headlam
group plc

DELIVERING MORE

Annual report and accounts 2017

FLOORCOVERINGS

Headlam Group plc ('Headlam' or 'the Company') is Europe's largest distributor of floorcoverings, providing the distribution channel between suppliers and its customers.

Headlam provides suppliers with an unparalleled route to market for their products, and its customers with the broadest product offering supported by excellent customer service and next day delivery.

Over the last 25 years, the Company has built and consolidated its market-leading position through organic growth, acquisition, considerable investment in its extensive distribution network and people, and strong relationships with suppliers and customers.

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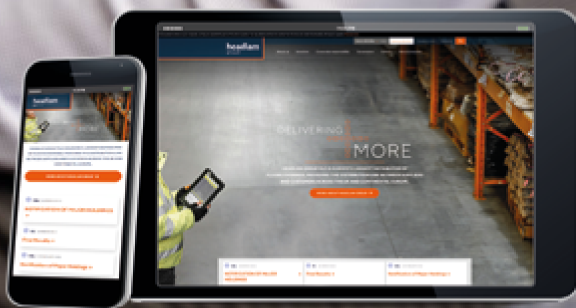


Visit www.headlam.com for more information

2017 OPERATIONAL HIGHLIGHTS

- Considerable new expertise added to the Board, Senior Management Team and at managerial level, both in the UK and Continental Europe, including the appointment of Chris Payne as Chief Financial Officer
- Three acquisitions completed during the year, most notably Domus Group of Companies Limited which meaningfully diversifies and broadens the Company's overall position in the market
- Efficiency actions and initiatives implemented, with a more unitised approach across the Company's businesses

*Before non-underlying items being intangibles amortisation relating to businesses acquired, acquisitions fees and non-recurring costs relating to personnel changes

2017 FINANCIAL HIGHLIGHTS

Revenue £million

£707.8m

+2.0% (2016: £693.6m)

Year	£million
2017	707.8
2016	693.6
2015	654.1
2014	635.2
2013	603.1

Underlying* Operating Profit £million

£43.8m

+6.6% (2016: £41.1m)

Year	£million
2017	43.8
2016	41.1
2015	36.8
2014	31.5
2013	27.7

Underlying* Profit before Tax £million

£43.1m

+7.5% (2016: £40.1m)

Year	£million
2017	43.1
2016	40.1
2015	35.6
2014	30.3
2013	26.4

(2017 Statutory Profit before Tax: £40.7m (2016: £38.2m))

Basic Earnings Per Share pence

39.1p

+6.3% (2016: 36.8p)

Year	pence
2017	39.1
2016	36.8
2015	33.8
2014	28.6
2013	18.0

Total Ordinary Dividends (declared and proposed in respect of 2017) pence

24.80p

+10.0% (2016: 22.55p)

Year	pence
2017	24.80
2016	22.55
2015	20.70
2014	17.50
2013	15.30

Net Cash Position £million

£35.3m

-32.9% (2016: £52.6m)

Year	£million
2017	35.3
2016	52.6
2015	43.9
2014	24.6
2013	14.0

At a Glance

WITH 63 BUSINESSES AND OPERATIONS IN FOUR COUNTRIES, WE ARE EUROPE'S LARGEST DISTRIBUTOR OF FLOORCOVERINGS

What we do and how we do it

Headlam provides the distribution channel between suppliers and customers of floorcoverings, providing suppliers with an unparalleled route to market for their products, and its customers with the broadest product offering supported by excellent customer service and next day delivery.

Our markets

UK
FRANCE
SWITZERLAND
NETHERLANDS

Revenue by geography

United Kingdom	86%
Continental Europe	14%

Revenue by sector

Residential	68%
Commercial	32%

For the year ended 31 December 2017.

BUILT LEADING POSITION OVER 25 YEARS

COUNTRIES OF OPERATION

2,427
EMPLOYEES

63
BUSINESSES

At a Glance continued

Built up over the last 25 years and employing 2,427 people, (as at 31 December 2017) Headlam has the greatest overall customer penetration in the UK and Continental Europe marketplace with an extensive distribution network enabling rapid delivery of almost 22,000 product units ('SKUs'). Through its market-leading capabilities and emphasis on the supplier and customer proposition, Headlam has supported the development and growth of both its suppliers and customers.

Headlam enables suppliers to focus on economic manufacturing without having to replicate a costly distribution channel for their focused product portfolio. Headlam's distribution network ensures that customers receive products more efficiently and within the typically short timescales required, whilst also supporting suppliers with the positioning and marketing of their products.

Headlam's customer base comprises principally independent retailers and flooring contractors and spans both the residential and commercial sectors, with the residential sector generating approximately two-thirds of annual revenue. While also operating in a number of more specialised market segments and distributing a number of niche products, the Company's core business is characterised by a high volume of small value orders, reflecting a predominance of orders for single room refurbishment.

The Company had 71,257 active customer accounts at 31 December 2017 (67,807 in the core business), with the breadth and strength of customer relationships achieved through the Company operating 63 individual businesses across the UK and Continental Europe (France, Switzerland and the Netherlands). Each business operates under their own unique trade brand and utilises their individual sales teams, thereby increasing the sales opportunity into the customer base and ultimately the Company's overall market penetration. By virtue of its market penetration, Headlam is involved with every facet of, and participant in, the floorcoverings industry.

The multiple business approach is additionally supported by the huge selection of floorcoverings on offer combined with the relationship-driven and regionalised nature of the marketplace. Sales representatives and delivery drivers are the main interface with the customers, with the latter typically delivering to the same customer on a daily basis.

Headlam enables, customers to satisfy the end-consumers' needs through offering the broadest range of products on a next day delivery basis, with end-consumers invariably wanting the product installed quickly once the purchase decision has been made. Customers are supported by Headlam's frequent and multiple sales representatives' visits, customer service, Point of Sale ('POS') materials, market awareness of new product lines and trends, and centralised financial and other resources including credit terms. The Company's extensive distribution network has been established over the last 25 years through considerable financial investment and technical and operational expertise, and represents a significant barrier to entry to competitors and potential new entrants. It currently comprises over 67 million cubic feet of warehouse capacity and its value is underpinned by property, plant and equipment assets totalling £101.6 million (net book value as at 31 December 2017). In 2017, 5.5 million customer orders were processed and delivered utilising a fleet of 404 commercial vehicles. Almost 9% of orders were place on-line during 2017, with strategies in place to grow this percentage.

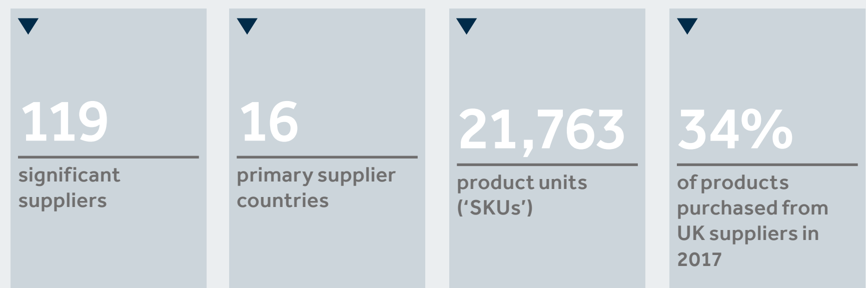
The core distribution network comprises four national distribution hubs in the UK and 18 regional distribution centres across the UK and Continental Europe, augmented by smaller warehouse premises, trade counters, showrooms and specification centres. The establishment of trade counters, showrooms and specification centres has been aimed at generating further sales through expanding the physical footprint and being closer to the customer, enhancing the regionalised customer service proposition, increasing awareness of the trade brands, and appealing to segments of the customer base who prefer a collection service.

The Company continues to invest in the network to support growth whilst also focusing on its optimisation to improve operational efficiency and cost-effectiveness, and ultimately its profitability.

Through organic growth, acquisition and optimisation of operations, Headlam will look to build on its market-leading core business whilst simultaneously diversifying and broadening its overall market position with entry into or increased weightings in more specialist market segments or product lines. These opportunities will be pursued across the UK and Continental Europe helping Headlam cement its position as the leading distributor across the European floorcoverings industry.

