estimated useful lives of customer lists are deemed to be between one and 24 months.

1 Accounting policies continued

Trade and other receivables

Trade and other receivables are initially stated at fair value and subsequently at amortised cost less impairment losses. Debts are provided for, the credit loss allowance, on specific receivables in full as soon as they are known to be 'bad' or it becomes apparent that payment is 'doubtful'.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost 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. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Allowances for inventory losses are determined by reference to each individual product and are calculated by assessing the age and quantity of each individual product.

Cash and cash equivalents

Cash and cash equivalents are carried in the Statement of Financial Position at amortised cost.

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

Impairment

The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each Statement of Financial Position date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

The recoverable amount for goodwill is estimated at each Statement of Financial Position date.

For the purposes of impairment testing, assets are Grouped together into the smallest Group of assets that generates cash flows from continuing use that are largely independent of the cash inflows from other Groups of assets.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

Impairment losses are recognised in the income statement.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of the other assets in the unit on a pro rata basis.

Calculation of recoverable amount

The recoverable amount of assets, with the exception of the Group's receivables, is the greater of their fair value less cost 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.

The recoverable amount of the Group's receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate, i.e. the effective interest rate computed at initial recognition of these financial assets. Receivables with a short duration are not discounted.

Notes to the Financial Statements

1 Accounting policies continued

Reversals of impairment

An impairment loss in respect of goodwill is not reversed.

In respect of other assets, an impairment loss is reversed when there is an indication that the impairment loss may no longer exist and there had 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.

Trade payables

Trade payables are initially recognised at fair value and then are stated at amortised cost.

Interest-bearing borrowings

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

Borrowing costs

Borrowing costs are capitalised where the Group constructs qualifying assets. All other borrowing costs are written off to the income statement as incurred.

Borrowing costs are charged to the income statement using the effective interest rate method.

Provisions

Provisions are recognised in accordance with IAS 37 'Provisions, Contingent Assets and Contingent Liabilities'. Provisions are made for property dilapidations where a legal obligation exists and when the decision has been made to exit a property, or where the end of the lease commitment is imminent and a reliable estimate of the exit liability can be made.

Employee benefits

The Company and the Group operate both defined benefit and defined contribution plans, the assets of which are held in independent trustee-administered funds. The pension cost is assessed in accordance with the advice of a qualified actuary.

Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

Defined benefit plans

The Group's net obligation in respect of defined benefit pension plans 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 plan assets is deducted. The liability discount rate is the yield at the Statement of Financial Position date using AA 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.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised as an expense in the income statement immediately.

To the extent that any benefits vest immediately, the expense is recognised directly in the income statement.

All actuarial gains and losses that arise in calculating the Group's obligation in respect of a scheme are recognised immediately in reserves and reported in the statement of comprehensive income.

Where the calculation results in a benefit to the Group, the asset recognised is limited to the present value of any future refunds from the plan or reductions in future contributions to the plan.

1 Accounting policies continued

The Group operates a UK defined benefit pension plan and a defined benefit plan in Switzerland. In the UK, there is no contractual agreement or stated Group policy for allocating the net defined benefit liability between the participating subsidiaries, and as such, the full deficit is recognised by the Company, which is the sponsoring employer.

The participating subsidiary companies have recognised a cost equal to contributions payable for the period as advised by a professionally qualified actuary.

Share-based payment transactions

The Company and Group operate various equity-settled share option schemes under the approved and unapproved executive schemes and savings-related schemes.

For executive share option schemes, the option price may not be less than the mid-market value of the Group's shares at the time when the options were granted or the nominal value.

Further details of the share plans are given in the Remuneration Report on pages 50 to 69.

The fair value of options granted is recognised as an employee expense with a corresponding increase in equity over the period that the employees unconditionally become entitled to the award. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the options. The fair value of the options granted is measured using an option valuation model, taking into account the terms and conditions upon which the options were granted. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest except where forfeiture is due only to market conditions such as share prices not achieving the threshold for vesting.

When options are granted to employees of subsidiaries of the Company, the fair value of options granted is recognised as an employee expense in the financial statements of the subsidiary undertaking together with the capital contribution received. In the financial statements of the Company, the options granted are recognised as an investment in subsidiary undertakings with a corresponding increase in equity.

Repurchase of share capital

When share capital recognised as equity is repurchased, the amount of the consideration paid, net of any tax effects, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to or from retained earnings.

Own shares held by Employee Benefit Trust

Transactions of the Group sponsored Employee Benefit Trust are included in the Group financial statements. In particular, the Trust's purchases of shares in the Company are debited directly to equity.

Revenue

Revenue from the sale of goods is measured at the fair value of the consideration and excludes intra-Group sales and value added and similar taxes. Revenue from the sale of goods is recognised when the significant risks and rewards of ownership of the goods are transferred to the buyer (which is the date on which goods are received by the customer), the amount of revenue can be reliably measured and it is probable that the economic benefits associated with the transaction will flow to the Group.

Lease payments

Leases are classified as finance leases whenever the lease transfers substantially all the risks and rewards of ownership to the Group. All other leases are treated as operating leases.

Assets held under finance leases are included in property, plant and equipment at the lower of fair value at the date of acquisition or the present value of the minimum lease payments. The capital element of outstanding finance leases is included in financial liabilities. The finance charge element of rentals is charged to the income statement at a constant period rate of charge on the outstanding obligations.

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

1 Accounting policies continued

Net financing costs

Net financing costs comprise interest payable, finance charges on shares classified as liabilities, finance leases, interest receivable on funds invested, foreign exchange gains and losses, and gains and losses on hedging instruments as outlined in the accounting policy relating to derivative financial instruments and hedging described above.

Interest income and interest payable is recognised in the income statement as it accrues, using the effective interest method. Dividend income is recognised in the income statement on the date the entity's right to receive payments is established.

The Group determines the net interest expense on the net defined benefit liability for the period by applying the discount rate used to measure the defined benefit obligation at the beginning of the annual period to the then net defined benefit liability, taking into account any changes in the net defined benefit liability during the period as a result of contributions and benefit payments.

Dividends

Paid

Interim and final dividends are recognised when they are paid or when approved by the members in a general meeting. Final dividends proposed by the Board and unpaid at the end of the year are not recognised in the financial statements.

Received

The Company receives dividends from its UK and Continental European subsidiaries. Dividends are recognised in the financial statements when they have been received by the Company.

Taxation

Income tax comprises current and deferred tax. 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 Statement of Financial Position date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit; and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the Statement of Financial Position date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Non-underlying items

In order to illustrate the underlying trading performance of the Group, presentation has been made of performance measures excluding those items which it is considered would distort the comparability of the Group's results. These non-underlying items are defined as those items that, by virtue of their nature, size or expected frequency, warrant separate additional disclosure in the financial statements in order to fully understand the underlying performance of the Group.

2 Segment reporting

On 31 December 2016, the Group had 56 operating segments in the UK and three operating segments in Continental Europe. On 28 February 2017, the Group acquired Mitchell Carpets Limited taking the total to 60 operating segments. Each segment represents an individual trading operation, and each operation is wholly aligned to the sales, marketing, supply and distribution of floorcovering products. The operating results of each operation are regularly reviewed by the Chief Operating Decision Maker, which is deemed to be the Group Chief Executive. Discrete financial information is available for each segment and used by the Group Chief Executive to assess performance and decide on resource allocation.

The operating segments have been aggregated to the extent that they have similar economic characteristics. The key economic indicators considered by management in assessing whether operating segments have similar economic characteristics are the products supplied, the type and class of customer, method of sale and distribution and the regulatory environment in which they operate.

As each operating segment is a trading operation wholly aligned to the sales, marketing, supply and distribution of floorcovering products, management considers all segments have similar economic characteristics except for the regulatory environment in which they operate, which is determined by the country in which the operating segment resides.

The Group's internal management structure and financial reporting systems differentiate the operating segments on the basis of the differing economic characteristics in the UK and Continental Europe and accordingly present these as two separate reportable segments. This distinction is embedded in the construction of operating reports reviewed by the Group Chief Executive, the Board and the executive management team and forms the basis for the presentation of operating segment information given below.

	UK		Continental Europe		Total	
	2016 £000	Restated* 2015 £000	**2016 £000**	Restated* 2015 £000	**2016 £000**	Restated* 2015 £000
Revenue						
External revenues	**602,104**	575,341	**91,468**	78,737	**693,572**	654,078
Reportable segment underlying operating profit	**40,944**	37,363	**793**	575	**41,737**	37,938
Reportable segment assets	**263,968**	255,189	**44,516**	36,030	**308,484**	291,219
Reportable segment liabilities	**(167,755)**	(158,859)	**(23,801)**	(13,087)	**(191,556)**	(171,946)

* See note 1.

During the year there were no inter-segment revenues for the reportable segments (2015: £nil).

Notes to the Financial Statements

2 Segment reporting continued

Reconciliations of reportable segment profit, assets and liabilities and other material items:

	2016 £000	2015 £000
Profit for the year		
Total profit for reportable segments	41,737	37,938
Non-underlying items	(1,927)	–
Unallocated expense	(665)	(1,161)
Operating profit	39,145	36,777
Finance income	756	738
Finance expense	(1,722)	(1,891)
Profit before taxation	38,179	35,624
Taxation	(7,216)	(7,213)
Profit for the year	30,963	28,411

	2016 £000	Restated* 2015 £000
Assets		
Total assets for reportable segments	308,484	291,219
Unallocated assets:		
Properties, plant and equipment	90,981	93,242
Deferred tax assets	1,138	629
Cash and cash equivalents	28,171	33,001
Total assets	428,774	418,091
Liabilities		
Total liabilities for reportable segments	(191,556)	(171,946)
Unallocated liabilities:		
Employee benefits	(22,950)	(19,014)
Other interest-bearing loans and borrowings	–	(20,000)
Income tax payable	(6,824)	(6,974)
Derivative liabilities	–	(516)
Deferred tax liabilities	(4,077)	(4,533)
Total liabilities	(225,407)	(222,983)

	UK £000	Continental Europe £000	Reportable segment total £000	Unallocated £000	Consolidated total £000
Other material items 2016					
Capital expenditure	1,808	872	2,680	283	2,963
Depreciation	2,388	732	3,120	2,156	5,276
Non-underlying items	–	–	–	1,927	1,927
Other material items 2015					
Capital expenditure	2,064	543	2,607	287	2,894
Depreciation	2,246	538	2,784	2,020	4,804
Amortisation	–	–	–	375	375

* See note 1.

2 Segment reporting continued

In the UK the Group's freehold properties are held within Headlam Group plc and a rent is charged to the operating segments for the period of use. Therefore, the operating reports reviewed by the Group Chief Executive show all the UK properties as unallocated and the operating segments report a segment result that includes a property rent. This is reflected in the above disclosure.

Each segment is a continuing operation.

The Group Chief Executive, the Board and the senior executive management team have access to information that provides details on revenue by principal product group for the two reportable segments, as set out in the following table:

Revenue by principal product group and geographic origin is summarised below:

	UK		Continental Europe		Total	
	2016 £000	2015 £000	2016 £000	2015 £000	2016 £000	2015 £000
Revenue						
Residential	**422,048**	399,453	**46,337**	40,281	**468,385**	439,734
Commercial	**180,056**	175,888	**45,131**	38,456	**225,187**	214,344
	602,104	575,341	**91,468**	78,737	**693,572**	654,078

3 Profit before tax

The following are included in profit before tax:

	2016 £000	2015 £000
Depreciation on property, plant and equipment	**5,276**	4,804
Amortisation of intangible assets	**–**	375
Profit on sale of property, plant and equipment	**(15)**	(31)
Operating lease rentals		
Plant and machinery	**10,972**	10,187
Land and buildings	**2,548**	1,444

Non-underlying items of £1,927,000 relate to non-recurring people costs paid out during the year and the relaxed tax of £385,000 on these costs.

Auditor's remuneration:

	2016 £000	2015 £000
Audit of these financial statements	**78**	78
Amounts received by the Auditor and their associates in respect of:		
Audit of financial statements of subsidiaries of the Company	**172**	166
Other tax advisory services	**–**	11
All other services	**–**	17
	250	272

Notes to the Financial Statements

4 Staff numbers and costs

The average number of people employed, including Directors, during the year, analysed by category, was as follows:

	Number of employees			
	Group		Company	
	2016	2015	**2016**	2015
By sector:				
Floorcoverings	**2,337**	2,271	**–**	–
Central operations	**11**	10	**11**	10
	2,348	2,281	**11**	10
By function:				
Sales and distribution	**2,200**	2,129	**–**	–
Administration	**148**	152	**11**	10
	2,348	2,281	**11**	10

The aggregate payroll costs were as follows:

	Group		Company	
	2016 £000	2015 £000	**2016 £000**	2015 £000
Wages and salaries	**80,336**	75,353	**3,245**	3,340
Equity settled share-based payment expense (note 21)	**1,239**	1,100	**338**	219
Social security costs	**10,213**	9,293	**460**	463
Pension costs (note 20)	**4,984**	4,958	**343**	496
	96,772	90,704	**4,386**	4,518

5 Emoluments of key management personnel

Executive and Non-Executive Directors are considered to be the key management personnel of the Group.

	2016 £000	2015 £000
Short-term employee benefits	**3,025**	2,181
Equity settled share-based payment expense	**304**	251
	3,329	2,432

Short-term employee benefits comprise salary and benefits earned during the year and bonuses awarded for the year. During 2016 a payment was made as compensation for loss of office. Further details on Directors' remuneration, share options, long-term incentive schemes, and compensation for loss of office are disclosed in the Remuneration Report on page 66.

6 Finance income and expense

	2016 £000	2015 £000
Interest income:		
Bank interest	**756**	699
Other	**–**	39
Finance income	**756**	738
Interest expense:		
Bank loans, overdrafts and other financial expenses	**(1,062)**	(1,150)
Net change in fair value of cash flow hedges transferred from equity	**(23)**	(125)
Net interest on defined benefit plan obligations (note 20)	**(566)**	(616)
Other	**(71)**	–
Finance expenses	**(1,722)**	(1,891)

7 Taxation

Recognised in the income statement

	2016 £000	2015 £000
Current tax expense:		
Current year	**8,434**	7,552
Adjustments for prior years	**(878)**	(317)
	7,556	7,235
Deferred tax expense:		
Origination and reversal of temporary differences	**(202)**	87
Effect of change in tax rates	**(104)**	(126)
Adjustments for prior years	**(34)**	17
	(340)	(22)
Total tax in income statement	**7,216**	7,213

	2016 £000	2015 £000
Tax relating to items (charged)/credited to equity		
Current tax on:		
Income and expenses recognised directly in equity	**(2)**	(87)
Deferred tax on:		
Share options	**21**	22
Deferred tax on other comprehensive income:		
Defined benefit plans	**(778)**	554
Cash flow hedge	**132**	(66)
Total tax reported directly in reserves	**(627)**	423

Factors that may affect future current and total tax charges

The UK headline corporation tax rate for the period was 20%. In the UK Budget on 8 July 2015, the UK Government proposed to reduce the main rate of UK corporation tax to 19% with effect from 1 April 2017 and to 18% with effect from 1 April 2020. Additionally, in the Budget on 16 March 2016, a further rate reduction to 17% was proposed from 1 April 2020, instead of the reduction to 18% as originally announced. The rate reduction to 17% was enacted during the period and has therefore been taken into account in the calculation of the UK related deferred tax balances as these balances will materially reverse after 1 April 2020.

Notes to the Financial Statements

7 Taxation continued

In addition, a reduction in the French corporation tax rate to 28% by 2020 was enacted in December 2016 which has also been taken into account in the calculation of the related deferred tax balance.

Reconciliation of effective tax rate

	2016		2015	
	%	£000	%	£000
Profit before tax		**38,179**		35,624
Tax using the UK corporation tax rate	**20.0**	**7,636**	20.2	7,213
Effect of change in UK tax rate	**(0.1)**	**(42)**	(0.4)	(128)
Effect of change in overseas tax rate	**(0.2)**	**(58)**	–	–
Non-deductible expenses	**1.5**	**588**	1.2	427
Effect of tax rates in foreign jurisdictions	**0.0**	**4**	–	1
Adjustments in respect of prior years	**(2.3)**	**(912)**	(0.8)	(300)
Total tax in income statement	**18.9**	**7,216**	20.2	7,213

8 Current tax liabilities

The Group's current tax liability of £6,824,000 (2015: £6,974,000) represents the amount of income tax payable in respect of current and prior year periods which exceed any amounts recoverable. The Company's current tax liability of £2,147,000 (2015: £2,691,000) represents the amount of income tax payable in respect of current and prior year periods which exceed any amounts recoverable.

9 Earnings per share

	2016 £000	2015 £000
Earnings		
Earnings for underlying basic and underlying diluted earnings per share	**32,505**	–
Earnings for basic and diluted earnings per share	**30,963**	28,411

	2016	2015
Number of shares		
Issued ordinary shares at 31 December	**85,363,743**	85,363,743
Effect of shares held in treasury	**(1,330,339)**	(1,331,576)
Weighted average number of ordinary shares for the purposes of basic earnings per share	**84,033,404**	84,032,167
Effect of diluted potential ordinary shares:		
Weighted average number of ordinary shares at 31 December	**84,033,404**	84,032,167
Dilutive effect of share options	**458,697**	282,078
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**84,492,101**	84,314,245

At 31 December 2016, the Company held 1,123,060 (2015: 1,130,592) shares which have been disclosed in the treasury reserve and these are excluded from the calculation of earnings per share.