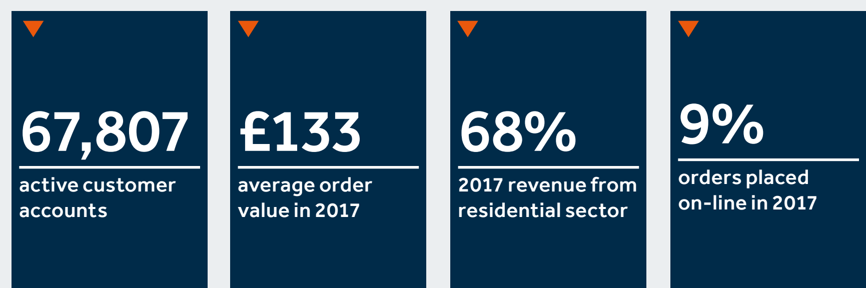
HEADLAM IN NUMBERS*

SUPPLIERS:



HEADLAM:

CUSTOMERS:



*Suppliers and Customers numbers provided above are for those of the core business only in 2017.

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"We are pleased with our performance during 2017, not just in terms of financial results, which were particularly pleasing given the softness in the UK market during the majority of the second half of the year, but also the progress made towards improving our operational processes and increasing efficiency across the Company."

Steve Wilson
Chief Executive

Investment Case

SIGNIFICANT BARRIERS TO ENTRY CREATED THROUGH YEARS OF INVESTMENT AND DEVELOPMENT OF OPERATIONAL EXPERTISE

1. MARKET LEADER

Market-leading position, significant scale, and longevity of operations

- Nearest competitors currently approximately 1/6th of size in terms of revenue
- Significant barriers to entry

2. RELATIONSHIPS

Depth and breadth of supplier and customer relationships

- Typically, suppliers' largest UK customer, with purchasing economies of scale
- Supporting the growth and development of all participants in the floorcoverings industry, particularly independent retailers and flooring contractors

3. CURRENCY EXPOSURES

Management of transactional currency risk

- Buy in sterling from the majority of suppliers so supplier manages the currency risk
- Supplier price increases passed along the chain and not absorbed by the business
- Negative aspects of currency deflation avoided by product re-engineering or price renegotiation

4. DEGREE OF RESILIENCE

Resilient core business characterised by high volume of small value orders

- More affordable purchase than other Repair, Maintenance and Improvement ('RMI') expenditure – average order value of £133 in 2017
- Not reliant on consumer credit

5. DISTRIBUTION NETWORK

Extensive distribution network with value underpinned by a largely freehold asset portfolio

- Significant time and resources to replicate
- Dense geographical footprint underpinning customer service proposition
- Freehold portfolio enables flexible response to change

6. OPERATIONAL GEARING

Operational gearing from increasing revenue and leveraging of the business model

- 19.1% underlying drop-through rate as a percentage of incremental revenue in 2017
- Combination of increased gross margin and a more efficient overhead base creating improved operating margin

7. FOCUS ON MARGIN

Focus on margin enhancement and efficiencies to increase level of profitability

- A number of efficiency initiatives underway and to be implemented
- Gross and underlying operating margin improvements of 50 and 30 basis points respectively in 2017

8. STRONG FINANCIALS

Strong cash flow and balance sheet

- Net funds of £35.3 million as at 31 December 2017
- Cash from operations of £54.5 million in 2017
- Strong operating cash generation at 109.8% of underlying EBITDA in 2017

9. DIVIDEND

Progressive dividend policy

- Ordinary dividend payments correlated to the increase in basic EPS, with total ordinary dividend payment of 24.80 pence in respect of 2017
- Additional policy of returning surplus cash to shareholders via special dividend when circumstances permit

10. GROWTH

Growing and broadening overall position in the industry

- Growing market-leading core business
- Supplementary growth and increased market penetration through acquisition

Chairman's Statement

Dick Peters
Non-Executive Chairman

As previously announced, having been on the Board of Headlam for almost half of the 25 years the Company has been operating, I am stepping down at the end of May 2018 after 12 years.

Between 2013, the year I became Chairman, and 2017, the Company has grown revenue and underlying profit before tax by 17.4% and 63.1% respectively, and paid and declared total dividends of 114.85 pence per share (in respect of the five years). This fantastic achievement is testament to the hard work, commitment and endeavour of all our employees across the UK and Continental Europe.

Headlam is a market-leading business with financial strength and, through years of investment and continuous development of operational expertise, has created significant barriers to entry in the UK market. Allied to this, the Company has ample opportunities to grow and improve its performance.

Since 2016, concerted actions and initiatives have been underway in the recognition that, despite the Company's recent successful history, its performance and operations could be further improved in a number of areas. These recent actions have been validated by the Company's performance during 2017, most notably in the area of gross and underlying operating margin improvement, which increased by 50 and 30 basis points respectively compared with 2016.

The Company demonstrated both resilience and robustness during 2017 and continued to grow despite softer market conditions compared with 2016. The outturn in 2017 is testament to the business model, collective industry experience, and an inherent predictability to the pattern of the revenue stream year-on-year, despite the lack of a tangible order book within the core business.

I believe the actions and initiatives put in place, operationally and in the areas of governance and corporate responsibility, will ensure a continued improvement in the Company's performance and its overall success.

We have made several notable additions to the Board and Senior Management Team during 2017 and early 2018 which will further assist in providing the necessary expertise and guidance to the Company going forward, and I remain confident about the Company's future prospects.

I have greatly valued and enjoyed my time at Headlam, particularly the support and interaction with my fellow Board members and a vast number of the Company's employees which has proven to be invaluable. I would like to express my sincere thanks to all of Headlam's stakeholders for their continued support of the Company and wish everyone well for the future.

Dick Peters
Non-Executive Chairman

6 March 2018

Chief Executive's Review

Steve Wilson
Chief Executive

INTRODUCTION

We are pleased with our performance during 2017, not just in terms of the financial results, which were particularly pleasing given the softness in the UK market during the majority of the second half of the year, but also the progress made towards improving our operational processes and increasing efficiency across the Company.

We have a clear intent to build on our market-leading position and financial strength, to deliver growth, enhanced customer service, operational and margin improvement and an enriched culture in order to create value for the benefit of all our stakeholders.

2017 FINANCIAL PERFORMANCE

Total revenue grew to £707.8 million in 2017, an increase of 2.0% on 2016 (1.2% in constant currency), with like-for-like revenue* growth in the UK and Continental Europe of 0.5% and 4.2% respectively representing a positive performance against a strong 2016 comparator. The second half of 2017 was characterised by weaker markets, with the first half delivering revenue growth of 4.0% compared with 2.0% for the year as a whole. Despite slower top-line growth, the Company was able to deliver an improved profit performance, increasing underlying** profit before tax by 7.5% to £43.1 million (2016 : £40.1 million) due to the concerted focus on margin enhancement and efficiencies throughout 2017.

The gross margin improvement of 50 basis points to 31.1% in 2017 (2016: 30.6%) was achieved through more effective organisation and streamlining of the Company's businesses' processes, with the largest contributor being the elimination of inconsistent pricing practices coupled with a move towards a more unitised pricing policy. Other actions implemented during 2017, and as detailed in the interim results announcement in August 2017, included reduction in the inventory aged profile, warehouse reconfiguration to improve capacity and delivery efficiency and an increasing focus on higher margin and exclusive products.

While the improvement in gross margin through a more cohesive and focused approach was pleasingly evident during 2017, the contributions from other efficiency initiatives will only begin to be realisable from 2018 onwards. Of key interest is the outcome from stock reordering trials and from other initiatives relating to more effective utilisation of the delivery fleet and expenditure incurred on goods and services not for resale.

INVESTMENTS AND ACQUISITIONS

Investments

In Continental Europe we appointed a new Managing Director, Pascal Pinard, in January 2018 to lead our French business, LMS. Pascal brings a wealth of international experience gained from 30 years in the floorcoverings industry, and it is anticipated that this positive step will address LMS's decline in performance which has been evident for a number of years. We remain encouraged by the performance of our Dutch business despite its currently modest size, and though the Swiss business may have been hampered by some transitional management gaps, actions are underway to address these and we remain confident that, with time, the business will regain its previous level of performance.

We believe the countries from which we operate in Continental Europe represent a platform for growth and potential consolidation, being a much more fragmented marketplace compared with the UK, and we will look to make further investments should the right opportunities arise, as illustrated by the Dutch acquisition announced today and detailed later in this review.

Significant investment and capital expenditure is expected to be undertaken during 2018 and 2019 in relation to the proposed new distribution centre in the Ipswich area, with capital expenditure anticipated to total approximately £24 million. We are now in a meaningful position to progress our plans having secured exclusivity in January 2018 on a site identified in late 2017. The site meets all our requirements in terms of investment criteria, operational considerations, growth capacity, and the support it will provide to several of our businesses in the wider area. Hopefully this will end the frustrating wait for a larger footprint in this part of the UK to support growth, and we are determined to commence operations from the centre as soon as possible having drawn up a schedule of works and stages which would see us able to do so in late 2019 or early 2020.