10 Property, plant and equipment

Group property, plant and equipment

	Restated* Land and buildings £000	Plant and equipment £000	Under construction £000	Restated* Total £000
Cost				
Balance at 1 January 2015	116,037	33,389	–	149,426
Acquisition	–	38	–	38
Additions	213	2,619	24	2,856
Disposals	–	(1,264)	–	(1,264)
Effect of movements in foreign exchange	39	(146)	–	(107)
Balance at 31 December 2015	**116,289**	**34,636**	**24**	**150,949**
Balance at 1 January 2016	**116,289**	**34,636**	**24**	**150,949**
Additions	**147**	**2,534**	**282**	**2,963**
Disposals	**–**	**(2,300)**	**(306)**	**(2,606)**
Effect of movements in foreign exchange	**2,000**	**1,176**	**–**	**3,176**
Balance at 31 December 2016	**118,436**	**36,046**	**–**	**154,482**
Depreciation and impairment				
Balance at 1 January 2015	22,634	23,331	–	45,965
Restatement	(2,796)	(618)	–	(3,414)
Balance at 1 January 2015 restated	19,838	22,713		42,551
Depreciation charge for the year	1,979	2,825	–	4,804
Disposals	–	(1,020)	–	(1,020)
Effect of movements in foreign exchange	48	(111)	–	(63)
Balance at 31 December 2015	21,865	24,407	–	46,272
Balance at 1 January 2016	**21,865**	**24,407**	**–**	**46,272**
Depreciation charge for the year	**2,133**	**3,143**	**–**	**5,276**
Disposals	**–**	**(2,219)**	**–**	**(2,219)**
Effect of movements in foreign exchange	**1,281**	**938**	**–**	**2,219**
Balance at 31 December 2016	**25,279**	**26,239**	**–**	**51,548**
Net book value				
At 1 January 2015	96,199	10,676	–	106,875
At 31 December 2015 and 1 January 2016	94,424	10,229	24	104,677
At 31 December 2016	**93,157**	**9,777**	**–**	**102,934**

* See note 1.

At 31 December 2016 the cost less accumulated depreciation of long leasehold property held by the Group was £7,611,000 (2015: £7,791,000).

Notes to the Financial Statements

10 Property, plant and equipment continued

Company investment properties and plant and equipment

	Investment properties £000	Plant and equipment £000	Under construction £000	Restated* Total £000
Cost				
Balance at 1 January 2015	103,230	164	–	164
Additions	166	97	24	121
Disposals	–	(156)	–	(156)
Balance at 31 December 2015	103,396	105	24	129
Balance at 1 January 2016	**103,396**	**105**	**24**	**129**
Additions	**–**	**1**	**282**	**283**
Disposals	**–**	**(34)**	**(306)**	**(340)**
Balance at 31 December 2016	**103,396**	**72**	**–**	**72**
Depreciation				
Balance at 1 January 2015	15,174	63	–	63
Depreciation charge for the year	1,693	42	–	42
Disposals	–	(85)	–	(85)
Balance at 31 December 2015	16,867	20	–	20
Balance at 1 January 2016	**16,867**	**20**	**–**	**20**
Depreciation charge for the year	**1,694**	**24**	**–**	**24**
Disposals	**–**	**(8)**	**–**	**(8)**
Balance at 31 December 2016	**18,561**	**36**	**–**	**36**
Net book value				
At 1 January 2015	88,056	101	–	101
At 31 December 2015 and 1 January 2016	86,529	85	24	109
At 31 December 2016	**84,835**	**36**	**–**	**36**

* See note 1.

At 31 December 2016 the cost less accumulated depreciation of long leasehold property held by the Company was £7,611,000 (2015: £7,791,000).

11 Intangible assets – Group

	Goodwill £000	Customer lists £000	Total £000
Cost			
Balance at 1 January 2015	13,210	4,457	17,667
Addition (note 23)	375	375	750
Balance at 31 December 2015	13,585	4,832	18,417
Balance at 1 January 2016 and 31 December 2016	**13,585**	**4,832**	**18,417**
Amortisation			
Balance at 1 January 2015	3,197	4,457	7,654
Charge for the year	–	375	375
Balance at 31 December 2015	3,197	4,832	8,029
Balance at 1 January 2016 and 31 December 2016	**3,197**	**4,832**	**8,029**
Net book value			
At 1 January 2015 and 31 December 2015	10,388	–	10,388
At 31 December 2016	**10,388**	**–**	**10,388**

Cumulative impairment losses recognised in relation to goodwill is £3,197,000 (2015: £3,197,000).

Impairment tests for cash-generating units containing goodwill ('CGU')

Goodwill is attributed to the businesses identified below for the purpose of testing impairment. These businesses are the lowest level at which goodwill is monitored and represent operating segments.

The aggregate carrying amounts of goodwill allocated to each CGU are as follows:

	Reported segment	2016 £000	2015 £000
Joseph, Hamilton & Seaton	**UK**	**4,348**	4,348
Crucial Trading	**UK**	**1,369**	1,369
Belcolor AG	**Continental Europe**	**3,342**	3,342
Other	**UK**	**1,329**	1,329
		10,388	10,388

Impairment

Each year, or whenever events or a change in the economic environment or performance indicates a risk of impairment, the Group reviews the value of goodwill balances allocated to its cash-generating units.

An impairment test is a comparison of the carrying value of the assets of a business or CGU to their recoverable amount. The recoverable amount represents the higher of the CGU's fair value less the cost to sell and value in use. Where the recoverable amount is less than the carrying value, an impairment results. During the year, all goodwill was tested for impairment, with no impairment charge resulting (2015: No impairment).

Value in use was determined by discounting the future cash flows generated from the continuing use of the CGU on a basis consistent with 2015, and applying the following key assumptions.

Notes to the Financial Statements

11 Intangible assets – Group continued

Key assumptions

Cash flows were projected based on actual operating results, the approved 2017 business plan and management's assessment of planned performance in the period to 2021. For the purpose of impairment testing the cash flows were assumed to grow into perpetuity at a rate of 2.5% beyond 2021.

The main assumptions within the operating cash flows used for 2017 include the achievement of future sales volumes and prices for all key product lines, control of purchase prices, achievement of budgeted operating costs and no significant adverse foreign exchange rate movements. These assumptions have been reviewed in light of the current economic environment.

The Directors have estimated the discount rate by reference to an industry average weighted average cost of capital. This has been adjusted to include an appropriate risk factor to reflect current economic circumstances and the risk profile of the CGUs. A pre-tax weighted average cost of capital of 10.6% (2015: 11.1%) has been used for impairment testing adjusted to 11.5% (2015: 12.0%) for Continental Europe to reflect the differing risk profile of that segment. The pre-tax discount rate has been applied to the pre-tax cash flows.

The CGUs in the UK have similar characteristics and risk profiles, and therefore a single discount rate has been applied to each UK CGU. Similarly, the Directors view the CGUs in Continental Europe as having consistent risk profiles and therefore a single risk factor has been applied. The CGUs in Continental Europe operate under a different regulatory environment and this is therefore reflected in the risk factor used to determine the discount rates in the UK and Continental Europe.

Sensitivity analysis

The Group has applied sensitivities to assess whether any reasonable possible changes in these key assumptions could cause an impairment that would be material to these Consolidated Financial Statements. The sensitivity analyses did not identify any material impairment risks with the exception of the goodwill attributed to Belcolor.

Belcolor

The key assumptions used in the Belcolor impairment review relates to the 2017 budgeted cash flows and the future growth rates assumed thereafter. The budget for 2017 assumes a 73% increase in operating profit (equivalent to a 6% increase in sales) compared with 2016. Subsequently, the calculations assume future annual growth in operating profit of between 1.5% and 2.5%, resulting in calculated headroom of £1.6 million. A reduction of 15% in the 2017 budgeted operating profit would reduce the headroom to zero. In the event that the 2017 budget is achieved but there is no subsequent growth, a goodwill impairment charge of £0.1 million would arise. The carrying value of goodwill of £3.3 million would be fully impaired if 2016 operating profit recurred in 2017 and there was no forecast future growth thereafter.

12 Investments in subsidiaries

Summary information on investments in subsidiary undertakings is as follows:

	£000
Cost	
Balance at 1 January 2015	88,985
Share options granted to employees of subsidiary undertakings	821
Balance at 31 December 2015	89,806
Balance at 1 January 2016	**89,806**
Share options granted to employees of subsidiary undertakings	**901**
Balance at 31 December 2016	**90,707**
Carrying value	
At 1 January 2015	88,985
At 31 December 2015	89,806
At 31 December 2016	**90,707**

A full list of the Group's subsidiaries are listed on page 140. There were no impairments recognised on the Company's investments in subsidiaries in the year ended 31 December 2016.

13 Deferred tax assets and liabilities – Group

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2016 £000	Restated* 2015 £000	2016 £000	Restated* 2015 £000	2016 £000	Restated* 2015 £000
Property, plant and equipment	–	–	(7,871)	(8,267)	(7,871)	(8,267)
Intangible assets	–	–	(180)	(206)	(180)	(206)
Employee benefits	4,792	4,060	–	–	4,792	4,060
Hedging	–	93	(40)	–	(40)	93
Other items	360	416	–	–	360	416
Tax assets/(liabilities)	5,152	4,569	(8,091)	(8,473)	(2,939)	(3,904)
Set-off of tax	(4,014)	(3,940)	4,014	3,940	–	–
	1,138	629	(4,077)	(4,533)	(2,939)	(3,904)

Movement in deferred tax during the year

	Restated* 1 January 2016 £000	Recognised in income £000	Recognised in equity £000	31 December 2016 £000
Property, plant and equipment	(8,267)	396	–	(7,871)
Intangible assets	(206)	26	–	(180)
Employee benefits	4,060	(25)	756	4,791
Hedging	93	–	(132)	(39)
Other items	416	(57)	1	360
	(3,904)	340	625	(2,939)

Movement in deferred tax during the prior year

	Restated* 1 January 2015 £000	Recognised in income £000	Recognised in equity £000	Restated* 31 December 2015 £000
Property, plant and equipment	(8,540)	273	–	(8,267)
Intangible assets	(211)	5	–	(206)
Employee benefits	4,746	(109)	(577)	4,060
Hedging	26	–	67	93
Other items	563	(147)	–	416
	(3,416)	22	(510)	(3,904)

* See note 1.

Unrecognised deferred tax assets and liabilities

At the Statement of Financial Position date the Group has unused capital losses of £10,797,000 (2015: £10,797,000) available for offset against future chargeable gains. No deferred tax asset has been recognised in respect of this amount as the Directors do not anticipate incurring significant chargeable gains in the foreseeable future.

Notes to the Financial Statements

13 Deferred tax assets and liabilities – Company

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2016 £000	Restated* 2015 £000	2016 £000	Restated* 2015 £000	2016 £000	Restated* 2015 £000
Property, plant and equipment	–	–	(6,571)	(6,817)	(6,571)	(6,817)
Employee benefits	3,324	3,063	–	–	3,324	3,063
Hedging	–	93	(40)	–	(40)	93
Other items	48	46	–	–	48	46
Tax assets/(liabilities)	3,372	3,202	(6,611)	(6,817)	(3,239)	(3,615)
Set-off of tax	(3,372)	(3,202)	3,372	3,202	–	–
	–	–	(3,239)	(3,615)	(3,239)	(3,615)

Movement in deferred tax during the year

	Restated* 1 January 2016 £000	Recognised in income £000	Recognised in equity £000	31 December 2016 £000
Property, plant and equipment	(6,817)	246	–	(6,571)
Employee benefits	3,063	(176)	437	3,324
Hedging	93	–	(133)	(40)
Other items	46	2	–	48
	(3,615)	72	304	(3,239)

Movement in deferred tax during the prior year

	Restated* 1 January 2015 £000	Recognised in income £000	Recognised in equity £000	Restated* 31 December 2015 £000
Property, plant and equipment	(7,063)	246	–	(6,817)
Employee benefits	3,855	(206)	(586)	3,063
Hedging	26	–	67	93
Other items	146	(100)	–	46
	(3,036)	(60)	(519)	(3,615)

* See note 1.

Unrecognised deferred tax assets and liabilities

At the Statement of Financial Position date the Company has unused capital losses of £10,797,000 (2015: £10,797,000) available for offset against future chargeable gains. No deferred tax asset has been recognised in respect of this amount as the Directors do not anticipate incurring significant chargeable gains in the foreseeable future.

14 Inventories

	Group 2016 £000	Group Restated* 2015 £000	Company 2016 £000	Company 2015 £000
Balance as at 31 December	**126,037**	119,143	**–**	–
Restatement*	**–**	(978)	**–**	–
Goods for resale	**126,037**	118,165	**–**	–

Cost of sales consists of the following:

	Group 2016 £000	Group 2015 £000	Company 2016 £000	Company 2015 £000
Material cost	**478,046**	450,498	**–**	–
Processing cost	**3,022**	3,070	**–**	–
	481,068	453,568	**–**	–

* See note 1.

The cost of inventories within cost of sales stated above includes movements in the provision for obsolete inventory of £245,000 release (2015: £197,000 charge).

15 Trade and other receivables

	Group 2016 £000	Group Restated* 2015 £000	Company 2016 £000	Company 2015 £000
Trade receivables	**97,589**	89,534	**–**	–
Prepayments and accrued income	**4,483**	3,935	**530**	26
Other receivables	**26,630**	26,791	**297**	189
Derivative assets used for economic hedging:				
Other derivatives at fair value	**232**	40	**232**	–
Amounts due from subsidiary undertakings	**–**	–	**16,292**	19,970
	128,934	120,300	**17,351**	20,185

* See note 1.

£849,000 (2015: £1,572,000) was recognised as an impairment loss in the Consolidated Income Statement in respect of trade receivables.

The impairment loss is attributable to the reportable segments as follows:

	2016 £000	2015 £000
UK	**734**	1,210
Continental Europe	**115**	362
	849	1,572

Notes to the Financial Statements

16 Cash and cash equivalents

	Group		Company	
	2016 £000	2015 £000	2016 £000	2015 £000
Cash	59,343	63,932	28,171	33,001
Bank overdrafts	(4)	–	–	–
Cash and cash equivalents per Statement of Financial Position	59,339	63,932	28,171	20,000

17 Other interest-bearing loans and borrowings

This note provides information about the contractual terms of the Group's and Company's interest-bearing loans and borrowings.

The Group completed a refinancing of its existing facilities, which were due for renewal on 8 March 2017, on 14 December 2016. The Group has entered into two separate agreements with Barclays Bank PLC and HSBC Bank Plc and include both Sterling and Euro term facilities. The Group's new banking arrangements, which run to 14 December 2021, increase the level of Sterling committed facilities from £40 million to £47.5 million, and have additional Euro facilities of €8.6 million. The Group also has short-term uncommitted facilities which have been reduced by £10 million to £25 million, and are renewable on an annual basis. In addition, the Group has existing facilities of £7,822,000 in Continental Europe. The total banking facilities available to the Group at 31 December 2016 were £87,651,000 (2015: £81,706,000).

For more information about the Group's and Company's exposure to interest rate and foreign currency risk, see note 23.

	Group		Company	
	2016 £000	2015 £000	2016 £000	2015 £000
Current liabilities				
Interest-bearing loan	224	–	–	–
	224	–	–	–
Non-current liabilities				
Interest-bearing loans	6,493	20,000	–	20,000
	6,493	20,000	–	20,000

The Group has undrawn borrowing facilities at 31 December 2016, which amounted to £80,931,000 (2015: £61,706,000). The facility conditions for drawdown had been met during the period. The facility is unsecured and there is a cross guarantee in place between the Company and its UK, French and Dutch subsidiaries. There is a downstream guarantee from the Company in relation to its borrowing facility in the Netherlands and France. Covenant calculations have been prepared for the year ending 31 December 2016 and there were no breaches.

The undrawn borrowing facilities are as follows:

	Interest rate %	2016 £000	Interest rate %	2015 £000
UK	1.32	72,500	2.01	55,000
Netherlands	2.13	1,466	2.31	1,106
France	1.15	2,984	1.15	2,211
Switzerland	2.20	3,981	2.25	3,389
		80,931		61,706

All the borrowing facilities above bear interest at floating rates, however the Group entered into two interest rate swaps on 11 June 2012 to fix £20 million of its sterling denominated borrowings. The swaps matured on 8 March 2016. The Swiss facility may be drawn as an overdraft or fixed rate loan with different rates depending on the term and amount.

18 Trade and other payables

	Group		Company	
	2016 £000	Restated* 2015 £000	2016 £000	2015 £000
Trade payables	**141,999**	131,153	**578**	307
Taxation and social security	**16,617**	15,291	**2,172**	2,012
Non-trade payables and accrued expenses	**24,658**	24,415	**3,507**	3,901
Amounts due to subsidiary undertakings	**–**	–	**31,886**	31,315
Derivative liabilities used for economic hedging:				
Derivatives used for hedging	**–**	516	**–**	516
Other derivatives at fair value	**30**	–	**–**	–
	183,304	171,375	**38,143**	38,051

* See note 1.

Included within non-trade payables and accrued expenses is an amount of £nil for accrued interest on unsecured bank loans (2015: £35,000).

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 23.

19 Provisions

	Property	
	2016 £000	Restated* 2015 £000
Balance at 1 January	**1,087**	787
Charged/(credited) to the income statement:		
Additional provisions	**444**	300
Balance at 31 December	**1,531**	1,087

* See note 1

The property provisions relate to property dilapidations.

20 Employee benefits

During the year, the Group operated UK and Swiss defined benefit plans and defined contribution plans in the UK, France and the Netherlands.

UK defined benefit plan

The Headlam Group plc Staff Retirement Benefits Scheme is the principal defined benefit plan which provides pensions in retirement and death benefits to members. The majority of members are entitled to receive pensions from age 65, equal to either 1/50 or 1/60 of final salary for each year of service that the employee provided, depending on which section of the plan the member is part of.

The plan is a registered scheme under UK legislation. The plan is legally separated from the Company and assets are held independently of the Company's finances.

The plan is subject to the scheme funding requirements outlined in UK legislation.

Notes to the Financial Statements

20 Employee benefits continued

The Company has a right to a refund of any surplus in the plan if the plan winds up, after payment of expenses, members benefits and any enhancements to the members' benefits as the Trustee sees fit. In addition, if the assets of the plan exceed the estimate by the actuary of the cost of buying out the benefits of all beneficiaries with an insurance company, including the associated expenses, and the plan is not being wound up, then the Company may request a payment of the excess funds. There have been no payments made to the Company out of the plan's assets over the year, and so no additional liability has been recognised on the balance sheet.

The plan was established from 11 February 1983 under trust and is governed by the plan's Trust Deed and Rules dated 26 March 2015. The Trustee of the plan comprises two employee representatives and four employer representatives. The Trustee of the plan is required by law to act in the best interests of the plan participants. The Trustee is responsible for the operation and the governance of the plan, including making decisions regarding the plan's funding and investment strategy in conjunction with the Company.

The ultimate cost of the plan to the Company will depend upon actual future events rather than the assumptions made. Many of the assumptions made are unlikely to be borne out in practice and as such the cost of the plan may be higher (or lower) than disclosed.

The plan exposes the Company to actuarial risks such as longevity risk, interest rate risk, market (investment) risk and currency risk. The risk to the Company is that the assumptions underlying the disclosures, or the calculation of contribution requirements, are not borne out in practice and the cost to the company is higher than expected. This could result in higher contributions required from the Company and a higher deficit disclosed. More specifically, the assumptions not being borne out in practice could include:

- The return on the plan assets being lower than assumed, resulting in an unaffordable increase in the required Company contribution rate.
- Falls in asset values not being matched by similar falls in the value of liabilities.
- Inflation being higher than that assumed, resulting in an increase in the value of the members' benefits and therefore a higher cost to the plan.
- Unanticipated future changes in mortality patterns leading to an increase in the plan's liabilities. Future mortality rates cannot be predicted with certainty.
- The potential exercise of options against the plan, for example taking early retirement or exchanging a portion of pension for a cash lump sum.

There have been no amendments, curtailments or settlements made to the plan during 2016.

The plan's investment strategy is to invest broadly 90% in return seeking assets and 10% in matching assets, mainly government bonds. This strategy reflects the plan's liability profile and the Trustee's and Company's attitude to risk. The matching fund seeks to match the return achieved on the liabilities.

The plan's investments include interest rate and inflation hedging.

The plan holds a number of annuity policies which match a portion of the pensions in payment.

The plan is funded partly by contributions from members and partly by contributions from the Company at rates advised by professionally qualified actuaries. The last scheme funding valuation of the plan was as at 31 March 2014 and revealed a funding deficit of £10,883,000. The Trustee of the plan commissioned an annual update valuation as at 31 March 2016 and this reported an increase in deficit from £10,883,000 to £15,805,000. The main factors that have combined to produce this change in the position since the last formal valuation are shown in the following table:

20 Employee benefits continued

	£000
Deficit as at 31 March 2014	(10,883)
Interest on deficit	(1,022)
Gain on investments	7,475
Contributions paid to repair the deficit	5,868
Change in market conditions	(17,496)
Other factors	253
Estimated deficit as at 31 March 2016	**(15,805)**

The main annual rate assumptions used by the actuary in the 2014 valuation were: increase in salaries 4.8%; increase of pensions in payment 3.3%; discount rate before retirement 5.46%; discount rate after retirement 3.71%; and inflation 3.3%. Assets were taken at their market value at the valuation date.

The main annual rate assumptions used by the actuary in the 2016 annual update valuation were: increase in salaries 4.47%; increase of pensions in payment 2.97%; discount rate before retirement 4.18%; discount rate after retirement 2.43%; and inflation 2.97%.

In the recovery plan dated 26 March 2015 the Company has agreed to pay contributions of £175,000 per month from 1 January 2016, increasing by 3.3% each subsequent 1 January, with the view to eliminating the shortfall by 30 April 2019.

In accordance with the recovery plans dated 29 July 2011 and 26 March 2015, payments were made to the plan during 2016 of £2,171,000 towards the deficit. The Company is expected to pay contributions of £3,062,000 over the next accounting period. This includes £2,169,000 for payments under the recovery plan and £893,000 for the accrual of benefits.

In addition to the recovery payments, under the schedule of contributions dated 26 March 2015, Company contributions are fixed at 35% of pensionable salaries each month.

In addition, the Company is expected to meet the cost of administrative expenses and insurance premiums for the plan.

The liabilities of the plan are based on the current value of expected benefit payment cash flows to members of the plan over the next 60 years or more. The weighted average duration of the liabilities is approximately 20 years.

During 2010, the UK Government announced a move to adopting Consumer Price Inflation ('CPI') rather than Retail Price Inflation ('RPI') as the basis for inflation assumptions underpinning retirement benefit obligations. The Directors have considered this change and associated guidance. Having taken advice, the Company has determined that RPI remains the appropriate basis for measuring its obligations, such that the change announced has had no impact on the Group's retirement benefit obligations.

20 Employee benefits continued

Swiss defined benefit plan

The plan provides occupational retirement, disability and survivors' benefits. The members are entitled to receive pensions from age 64 (female) or 65 (male), equal to the old age savings balance multiplied with a conversion rate of 6.8% for the mandatory part of the savings balance and 5.85% for the part beyond the mandatory part. The minimum interest rate on old age savings has legally been fixed.

The Company left the Columna Sammelstiftung on 1 January 2016 and affiliated to the Sammelstiftung berufliche Vorsorge Swiss Life, Sammelstiftung mit Anlagerisiko. The pension plans remained unchanged. The plan is legally separated from the Company. The executive body of the collective foundation is the board of trustees, which is elected directly by the insured of the affiliated companies/occupational benefits funds and functions independently of Swiss Life. Its members include employer and employee representatives from a wide range of occupations and companies of different sizes. The board of trustees' responsibilities include, among other things, supervising compliance with legal provisions and issuing the regulations that govern the various activities. The Company elects an occupational benefits fund commission (OBC).

The collective foundation is reinsured for risk benefits with Swiss Life insurance company.

The plan exposes the Company to the market (investment) risk. The risk to the Company is that return on assets may be lower than legally required. This could result in higher contributions required from the Company and a higher deficit disclosed.

There have been no amendments, curtailments or settlements made to the plan during 2016.

The occupational benefits fund commission (OBC) defines the investment strategy; the affiliated occupational benefits fund itself bears the investment risk. The investments are managed with Credit Suisse.

The last (provisional) scheme funding valuation of the plan was as at 31 December 2016 and revealed cover ratio of 113.34% (overfunding). This overfunding is appropriate to Swiss legislation and cannot be considered in the context of IAS 19. According to Swiss rules there is no need to evaluate the scheme using assumptions for future changes of salary increase, benefit increase or inflation.

The last IAS 19 valuation at year-end 2016 revealed a funding deficit of £4,325,000 (2015: £2,517,000). The Group is expected to pay £813,000 for future service costs over the next accounting period.

The liabilities of the plan are based on the current value of expected benefit payment cash flows to members of the plan over the next 50 years or more. The weighted average duration of the liabilities is approximately 20.9 years.

Defined benefit obligation

In the UK there is no contractual agreement or stated Group policy for allocating the net defined benefit liability between the participating subsidiaries and as such the full deficit is recognised by the Company, which is the sponsoring employer. The participating subsidiary companies have recognised a cost equal to contributions payable for the period as advised by a professionally qualified actuary. The Company recognises a cost equal to its contributions payable for the period net of amounts recharged in relation to the Group deficit to the participating subsidiary companies.

	Group		Company	
	2016 £000	2015 £000	2016 £000	2015 £000
Present value of funded defined benefit obligations	**(141,947)**	(115,849)	**(128,002)**	(102,766)
Fair value of plan assets	**119,339**	97,167	**109,719**	86,601
Net obligations	**(22,608)**	(18,682)	**(18,283)**	(16,165)
Other long-term employee benefits	**(343)**	(332)	**–**	–
Total employee benefits	**(22,951)**	(19,014)	**(18,283)**	(16,165)
Analysed as:				
Current liabilities	**(2,169)**	(2,171)	**(2,169)**	(2,171)
Non-current liabilities	**(20,781)**	(16,843)	**(16,114)**	(13,994)
Total employee benefits	**(22,951)**	(19,014)	**(18,283)**	(16,165)

20 Employee benefits continued

Movements in present value of defined benefit obligation

	Group		Company	
	2016 £000	2015 £000	2016 £000	2015 £000
At 1 January	**115,849**	117,639	**102,766**	106,297
Current service cost	**2,061**	2,173	**1,329**	1,541
Interest cost	**3,863**	3,714	**3,734**	3,570
Net remeasurement losses/(gains) – financial	**26,825**	(4,108)	**25,640**	(4,581)
Net remeasurement (gains)/losses – demographic	**(358)**	–	**–**	–
Net remeasurement (gains)/losses – experience	**(571)**	(478)	**(535)**	(217)
Benefits paid	**(5,675)**	(4,050)	**(5,103)**	(4,036)
Settlement	**(2,587)**	–	**–**	–
Contributions by members	**392**	393	**171**	192
Effect of movements in foreign exchange	**2,148**	566	**–**	–
At 31 December	**141,947**	115,849	**128,002**	102,766

Movements in fair value of plan assets

	Group		Company	
	2016 £000	2015 £000	2016 £000	2015 £000
At 1 January	**97,167**	96,190	**86,601**	86,907
Interest income on plan assets	**3,297**	3,098	**3,194**	2,978
Return on assets, excluding interest income	**21,560**	(3,294)	**21,673**	(3,460)
Contributions by employer:				
Future service contributions	**1,376**	1,397	**1,052**	1,052
Past service deficit contributions	**2,088**	2,925	**2,088**	2,925
Additional past service deficit contributions	**43**	43	**43**	43
Contributions by members	**392**	393	**171**	192
Benefits paid	**(5,675)**	(4,050)	**(5,103)**	(4,036)
Settlement	**(2,587)**	–	**–**	–
Effect of movements in foreign exchange	**1,678**	465	**–**	–
At 31 December	**119,339**	97,167	**109,719**	86,601

20 Employee benefits continued

The fair value of the plan assets were as follows:

	Group		Company	
	2016 £000	2015 £000	**2016 £000**	2015 £000
Equities	**38,672**	40,715	**36,357**	38,639
Government debt	**21,220**	13,396	**21,220**	13,396
Corporate bonds	**32,514**	29,528	**27,566**	24,374
Annuities	**5,442**	5,019	**5,442**	5,019
Hedge funds	**699**	(2,229)	**699**	(2,229)
Other	**20,792**	10,738	**18,435**	7,402
	119,339	97,167	**109,719**	86,601

Expense recognised in the income statement relating to defined benefit obligation

	Group	
	2016 £000	2015 £000
Service cost	**2,061**	2,173
Net interest on the net defined benefit liability (note 6)	**566**	616
Total	**2,627**	2,789

The expenses recognised in the following line items in the Consolidated Income Statement are:

	Group	
	2016 £000	2015 £000
Administrative expenses	**2,061**	2,173
Net financing income (note 6)	**566**	616
	2,627	2,789

Remeasurement of the net defined benefit liability in the Statement of Comprehensive Income:

	Group	
	2016 £000	2015 £000
Net remeasurement – financial	**26,825**	(4,108)
Net remeasurement – demographic	**(358)**	–
Net remeasurement – experience	**(571)**	(478)
Return on assets, excluding interest income	**(21,560)**	3,294
	4,336	(1,292)

20 Employee benefits continued

Principal actuarial assumptions are as follows:

	UK		Swiss	
	2016 %	2015 %	**2016 %**	2015 %
Discount rate	**2.7**	3.7	**0.5**	1.0
Future salary increases	**4.9**	4.8	**2.0**	2.0
Future pension increases	**3.4**	3.3	**–**	–
Inflation rate	**3.4**	3.3	**2.0**	2.0
Mortality table assumptions:				
UK pre-retirement	**AC00 (Ultimate) table**	AC00 (Ultimate) table	**–**	–
UK post-retirement – future pensioners	**94%(M)/100%(F) of the S1PA tables with future improvements from 2004 in line with the CMI mortality projections model CMI_2013 with a long-term rate of improvement of 1.5% per annum.**	94%(M)/100%(F) of the S1PA tables with future improvements from 2004 in line with the CMI mortality projections model CMI_2013 with a long-term rate of improvement of 1% per annum.		
UK post-retirement – current pensioners	**94%(M)/100%(F) of the S1PA tables with future improvements from 2004 in line with the CMI mortality projections model CMI_2013 with a long-term rate of improvement of 1.5% per annum.**	94%(M)/100%(F) of the S1PA tables with future improvements from 2004 in line with the CMI mortality projections model CMI_2013 with a long-term rate of improvement of 1.5% per annum.		
Swiss scheme	**–**	–	**BVG 2015**	BVG 2010

The mortality assumption implies the expected future lifetime from age 65 is as follows:

	Group		Company	
	2016 £000	2015 £000	**2016 £000**	2015 £000
Non-pensioner male	**25.2**	25.1	**25.2**	25.1
Pensioner male	**22.9**	22.8	**22.9**	22.8
Non-pensioner female	**27.1**	27.0	**27.1**	27.0
Pensioner female	**24.8**	24.7	**24.8**	24.7

Notes to the Financial Statements

20 Employee benefits continued

Company

The principal actuarial assumptions for the Company are the same as those disclosed for the UK above.

Sensitivity analysis

The tables below for the UK and Swiss defined benefit plans show the impact on the defined benefit obligation of changing each of the most significant assumptions in isolation.

UK defined benefit plan

		Impact on scheme liabilities 2016		Impact on scheme liabilities 2015	
Effect in £millions	**Change in assumption**	**Increase**	**Decrease**	Increase	Decrease
Discount rate	0.25% movement	**(6.8)**	**7.3**	(5.0)	5.3
Rate of inflation (RPI)*	0.25% movement	**6.2**	**(5.8)**	4.5	(4.2)
Salary increases	0.25% movement	**1.6**	**(1.6)**	1.2	(1.2)
Assumed life expectancy	one year movement	**5.8**	**(6.0)**	4.1	(4.2)

* With corresponding changes to the salary and pension increase assumptions.

The figures in the table as at 31 December 2016 have been calculated using the same valuation method that was used to calculate the UK defined benefit obligation at the same date. The figures in the table as at 31 December 2015 have been calculated by applying the same percentage increase or decrease as at 31 December 2016.

Extrapolation of the sensitivity analysis beyond the ranges shown may not be appropriate.

Swiss defined benefit plan

		Impact on scheme liabilities 2016		Impact on scheme liabilities 2015	
Effect in £millions	**Change in assumption**	**Increase**	**Decrease**	Increase	Decrease
Discount rate	0.25% movement	**(0.7)**	**0.8**	(0.6)	0.6
Rate of inflation (RPI)*	0.25% movement	**0.5**	**–**	0.4	–
Salary increases	0.25% movement	**0.1**	**(0.1)**	0.0	(0.0)
Assumed life expectancy	one year movement	**0.2**	**(0.1)**	0.2	(0.2)

* With corresponding changes to the salary and pension increase assumptions.

The figures in the table as at 31 December 2016 have been calculated using the same valuation method that was used to calculate the Swiss defined benefit obligation at the same date. The figures in the table as at 31 December 2015 have been calculated by applying the same percentage increase or decrease as at 31 December 2016.

Extrapolation of the sensitivity analysis beyond the ranges shown may not be appropriate.