Acquisitions

We completed three acquisitions during the year, Mitchell Carpets Limited, McMillan Flooring Distributors Limited and Domus Group of Companies Limited ('Domus'), for an anticipated total consideration of £31.9 million and increasing our total number of businesses to 62 at the year-end. All three acquisitions added key strategic locations in the UK and further supplemented our network, while Domus additionally significantly increased the Company's presence in the commercial specification market.

During 2017 the Company largely refocused its acquisition strategy towards acquiring market-leading businesses with meaningful income streams that bring strategic benefits, further geographic coverage, increase or expand the Company's market presence into certain underweight product lines and market segments, and provide market segment consolidation opportunities. The strategy is aimed at diversifying and broadening the Company's overall position in the floorcoverings market by providing a complement to the Company's market-leading and long-established core distribution business which is characterised by the supply of high volume small value orders into both the residential and commercial sectors. During 2017, the Company's average order value was £133 (2016: £127).

The earnings enhancing acquisition of Domus as announced in December 2017 is a perfect illustration of the refocused acquisition strategy. Acquired for £24.2 million of cash on completion with deferred discounted consideration of £4.9 million, Domus is the UK's leading specification consultant and supplier of hard surfaces for premium construction and refurbishment projects, with a core product offering of premium ceramic tiles and additionally engineered flooring for application in the residential and commercial project markets. Domus's areas of expertise and position in the marketplace is almost entirely complementary to Headlam's, with minimal overlap in terms of product lines, suppliers and customer base, and we look forward to exploring the available growth opportunities.

In addition, we are delighted to announce today the acquisition of Dersimo BV ('Dersimo') based in Western Netherlands, bringing our total number of businesses to 63. For the year ended 31 December 2017, Dersimo's revenue and profit before tax amounted to €10.1 million and €0.4 million respectively. Established in 1972, Dersimo is a highly-regarded family-owned floorcoverings distribution business involved in both the residential and commercial sectors and employing 23 people. The acquisition of Dersimo is also earnings enhancing and firmly in-line with the refocused acquisition strategy, providing an increased weighting in the commercial sector in the Netherlands where we were previously underweight, improved geographic coverage across the country, and a much more meaningful overall market position. Combined with our existing Dutch business Headlam BV, the acquisition is believed to position us within the top three or four in the Dutch marketplace in terms of size. Dersimo will continue to be operated as a standalone business under its own trade brand and from its existing premises. Going forward it is anticipated that Dersimo and Headlam BV will support each other in terms of deliveries and stock giving rise to operating efficiencies.

The pipeline of acquisition opportunities remains strong but it is the Company's intention to retain a disciplined approach, targeting only the most rewarding opportunities without recourse to excessive leverage.

DIVIDENDS

The following Financial Review reiterates our polices in relation to progressive ordinary dividends and the potential returning of surplus cash to shareholders via special dividends when circumstances permit. In-line with the Board's ordinary dividend policy, a final dividend of 17.25 pence (2016: 15.85 pence) has been proposed, payable on 6 July 2018 to shareholders on the register at 1 June 2018, bringing the total ordinary dividend declared and proposed in respect of 2017 to 24.80 pence (2016: 22.55 pence). This 10.0% increase in the total ordinary dividend reflects the Company's ongoing commitment to increasing the ordinary dividend based upon basic earnings per share uplift, and the slight improvement arising from the cover ratio being rounded to 1.6.

OUR PEOPLE

To help deliver our strategic aims, considerable new expertise has been added during 2017 and the beginning of 2018 to complement the unrivalled knowledge and unique collective experience of the industry held by the existing members of the Board, the Senior Management Team and our business leaders.

At Board level, Tony Judge, who has worked at the Company since March 1992, was appointed as Chief Operating Officer in March 2017; Chris Payne joined the Company as Chief Financial Officer in September 2017; and, subsequent to the period-end, Amanda Aldridge was appointed a Non-Executive Director.

As previously announced, Dick Peters, the Company's Non-Executive Chairman, is stepping down from the Board on 31 May 2018 after 12 years and Philip Lawrence, a Non-Executive Director since June 2015, will be appointed Non-Executive Chairman with effect from 1 June 2018. I would again like to offer my sincere thanks and gratitude to Dick for his invaluable contribution to the development of Headlam over the past 12 years, and to Philip for assuming the position of Chairman allowing the Company to continue building on Dick's legacy and Philip's in-depth knowledge.

At a Senior Management and managerial level, we have made key appointments in the areas of Human Resources, Health & Safety, Communications, Company Secretarial and Legal Counsel. The introduction of these additional resources and expertise will be instrumental in enabling us to uphold the highest standards in all areas of operational processes, governance and corporate responsibility. We remain firmly committed to the continued investment in our business to support its operational and financial performance, the delivery of the strategic aims, and the success and wellbeing of all our employees.

CURRENT TRADING

Against a very strong January 2017 comparator, the Company's overall like-for-like revenue* declined 5.9% in January 2018, with the UK showing a more pronounced reduction, 6.7%, predominantly due to the performance of the residential sector and the adverse impact of a reduction of orders from one of our larger customers. In contrast, Continental Europe delivered a strongly positive result for the residential sector in the month, 6.5% on a like-for-like revenue* basis. The negative UK performance in the month was largely attributable to a very soft first working week following the New Year holiday, with the rest of the month showing some recovery but remaining moderately below our expectations.

The like-for-like revenue* performance in February 2018 was similar to January 2018, with a continued reduction of orders from the larger customer mentioned above and generally softer markets. However, given the very early stage in the year and our greater focus on profit rather than top-line growth, with organic revenue growth being a lesser contributor to the Company achieving its overall plans and expectations, our expectations for 2018 remain unchanged at this stage despite the weaker markets.

CONCLUSION

As previously stated, we are pleased with our performance during 2017, exhibiting further growth against what was qualitatively viewed as an overall flat market, robustness in the face of a weaker second half of the year, and improved profitability as a consequence of our focus on efficiency initiatives. The acquisitions of Domus and Dersimo illustrate that we have ample opportunities to grow and broaden our overall leading position in the industry while continuing to invest in the business to support organic growth. I personally wish to thank all our people for their contribution to the 2017 result, and look forward to delivering further improvements in 2018.

Steve Wilson
Chief Executive

6 March 2018

*Like-for-like revenue is calculated based on constant currency from activities and businesses that made a full contribution in both the 2017 and 2016 periods and is adjusted for any variances in working days

**Before non-underlying items being intangibles amortisation relating to businesses acquired, acquisitions fees and non-recurring costs relating to personnel changes

Financial Review

Chris Payne
Chief Financial Officer

REVENUE

During the year, total revenue improved by 2.0% from £693.6 million to £707.8 million, an increase of £14.2 million. Like-for-like revenue* growth in the UK and Continental Europe was 0.5% and 4.2% respectively.

	£000	%	£000	%
Revenue for the year ended 31 December 2016				
UK	602,104	86.8		
Continental Europe	91,468	13.2		
			693,572	100.0
Items contributing to growth during the 12-month period to 31 December 2017				
UK:				
Like-for-like* growth	3,043	0.5		
One less working day	(2,421)	(0.4)		
Acquisitions	4,508	0.8		
			5,130	0.9
Continental Europe:				
Like-for-like* growth	3,860	4.2		
Changes in working days	(617)	(0.7)		
Translation effect	5,819	–		
			9,062	9.9
Total movement			14,192	2.0
Revenue for the year ended 31 December 2017				
UK	607,234	85.8		
Continental Europe	100,530	14.2		
			707,764	**100.0**

*Like-for-like revenue is calculated based on constant currency from activities and businesses that made a full contribution in both the 2017 and 2016 periods and is adjusted for any variances in working days

UK

The Company's UK overall growth of 0.9% was achieved in a softer market compared with 2016, particularly in the commercial sector, and was based on organic growth of £3.0 million, contributions from acquired businesses amounting to £4.5 million and then, due to 2016 having one additional working day, lost revenue opportunity in 2017 amounting to £2.4 million.

The residential sector represented 70.4% of UK revenue in 2017 and increased by 1.0% on a like-for-like* basis. Conversely the commercial sector, representing 29.6% of UK revenue in 2017, decreased by 0.7% on a like-for-like* basis.

Continental Europe

The contribution and performance from the Continental European businesses improved throughout the year with the first half like-for-like revenue* growth of 3.0% increasing to 4.3% during the second half giving rise to an annual increase of 4.2%. Continental Europe accounted for 14.2% of total revenue in 2017, up from 13.2% in 2016. Each of the businesses on the Continent performed well in the year, in particular the businesses in the Netherlands and France showing good revenue growth and the Swiss business showed growth at more modest levels compared to 2016. The weighting between residential and commercial sector revenue in Continental Europe showed a slight movement towards residential compared with 2016, accounting for 52.6% of revenue (2016: 50.7%).

GROSS MARGIN

Gross margin increased by 50 basis points in the year from 30.6% to 31.1%. As detailed in the Chief Executive's Review, this was largely as a result of more effective organisation and the successful implementation of 'self-help' measures aimed at ensuring the Company maintained pricing discipline. Many of the measures were instigated toward the end of 2016 and were effectively maintained during 2017.

EXPENSES

Combined distribution and administrative expenses increased by 3.1%, up £5.3 million to £178.7 million. On an underlying basis the increase was marginally lower at 2.8% which largely reflects inflationary increases and the cost of living award given to all employees earning £42,500 or below of 2.0%. The percentage proportions of distribution and administration expenses of total expenses for 2017 remained largely unaltered compared with 2016, being 73.0% and 27.0% respectively (2016: 73.8% and 26.2%).

The increase in people cost of £1.2 million was again the largest underlying component increase, being 32.3% of the gross underlying expenses increase before currency translation reflecting the 2.0% cost of living award to employees.

The investment in sampling decreased year-on-year by £1.1 million following an efficiency focus to minimise sampling spend, particularly in the Company's Lifestyle branded products. Legal and professional fees increased by £1.0 million largely as a result of strategic objective related spend.

The non-underlying costs are discussed in more detail in the notes to the accounts.

Costs relating to the currency translation of the Continental European businesses amounted to £1.6 million, reflecting the degree to which Sterling depreciated against the Euro and Swiss Franc in 2017.

	Total expenses		Distribution		Administration	
	£000	**%**	**£000**	**%**	**£000**	**%**
Expenses for 2016	173,359		127,982	73.8	45,377	26.2
Significant movements in 2017:						
People cost	1,211	32.3	2,391	204.7	(1,180)	(45.7)
Vehicle expenses	483	12.9	537	46.0	(54)	(2.1)
Carriage and packaging costs	293	7.8	293	25.1	–	–
Sampling investment	(1,051)	(28.0)	(1,051)	(90.0)	–	–
Bad debts	348	9.3	348	29.8	–	–
Depreciation	(234)	(6.2)	(120)	(10.3)	(114)	(4.4)
Legal and professional fees	1,023	27.3	–	–	1,023	39.6
IT	418	11.1	–	–	418	16.2
Prior year exchange gain	471	12.6	–	–	471	18.2
Pension costs	415	11.1	–	–	415	16.1
Other	(100)	(2.7)	(1,230)	(105.3)	1,130	43.8
Underlying sub total	3,277	87.4	1,168	100.0	2,109	81.7
Non-underlying	472	12.6	–	–	472	18.3
Total before currency translation	3,749	100.0	1,168	100.0	2,581	100.0
Currency translation	1,589		1,326		263	
Expenses for 2017	**178,697**		**130,476**	**73.0**	**48,221**	**27.0**

Financial Review continued

OPERATING PROFIT

The underlying operating profit for 2017 increased by 6.6% compared to 2016 with the operating margin at 6.2%, improving from 5.9%, reflecting the absolute gain in gross margin due to the pricing discipline initiatives instigated toward the end of 2016. The operating margin generated by the incremental revenue ("drop through rate") of 19.1% compared with 10.9% in 2016 demonstrates the strong operational gearing inherent in the business model.

	Underlying £000	Non-underlying £000	Total £000
Operating profit 2016	41,072	(1,927)	39,145
Gross margin improvement in 2017			
Volume benefit	3,011	–	3,011
Pricing benefit	3,137	–	3,137
Effect of acquisitions	1,429	–	1,429
	7,577	–	7,577
Expenses increase			
Distribution	(1,557)	–	(1,557)
Administration	(1,745)	(472)	(2,217)
Effect of acquisitions	(1,564)	–	(1,564)
Total increase	(4,866)	(472)	(5,338)
Operating profit 2017	43,783	(2,399)	41,384
Drop through rate %	19.1		15.8
Operating margin %	6.2		5.8
Improvement %	6.6		5.7

TAX

The underlying effective tax rate for 2017 was 18.5% (2016: 18.9%) which is lower than the headline rate of corporation tax in the UK of 19.25%. The main reason for this difference was due to a release in provisions for uncertain tax positions following the ongoing review of the level of tax risks in the Company. The anticipated effective underlying rate for 2018 is expected to be 17.5%. The full effective rate of tax in 2017 was 19.1% (2016: 18.9%) since some of the non-underlying costs were disallowable for tax.

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".

EARNINGS AND DIVIDEND

Ordinary dividends

The Board's ordinary dividend policy is aimed at improving both the interim and final dividends, such that the total of the interim and final dividends for any particular 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 and adequacy of distributable reserves.

Over the last five years (inclusive of 2017), the Company's total ordinary dividends and basic earnings per ordinary share have grown at a compound average growth rate of 12.8% and 21.4% respectively.

Year ending 31 December	Basic EPS pence	Total Ordinary Dividend pence	Cover ratio
2013	18.0	15.30	1.2
2014	28.6	17.50	1.6
2015	33.8	20.70	1.6
2016	36.8	22.55	1.6
2017	39.1	24.80	1.6

The relationship between ordinary dividends and basic earnings per share can alternatively be expressed as a cover ratio as shown above.

The Board believes that although there is a continuing underlying risk relating to potential volatility around future maintainable growth in European floorcovering markets and the consequential impact this could have on earnings, it is nonetheless of the view that the current policy should continue during the medium-term. Additionally, and subject to the nature and term of any adverse movement in earnings and assessments around future trading, the Board may allow a change in the cover ratio in order to maintain the dividend.

In implementing the policy, the Board ensures the parent company has sufficient distributable reserves from which to make the distribution. The table below illustrates the reserves position for the last five years and the ability of the parent to fund the dividend payment as measured by the number of years cover. On average, over the last five years, the parent has maintained reserves sufficient to cover 4.4 years of dividend. Details of current year distributable reserves are shown in the retained earnings column in the Statement of Changes in Equity.

	Distributable reserves		Proposed	
Year ending 31 December	Parent £000	Group £000	Dividends £000	Years cover
2013	71,220	124,465	12,689	5.6
2014	57,241	126,018	14,655	3.9
2015	76,452	137,603	22,464	4.4
2016	85,795	143,315	25,729	3.3
2017	105,128	157,903	20,932	5.0

SPECIAL DIVIDENDS

The Company has previously undertaken an expansive investment programme to improve and increase the capacity and reach of its infrastructure.

However, from time to time, the Company's commitment to expansionary capital expenditure will pause, as was the case during 2016 and 2017 and therefore, subject to ongoing levels of cash generation being maintained, the Company may carry a capital position in excess of that which would be required to maintain its asset base.

This situation may leave the way open for a return of surplus capital to shareholders, and in the Board's opinion, this can be best achieved through the payment of special dividends as was the case in 2016 and 2017, amounting to 6.0 pence and 8.0 pence per share respectively.

As outlined in the Final Results announcement and Annual Report and Accounts for the year ended 31 December 2015, the conditions that will apply to any special dividend payments are; i) 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 EBITDA; ii) the cover ratio of the aggregated ordinary and special dividends when expressed in terms of dividend cover will not be less than one and; iii) the payment must be made from available distributable reserves.

Having assessed the Company's cash effect of its future spend in the investment programme (for example in the development of the Ipswich distribution centre in 2018 and 2019) and in pursuing the strategic aim of acquisitive growth, the Company is not declaring a special dividend for 2018.

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

Dividend	Status and date announced	Approval	Approximate payment date
Current ordinary interim	Declared August	The Board August	January in the year following announcement
Current ordinary final	Recommended March	AGM by shareholders May	July

GOODWILL AND OTHER INTANGIBLE ASSETS

The recent acquisition of Domus Group of Companies Limited ('Domus') has caused the Board to consider and then re-evaluate the Company's approach to valuing goodwill and the associated intangible assets generated. The two smaller acquisitions made earlier in 2017 were treated in a similar way to previous acquisitions whereby any intangible assets generated from the customer relationships or order books, which were typically low value, were fully written down in the year of acquisition. This approach was deemed to be inappropriate for the much larger acquisition of Domus.