History of plans

The history of the plans for the current and prior periods is as follows:

Statement of Financial Position

Group	**2016 £000**	2015 £000	2014 £000	2013 £000	2012 £000
Present value of defined benefit obligation	**(141,947)**	(115,849)	(117,639)	(97,085)	(93,499)
Fair value of plan assets	**119,339**	97,167	96,190	82,263	76,388
Deficit	**(22,608)**	(18,682)	(21,449)	(14,822)	(17,111)

20 Employee benefits continued

Company	2016 £000	2015 £000	2014 £000	2013 £000	2012 £000
Present value of defined benefit obligation	**(128,002)**	(102,766)	(106,297)	(87,111)	(82,735)
Fair value of plan assets	**109,719**	86,601	86,907	73,704	67,391
Deficit	**(18,283)**	(16,165)	(19,390)	(13,407)	(15,344)

The Group operated an employment indemnity scheme in connection with a foreign subsidiary undertaking to provide for lump sum cash payments due to employees retiring on their normal retirement date. The present value of the retirement indemnity obligation at 31 December 2016 is £343,000 (2015: £332,000). This was reported as other long-term employee benefits within the employee benefits disclosure.

Total Group pension costs

Included within the total staff costs as disclosed in note 4 are costs relating to the Group's defined contribution plans. The pension cost for the year represents contributions payable by the Group to the plans and amounted to £2,922,000 (2015: £2,785,000). Contributions amounting to £176,000 (2015: £166,000) in respect of the December 2016 payroll were paid in January 2017.

The total Group cost of operating the plans during the year was £4,984,000 (2015: £4,958,000) and, at 31 December 2016, there was an amount of £319,000 (2015: £321,000) owed to the plans, being employer and employee contributions due for December 2016, which was paid in January 2017.

21 Share-based payments

Group and Company

Executive Directors and executive management currently participate in executive share option schemes. The option price may not be less than the greater of the mid-market value of the Group's shares at the time when the options were granted or the nominal value. Options granted under the 1998 Inland Revenue approved scheme are normally exercisable between the third and tenth anniversaries of their date of grant, subject to the movement of the Group's basic earnings per share exceeding RPI over the relevant period.

Options granted under the 1998 unapproved scheme are normally exercisable between the third and seventh anniversaries of their date of grant. Awards are subject to the movement of the Group's basic earnings per share exceeding RPI between 3% and 5% per annum respectively over the relevant period.

Additionally, the Group operates a savings-related share option scheme ('Sharesave scheme') which is open to employees subject to eligibility criteria determined by the Directors prior to each option grant. The most recent grant was on 4 May 2016 when employees with over one month's service were invited to participate.

The Group also operates a 2008 HMRC approved scheme, a 2008 unapproved scheme, the Headlam Group Performance Share Plan 2008 and the Headlam Group Co-Investment Plan 2008. Further details of these schemes and plans are given in the Remuneration Report on pages 50 to 69.

Notes to the Financial Statements

21 Share-based payments continued

The terms and conditions of the grants are as follows, whereby all options are settled by physical delivery of shares:

Grant date/employees entitled	Number of instruments 2016	2015	Vesting conditions	Contractual life of options
Five-year Sharesave scheme granted to other employees 11 May 2011	**–**	42,006	Continuous service	01/07/16 – 01/01/17
Three-year Sharesave scheme granted to other employees 11 May 2012	**–**	151	Continuous service	01/07/15 – 01/01/16
Five-year Sharesave scheme granted to other employees 11 May 2012	**49,905**	49,905	Continuous service	01/07/17 – 01/01/18
Three-year Sharesave scheme granted to other employees 10 May 2013	**656**	117,762	Continuous service	01/07/16 – 01/01/17
Five-year Sharesave scheme granted to other employees 10 May 2013	**42,136**	46,731	Continuous service	01/07/18 – 01/01/19
Headlam Group Co-Investment Plan 2008 granted to key management 1 April 2014*	**243,585**	249,418	If the real earnings per share growth is over 3% p.a. – 50% vesting, over 6% – 100% vesting. TSR – if Company is ranked at median or above – 50%, upper quartile – 100%	02/04/17 – 02/04/24
Three-year Sharesave scheme granted to other employees 8 May 2014	**160,970**	177,869	Continuous service	01/07/17 – 01/01/18
Five-year Sharesave scheme granted to other employees 8 May 2014	**58,959**	70,689	Continuous service	01/07/19 – 01/01/20
Headlam Group Co-Investment Plan 2008 granted to key management 1 May 2015*	**225,874**	263,495	If the real earnings per share growth is over 3% p.a. – 50% vesting, over 6% – 100% vesting. TSR – if Company is ranked at median or above – 50%, upper quartile – 100%	02/05/18 – 02/05/25
Three-year Sharesave scheme granted to other employees 5 May 2015	**342,107**	362,651	Continuous service	01/07/18 – 01/01/19
Five-year Sharesave scheme granted to other employees 5 May 2015	**211,736**	226,113	Continuous service	01/07/20 – 01/01/21
Headlam Group Co-Investment Plan 2008 granted to key management 6 May 2016*	**162,647**	–	If the real earnings per share growth is over 3% p.a. – 50% vesting, over 6% – 100% vesting. TSR – if Company is ranked at median or above – 50%, upper quartile – 100%	07/05/19 – 07/05/26
Three-year Sharesave scheme granted to other employees 4 May 2016	**248,631**	–	Continuous service	01/07/19 – 01/01/20
Five-year Sharesave scheme granted to other employees 4 May 2016	**48,167**	–	Continuous service	01/07/21 – 01/01/22
Total share options	**1,794,868**	1,606,790		

* Further details are provided on pages 50 to 69 of the Remuneration Report.

21 Share-based payments continued

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

	Weighted average exercise price 2016	Number of options 2016	Weighted average exercise price 2015	Number of options 2015
Outstanding at the beginning of the year	**225.4**	**1,606,790**	245.4	1,418,393
Exercised during the year	**(266.7)**	**(158,532)**	(257.2)	(390,866)
Granted during the year	**231.9**	**539,281**	238.3	880,521
Lapsed during the year	**(158.9)**	**(192,671)**	(316.0)	(301,258)
Outstanding at the end of the year	**230.9**	**1,794,868**	225.4	1,606,790
Exercisable at the end of the year	**274.0**	**656**	0.0	263,495

The weighted average share price for options exercised during the year was 434.5p (2015: 468.5p).

The options outstanding at the year end have an exercise price in the range of 0.0p to 400.2p and a weighted average contractual life of 2.0 years.

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. In order to estimate the fair value of the services received the Company uses an appropriate option pricing model, either the Black–Scholes or the Monte Carlo option pricing model.

It is expected that the options will be exercised as soon as they reach maturity.

The expected volatility is based on historic volatility calculated over the weighted average remaining life of the share options.

Details of share options granted during 2016 are shown below:

2016		Three-year Co-Investment Plan 2008	Three-year Sharesave scheme	Five-year Sharesave scheme
Number of options		**226,791**	**252,330**	**60,160**
Fair value at measurement date:				
No performance conditions		**–**	**133.8p**	**118.2p**
Performance conditions	EPS 80% & TSR 20%	**418.5p**	**–**	**–**
Share price at 31 December		**487.8p**	**487.8p**	**487.8p**
Exercise price		**–**	**400.2p**	**400.2p**
Expected volatility		**43.8%**	**43.8%**	**35.1%**
Option life		**three years**	**three years**	**five years**
Dividend yield		**4.3% p.a.**	**4.3% p.a.**	**4.3% p.a.**
Risk-free rate of interest		**0.6% p.a.**	**0.6% p.a.**	**0.9% p.a.**

Notes to the Financial Statements

21 Share-based payments continued

Details of share options granted during 2015 are shown below:

2015		Three-year Co-Investment Plan 2008	Three-year Sharesave scheme	Five-year Sharesave scheme
Number of options		263,495	381,121	235,905
Fair value at measurement date:				
No performance conditions		–	136.1p	136.8p
Performance conditions	EPS 80% & TSR 20%	411.7p	–	–
Share price at 31 December		499.3p	499.3p	499.3p
Exercise price		–	340.0p	340.0p
Expected volatility		36.8% p.a.	36.8% p.a.	34.9% p.a.
Option life		three years	three years	five years
Dividend yield		4.1% p.a.	4.1% p.a.	4.1% p.a.
Risk-free rate of interest		0.8% p.a.	1.0% p.a.	1.5% p.a.

21 Share-based payments continued

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

	Group		Company		Subsidiaries	
	2016 £000	2015 £000	2016 £000	2015 £000	2016 £000	2015 £000
Share options granted in 2010 under the SAYE five-year scheme	–	5	–	–	–	5
Share options granted in 2011 under the SAYE five-year scheme	6	17	–	–	6	17
Share options granted in 2012 under the SAYE three-year scheme	–	31	–	–	–	31
Share options granted in 2012 under the SAYE five-year scheme	14	14	–	–	14	14
Headlam Group Co-Investment Plan 2008 (awarded 2012)	–	48	–	20	–	28
Share options granted in 2013 under the SAYE three-year scheme	10	28	–	–	10	28
Share options granted in 2013 under the SAYE five-year scheme	7	7	–	–	7	7
Headlam Group Co-Investment Plan 2008 (awarded 2014)	408	468	137	133	271	335
Share options granted in 2014 under the SAYE three-year scheme	76	76	1	1	75	75
Share options granted in 2014 under the SAYE five-year scheme	39	39	5	4	34	35
Headlam Group Co-Investment Plan 2008 (awarded 2015)	284	242	126	117	158	125
Share options granted in 2015 under the SAYE three-year scheme	138	91	6	4	132	87
Share options granted in 2015 under the SAYE five-year scheme	52	34	–	–	52	34
Headlam Group Co-Investment Plan 2008 (awarded 2016)	138	–	63	–	75	–
Share options granted in 2016 under the SAYE three-year scheme	59	–	–	–	59	–
Share options granted in 2016 under the SAYE five-year scheme	8	–	–	–	8	–
Total expense recognised	1,239	1,100	338	279	901	821

Notes to the Financial Statements

22 Capital and reserves

Share capital

	Ordinary shares 2016	Ordinary shares 2015
Number of shares		
On issue at 1 January and 31 December – authorised	**107,840,000**	107,840,000
On issue at 1 January and 31 December – fully paid	**85,363,743**	85,363,743

	2016 £000	2015 £000
Allotted, called up and fully paid		
Ordinary shares of 5p each	**4,268**	4,268
	4,268	4,268
Shares classified as liabilities	**–**	–
Shares classified in Shareholders' funds	**4,268**	4,268
	4,268	4,268

At 31 December 2016, the Company held 1,123,060 (2015: 1,130,592) shares which have been disclosed in the treasury reserve. Dividends are not payable on these shares and they are excluded from the calculation of earnings per share. The shares held in treasury represent 1.3% (2015: 1.3%) of the issued share capital with a nominal value of £56,153 (2015: £56,530).

In the period from 31 December 2016 to 7 March 2017 no shares have been purchased by the Company.

Ordinary shares

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

Dividends

	2016 £000	2015 £000
Interim dividend for 2015 of 6.00p paid 2 January 2016	**5,048**	–
Special dividend for 2015 of 6.00p paid 25 April 2016	**5,048**	–
Final dividend for 2015 of 14.70p paid 1 July 2016	**12,368**	–
Interim dividend for 2014 of 5.20p paid 2 January 2015	**–**	4,355
Final dividend for 2014 of 12.30p paid 1 July 2015	**–**	10,300
	22,464	14,655

Interim dividends of 6.70p per share (2015: 6.00p per share) are provided for when the dividend is paid. The dividend was paid on 3 January 2017 and totalled £5,637,000.

The final proposed dividend of 15.85p per share (2015: 14.70p per share) will not be provided for until authorised by Shareholders at the forthcoming AGM. There are no income tax consequences.

The total value of dividends proposed but not recognised at 31 December 2016 is £18,974,000 (2015: £17,416,000).

A special dividend has been declared of 8.0p per share that will be paid on 24 April 2017.

Reserves

Other reserves

Other reserves as disclosed on the Statement of Financial Position comprise the capital redemption reserve, translation reserve, cash flow hedging reserve and treasury reserve. For the Company this also includes a special reserve.

22 Capital and reserves continued

Capital redemption reserve

The capital redemption reserve represents the nominal value of shares repurchased and cancelled during 2007.

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Cash flow hedging reserve

The cash flow hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments relating to hedged transactions that have not yet occurred.

Treasury reserve

The treasury reserve comprises the cost of the Company's shares held by the Group.

Special reserve

The special reserve arose on the issuance of shares in connection with acquisitions made by the Company in earlier years.

23 Financial instruments

The main financial risks arising in the normal course of the Group's business are credit risk, liquidity risk, and market risks arising from interest rate risk and foreign currency risk. This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risks and the Group's management of capital. Further quantitative disclosures are included throughout these financial statements.

Credit risk and credit quality

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's trade receivables.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset and, as at the Statement of Financial Position date, in the Directors' opinion, there were no significant concentrations of credit risk likely to cause financial loss to the Group.

The Group has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all new customers requiring credit and these are frequently reviewed by management to limit exposure. Businesses must obtain central approval from Executive Directors or senior executive management for credit limits in excess of £10,000. The Group does not require collateral in respect of financial assets.

The credit control procedures described above, coupled with the diversified nature of the Group's trade receivables, lead the Directors to believe that there is limited credit risk exposure and that the credit quality of these assets is robust.

Other receivables comprise amounts due to the Group which historically have been received within three months of the year-end. The Directors have considered the inherent risk profile of other receivables at the year-end and are of the view that this historical experience will prevail for the foreseeable future and accordingly consider the credit quality of these assets to be robust.

Cash and cash equivalents represent deposits with reputable financial institutions in the UK and Continental Europe and hence, the Directors consider the credit quality of cash and cash equivalents to be robust.

The carrying amount of financial assets at the Statement of Financial Position date was:

	Group		Company	
	2016 £000	Restated* 2015 £000	**2016 £000**	2015 £000
Trade and other receivables (note 15)	**124,219**	116,325	**16,589**	20,159
Derivative assets (note 15)	**232**	40	**232**	–
Cash and cash equivalents (note 16)	**59,339**	63,932	**28,171**	33,001
	183,790	180,297	**44,992**	53,160

Notes to the Financial Statements

23 Financial instruments continued

The fair values of the above financial assets at both 31 December 2016 and 2015, are deemed to approximate to carrying value due to the short-term maturity of the instruments.

The maximum exposure to credit risk for trade receivables at the Statement of Financial Position date by geographic region was:

	Group		Company	
	2016 £000	Restated* 2015 £000	2016 £000	2015 £000
UK	**85,207**	79,730	**–**	–
Continental Europe	**12,382**	9,804	**–**	–
	97,589	89,534	**–**	–

* See note 1.

The ageing of trade receivables at the Statement of Financial Position date was:

	2016		2015	
Group	Gross £000	Impairment £000	Gross £000	Restated* Impairment £000
Not past due	**87,384**	**–**	80,543	(167)
Past due 0–30 days	**8,382**	**(234)**	7,764	(335)
Past due 31–120 days	**4,192**	**(2,135)**	3,815	(2,086)
	99,958	**(2,369)**	92,122	(2,588)

* See note 1.

All other receivables and derivative financial assets are not past due (2015: not past due).

The Company had trade receivables of £nil (2015: £nil).

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

	Group		Company	
	2016 £000	Restated* 2015 £000	2016 £000	2015 £000
Balance at 1 January	**2,588**	2,043	**–**	–
Amounts provided	**849**	1,572	**–**	–
Amounts utilised	**(1,205)**	(1,005)	**–**	–
Effect of movements in foreign exchange	**137**	(22)	**–**	–
Balance at 31 December	**2,369**	2,588	**–**	–

* See note 1.

Based on historic default rates, the Group believes that no general impairment allowance is necessary in respect of trade receivables, however, the Group provides fully for specific debts when required. During the year the Group's impairment loss as a percentage of revenue amounted to 0.12% (2015: 0.24%).

Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, with sufficient headroom to cope with abnormal market conditions. As at 31 December 2016 cash and cash equivalents covered the amounts of borrowings maturing in the next 12 months with a net positive liquidity of £59,115,000 (2015: £63,932,000). Details of the total facilities that the Group has access to are given in note 17.