In arriving at a value for goodwill and the associated intangible assets, the Group has taken a judgment on the discounted fair value of the contingent consideration (a maximum gross value of £2.7 million) which is payable three years after completion. Similarly, the Company has taken judgments over attributing values for the intangible assets of order book, brand value and customer relationships together with a useful economic life over which to amortise the assets. This ranges from circa two years for the order book, to 15 years for the brand and ten years for the customer relationships. After evaluating the above, this leaves the Group with a residual goodwill value of £23.0 million which reflects the overall value to the Group as a result of having a more diverse product range and route to market.

The amortisation charge to the Consolidated Income Statement for this transaction was £0.1 million in 2017 and is expected to be £1.3 million in 2018, although this will decline in future years as the intangible assets become fully written down.

Financial Review continued

Going forward it is anticipated that this revised approach will be applied to future acquisitions meaning there is likely to be an assessment of goodwill, intangible asset value and associated amortisation in the Consolidated Income Statement for each transaction carried out.

EMPLOYEE BENEFITS

The liability attaching to employee benefits is as follows:

	2017 £000	2016 £000
Current liabilities	**2,235**	2,169
Non-current liabilities	**10,481**	20,781
Total	**12,716**	22,950

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 decrease in the deficit amounts to £10.2 million. This was mainly caused by the positive changes in the returns on asset performance, liability experience gains and minor changes in the demographic assumptions offset by a decrease in the liability discount rate assumption from 2.7% to 2.4%.

CASH FLOW

Net cash flow from operating activities

During the year, net cash flow from operating activities increased by £10.6 million from £32.6 million to £43.2 million. The key drivers of the positive cash flow generation are shown in the table below.

	2017 £000	2016 £000
Cash flows from operating activities		
Profit before tax for the year	**40,719**	38,179
Depreciation, amortisation and impairment	**5,845**	5,276
Net finance cost	**665**	966
Profit on sale of property, plant and equipment	**(45)**	(15)
Share-based payments	**1,218**	1,239
Working capital changes	**(6,108)**	(1,998)
Cash generated from the operations	**54,510**	43,648
Interest paid	**(761)**	(1,133)
Tax paid	**(8,388)**	(7,703)
Pension contributions	**(2,164)**	(2,171)
Net cash from operating activities	**43,197**	**32,641**

Cash generated from operations increased year on year by £10.6 million driven by profit before tax, an improvement in working capital and an increase in amortisation resulting from the acquisitions in 2017. To offset these cash inflows, there was an increase in the tax payment during the year of £0.7 million.

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 £60.4 million, with the two main factors being the payment of dividends and the acquisition consideration and associated fees, largely related to Domus.

	2017 £000	2016 £000
Cash flows from investing activities		
Proceeds from sale of property, plant and equipment	**190**	401
Interest received	**576**	752
Acquisition of subsidiary, net of cash and debt acquired and repaid	**(31,805)**	–
Acquisition of property, plant and equipment	**(3,058)**	(2,963)
Net Cash from investing activities	**(34,097)**	(1,810)
Cash flows from financing activities		
Share movement	**(377)**	(224)
Net movement on borrowings	**(230)**	(13,544)
Dividends paid	**(25,729)**	(22,464)
Net cash from financing activities	**(26,336)**	(36,232)

NET DEBT

As detailed in the table below, Group net funds at the end of the year decreased by £17.3 million (32.9%), from £52.6 million to £35.3 million mainly as a result of the net cash outflows arising from operating, investing and financing activities outlined above.

	At 1 January 2017 £000	Cash flows £000	Translation differences £000	At 31 December 2017 £000
Cash at bank and in hand	59,343	**(17,240)**	**(73)**	**42,030**
Bank overdraft	(4)	**4**	**–**	**–**
Debt due within one year	(224)	**–**	**(9)**	**(233)**
Debt due after one year	(6,493)	**230**	**(256)**	**(6,519)**
	52,622	**(17,006)**	**(338)**	**35,278**

FUNDING AND GOING CONCERN

The Company increased its existing UK banking facilities by a further £25.0 million on 8 December 2017. The increased facility was equally split across the two separate agreements the Company has in place with Barclays Bank PLC and HSBC Bank Plc. The increased banking arrangements retain the original terms and end dates of 14 December 2021. The Sterling committed facilities increase from £47.5 million to £72.5 million, with maintained Euro facilities of €8.6 million. The Company also has short-term uncommitted facilities which amount to £25.0 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 2017, 94.0% of the total facilities were undrawn as shown below.

	Drawn £000	Undrawn £000	Total facility £000
Less than one year	**233**	**32,343**	**32,576**
Over one year and less than five years	**6,519**	**73,369**	**79,888**
	6,752	**105,712**	**112,464**

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.

Chris Payne
Chief Financial Officer

6 March 2018

Our Marketplace

HEADLAM'S MARKET-LEADING CORE BUSINESS IS PREDICATED ON SUPPLING A HIGH VOLUME OF SMALL VALUE ORDERS INTO BOTH THE RESIDENTIAL AND COMMERCIAL SECTORS

There are few officially recognised statistics specifically covering the UK and Continental European floorcoverings markets but one estimate puts the value of the UK market for 2017, expressed by reference to manufacturer's selling price, at £1.95 billion (Source: AMA).

Key components contributing to the size of the UK market are:

- General maintenance, repair and refurbishment cycle – Qualitative data suggests that the residential end-consumer changes their flooring approximately every 10 years, the refreshment typically relating to one room at a time;
- Aged property profile within both the residential and commercial sectors – 76% of housing stock in England was built before 1980, 20% before 1919 (Source: UK Government, Department for Communities and Local Government);
- Under-investment in existing housing stock in both the public and private sector – In 2015, 19% of all residential dwellings in England failed to meet the Decent Homes Standard (Source: UK Government, Department for Communities and Local Government);
- Health and Safety regulations supporting Repair, Maintenance and Improvement ('RMI') spend in the commercial sector; and
- General consumer perception and economic environment.

New build construction is not considered to materially contribute to the prevailing market size as in recent years the UK has recorded modest new build construction numbers. In 2015 and 2016, annual new build dwelling completions in England accounted for only 0.6% of total dwellings (Source: UK Government, Department for Communities and Local Government).

An increase in construction activity, to increase housing stock undersupply issues for example, would provide an additional market growth catalyst. Likewise, consumer confidence and increased housing transactions augment growth rates due to the likelihood of several rooms being refurbished simultaneously within a property rather than being phased over time or delayed until a necessity.

Headlam's total revenue split between the residential and commercial sectors is believed to reflect the overall revenue split in the UK market, and has remained fairly constant in recent years at approximately two-thirds residential and one-third commercial. The Company's revenue from Continental Europe is more weighted towards commercial than the UK due to the Company's French business's social housing refurbishment activity.

Headlam's market-leading core business is predicated on suppling a high volume of small value orders into both the residential and commercial sectors, with the Company's principal customers being independent retailers and flooring contractors. As at 31 December 2017, the Company had 67,807 active customer accounts within the core business, of which approximately 75% were in the residential sector reflecting the bias towards residential revenue.

The average floorcoverings requirement and order in the residential sector is significantly smaller than the commercial equivalent, and this in conjunction with the Company's core product range being largely within the low to middle-end of the market in terms of price points means the Company's average order value is proportionately low thereby representing a comparatively more affordable purchase compared to other RMI expenditure.

The Company processed 5.5 million orders in 2017 of which only 5% were full roll orders, with the vast majority of the Company's orders requiring preparation before delivery. This includes 'cut length' or 'pack' orders whereby the rolls of carpet and vinyl and boxes of palletised goods are cut to length or broken-down to satisfy the customer's specific order requirement. The predominance of cut length orders, as opposed to full roll orders, again reflects the small orders and residential bias to the Company's revenue, with this revenue segment generating higher gross margins for the Company.

The Company's core market-positioning provides a degree of robustness and protection from weaker markets as the financial performance is typically based on many small orders and is not reliant on either key seasonal discounted sale periods or end-consumer credit, often used to subsidise and create demand for more expensive purchases. In addition, demand for floorcoverings tends to be inelastic to price increases in an inflationary environment due to the relative infrequency of purchases by the end-consumer; order values being relatively modest when compared to other RMI expenditure; and the large variety of product catering to every price point. The regular stream of new collections entering the market assists with the competitive positioning of product and ultimately helps maintain affordability in inflationary environments, with suppliers re-engineering their products to maintain price points.