23 Financial instruments continued

The following are the contractual maturities of financial liabilities:

31 December 2016 Group	Carrying amount £000	Contractual cash flows £000	1 year or less £000	1–2 years £000	2–5 years £000	More than 5 years £000
Non-derivative financial liabilities						
Bank overdraft	4	(4)	(4)	–	–	–
Unsecured bank loans	6,717	(7,062)	(298)	(295)	(584)	(5,885)
Trade and other payables	166,657	(166,657)	(166,657)	–	–	–
Derivative financial liabilities						
Other derivatives	30	(30)	(30)	–	–	–
	173,408	(173,753)	(166,989)	(295)	(584)	(5,885)

31 December 2015 Group	Carrying amount £000	Contractual cash flows £000	1 year or less £000	1–2 years £000	2–5 years £000	More than 5 years £000
Non-derivative financial liabilities						
Unsecured bank loans	20,000	(20,676)	(579)	(20,097)	–	–
Trade and other payables	155,568	(155,568)	(155,568)	–	–	–
Derivative financial liabilities						
Interest rate swaps used for hedging	30	(30)	(30)	–	–	–
Diesel commodity swap used for hedging	486	(486)	(424)	(62)	–	–
	176,084	(176,760)	(156,601)	(20,159)	–	–

31 December 2016 Company	Carrying amount £000	Contractual cash flows £000	1 year or less £000	1–2 years £000	2–5 years £000
Non-derivative financial liabilities					
Trade and other payables	35,971	(35,971)	(35,971)	–	–

31 December 2015 Company	Carrying amount £000	Contractual cash flows £000	1 year or less £000	1–2 years £000	2–5 years £000
Non-derivative financial liabilities					
Unsecured bank loans	20,000	(20,676)	(579)	(20,097)	–
Trade and other payables	35,523	(35,523)	(35,523)	–	–
Derivative financial liabilities					
Interest rate swaps used for hedging	30	(30)	(30)	–	–
Diesel commodity swap used for hedging	486	(486)	(424)	(62)	–
	56,039	(56,715)	(36,556)	(20,159)	–

23 Financial instruments continued

The value of the Group's and Company's financial liabilities as detailed above at 31 December 2016 and 2015 were not materially different to the carrying value. Fair values were calculated using market rates, where available. Where market values are not available, fair values have been estimated by discounting expected future cash flows using prevailing interest rate curves. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the Statement of Financial Position date.

The table below sets out the Group's accounting classification of each class of financial assets and liabilities at 31 December 2016 and 2015.

31 December 2016	Available for sale £000	Other derivatives at fair value £000	Amortised cost £000	Total carrying value £000
Cash and cash equivalents	–	–	59,343	59,343
Bank overdraft	–	–	(4)	(4)
Borrowings due within one year	–	–	(224)	(224)
Borrowings due after one year	–	–	(6,493)	(6,493)
Trade payables	–	–	(141,999)	(141,999)
Non-trade payables	–	–	(24,658)	(24,658)
Trade receivables	–	–	97,589	97,589
Other receivables	–	–	26,630	26,630
Provisions	–	–	(1,531)	(1,531)
Derivative liabilities	–	(30)	–	(30)
Derivative assets	–	232	–	232
	–	202	8,653	8,855

31 December 2015	Available for sale £000	Other derivatives at fair value £000	Restated* Amortised cost £000	Restated* Total carrying value £000
Cash and cash equivalents	–	–	63,932	63,932
Borrowings due after one year	–	–	(20,000)	(20,000)
Trade payables	–	–	(131,153)	(131,153)
Non-trade payables	–	–	(24,415)	(24,415)
Trade receivables	–	–	89,534	89,534
Other receivables	–	–	26,791	26,791
Provisions	–	–	(1,087)	(1,087)
Derivative liabilities	–	(516)	–	(516)
Derivative assets	–	40	–	40
	–	(476)	3,602	3,126

Under IAS 39, all derivative financial instruments not in a hedge relationship are measured at fair value through the income statement. The Group does not use derivatives for speculative purposes. All transactions in derivative financial instruments are undertaken to manage the risks arising from underlying business activities.

* See note 1.

23 Financial instruments continued

Interest rate risk

The Company and Group are exposed to interest rate fluctuations on their borrowings and cash deposits. Borrowings are principally held in sterling and euros at both fixed and floating rates. Deposits are in sterling, euros and Swiss francs at floating rates.

Floating rate borrowings are linked to the London Interbank Offered Rate and Euribor Over Night Index Average. The Group adopts a policy of reviewing its floating rate exposure to ensure that if interest rates rise the effect on the Group's income statement is manageable.

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

	Group Carrying amount		Company Carrying amount	
	2016 £000	2015 £000	**2016 £000**	2015 £000
Variable rate instruments				
Financial assets	**59,343**	63,932	**28,171**	33,001
Financial liabilities	**(6,721)**	(20,000)	**–**	–
	52,622	43,932	**28,171**	33,001

Sensitivity analysis

A change of 100 basis points in the interest rates at the reporting date would have increased/(decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2015.

	Group				Company			
	Profit or loss		Equity		Profit or loss		Equity	
	100bp increase £000	100bp decrease £000	100bp increase £000	100bp decrease £000	100bp increase £000	100bp decrease £000	100bp increase £000	100bp decrease £000
31 December 2016								
Variable rate instruments	**526**	**(526)**	**–**	**–**	**282**	**(282)**	**–**	**–**
31 December 2015								
Variable rate instruments	439	(439)	–	–	130	(130)	–	–

Commodity risk

The Company and Group are exposed to the commodity risk of rising fuel prices. On 1 November 2015, in order to manage this risk, the Group entered into a hedging instrument that is a two-year commodity transaction swap. The risk hedged is the diesel fuel price risk, being the change in fuel price payments on the specified diesel consumption. The notional amount is 6,768 metric tons, under which a fixed diesel price of £348.25 per metric ton is paid monthly and the floating price according to Platts European is received.

The fair value of this diesel commodity swap is included in the Statement of Financial Position as a £232,000 derivative asset (2015: £486,000 liability).

Sensitivity analysis

A change of 100 basis points in the diesel price at the reporting date would have increased/(decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables remain constant. The analysis is performed on the same basis for 2015.

23 Financial instruments continued

	Group				Company			
	Profit or loss		Equity		Profit or loss		Equity	
	100bp increase £000	100bp decrease £000	100bp increase £000	100bp decrease £000	100bp increase £000	100bp decrease £000	100bp increase £000	100bp decrease £000
31 December 2016								
Variable rate instruments	**2**	**(2)**	**–**	**–**	**2**	**(2)**	**–**	**–**
31 December 2015								
Variable rate instruments	5	(5)	–	–	5	(5)	–	–

Foreign currency risk

The Group and Company are exposed to movements in currency exchange rates arising from transaction currency cash flows and the translation of the results and net assets of overseas subsidiaries. The currencies giving rise to this risk are primarily the euro, Swiss franc and US dollar.

The Group and Company use forward exchange contracts to hedge their foreign currency transactional risk. A future foreign currency contract would be entered into where there was a known requirement for the currency due to planned imports that are not invoiced in the functional currency of the acquiring company. These forward exchange contracts would have a maturity of less than one year after the Statement of Financial Position date. The Group also enters into foreign currency contracts at spot rate where the amounts are not frequent or material. Gains and losses on currency contracts recognised as a liability at 31 December 2016 amounted to £30,000 (2015: asset of £40,000).

For the 12-month period to 31 December 2016, 2.0% (2015: 1.6%) of the Group's operating profit was derived from overseas subsidiaries and at 31 December 2016, 17.7% (2015: 17.4%) of the Group's net operating assets related to overseas subsidiary operations. Hedge accounting, following the adoption of IFRS, has not been applied to these operations.

The Group and Company do not use derivatives other than as described above.

The exposure to foreign currency risk was as follows:

	Group			Company		
2016	**Euro amount £000**	**Other amount £000**	**Total £000**	**Euro amount £000**	**Other amount £000**	**Total £000**
Trade and other receivables	**65**	**195**	**260**	**–**	**–**	**–**
Cash and cash equivalents	**420**	**597**	**1,017**	**177**	**1**	**178**
Trade and other payables	**(1,472)**	**(2,211)**	**(3,683)**	**–**	**–**	**–**
	(987)	**(1,419)**	**(2,406)**	**177**	**1**	**178**

	Group			Company		
2015	Euro amount £000	Other amount £000	Total £000	Euro amount £000	Other amount £000	Total £000
Trade and other receivables	127	163	290	4,690	109	4,799
Cash and cash equivalents	374	516	890	64	–	64
Trade and other payables	(879)	(2,322)	(3,201)	–	–	–
	(378)	(1,643)	(2,021)	4,754	109	4,863

23 Financial instruments continued

Sensitivity analysis

A 10% weakening of sterling against the following currencies at 31 December would have increased/(decreased) profit or loss by the amounts shown below; there is no equity effect. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2015.

	Group		Company	
	2016 £000	2015 £000	**2016 £000**	2015 £000
Euro	**(99)**	(38)	**18**	475
Other	**(142)**	(164)	**–**	11

A 10% strengthening of sterling against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Fair values hierarchy

The financial instruments carried at fair value are categorised according to their valuation method. The different levels have been defined below:

- 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, as prices or indirectly, derived from prices.
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Group has a diesel commodity swap used for hedging which was fair valued in accordance with level 2 for the year ended 31 December 2016 (2015: level 2) and forward currency contracts which were fair valued in accordance with level 2 (2015: level 2).

Fair values

The carrying amounts shown in the Statement of Financial Position for financial instruments are a reasonable approximation of fair value.

Trade receivables, trade payables and cash and cash equivalents

Fair values are assumed to approximate to cost due to the short-term maturity of the instrument.

Borrowings, other financial assets and other financial liabilities

Where available, market values have been used to determine fair values. Where market values are not available, fair values have been estimated by discounting expected future cash flows using prevailing interest rate curves. Amounts denominated in foreign currencies are valued at the exchange rate prevailing at the Statement of Financial Position date.

Capital management

The Group views its finance capital resources as primarily comprising share capital, bank loans and operating cash flow.

23 Financial instruments continued

The Board's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board closely monitors its Shareholder base, dividend yield and earnings per share. In the medium-term the Group aims to maintain a dividend cover of 1.6 times.

The Board encourages employees of the Group to hold the Company's ordinary shares. The Group operates a number of employee share option schemes. In previous years the Company has acquired a number of its own shares under a share buy-back programme, and some of these shares have been used for issuing shares under the Group's various share option incentive schemes.

Certain of the Company's subsidiaries are required to maintain issued share capital at levels to support capital adequacy requirements prevailing in the legislative environment in which they operate.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends made payable to Shareholders, return capital to Shareholders, issue new shares or sell assets to reduce debt.

On 14 December 2016, the Group completed a refinancing of its banking facilities. The new facilities comprise a £47.5 million sterling committed facility, a €8.6 million euro committed facility and a £25 million sterling uncommitted facility. This represents, taking into account exchange movements on existing overseas facilities, an increase in total available facilities of £5.9 million. In addition, the Group has existing facilities of £7,822,000 in Continental Europe.

The uncommitted facility, coupled with cash generated from operations, is used to fund the Group's ongoing working capital requirements. The committed facility is in place to support the Group's strategic investment plans.

No changes were made to the objectives, policies or processes during the years ended 31 December 2016 and 31 December 2015.

24 Acquisitions

There were no acquisitions made by the Group during the year ended 31 December 2016.

Prior year acquisitions

On 30 January 2015, a wholly owned Group subsidiary company acquired the business and certain assets of Matty's Wholesale Carpets Limited (Matty's).

Matty's is a distributor of residential floorcovering to independent flooring retailers, principally in the Midlands.

Cash consideration was paid of £1,977,000. Following its acquisition the business contributed revenue of £3.4 million and a profit of £0.3 million to the Consolidated Statement of Comprehensive Income for the year ended 31 December 2015. If the acquisition had occurred on 1 January 2015, Group revenue for the year ended 31 December 2015 would have been an estimated £3.6 million higher and profit after tax would have been an estimated £0.3 million higher.

24 Acquisitions continued

	Acquiree's book value £000	Fair value adjustments £000	Acquisition amounts £000
Acquiree's net assets at the acquisition date:			
Intangible assets	–	375	375
Tangible fixed assets	38	–	38
Inventories	974	–	974
Trade and other receivables	216	–	216
Trade and other payables	(1)	–	(1)
Net identifiable assets and liabilities	1,227	375	1,602
Goodwill on acquisition		375	375
Consideration paid			1,977
Satisfied by:			
Cash			1,977
Analysis of cash flows:			
On completion			1,977
Costs of acquisition			24
			2,001

Professional fees of £24,000 were incurred on the acquisition and have been expensed to the income statement within administration expenses.

The book value of receivables given in the table above represents the gross contracted amounts receivable. At the acquisition date, the entire book value of receivables was expected to be collected.

Goodwill of £375,000 arose on the acquisition of the business and certain assets of Matty's Wholesale Carpets Limited. There were also intangible assets on acquisition of £375,000 which were attributed to customer order books.

Following acquisition, it is the Group's normal practice to implement its operational and financial procedures and standard IT systems.

Furthermore, acquired businesses gain access to the Group's extensive product ranges and benefit from enhanced sales and marketing investment. These changes typically enable acquired businesses to enhance the service provided to their customers and ultimately, develop and grow.

Whilst acquired customer order books are a key component at the point of acquisition, this position quickly dissipates during the post acquisition period. The dynamic and renewable nature of this class of asset is the reason the Group elects to amortise it over a period of one to 24 months, the precise period being dependent upon the size of the acquired business.

25 Operating leases

The aggregate payments, for which there are commitments under non-cancellable operating leases as at the end of the year, fall due as follows:

	2016			2015		
Group	Land and buildings £000	Plant and machinery £000	Total £000	Land and buildings £000	Plant and machinery £000	Total £000
Less than one year	1,879	9,855	11,734	1,843	9,984	11,827
Between one and five years	3,993	15,348	19,341	3,557	16,612	20,169
More than five years	2,989	169	3,158	2,468	–	2,468
	8,861	25,372	34,233	7,868	26,596	34,464

	2016			2015		
Company	Land and buildings £000	Plant and machinery £000	Total £000	Land and buildings £000	Plant and machinery £000	Total £000
Less than one year	26	8	34	26	8	34
Between one and five years	105	3	108	105	10	115
More than five years	1,828	–	1,828	1,854	–	1,854
	1,959	11	1,970	1,985	18	2,003

The Group leases the majority of its motor and commercial vehicles on terms that range between three and five years and during the year ended 31 December 2016, total operating lease expense of £13,520,000 was recognised in the Consolidated Income Statement (2015: £11,631,000).

26 Capital commitments

Group

During the year ended 31 December 2016, the Group entered into commitments to purchase property, plant and equipment for £663,000 (2015: £728,000). These commitments are expected to be settled in the following financial year.

Company

At the year ended 31 December 2016, the Company had no commitments to purchase property, plant and equipment (2015: £nil).

27 Related parties

Group and Company

Identity of related parties

The Group has a related party relationship with its subsidiaries and with its Directors and executive officers.

Transactions with key management personnel

The Group annually re-evaluates its interpretation of key management personnel and considers that this relates to the Executive and Non-Executive Directors of the Group as identified on pages 36 and 37.

As at 31 December 2016, Directors of the Company and their immediate relatives controlled 1.3% of the voting shares of the Company (2015: 1.3%).

Non-Executive Directors receive a fee for their services to the Board.

Other than disclosed in the Remuneration Report, there were no other transactions with personnel in either the current or preceding year. The cost charged to administrative expenses relating to share plans of key personnel amounted to £304,000 (2015: £251,000).

Company only

In addition to the transactions with key personnel, the Company has the following transactions:

Transactions with other Group companies

	Highest during the year £000	Balance at 31 December 2016 £000	Highest during the year £000	Balance at 31 December 2015 £000
Amounts due from subsidiaries	**16,292**	**16,292**	19,970	19,970
Amounts due to subsidiaries	**(31,886)**	**(31,886)**	(31,315)	(31,315)

Transactions with Group companies typically comprise management, rent and interest charges during the period.

The disclosure of the year-end balance and the highest balance during the year is considered to provide a meaningful representation of transactions between the Company and its subsidiaries in the year. The highest balance is generally at the start or close of the financial year since this is the time when the Company levies its recharge of its operating expenses.

Related party transactions reported in the income statement

	For year ended 31 December 2016 £000	For year ended 31 December 2015 £000
Rental income	**7,971**	7,202
Dividends received	**31,522**	35,947
Recharge of operating expenses	**1,454**	1,192
Interest income	**163**	170

28 Subsequent events

Management has given due consideration to any events occurring in the period from the reporting date to the date these financial statements were authorised for issue and has concluded that there are no material adjusting or non-adjusting events to be disclosed in these financial statements, with the exception of the acquisition of Mitchell Carpets Limited. On 28 February 2017, a Group subsidiary company acquired 100% of the issued share capital of Mitchell Carpets Limited, a floorcovering distribution business based in Poole, Dorset, for a consideration of £1,980,000, subject to finalising the net assets position.

Group Subsidiaries

Company	Number	Type	Place of incorporation
HFD Limited	02674152	Trading	Great Britain*
MCD Group Limited	00423062	Trading	Great Britain*
NCT (International) Limited	9127711	Trading	Great Britain*
Headlam BV		Trading	Netherlands**
LMS SA		Trading	France***
Belcolor AG		Trading	Switzerland****
Headlam (European) Limited	5272085	Holding Company	Great Britain*
Headlam Holdings BV		Holding Company	Netherlands**
Headlam SAS		Holding Company	France***
Yourfloors Plc	3968487	Dormant	Great Britain*
Crossforge Limited	01290315	Dormant	Great Britain*
Gorsey Eleven Limited	2398926	Dormant	Great Britain*
Headlam Group Employee Trust Company Limited	03402470	Dormant	Great Britain*
Headlam Group Pension Trustees Limited	3666554	Dormant	Great Britain*
Mercado Group Limited	9725622	Dormant	Great Britain*

All of these subsidiaries are wholly owned and their principal activities are wholly aligned to the sales, marketing, supply and distribution of floorcovering and certain other ancillary products.

* Registered address for UK subsidiaries: PO Box 1, Gorsey Lane, Coleshill, Birmingham, B46 1LW, UK.
** Registered address for Dutch subsidiaries: Bettinkhorst 4, 7207 BP Zutphen, the Netherlands.
*** Registered address for French subsidiaries: 7/14 Rue Du Fosse Blanc, 92230, Gennevilliers, France.
**** Registered address for Swiss subsidiaries: Zücherstrasse 493, 9015 St. Gallen, Switzerland.

Financial Record

	2016 £000	Restated* 2015 £000	Restated* 2014 £000	Restated* 2013 £000	Restated** 2012 £000
Trading results					
Revenue	**693,572**	654,078	635,242	603,051	585,984
Gross profit	**212,504**	200,510	190,540	181,255	175,733
Overheads	**(171,432)**	(163,733)	(159,078)	(153,575)	(146,419)
Underlying operating profit	**41,072**	36,777	31,462	27,680	29,314
Underlying profit before net financing costs	**41,072**	36,777	31,462	27,680	29,314
Net financing costs	**(966)**	(1,153)	(1,162)	(1,241)	(1,463)
Underlying profit on ordinary activities before tax	**40,106**	35,624	30,300	26,439	27,851
Taxation	**(7,601)**	(7,213)	(6,515)	(6,146)	(6,939)
Underlying profit on ordinary activities after taxation	**30,963**	28,411	23,785	20,293	20,912
Profit before tax	**38,179**	35,624	30,300	21,087	27,851
Shareholder value					
Paid interim and final dividend per share	**20.70p**	17.50p	15.30p	14.85p	14.15p
Paid special dividend per share	**6.00p**	–	–	–	–
Proposed dividend per share	**22.55p**	20.70p	17.50p	15.30p	14.85p
Earnings per share	**36.8p**	33.8p	28.6p	18.0p	25.3p
Underlying earnings per share	**38.7p**	33.8p	28.6p	24.5p	25.3p
Net assets					
Non-current assets					
Property, plant and equipment	**102,934**	104,677	106,875	106,493	99,596
Intangible assets	**10,388**	10,388	10,013	10,013	13,210
Deferred tax assets	**1,138**	629	515	354	442
	114,460	115,694	117,403	116,860	113,248
Current assets					
Inventories	**126,037**	118,165	115,591	114,700	114,354
Trade and other receivables	**128,934**	120,300	118,962	119,634	108,216
Cash and cash equivalents	**59,343**	63,932	47,589	47,477	49,798
Assets held for sale	**–**	–	–	–	212
	314,314	302,397	282,142	281,811	272,580
Total assets	**428,774**	418,091	399,545	398,671	385,828
Current liabilities					
Bank overdraft	**(4)**	–	–	–	–
Other interest-bearing loans and borrowings	**(224)**	–	(204)	(218)	(213)
Trade and other payables	**(183,304)**	(171,375)	(165,240)	(164,856)	(153,999)
Employee benefits	**(2,169)**	(2,171)	(2,933)	(2,842)	(2,754)
Income tax payable	**(6,824)**	(6,974)	(6,073)	(7,022)	(7,117)
	(192,525)	(180,520)	(174,450)	(174,938)	(164,083)
Non-current liabilities					
Other interest-bearing loans and borrowings	**(6,493)**	(20,000)	(22,818)	(33,239)	(33,371)
Provisions	**(1,531)**	(1,087)	(787)	(790)	(907)
Deferred tax liabilities	**(4,077)**	(4,533)	(3,931)	(2,742)	(2,818)
Employee benefits	**(20,781)**	(16,843)	(18,803)	(12,780)	(14,641)
	(32,882)	(42,463)	(46,339)	(49,551)	(51,737)
Total liabilities	**(225,407)**	(222,983)	(220,789)	(224,489)	(215,820)
Net assets	**203,367**	195,108	178,756	174,182	170,008

*See note 1.

** Restated to reflect the changes for revised IAS 19 and see note 1.

Annual General Meeting 2017

Chairman's letter and Notice of Annual General Meeting

7 March 2017

Dear Shareholder

I am pleased to invite you to the 69th Annual General Meeting ('AGM') of Headlam Group plc (the 'Company') which is to be held at the Group's distribution facility located at Gorsey Lane, Coleshill, Birmingham, B46 1JU at 10.00 am on Thursday 25 May 2017. The AGM is an important event providing the Directors with an opportunity to present the Company's performance to Shareholders and to respond to your questions.

The formal notice of AGM stating the business to be considered at the meeting, explanatory notes to the proposed resolutions and information for Shareholders are set out below. The annual report and accounts are also available from our website at www.headlam.com/investor-relations.

Voting at the meeting

At the meeting, voting on each resolution will normally be conducted by way of a show of hands, where each person attending has one vote, unless a poll is demanded in accordance with the Company's articles. A poll allows all Shareholders, present in person, by proxy or unable to attend, to vote on all resolutions in proportion to their shareholding. The Company will release the results of voting, including proxy votes on each resolution, on its website on the next business day and announce them through a Regulatory Information Service.

Voting by proxy

If you are unable to attend the AGM, you can appoint a proxy to exercise all or any of your rights to attend, vote and speak at the AGM. You may register your appointment of a proxy by returning the enclosed Proxy Form. CREST members should use the CREST electronic proxy appointment service. Further details on how to appoint a proxy and submit your voting instructions are set out below.

Recommendations

The Board considers that the resolutions to be put to the AGM will promote the success of, and are in the best interests of, the Company and its Shareholders as a whole.

Regarding the election and re-election of Directors, following formal evaluation, the Board is of the opinion that the two Directors continue to make an effective and valuable contribution and demonstrate commitment to their role. The Board is satisfied that Andrew Eastgate, the Non-Executive Director being proposed for re-election, remains independent in character and judgement and that there are no relationships or circumstances likely to affect his character or judgement. It unanimously recommends the respective election and re-election of the Directors standing for election and re-election.

The Directors unanimously recommend that you vote in favour of all the proposed resolutions as they intend to do in respect of their own beneficial holdings.

On behalf of the Board, I look forward to seeing many of you at our meeting and thank you for your continued support.

Yours faithfully

Dick Peters
Chairman

Note – If you have sold or otherwise transferred all of your shares in Headlam Group plc, please send the report and accounts, and the accompanying form of proxy, at once to the purchaser or transferee or to the stockbroker, bank or other agent through whom the sale or transfer was effected, for delivery to the purchaser or transferee.

Notice of Annual General Meeting

Notice is hereby given that the 69th Annual General Meeting of Headlam Group plc will be held at the Group's distribution facility located at Gorsey Lane, Coleshill, Birmingham, B46 1JU on Thursday 25 May 2017 at 10.00 am for the following purposes.

To propose the following as ordinary resolutions

1. To receive, consider and adopt the Annual Report and Accounts, the reports of the Directors and the Independent Auditor's Report for the year ended 31 December 2016.
2. To declare a final ordinary dividend for the year ended 31 December 2016 of 15.85p per ordinary share.
3. To elect as a Director Tony Judge who is to be appointed with effect from 31 March 2017 and who will retire in accordance with the Company's Articles of Association.
4. To re-elect as a Director Andrew Eastgate who is retiring by rotation in accordance with the Company's Articles of Association.
5. To reappoint PricewaterhouseCoopers LLP as the independent Auditor of the Company from the conclusion of the meeting until the conclusion of the next general meeting at which accounts are laid before the Shareholders.
6. To authorise the Directors to determine the independent Auditor's remuneration.
7. To approve the Directors' Remuneration Report for the year ended 31 December 2016.
8. To approve the Directors' Remuneration Policy, the full text of which is contained in the Directors' Remuneration Report for the year ended 31 December 2016.
9. That, with effect from the passing of the resolution, Article 115 of the Articles of Association of the Company be amended such that the maximum aggregate sum of ordinary remuneration payable to Non-Executive Directors in respect of any year be increased by £150,000 to £350,000.

10. Authority to allot shares

(a.) That the Directors be generally and unconditionally authorised pursuant to section 551 of the Companies Act 2006 (the 'Act') to allot shares in the Company, and to grant rights to subscribe for or to convert any security into shares in the Company, up to an aggregate nominal amount of £620,000 for a period expiring (unless previously renewed, varied or revoked by the Company in general meeting) at the end of the 2018 AGM (or, if earlier, at the close of business on 30 June 2018), and save that the Company may before such expiry make an offer or agreement which would or might require shares to be allotted, or rights to subscribe for or convert any security into shares to be granted, after expiry of this authority and the Directors may allot shares and grant rights in pursuance of any such offer or agreement as if this authority had not expired;

(b.) that, subject to paragraph (c), all existing authorities given to the Directors pursuant to section 551 of the Act be revoked by this resolution; and

(c.) that paragraph (b) shall be without prejudice to the continuing authority of the Directors to allot shares or grant rights to subscribe for or convert any security into shares pursuant to an offer or agreement made by the Company before the expiry of the authority pursuant to which such offer or agreement was made.

11. The Headlam 2017 Performance Share Plan

That:

(a.) the rules of the Headlam 2017 Performance Share Plan, in the form produced to the meeting and initialled by the Chairman of the meeting for the purposes of identification (the 'PSP'), the principal terms of which are summarised in the explanatory notes to resolutions 11 and 12 in this Notice of Annual General Meeting, be and are hereby approved and the Directors be and are hereby authorised to adopt the PSP and to do all acts and things that they consider necessary or expedient to give effect to the PSP; and

(b.) the Directors be and are hereby authorised to adopt further schemes based on the PSP but modified to take account of local tax, exchange control or securities laws in overseas territories, provided that any shares made available under such further schemes are treated as counting against any limits on individual or overall participation in the PSP.

Notice of Annual General Meeting

12. The Headlam 2017 Deferred Bonus Plan

That:

(a.) the rules of the Headlam 2017 Deferred Bonus Plan, in the form produced to the meeting and initialled by the Chairman of the meeting for the purposes of identification (the 'DBP'), the principal terms of which are summarised in the explanatory notes to resolutions 11 and 12 in this Notice of Annual General Meeting, be and are hereby approved and the Directors be and are hereby authorised to adopt the DBP and to do all acts and things that they consider necessary or expedient to give effect to the DBP; and

(b.) the Directors be and are hereby authorised to adopt further schemes based on the DBP but modified to take account of local tax, exchange control or securities laws in overseas territories, provided that any shares made available under such further schemes are treated as counting against any limits on individual or overall participation in the DBP.

To propose the following as special resolutions:
13. Disapplication of pre-emption rights

That, subject to the passing of resolution 10 in this Notice and in place of all existing powers to allot securities given to the Directors, the Directors be generally empowered pursuant to section 570 and section 573 of the Act to allot equity securities (as defined in section 560 of the Act) for cash, pursuant to the authority conferred by resolution 10 in this Notice, as if section 561 of the Act did not apply to the allotment.

This power:

(a.) expires (unless previously renewed, varied or revoked by the Company in general meeting) at the end of the 2018 AGM if passed (or, if earlier, at the close of business on 30 June 2018), save that the Company may, before such expiry, make an offer or agreement which would or might require equity securities to be allotted after such expiry and the Directors may allot equity securities in pursuance of any such offer or agreement as if this power had not expired; and

(b.) shall be limited to:

(i.) the allotment of equity securities in connection with an issue to holders of ordinary shares of 5p in the capital of the Company in proportion (as nearly as may be practicable) to their existing holdings and to people who hold other equity securities, if this is required by the rights of those securities or, if the Directors consider it necessary, as permitted by the rights of those securities and so that the Directors may impose any limits or restrictions and make any arrangements which they consider necessary or appropriate to deal with treasury shares, fractional entitlements, record dates, legal, regulatory or practical problems in, or under the laws of, any territory or any other matter; and

(ii.) the allotment of equity securities for cash otherwise than pursuant to paragraph 13(b)(i) up to an aggregate nominal amount of £213,000.

This power applies in relation to a sale of shares which is an allotment of equity securities by virtue of section 560(3) of the Act as if, in the first paragraph of this resolution, the words 'pursuant to the authority conferred by resolution 10 in this Notice' were omitted.

14. Authority to purchase own shares

That the Company be and is hereby generally and unconditionally authorised for the purposes of section 701 of the Act to make market purchases (within the meaning of section 693(4) of the Act) of ordinary shares in the capital of the Company, subject to the following conditions:

(a.) the maximum number of ordinary shares which may be purchased is 8,536,000;

(b.) the minimum price (exclusive of expenses) which may be paid for an ordinary share is 5p;

(c.) the maximum price (exclusive of expenses) which may be paid for each ordinary share is the higher of:

  (i.) an amount equal to 105% of the average of the middle market quotations of an ordinary share of the Company as derived from the London Stock Exchange Daily Official List for the five business days immediately preceding the day on which the share is contracted to be purchased; and (ii) an amount equal to the higher of the price of the last independent trade of an ordinary share and the highest current independent bid for an ordinary share as derived from the London Stock Exchange Trading System; and

(d.) the authority conferred by this resolution shall expire at the conclusion of the 2018 AGM or, if earlier, at the close of business on 30 June 2018 (except in relation to the purchase of shares, the contract for which was made before the expiry of this authority and which might be concluded wholly or partly after such expiry).

15. Notice period for general meetings

That the Company be and is hereby generally and unconditionally authorised to hold general meetings (other than annual general meetings) on 14 days' clear notice from the date of the passing of this resolution, provided that the authority shall expire at the conclusion of the AGM of the Company to be held in 2018 or 30 June 2018, whichever is the earlier.

By order of the Board

Geoff Duggan
Company Secretary
7 March 2017

Headlam Group plc
Registered No. 460129, England
Registered office:
PO Box 1
Gorsey Lane, Coleshill
Birmingham, B46 1LW

Explanatory Notes to the Proposed Resolutions

This year's AGM will be held at the Group's distribution facility at Gorsey Lane, Coleshill, Birmingham B46 1JU on Thursday 25 May 2017 at 10.00 am.

A description of the resolutions that will be proposed at the meeting is set out below.

Resolutions 1 to 12 inclusive are proposed as ordinary resolutions which means that for each of these resolutions to be passed, more than half the votes cast must be cast in favour of the resolution. Resolutions 13 to 15 inclusive are proposed as special resolutions, which means that for each of those resolutions to be passed, at least three-quarters of the votes cast must be cast in favour of the resolution.

Resolution 1 – Annual Report and Accounts

The Company is required by law to present to Shareholders at the AGM its audited accounts and the Directors' and Independent Auditor's Reports for the financial year ended 31 December 2016. Shareholders are invited to vote to receive and adopt the Annual Report and Accounts for the year ended 31 December 2016.

Resolution 2 – Declaration of ordinary dividend

The Directors recommend the payment of a final ordinary dividend of 15.85p on each of the ordinary shares entitled thereto, which, together with the interim ordinary dividend of 6.70p, gives a total ordinary dividend of 22.55p for the year ended 31 December 2016. Subject to approval of the declaration of the final ordinary dividend at the AGM, the final ordinary dividend will be paid on 3 July 2017 to the holders of ordinary shares whose names are recorded on the register of members at the close of business on 2 June 2017.

Resolution 3 – Election of Tony Judge as a Director

Tony Judge is to be appointed to the Board with effect from 31 March 2017. In accordance with the Company's Articles of Association, he offers himself for election at the forthcoming AGM. Tony is the Company's Chief Operating Officer, prior to which he was a member of the senior executive management, having operational responsibility for businesses trading from distribution facilities located in Coleshill, Tamworth, Thatcham, Gildersome and Stockport. The Board believes that Tony Judge should be elected and makes such a recommendation to Shareholders.

Resolution 4 – Re-election of Andrew Eastgate as a Director

Andrew Eastgate is retiring by rotation in accordance with the Company's Articles and is offering himself for re-election by Shareholders. Under the Articles, Directors are required to retire every three years. Andrew was appointed a Non-Executive Director in May 2010 at which time he joined the Nomination, Audit and Remuneration Committees, becoming Chairman of the Audit Committee on 1 September 2013. With effect from 1 June 2015, Andrew stepped down as Chairman of the Audit Committee, at which time he was appointed Chairman of the Remuneration and Nomination Committees and Senior Independent Director.

In accordance with the recommendations of the UK Corporate Governance Code in respect of Non–Executive Directors, the Board believes that Andrew Eastgate continues to make an effective contribution to the business and to demonstrate commitment to the role and that he should be re-elected and makes such a recommendation to Shareholders.

Resolution 5 – To re-appoint PricewaterhouseCoopers LLP as the Company's Auditor

The Company is required to appoint or re-appoint an Auditor at each general meeting at which accounts are laid before the Company, to hold office until the end of the next such meeting. This resolution proposes the re-appointment of an Auditor. PricewaterhouseCoopers LLP has advised its willingness to stand for re-appointment as Auditor of the Company.

Resolution 6 – Agreement of Auditor remuneration

In addition to the Company's requirement to appoint an Auditor, Shareholder authority is sought for the Directors to determine the remuneration to be paid to the Auditor for the period of appointment.