Constant technical innovation, improved materials and design trends helps create strong ongoing demand for floorcoverings. Driven by the demand for hard flooring, and following significant investments in technology and manufacturing processes, LVT ('luxury vinyl tile') is the fastest growing product category being durable, warm under foot and offering realistic stone, wood and ceramic effects. Likewise, advances in yarn technology have resulted in softer polypropylene and polyester ranges.

Independent retailers and flooring contractors comprise the vast majority of the Company's customer base and accounted for almost 90% of the Company's UK revenue in 2017. The Company's performance over recent years coupled with anecdotal evidence suggests that this segment of the customer base has been growing and gaining market share, in particular independent retailers who are thought to hold an approximate 60% share of the UK floorcoverings market. In the last few years, the Company's active customer accounts within the residential sector has grown steadily with the Company's UK residential sector revenue growing 27% between 2012 and 2017, far exceeding the estimated overall UK floorcoverings market growth of 15% (Source: AMA).

The Independent Retailer

The success of the independent retailer in the floorcoverings market is in marked contrast to the fortunes of independent retailers in many other markets, and the Company's business model and customer service proposition is centred on supporting and assisting their growth through:

- Mitigating their need to hold stock with next-day and 'just in-time' delivery – allowing smaller premises and lower–overheads;
- Providing a comprehensive product range which is frequently refreshed;
- Providing Point of Sale ('POS') materials and new product training when necessary to assist with marketing;
- Dedicated sales representative relationships, frequent visits and sophisticated CRM app to assist account management; and
- Provision of credit.

Our Business Model

OUR EXCEPTIONAL SUPPLIER AND CUSTOMER PROPOSITION AND MARKET–LEADING POSITION CREATES VALUE FOR STAKEHOLDERS AND PROVIDES FOR GROWTH THROUGH RE-INVESTMENT INTO THE BUSINESS

WHAT WE DO:

SUPPLIERS

Global manufacturing supply base, covering multiple product categories

headlam
group plc

Exceptional supplier and customer proposition

Suppliers	Customers
Unparalleled route to market for products	Broadest product offering supported by excellent customer service

CUSTOMERS

Most extensive customer base in the UK and Continental Europe, comprising principally independent retailers and flooring contractors

HOW WE DO IT:

OUR COMPETITIVE ADVANTAGE MAKES HEADLAM THE PARTNER OF CHOICE:

- 'Global to local'
- Extensive market reach
- Highly experienced and knowledgeable management teams
- Lasting relationships with suppliers and customers
- Operational scale
- Financial strength

CREATING SUSTAINABLE VALUE:

CREATING VALUE FOR THE BENEFIT OF ALL OUR STAKEHOLDERS:

- Highly cash generative
- Leveraging market-leading position
- Ongoing capex and opex investment
- Continued expansion and optimisation of the distribution network
- Progressive ordinary dividend policy

GROWTH THROUGH RE-INVESTMENT:

SUPPORTING THE FUTURE DEVELOPMENT AND SUCCESS OF OUR COMPANY:

- Continue growing the core business through organic growth, bolt-on acquisitions and product expansion
- Diversification and increased breadth into complementary market segments through targeted M&A
- Investment in the network
- Investment in people, the working environment and culture to attract and retain the best people

Our Strategic Pillars

WITH THE STRATEGIC AIM OF CREATING VALUE FOR THE BENEFIT OF ALL STAKEHOLDERS

GROWTH

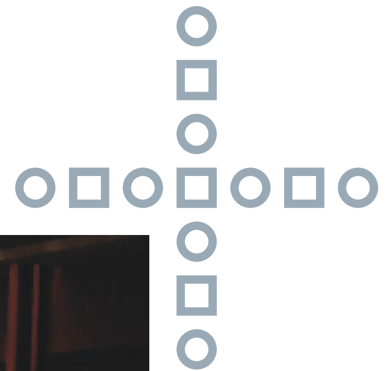
- Continue growing market-leading core business
- Diversify and broaden overall position in the industry
- Accelerate growth through M&A (product, geography, segment)

CUSTOMERS

- Customer service and satisfaction at core of the business model
- Expand offering and customer base - support their growth through reciprocal relationship
- Evolution and innovation to respond to evolving demands

DYNAMIC MODEL

- Position at the forefront for another 25 years – 'the partner of choice'
- Build the distribution channel model – indispensable part of the chain
- Continually appraise opportunities to ultimately reward all stakeholders



MARGIN IMPROVEMENT

- Optimise the distribution network and processes
- Leverage scale to increase returns and operational gearing
- Pursue multiple efficiency initiatives (incremental and larger)

CULTURE & ETHOS

- Focus on culture to attract and retain the best talent
- Invest in people through training, support and working environment
- Common purpose and aligned goals to deliver success

CREATE VALUE FOR THE BENEFIT OF ALL STAKEHOLDERS

"Between 2013, the year I became Chairman, and 2017, the Company has grown revenue and underlying profit before tax by 17.4% and 63.1% respectively, and paid and declared total dividends of 114.85 pence per share (in respect of the five years). The fantastic achievement is testament to the hard work, commitment and endeavour of all our employees across the UK and Continental Europe."

Dick Peters
Non-Executive Chairman

Key Performance Indicators

The Board believes the Key Performance Indicators ('KPIs') below provide a comprehensive and relevant list of measurements with which to assess the Company's financial, operational and social performance towards the achievement of its Strategic Pillars.

	Measurement	Why it's important	2017 Performance	Initiatives and actions for improvement
FINANCIAL				
Like for like revenue* growth	Year on year revenue growth as a % adjusted to normalise currency, businesses making a full year's contribution and consistent working days	Allows a consistent measure of year on year performance	1.0% *2016: 4.1%*	Organic growth focus for regional businesses and universal product coverage
Gross profit margin	Measured as a % of revenue	Shows the effectiveness of gross profit generation from revenue	31.1% *2016: 30.6%*	Pricing discipline and product expansion
Underlying operating profit margin**	Measured as a % of revenue	Shows the effectiveness of sustainable operating profit generation from revenue	6.2% *2016: 5.9%*	Margin improvement initiatives
Basic earnings per share ('EPS')	Profit after tax divided by average weighted number of shares	Demonstrates the level of profit per share attributable to the shareholders	39.1 pence *2016: 36.8 pence*	In line with profit performance
Return on capital employed ('ROCE')	Measured as EBIT as a % of capital employed	Demonstrates the relative level of profit generated by the capital employed	26.2% *2016: 26.9%*	May be offset in the short term by infrastructure investment, for example on Ipswich distribution centre development
Underlying operating cash from operations**	Measured as a % of EBITDA	Cash conversion measures the success of the Company in converting operating profit (measured as EBITDA) to cash, which underpins the quality of the Company's earnings and reflects the effectiveness of working capital management	109.8% *2016: 94.2%*	Should be held above 90% to ensure profit growth is cash generative. It is anticipated that improvements in inventory turn (see KPI below) will also lead to improvements in cash conversion %
Underlying selling, general and administrative ('SG&A') costs**	Measured as a % of Revenue	Shows how effective the Company is at converting gross profit into operating profit	24.9% *2016: 24.7%*	Maintain cost control to ensure increases remain below revenue growth

	Measurement	Why it's important	2017 Performance	Initiatives and actions for improvement
NON-FINANCIAL				
Inventory turn	Annual ratio measured by comparing cost of goods sold during the financial period with the average annual inventory level (using averaged data points at 1 January, 30 June and 31 December)	A higher inventory turn is an indicator of efficient revenue generation, reduced risk of inventory obsolescence and more effective utilisation of distribution centre capacity	3.8x *2016: 3.9x*	Moving from a manual reordering system to a computerised reordering algorithm in order to optimise the level of inventory held, match revenue demand with inventory availability, ensure excess inventory positions are minimised and supplier ordering is structured, inventory requirements communicated to fit in with supplier production schedules and deliveries scheduled to ensure adequate availability
Employee retention	Retention measures the ability to retain employees in the current year compared to previous years. Measured as a percentage of employees retained in the Company between 1 January and 31 December	Retention demonstrates the Company's ability to retain employees. The Company's medium-term objective is to further develop a cultural ethos which attracts and retains the best talent in order to ensure valuable workforce knowledge is retained to support delivery of the strategic objectives and reduce the substantial costs involved in hiring and training employees	74.0% *2016: 74.0%*	Further develop employee engagement; Introduce people strategies based on insight gathered from the employee engagement survey; and Identify future skills gaps and implement learning strategies
Reportable incidents ('RIDDOR Reports')	Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 2013. These regulations require employers, the self-employed and those in control of premises to report specified workplace incidents	By measuring reportable injuries, can benchmark and identify any deficiencies in the Company's processes, allowing continuous improvement in H&S standards in the pursuit of excellence	25 *2016: 17*	Writing Safe Systems of Work with effect Q1 2018 to improve training standards, and additionally increase frequency of in-house H&S visits to identify and limit failures in compliance

* Like-for-like revenue is calculated based on constant currency from activities and businesses that made a full contribution in both the 2017 and 2016 periods and is adjusted for any variances in working days

** Before non-underlying items being intangibles amortisation relating to businesses acquired, acquisitions fees and non-recurring costs relating to personnel changes

Risk Management and Principal Risks & Uncertainties

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.