Resolution 7 – Directors' Remuneration Report

Shareholders are being asked to approve the 2016 Directors' Remuneration Report (excluding the Directors' remuneration policy, which is the subject of resolution 8), which gives details of the Directors' remuneration for the period ended 31 December 2016 and is set out on pages 62 to 69 of the Company's Annual Report and Accounts. Whilst the payment of remuneration to the Directors is not dependent on the passing of the resolution, the Board will take the vote into account when considering the future development and operation of the Company's remuneration policy and practice. As required by the Directors' Remuneration Report Regulations 2002, PricewaterhouseCoopers LLP has audited those parts of the Directors' Remuneration Report capable of being audited and their report can be found on pages 80 to 85 of the Annual Report and Accounts.

Resolution 8 – Directors' Remuneration Policy

The Company's current Directors' Remuneration Policy was approved by Shareholders at the 2014 AGM. The Company is required to seek Shareholder approval for a new policy at the 2017 AGM and this is set out on pages 52 to 62 of the Company's Annual Report and Accounts. Subject to approval, the policy will take effect from the close of the meeting.

Resolution 9 – Directors' fees

Article 115 of the Articles of Association of the Company prescribes the maximum amount in fees payable in aggregate to Non-Executive Directors each year. Current fees for Non-Executive Directors are approaching this figure and the Board believes that it is prudent to raise the authority thereunder to allow the Board, should it deem it appropriate, to appoint an additional Non-Executive Director and/or increase Non-Executive fees beyond that level. It is therefore proposed to increase the maximum amount from £200,000 to £350,000.

Resolution 10 – Authority to allot shares

Shareholders are being asked to pass the necessary resolution to grant to the Directors a general authority, for the purpose of section 551 of the Companies Act 2006, to allot relevant securities. With due regard to the Investment Association's guidelines and to comments received from Shareholders, the proposed general authority, similar to last year, is to allot up to an aggregate nominal amount of £620,000 representing 12,400,000 ordinary shares (15% of the Company's ordinary share capital (excluding treasury shares) in issue at 7 March 2017). As at 7 March 2017, the Company held 743,032 treasury shares, which represented approximately 0.9% of the Company's issued share capital (excluding treasury shares), which the Company can cancel or hold for sale or use to meet the obligations under the Company's employee share schemes.

This authority will lapse at the conclusion of the AGM to be held in 2018, or, if earlier, on 30 June 2018. The Directors consider that this authority is desirable to allow the Company to retain flexibility, although they have no current intention of exercising this authority.

Resolutions 11 and 12 – the Headlam 2017 Performance Share Plan and the Headlam 2017 Deferred Bonus Plan

Resolutions 11 and 12 relate to the proposal to adopt two new employee share plans. The reasons for the proposal of these plans are described in the Directors' Remuneration Report for the year ended 31 December 2016 set out on pages 50 to 51 of the Company's Annual Report and Accounts.

Summaries of the principal terms of the plans are set out below. Certain provisions which apply to both plans are set out after the plan specific summaries.

The Headlam 2017 Performance Share Plan (the 'PSP')

The PSP is a discretionary share plan which will be administered by the Board or a Committee appointed by the Board. Decisions in relation to the participation in the PSP by Executive Directors of the Company will be taken by the Remuneration Committee, and references in this summary to the Board should be read accordingly.

Eligibility

Any employee (including an Executive Director) of the Company or any of its subsidiaries will be eligible to participate in the PSP at the discretion of the Board.

Form of Awards

An Award under the PSP may be in the form of:

(a.) a conditional right to acquire ordinary shares in the Company ('Shares') at no cost (a 'Conditional Award');

(b.) an option to acquire Shares at no cost or for a nominal exercise price (an 'Option'); or

(c.) a right to a cash amount related to the value of a number of Shares (a 'Cash Award').

In this summary, Conditional Awards, Options and Cash Awards are together referred to as 'Awards'. References to Shares include notional Shares to which a Cash Award relates. Before Shares have been delivered, the Board may decide to pay a cash amount equal to the value of the Shares the participant would otherwise have received.

Explanatory Notes to the Proposed Resolutions

Performance conditions

Unless the Board determines otherwise, Awards will be subject to the satisfaction of a performance condition which will determine the proportion (if any) of the Award which will vest at the end of a performance period. A performance period will usually be three years long.

Awards granted to Executive Directors of the Company will ordinarily be subject to performance conditions. However, awards granted to facilitate the recruitment of an Executive Director may be granted without a performance condition.

A performance condition may be amended or substituted if an event occurs which causes the Board to consider that an amendment/substitution would be appropriate. Any amended or substituted performance condition would not be materially less difficult to satisfy.

Individual limits

Ordinarily, a participant shall not be granted an Award in respect of any financial year of the Company over Shares with a market value (as determined by the Board) in excess of 100% of his annual base salary. In exceptional circumstances, this limit may be increased to 200% of salary.

Vesting and exercise

Awards subject to a performance condition will normally vest as soon as practicable after the end of the performance period to the extent that the performance condition has been satisfied. Awards not subject to a performance condition will usually vest on the third anniversary of the grant date (or on such other date or dates as the Board determines).

Awards may be subject to a 'Holding Period' of up to two years following vesting and will ordinarily be released (so that the participant is entitled to acquire the Shares) following the Holding Period. Awards not subject to a Holding Period will ordinarily be released at vesting.

Options will normally be exercisable from the date of release until the tenth anniversary of the grant date.

The Headlam 2017 Deferred Bonus Plan (the 'DBP')

The DBP is a discretionary share plan which will be administered by the Board or a Committee appointed by the Board. Decisions in relation to the participation in the DBP by Executive Directors of the Company will be taken by the Remuneration Committee, and references in this summary to the Board should be read accordingly.

Eligibility

Any employee (including an Executive Director) or former employee of the Company or any of its subsidiaries will be eligible to participate in the DBP at the discretion of the Board. Awards under the DBP will only be granted to an eligible employee who is to receive some or all of his bonus as an award under the DBP.

Form of Awards

Awards under the DBP can be granted in the same form as awards under the Headlam 2017 PSP.

Individual limits

Awards will be granted over Shares with a market value (as determined by the Board) equal to the amount of the bonus to be delivered in the form of an Award.

Vesting and exercise

Awards will usually vest and be released (so that the participant is entitled to acquire the Shares) on the second anniversary of the date on which the bonus in respect of which the Award was granted is determined.

Options will normally be exercisable from the date of release until the tenth anniversary of the grant date.

Provisions which are common to the PSP and DBP

Grant of Awards

Awards may be granted within the six-week period following the Company's 2017 Annual General Meeting. Thereafter, ordinarily Awards may only be granted within the six-week period following announcement of the Company's results for any period or, in the case of the DBP, the period of six weeks following the determination of the bonus in respect of which the Award is granted. However, the Board may grant Awards at other times in exceptional circumstances. If Awards cannot be granted in any of these periods due to regulatory restrictions, they may be granted within the period of six weeks following the lifting of the restriction.

Overall limits

Awards may be granted over newly issued Shares, treasury Shares or Shares purchased in the market. In any 10 year period:

- the number of Shares which may be issued under the PSP and DBP and under any other discretionary employees' share plan adopted by the Company may not exceed 5% of the issued ordinary share capital of the Company from time to time; and
- the number of Shares which may be issued under the PSP and DBP and under any other employees' share plan adopted by the Company may not exceed 10% of the issued ordinary share capital of the Company from time to time.

Treasury Shares will be treated as newly issued for the purpose of these limits until such time as guidelines published by institutional investor representative bodies determine otherwise.

Dividends

On the release of an Award (or on the exercise of an Award granted in the form of an Option), the Company may provide cash or additional Shares to a participant based on the value of dividends paid on vested Shares over the deferral period (in the case of the DBP) and the period from the start of the Holding Period until the date of release (in the case of the PSP). The Board shall determine the basis on which this amount is calculated, which may assume the reinvestment of the dividends into Shares.

Cessation of employment

Unvested Awards

If a participant ceases employment by reason of death, ill-health, injury, disability or for any other reason at the Board's discretion (a 'Good Leaver'), any unvested Award he holds will usually continue and be released at the normal release date. The Board will have discretion to release the Award at cessation or at some other time (such as following the end of the performance period in the case of an Award under the PSP which would otherwise be subject to a Holding Period).

The extent to which a PSP Award held by a Good Leaver is released will be determined by reference to the extent to which any performance condition has been satisfied (as determined by the Board in the event of release before the end of the performance period).

Unless the Board determines otherwise, the extent to which a PSP Award or DBP Award is released will be reduced to take account of the proportion of the performance period that has elapsed at the date of cessation (in the case of a PSP Award subject to a performance condition) or the proportion of the period from grant to the originally anticipated vesting date that has elapsed at the date of cessation (in the case of a PSP Award not subject to a performance condition, or a DBP Award).

Vested but unreleased PSP Awards

If a PSP Award is granted subject to a Holding Period and the participant ceases employment during the Holding Period, the Award will be released, to the extent vested, at the normal release date unless the participant is summarily dismissed (in which case the Award will lapse). The Board will have discretion to release the Award at the date of cessation.

Exercise period for Options

If a participant ceases employment while holding an Award in the form of an Option, that Option (unless it lapses on cessation) may be exercised for a period of six months (12 months in the event of death) beginning with the date of cessation (if it had already been released) or the date of release (if it had not already been released). The Board may permit the exercise of an Option in a longer period.

Explanatory Notes to the Proposed Resolutions

Corporate events

In the event of a change of control of the Company, unvested Awards will vest and be released (and vested but unreleased PSP Awards will be released) as soon as practicable.

Unvested PSP Awards will vest taking into account the extent to which any performance condition has been satisfied at the date of change of control (as determined by the Board) and, unless the Board determines otherwise, taking into account the proportion of the performance period (or vesting period in the case of a PSP Award that is not subject to a performance condition) that has elapsed.

If other events occur such as a winding-up of the Company, demerger, delisting, special dividend or other event which, in the opinion of the Board, may affect the current or future value of Shares, the Board may determine that Awards will vest conditional on the event occurring. Vesting of PSP Awards will be subject to the satisfaction of the performance condition (as determined by the Board) and, unless the Board determines otherwise, the proportion of the performance period (or vesting period in the case of a PSP Award not subject to a performance condition) that has elapsed.

Malus and clawback

The malus and clawback provisions referred to below may be applied:

- for up to two years following the payment of a cash bonus in respect of which a DBP Award is granted; and
- at any time up to the end of the Holding Period relating to a PSP Award (or the second anniversary of the vesting date in the case of a PSP Award which is not subject to a Holding Period).

If the malus and clawback provisions are to be applied, the Board may cancel the relevant Award or impose further conditions on it (if Shares have not been delivered in respect of it) or may require the participant to make a payment to the Company in respect of some or all of the Shares acquired.

The malus and clawback provisions may be applied if: (1) the participant's gross negligence, fraud, dishonesty or other misconduct has caused or contributed to the Company having to restate its financial statements; (2) the participant's conduct is such that it entitles or would have entitled his employer to terminate his employment summarily; (3) a material error has occurred in determining whether any performance conditions relating to the Award (or the bonus in respect of which the DBP Award was granted) have been met (or any other material error having occurred in calculating the amount of the Award or bonus); or (4) other exceptional circumstances arise which in the Board's opinion justify the application of the malus and clawback provisions.

Adjustment of Awards

In the event of a variation of the Company's share capital or a demerger, delisting, special dividend, rights issue or other event, which may, in the Board's opinion, affect the current or future value of Shares, the number of Shares subject to an Award, any exercise price and/or any performance condition attached to Awards, may be adjusted.

Amending the plans, termination of the plans and further terms of Awards

The Board may amend the PSP or the DBP at any time, provided that the approval of the Company's Shareholders in a general meeting will be required for any amendments to the advantage of participants relating to eligibility, limits, the basis for determining a participant's entitlement to, and the terms of, the Shares or cash comprised in an Award and the impact of any variation of capital to become effective.

However, any minor amendment to benefit administration, to take into account legislative changes, or to obtain or maintain favourable tax treatment, exchange control or regulatory treatment may be made by the Board without Shareholder approval.

The PSP and DBP will usually terminate on the tenth anniversary of their approval by Shareholders but the rights of existing participants will not be affected by any termination.

Awards are not transferable (other than on death). No payment will be required for the grant of an Award. Awards will not form part of pensionable earnings.

Resolution 13 – Disapplication of pre-emption rights (SPECIAL RESOLUTION)

Shareholders are being asked to pass a resolution to empower the Directors to allot equity securities, or sell treasury shares, for cash as if section 561 of the Companies Act 2006 (which gives Shareholders certain pre-emption rights on the issue of shares or rights to subscribe for or convert securities into shares) did not apply to any such allotment. The resolution allows the issue or sale of shares of up to an aggregate nominal amount of £620,000 representing 12,400,000 ordinary shares in respect of rights issues and other issues pro rata to existing entitlements, and also allows issues or sales for cash (other than in relation to a rights issue or other pre-emptive issue) limited to shares up to an aggregate nominal amount of £213,000 (5% of the Company's ordinary share capital in issue at 7 March 2017). The authority will lapse at the conclusion of the AGM to be held in 2018 or, if earlier, on 30 June 2018.

The Directors confirm that they have no present intention of exercising this authority.

In accordance with the Pre-Emption Group's Statement of Principles available at www.pre-emptiongroup.org.uk, the Directors also confirm their intention that no more than 7.5% of the issued share capital of the Company (excluding treasury shares) will be issued for cash on a non-pre-emptive basis during any rolling three-year period.

Resolution 14 – Purchase of own shares (SPECIAL RESOLUTION)

The Directors believe that it is in the interests of the Company and its members to continue to have the flexibility to purchase its own shares and this resolution seeks authority from members to do so. The Directors intend only to exercise this authority where, after considering market conditions prevailing at the time, they believe that the effect of such exercise would be to increase the earnings per share and be in the best interests of Shareholders generally. The effect of such purchases would either be to cancel the number of shares in issue or the Directors may elect to hold them in treasury pursuant to the Companies Act 2006. That Act enable companies to hold shares in treasury, as an alternative to cancelling them, following a purchase of own shares.

Shares held in treasury may subsequently be cancelled, sold for cash or used to satisfy share options and share awards under a Company's employee share scheme. Once held in treasury, a Company is not entitled to exercise any rights, including the right to attend and vote at meetings in respect of the shares. Further, no dividend or other distribution of the Company's assets may be made to the Company in respect of the treasury shares.

This resolution renews the authority given at the AGM held in 2016. The authority is in respect of 10% of the Company's issued ordinary share capital as at 7 March 2017 and will lapse at the conclusion of the AGM to be held in 2018 or, if earlier, on 30 June 2018. The resolution specifies the maximum and minimum prices at which the shares may be bought. If the Company buys any of its shares under the authority proposed by resolution 14, the Board will decide at the time whether to cancel them immediately or hold them in treasury.

The purchase of shares will be dependent on market conditions and will also take into account the cash generated in the business and other investment opportunities that may arise over time.

During the year the Company made no purchases of its own shares.

Details of share options outstanding and treasury share movements including details of own shares acquired by the Company are shown respectively in notes 21 and 22 to the financial statements.

Resolution 15 – Notice period for general meetings (SPECIAL RESOLUTION)

This will be proposed as a special resolution to approve the holding of general meetings, other than AGMs, on 14 clear days' notice. Although the Company's Articles currently permit this, the Companies Act 2006 now requires a Shareholder resolution to be passed to authorise general meetings to be held on 14 days' notice. Without the passing of resolution 15, the minimum notice period under the Act would be 21 days. If resolution 15 is passed by Shareholders, the Act would only allow the Company to call a general meeting on 14 days' notice if it were to make a system of electronic voting available to its Shareholders in respect of the meeting in question. The Directors consider it to be in the best interest of Shareholders to pass resolution 15, which is a repeat of the same resolution passed at the AGM in 2016, in order to prevent being constrained by the Act. It will be necessary for a similar resolution to be put to Shareholders at each subsequent AGM. It is intended that this flexibility will only be used for non-routine business and where merited in the interests of Shareholders as a whole.

Explanatory Notes to the Notice of Meeting

Notes 1 to 17 below give further explanation as to the proxy, voting and attendance procedures at the AGM.

1. Entitlement to appoint proxies

A member entitled to attend and vote at the meeting is also entitled to appoint a proxy or proxies to attend, speak and vote instead of him.

A member may appoint more than one proxy in relation to the meeting, provided that each proxy is appointed to exercise the rights attached to a different share or shares held by that member. A proxy need not be a member of the Company.

Appointment of a proxy will not preclude a member from attending and voting in person at the meeting. To appoint more than one proxy, a member must complete a photocopy of the enclosed proxy card or obtain additional forms from our registrars, Capita Asset Services, telephone 0871 664 0300 (calls cost 12p per minute plus your phone Company's access charge). Calls outside the United Kingdom will be charged at the applicable international rate. Capita are open between 09:00 – 17:30, Monday to Friday excluding public holidays in England and Wales). Please also indicate by ticking the relevant box if the proxy appointment is one of multiple appointments being made.