In 2018 the Board has established a risk committee, chaired by the Company's Chief Financial Officer, that will enable a more granular review of business risks. The committee will be made up of cross function and business leaders and will report back to the Board on detailed risks and mitigation plans on a quarterly basis.

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.	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 IT system 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 IT infrastructure 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.
People	The Company's ability to deliver continued success is very dependent upon its people.	An inadequate pool of suitably qualified and motivated 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 driving employee engagement through direct communication, listening groups and employee champion forums.
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 2017, the Company's pension deficit was £12.7 million with the vast majority being the UK plan. An increase in the plan deficit could require the Company to increase the deficit reduction contributions.	As a result of an agreed deficit reduction plan in 2015, the Company makes deficit reduction contributions of circa £2.2 million in 2017 rising by 3.3% each 1 January, with a view to eliminating the shortfall by 30 April 2019. The Company's most recent valuation of the UK plan as at 31 December 2017 showed a significant reduction in the valuation deficit.
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.

Viability Statement

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 2020, 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 extended on 7 December 2017, through to 31 December 2020, 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 2020. This longer-term assessment process supports the Board's statements on both viability and going concern.

In 2017, 5.5 million customer orders were processed and delivered utilising a fleet of 404 commercial vehicles. Almost 9% of orders were placed on-line, with strategies in place to grow this percentage.

Corporate Responsibility

WE REMAIN COMMITTED TO MANAGING OUR COMPANY IN A SOCIALLY RESPONSIBLE WAY, CONTINUALLY REVIEWING OUR PERFORMANCE IN ALL AREAS OF CORPORATE RESPONSIBILITY

Introduction to Corporate Responsibility

We remain committed to managing our Company in a socially responsible way, continually reviewing our performance in all areas of Corporate Responsibility, and were delighted during 2017 to become a constituent of the FTSE4Good Index. Launched by the global index provider FTSE Russell, the FTSE4Good Index Series is designed to identify companies that demonstrate strong environmental, social and governance ('ESG') practices, measured against globally recognised standards.

A key constituent of our Corporate Responsibility is the relationships with our stakeholders, encompassing employees; suppliers; customers; investors; and the communities in which we operate. These relationships, many of which span the 25 years we have been operating, are of paramount importance and pivotal to our performance and we are committed to continuing the investment in these relationships to promote and ensure their longevity. We endeavour to have a positive impact on all our stakeholders with the strategic aim of creating value for the benefit of all stakeholders whilst supporting the end-consumer by providing an exceptional package of goods and services.

We have undertaken further investment in people and training during 2017 and 2018, most notably in the areas of Human Resources ('HR') and Health & Safety ('H&S'), expanding our teams and updating our policies and procedures to strive for the highest standards in all areas of our operations.

Our ambition is to embed Corporate Responsibility within the Company's culture with an ethos of supporting all stakeholders and upholding the highest standards to support the continued growth and success of the business.

Dick Peters
Non-Executive Chairman

Steve Wilson
Chief Executive

Stakeholder Engagement

THE COMPANY CONSIDERS THE ONGOING ENGAGEMENT AND EFFECTIVE COMMUNICATION WITH ALL ITS STAKEHOLDERS TO BE OF SIGNIFICANT IMPORTANCE

INTRODUCTION

The Company considers the ongoing engagement and effective communication with all its stakeholders to be of significant importance, and it is undertaken in various forms throughout the year to provide the necessary support to each audience.

EMPLOYEES

Employee communication and engagement is undertaken via formal and informal meetings, presentations, regular emails and bulletins, use of notice boards, and the Company's website and intranet. Conducted at both Company and individual business level, subjects include H&S and HR matters, updates to policies and procedures, notable achievements, and commentary on financial and operational performance and strategic aims. During 2017, to expand its engagement channels, the Company conducted its first Employee Survey and initiated a monthly HR Bulletin.

Executive Directors and members of the Senior Management team have ongoing dialogue and regular meetings with teams at each of the Company's businesses. In addition, twice a year, the Chief Executive, Chief Financial Officer, Chief Operating Officer and Commercial Director conduct a tour of the Company's locations to meet with management to discuss operational and other matters and obtain any feedback. The Company looks to foster an open and transparent environment and actively encourages all employees to provide feedback should they wish. Feedback is reflected upon and any actions duly taken and communicated.

CUSTOMERS

Customer engagement and interaction is mainly undertaken via the frequent visits by sales representatives and managers, telephonically with members of the customer service teams, and the delivery drivers. Customers' successful operations and wellbeing are essential to the performance of the Company and any feedback is discussed as appropriate and used to improve and enhance the customer service proposition.
Having conducted customer satisfaction surveys in the past involving a small cross-section of the customer base, the Company will engage with a larger proportion of the customer base through surveys during 2018. In addition, sales managers and directors regularly visit customers to ensure they are content with the service received.

Many of the Company's businesses offer open house or trade days several times a year, allowing customers to visit facilities and learn about any special offers and new initiatives, which may include product and POS innovations.

SUPPLIERS

Engagement with suppliers is undertaken through regular contact by individuals at both the Company and individual business or location level, and by individuals holding various positions within the organisation.

Each of the Company's distribution centres has autonomy to develop products in conjunction with approved suppliers that may better suit the country or region they operate in. The Company's buyers work closely with suppliers, meeting with them on a regular basis at their showrooms and production facilities in addition to the Company's premises.

SHAREHOLDERS AND ANALYSTS

Ongoing interaction with shareholders and the wider investment community, including analysts and investors not currently holding shares in Headlam, is essential to their understanding of the Company; their ability to appraise the performance and management of the Company; and consideration of the Company as an investment proposition.

The Company strives to provide a clear, balanced and comprehensive level of information and written material. The Company maintains a corporate website which contains regularly updated regulatory and other information, including presentations used to update the investment community, and issues both statutory and non-statutory regulatory news announcements throughout the year to update on financial, operational and other matters. The Company offers its larger shareholders, either directly or via its broker, face-to-face meetings on a bi-annual basis at a minimum to present and discuss performance and other matters, and obtain any feedback. These meetings are hosted by several of the Executive Directors and the Company's Director of Communications. The Company also hosts a briefing for analysts, arranged by the Company's Financial PR and IR adviser, twice a year to coincide with the announcement of its half year and full year financial results to present and discuss the same matters.

Meetings are periodically held at various of the Company's locations to better illustrate the Company's operations and aid understanding, and in early 2018 the Company hosted a Capital Markets Event for analysts and institutional investors at a Domus specification centre in London. Domus was acquired by the Company in December 2017 and the event was to provide a detailed overview of its operations and the strategic rationale for its acquisition, and it is anticipated that similar events will be held going forward.

The Non-Executive Directors, including the Chairman, attend certain events and briefings during the year where shareholders are present in addition to the AGM, and the Board's Non-Executive Directors are committed to facilitating a direct channel of communication with the Company's larger shareholders to hear any views and concerns.

The Company actively seeks shareholder feedback, and feedback is collated by both the Company and its advisers, discussed at Board and senior management team level and considered in relation to all aspects of the Company and help inform its written and verbal communications.

LOCAL COMMUNITIES

The Company is committed to advertising and employing locally when it is able, soliciting feedback, and reacting positively to this feedback and any requests for its involvement including support of local events.

Our People

OF PRIMARY IMPORTANCE IS THE PROVISION OF A SAFE AND ENVIRONMENTALLY SOUND WORKPLACE FOR EMPLOYEES, AND ONE WHERE THEY ARE ENCOURAGED TO PROGRESS

INTRODUCTION

Of primary importance to the Company is the provision of a safe and environmentally sound workplace for employees and visitors and one where employees are encouraged to progress and achieve their full potential.