Multiple proxy appointments should be returned together in the same envelope. Enter in the box provided the number of shares in relation to which your proxy is authorised or leave the box blank to authorise your proxy to act in relation to your full voting entitlement.

2. Appointing proxies

To be effective, the instrument appointing a proxy and any power of attorney or other authority under which it is executed (or a notarially certified copy of such power or authority) must reach Capita Asset Services, Proxies Department, The Registry, 34 Beckenham Road, Beckenham, Kent, BR3 4TU not less than 48 hours before the time for holding the meeting. A form of proxy is enclosed with this Notice.

3. Electronic proxy appointment through CREST

CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so by using the procedures described in the CREST manual (available via www.euroclear.com). CREST personal members or other CREST sponsored members, and those CREST members who have appointed a voting service provider(s), should refer to their CREST sponsor or voting service provider(s) who will be able to take the appropriate action on their behalf.

In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a 'CREST Proxy Instruction') must be properly authenticated in accordance with Euroclear UK & Ireland Limited's ('Euroclear UK & Ireland') specifications and must contain the information required for such instructions, as described in the CREST manual. The message, regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy must, in order to be valid, be transmitted so as to be received by the issuer's agent (ID RA10) by the latest time for the receipt of proxy appointments specified in note 2 above. For this purpose, the time of receipt will be taken to be the time (as determined by the timestamp applied to the message by CREST application host) from which the issuer's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.

CREST members and, where applicable, their CREST sponsors or voting service providers should note that Euroclear UK and Ireland does not make available special procedures in CREST for any particular message. Normal system timing and limitations will, therefore, apply in relation to the input of CREST proxy instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST personal member, or sponsored member, or has appointed a voting service provider, to procure that his CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting service providers are referred, in particular, to those sections of the CREST manual concerning practical limitations of the CREST systems and timing.

The Company may treat as invalid a CREST proxy instruction in the circumstances set out in Regulation 35(5)(a) of the Uncertificated Securities Regulations 2001.

4. Joint holders
In the case of joint holders of a share the vote of the senior who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders. For this purpose seniority is determined by the order in which the names of the holders stand in the register of members in respect of the joint holding.

5. Entitlement to attend and vote
Pursuant to Regulation 41 of the Uncertificated Securities Regulations 2001, the time by which a person must be entered on the register of members in order to have the right to attend and vote at the AGM is close of business on 23 May 2017 or, if the meeting is adjourned, close of business on the date two days before the date for the adjourned meeting. Changes to entries on the register of members after that time will be disregarded in determining the right of any person to attend or vote at the meeting.

6. Corporate representatives
Corporations may appoint one or more corporate representatives who, on its behalf, may exercise all of its powers as a member, provided that no more than one corporate representative exercises powers over the same share.

7. Nominated person
If you are a person who has been nominated under section 146 of the Companies Act 2006 to enjoy nomination rights (a 'Nominated Person') you may, under an agreement between you and the member of the Company who has nominated you, have a right to be appointed (or have someone else appointed) as a proxy for the meeting. If you do not have such a proxy appointment right, or you do but do not wish to exercise it, you may have a right to give instructions to the member who has appointed you as to the exercise of voting rights. If you are a Nominated Person, the statement of the rights of members in relation to the appointment of proxies above does not apply. Such rights can only be exercised by a registered member of the Company.

8. Issued share capital/voting rights
As at 7 March 2017, being the latest practicable date prior to the publication of this document, the Company's issued share capital, including treasury shares, consisted of 85,363,743 ordinary shares of 5p ('shares'). Of these, 743,032 shares were held in treasury, the voting rights and entitlement to dividend of which were automatically suspended. Accordingly, the total number of voting rights in the Company as at that date was 84,620,711.

9. Right to ask questions
A Shareholder attending the meeting has the right to ask questions relating to the business being dealt with at the meeting in accordance with section 319A of the Act. In certain circumstances prescribed by section 319A of the Act, the Company need not answer a question.

10. Shareholder requests under section 527 of the Act
Under section 527 of the Companies Act 2006, members of the Company representing at least 5% of the total voting rights of the Company, or at least 100 members who have a right to vote and hold shares in the Company on which there has been paid up an average sum per member of at least £100, may require the Company to publish on its website a statement setting out any matter relating to the audit of the Company's accounts.

Where the Company is required to publish such a statement on its website, it may not require the members making the request to pay its expenses in complying with the request. The Company must forward the statement to the Company's Auditor not later than the time when it makes the statement available on its website. The business of the meeting includes any such statement that the Company has been required to publish on its website.

11. Non-Shareholder attendance
Persons who are not Shareholders in the Company will not be admitted to the meeting unless prior arrangements are made with the Company.

Explanatory Notes to the Notice of Meeting

12. Access arrangements

Should any Shareholder with special needs wish to attend the meeting, please contact the Company so that appropriate arrangements can be made.

13. Communicating with the Company in relation to the AGM

Except as provided above, members who wish to communicate with the Company in relation to the AGM should do so using the following means:

(a.) by writing to the Company Secretary at the Company's registered office address at: PO Box 1, Gorsey Lane, Coleshill, Birmingham, B46 1LW; or

(b.) by writing to: Capita Asset Services, The Registry, 34 Beckenham Road, Beckenham, Kent, BR3 4TU.

No other methods of communication will be accepted. In particular, you may not use any electronic address provided either in this Notice or in any related documents (including, without limitation, the Annual Report and Accounts 2016 and the form(s) of proxy) to communicate with the Company for any purpose other than those expressly stated in this Notice or in such other related documents.

14. Inspection of documents

Copies of the Directors' service contracts and, where appropriate, letters of appointment, a summary of the Directors' transactions in the Company's shares during the year and the written terms of reference for each of the Remuneration, Audit and Nomination Committees will be available for inspection at the registered office of the Company during normal business hours on any weekday (Saturday, Sundays and public holidays excluded) from the date of this Notice until the close of business on the business day preceding the AGM and will also be available for inspection for at least 15 minutes prior to the meeting and throughout the meeting.

There are no service agreements between any Director and any subsidiary of the Company.

The rules of the Headlam 2017 Performance Share Plan and the Headlam 2017 Deferred Bonus Plan will be available for inspection at the offices of Deloitte LLP (Company Secretarial Department), 2 New Street Square, London, EC4A 3BZ during normal business hours on any weekday (public holidays excepted) until the close of the meeting, and at the place of the meeting for at least 15 minutes before the meeting and during the meeting.

15. Voting results

The results of the voting at the AGM will be announced through a Regulatory Information Service and will appear on our website www.headlam.com.

16. Website

A copy of this Notice, and other information required by section 311A of the Act, can be found at www.headlam.com.

17. Data protection statement

Your personal data includes all data provided by you, or on your behalf, which relates to you as a Shareholder, including your name and contact details, the votes you cast and your Reference Number (attributed to you by the Company).

The Company determines the purposes for which and the manner in which your personal data is to be processed. The Company and any third party to whom it discloses the data (including the Company's registrars) may process your personal data for the purposes of compiling and updating the Company's records, fulfilling its legal obligations and processing the Shareholder rights you exercise.

Shareholder Information

Shareholder helpline

The Company's Shareholder register is maintained by Capita Asset Services ('Capita'), who are responsible for making dividend payments and updating the register, including details of changes to Shareholders' addresses and purchases or sales of Company shares. If you have a question about your shareholding in the Company you should contact: Capita Asset Services, The Registry, 34 Beckenham Road, Beckenham, Kent, BR3 4TU.

Email: ssd@capitaregistrars.com, telephone 0871 664 0300. (Calls cost 12p per minute plus your phone Company's access charge. Calls outside the United Kingdom will be charged at the applicable international rate. Capita are open between 09:00 – 17:30, Monday to Friday excluding public holidays in England and Wales.)

Frequent Shareholder enquiries

If you change your address

Please notify Capita in writing. If shares are held in joint names, the notification must be signed by all named Shareholders.

If you change your name

Please notify Capita in writing and enclose a copy of any marriage certificate or change of name deed as evidence.

Lost share certificates

If your share certificate is lost or stolen, you should call Capita immediately. A letter of indemnity will be sent to you to sign. Capita will charge for this service.

Duplicate Shareholder accounts

If you receive more than one copy of the Company's communications you may have your shares registered inadvertently in at least two accounts.

This happens when the registration details of separate transactions differ slightly. If you wish to consolidate such multiple accounts, write to Capita to request the accounts are consolidated.

Buying and selling shares in the UK

If you wish to trade in the Company's shares, you can do so at Capita's website, www.capitadeal.com or alternatively use a stockbroker or high street bank which trades on the London Stock Exchange. There are many telephone and online services available. If you are selling, you will need to present your share certificate at the time of sale.

Transferring shares

Transferring shares to someone else requires the completion of a stock transfer form. This form, and details of the procedure you need to follow, is available from Capita's website www.capitaassetservices.com. Stamp duty is not normally payable if the transfer is to a relative or if there is no money being paid in exchange for the shares.

Share prices information

Shareholders can find share prices listed in certain national newspapers. For a real-time buying or selling price, you should contact a stockbroker. Additionally, there is a link to the London Stock Exchange on the Company's website.

The Company's website

The Company's website at www.headlam.com provides news, details of activities, and information on the share price. The investor information section of the website contains up to date information for Shareholders including the Company's latest results and key dates such as dividend payment dates.

Dividend payments

Effective from 6 April 2016, HMRC introduced a new zero rate tax to dividends replacing the Dividend Tax Credit resulting in the removal of the dividend tax credit and the introduction of a 'dividend confirmation'.

Previously, all UK dividends were paid with a notional 10% tax credit, so for every £1,000 of dividend income received it was assumed that £111 in basic rate tax had already been paid (the total dividend was therefore £1,111). For this reason, non and basic rate taxpayers had no further tax liability on dividends received. This tax credit was scrapped, resulting in all dividend income being treated as gross (i.e. untaxed) income.

From April 2016, there is an income tax charge on dividends at the rate of 7.5% for basic rate taxpayers, 32.5% for higher rate taxpayers and 38.1% for additional rate taxpayers.

The long-standing system of tax credits attached to dividends was replaced with a tax-free Dividend Allowance. This means that there will be no tax to pay on the first £5,000 of dividend income, no matter what non-dividend income a Shareholder may have. Dividends paid on shares held within pensions and ISAs were unaffected, remaining tax-free.

Non-taxpayers and basic rate taxpayers who receive dividend income of more than £5,001 will need to make a self-assessment declaration to HMRC.

Shareholder Information

ShareGift

ShareGift, the charity share donation scheme, is a free service for Shareholders wishing to give shares to charitable causes. It may be especially useful for those who wish to dispose of a small parcel of shares which would cost more to sell than they are worth. There are no capital gains tax implications (i.e. no gain or loss) on gifts of shares to charity and it is also possible to obtain income tax relief. Further information can be obtained at www.sharegift.org.

The Unclaimed Assets Register

The Unclaimed Assets Register is a unique search service that helps individuals to find their lost assets and re-establish contact with financial institutions. It has a database of unclaimed life policies, pensions, unit trust holdings, and share dividends drawn from many companies and can search for lost assets and entitlements.

The Unclaimed Assets Register charges a small fixed fee for each search, 10% of which goes to charity. For further information, visit www.uar.co.uk.

Warning to Shareholders – boiler room scams

We have been made aware of our Shareholders receiving unsolicited telephone calls from companies offering to buy Headlam shares at a substantial premium to the prevailing market price for a large Shareholder intending to make a takeover bid. These callers, who can be extremely persuasive and persistent, are usually based overseas and are commonly known as 'boiler room scams'. Shareholders are advised to be wary of any unsolicited investment advice or approach to buy or sell shares; if it sounds too good to be true, it probably is.

If you receive an unsolicited investment approach, you should:

- Confirm the name of the person calling and the organisation they represent.
- Check that they are registered with the Financial Conduct Authority (FCA) by calling 0800 111 6768 or by visiting www.fca.org.uk and contact the firm using the details on the register.
- Report the matter to the FCA by calling 0800 111 6768 or by visiting www.fca.org.uk.

Please note that if you deal with an unauthorised firm, you will not be eligible to receive payment under the Financial Services Compensation Scheme. Further information on this or similar activity can be found on the FCA website www.moneymadeclear.org.uk. If you have any queries, please contact the Company Secretary.

Advisers

Auditor
PricewaterhouseCoopers LLP
Cornwall Court
19 Cornwall Street
Birmingham B3 2DT

Taxation Advisers
Deloitte LLP
Four Brindleyplace
Birmingham B1 2HZ

Principal Bankers
Barclays Bank PLC
PO Box 3333
One Snowhill
Snow Hill
Queensway
Birmingham B3 2WN

The Royal Bank of Scotland plc
Corporate and Institutional Banking
5th Floor, 2 St Philips Place
Birmingham B3 2RB

HSBC Bank Plc
Level 6, Metropolitan House
CBX 3
321 Avebury Boulevard
Milton Keynes MK9 2GA

Solicitors
Pinsent Masons LLP
3 Colmore Circus
Birmingham B4 6BH

Stockbrokers
Arden Partners plc
Arden House
17 Highfield Road
Edgbaston
Birmingham B15 3DU

Investec Bank plc
2 Gresham Street
London EC2V 7QP

Financial PR and IR
Buchanan
107 Cheapside
London EC2V 6DN

Registrars
Capita Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent BR3 4TU

Financial Calendar

Announcements

Annual General Meeting	25 May 2017
Interim results announced	21 August 2017
Full year results announced	March 2018

Dividend Dates

Final dividend for 2016, if approved, payable to qualifying shareholders on the register as at 2 June 2017	3 July 2017
Special dividend for 2016 payable to qualifying shareholders on the register as at 31 March 2017	24 April 2017
Interim dividend for 2017 declared	21 August 2017
Interim dividend for 2017 payable	2 January 2018

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Notes

headlam group plc

Company Business Directory

3D Flooring Supplies:
• Taunton • Swansea
• Cardiff • Bristol

Alvin Morris:
• Leeds • Liverpool
• Hull • Derby

Anderson Grant:
• Chelmsford

Baileys:
• Corston, Bath

Baileys:
• Plymouth

Beauvale:
• Coleshill, Birmingham

Beds Flooring:
• Bedford

Belcolor:
• St. Gallen, Switzerland

Betrex:
• Birmingham • Cheltenham

BMK:
• Leeds

C K Davie:
• Aberdeen • Dundee

Central Flooring:
• Coleshill, Birmingham

Cheshires:
• Nottingham • Sheffield

Clarendon:
• Tamworth

Clifford Carpets:
• Rochester

Concept Flooring:
• Smethwick
• Stoke on Trent

Company Business Directory

Crucial Trading:
• Coleshill, Birmingham

DJ Hann:
• Thatcham • Hayes

Faithfulls:
• Hadleigh, Suffolk
• Dartford • Walthamstow

Fell's Carpets:
• Gildersome, Leeds

Flooring Accessories Limited (FAL):
• Cardiff

Florco:
• Thatcham

Florprotec:
• Tamworth

GAAS Flooring:
• Bedford

Garrard Waters:
• Northampton • Leicester
• Peterborough • Coventry

Garrods:
• Hadleigh, Suffolk

Gaskell Wool Rich
• Tamworth

Hadfields:
• Stockport

Haldon Thompson:
• Stockport • Trafford Park
• Warrington

Hall's Flooring:
• Enfield

HBS:
• Stockport

Headlam:
• Gateshead • Carlisle
• Middlesbrough

Headlam:
• Glasgow

Headlam BV:
• Zutphen, the Netherlands
• Rotterdam • Houten

Home Foundations:
• Coleshill, Birmingham

Joseph, Hamilton, Seaton (JHS):
• Tamworth

Kersaint Cobb:
• Coleshill, Birmingham

Kingsmead:
• Tamworth

KJC Carpets:
- Coleshill, Birmingham

La Maison du Sol (LMS):
- Gennevilliers, Paris, France

LGS:
- Gateshead

Lifestyle Floors:
- Coleshill, Birmingham

Manx Tomkinson:
- Tamworth

Matty's:
- Coleshill, Birmingham

MCD Culpeck:
- Strood

MCD Kidderminster:
- Kidderminster

MCD Scotland:
- Uddingston, Glasgow

MCD Wales:
- Bridgend

Mercado:
- Leeds

Mercado:
- Belfast

Mercado Floorsales:
- Belfast

Mitchell Carpets:
- Poole

Mytton Flooring:
- Norwich

National Carpets:
- Rochdale

Oriental Weavers:
- Leeds

Plantation Rug Company:
- Stockport

Richards:
- Bristol • Southampton

RPS Flooring:
- Nottingham

Solmere Carpets:
- Stockton-on-Tees

Wilkies:
- Gildersome, Leeds
- Bradford
- Darwen (soon to open)

Registered office
Headlam Group plc
PO Box 1
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B46 1LW

Tel: 01675 433000
Fax: 01675 433030

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www.headlam.com

Email
headlamgroup@headlam.com

Registration
Registered in England and Wales
Number 460129

Visit us online at
www.headlam.com