Both the H&S and HR teams was expanded during 2017, most notably with the engagement of a National Health & Safety Manager and People Director (see page 36 for further details on Health & Safety). A number of initiatives were launched by the HR team during the year to support the overall wellbeing of the Company's employees, including:

- Employee Assistance Programme
- HR and employee relations support
- Employee satisfaction survey
- Monthly HR Bulletin
- Occupational Health

TENURE, RECRUITMENT AND INTERNAL VACANCIES

The Company actively recruited in all departments throughout 2017 and the total number of employees grew year-on-year to 2,427 as at 31 December 2017 (2016: 2,384). Recruitment is undertaken through a number of avenues including the Company's own website, recognised job boards and, where appropriate, recruitment providers. The circulation of an internal vacancy list was introduced in December 2016 to give employees greater visibility of the vacancies available across the Company and encourage internal moves as a measure to retain talent and experience. This reflects the Company's commitment to giving all employees the opportunity to progress their careers within Headlam, supported by ongoing training and development. It is the Company's intention to supplement the level of training available to its employees over the coming years. Employee retention and tenure is a key metric for the Company and 39% of UK employees have been with the Company for 10 years or more, with 135 employees having been with the Company since its establishment in 1992.

As is not uncommon in the sector, a high proportion of employee turnover is among those with less than six months' service and the focus is on reducing this through improved recruitment, induction and onboarding practices. The Company employee retention metrics for 2017 and 2016, and initiatives for improvement, are given within the Key Performance Indicators on page 24 of this Annual Report.

EMPLOYEE SURVEY 2017 AND 2018

Headlam undertook its first employee survey in May 2017 with the aim of giving all UK employees the opportunity to express their views on a confidential basis and help identify areas for improvement. The survey was completed by 53% of employees, considered acceptable for a first survey, with an overall engagement score of 77%.

Individual survey reports were provided to all the Company's businesses, with workshops and action planning subsequently undertaken at both group and local level involving champions from all departments, with ideas and concerns discussed and actions agreed. Actions subsequently implemented include improvements to the physical working environment, efforts to improve internal communications, introducing local social and team events, job shadowing to create better understanding of different job functions, and modifications to some operational processes and CRM systems. The Company is committed to continuing and broadening these actions to improve the overall working environment and deliver a culture where all employees are confident their ideas and concerns are listened to and acted upon. To this end, the Company intends to hold another survey in May 2018 and is focused on improving the response rate, particularly in the departments of Transport and Warehouse, so it can better ascertain the views of all its employees.

EMPLOYEE ASSISTANCE PROGRAM

The Employee Assistance Program ('EAP') was introduced in November 2017 as a continuum to improving employees' wellbeing and in response to employee feedback. Delivered via a company called LifeWorks, EAP is a confidential telephone and internet/app-based service available to all employees and their immediate families providing advice, information and support on a range of issues spanning the categories of Work, Health, Life, Family and Money. It is designed to offer assistance and specialist support to employees and their families through difficult times should they need it.

COST OF LIVING PAY AWARD

The cost of living award is designed to benefit employees through helping offset the effect of inflation and the rising cost of living. For 2017, the Company elected to award a cost of living increase of 2.0% to base salary to all its UK employees earning £42,500 or below. The Company has determined to award an increase of 2.0% for 2018 to all employees, with the exception of the Board and Senior Management team who elected not to receive it. In relation to its employees in Continental Europe, the Company followed local market practice for both 2017 and 2018.

EQUAL OPPORTUNITIES

The Company is fully committed to upholding the principles of equal opportunities in employment and in the provision of our services. The Company's policy is to ensure that no job applicant or employee, whether permanent, temporary, part time, fixed term, or former receives more or less favourable treatment on the grounds of gender, gender reassignment, sexual orientation, marital or civil partnership status, colour, race, nationality, ethnic or national origins, religion or belief, age, disability, pregnancy or maternity, or is disadvantaged by a provision, criterion or practice which cannot be shown to be justifiable. As the Company has businesses in Continental Europe, the policies 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 the Company's responsibilities under the Disability Discrimination Act. Where practicable, subject to the nature of the Company's activities, employees who develop a disability during employment are given the opportunity to retrain for alternative employment within the Group. The policy applies equally to the treatment of the Company's customers, suppliers and members of the public.

Recruitment and selection criteria and procedures will ensure that potential and current employees are selected, promoted, trained and treated on an equal basis and that all individuals are treated with dignity and respect.

Each individual associated with the Company, is individually responsible for implementing the Company's commitment to the principle of equality.

The Company will not tolerate acts of unlawful discrimination or harassment and all instances of such behaviour or alleged behaviour will be treated seriously, be fully investigated and may result in disciplinary proceedings (up to and including dismissal).

The Company's recruitment, training and development processes are designed to ensure that it has suitably skilled and qualified employees to meet the operational needs of the business. The Company recognises 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. The Company is committed to developing the potential of its people, offering opportunities for employees to develop and grow and periodically reviewing succession planning processes.

HUMAN RIGHTS

The Company is committed to improving its practices to combat slavery and human trafficking.

It understands that the issue of slavery and human trafficking is a global issue and that no business sector will be able to eliminate or be free of slavery within their supply train without working collaboratively within its industry. The Company has a zero tolerance to slavery and human trafficking and will strive to eliminate any slavery and human trafficking found to be in its supply chain.

The Company sources an extensive range of floorcovering products including carpet, residential vinyl, wood, laminate, luxury vinyl tile, rugs, underlay and commercial flooring. In 2017, following the acquisition of Domus, the business of the enlarged Group diversified into ceramics and increased its presence in specification services. In 2017, the Company purchased from significant suppliers based in 16 countries. As for 2016, in 2017 over 90% of purchases were from suppliers in the EU.

The Company is committed to ensuring that there is no modern slavery or human trafficking in its supply chains or in any part of the business. This reflects the commitment to acting ethically and with integrity in all business relationships and to implementing and enforcing effective systems and controls, working towards ensuring that slavery and human trafficking is not taking place anywhere in the Company's supply chains.

As part of the Company's initiative to identify and mitigate risk, representatives from the Company visit suppliers and inspect their manufacturing facilities. During 2018, the Company will maintain its regular schedule of overseas visits to ensure anti-slavery practices are being monitored, reviewed and maintained within the supply chain. Greater internal training will be given to relevant employees to help them investigate and identify slavery or human trafficking practices which are not acceptable.

Further, systems will be put in place to:

- Identify and assess potential risk areas in the supply chains.
- Mitigate the risk of slavery and human trafficking occurring in the supply chains.
- Monitor potential risk areas in the supply chains.
- Protect whistle blowers.

The Company is committed to taking the necessary steps to ensure that slavery and human trafficking are not taking place in its businesses and seeks to gain transparency within the supply chain. Further information on activities will be made available on the Company's website.

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 it expects all employees and individuals that work at its sites to follow health and safety policies and procedures and be free from substance abuse at all times.

ANTI-BRIBERY AND CORRUPTION

It is the Company's policy to conduct all business in an honest and ethical manner. The Company takes a zero-tolerance approach to bribery and corruption and is committed to acting professionally, fairly and with integrity in all business dealings and relationships.

The policy applies to all employees, directors, officers, agency workers, seconded workers, volunteers, interns, agents, contractors, external consultants, third-party representatives and business partners. Any individual who breaches the policy will face action, which in the case of employees could result in dismissal for gross misconduct. Any non-employee who breaches the policy may have their contract terminated with immediate effect.

Our People continued

All employees and those working for the Company are expected to ensure that the interests of the business remains paramount at all times; be impartial and honest in the conduct of their official business; use the funds and resources of the Company to the best advantage of the Company, always ensuring value for money; not abuse their position of employment for personal gain or to benefit their family or friends; and not to seek advantage or further private business or other interests in the course of their official duties.

It is strictly forbidden for an employee corruptly to accept any inducement or reward for doing or refraining from doing anything, in his or her official capacity, or corruptly showing favour, or disfavour in the handling of contracts.

Gifts must be of an appropriate type and value depending on the circumstances and taking account of the reason for the gift. Employees are required to declare and keep a written record of all material hospitality or gifts given or received and are also required to submit all expenses claims relating to hospitality, gifts or payments to third parties in accordance with the Company's expenses policy and record the reason for expenditure. All employees who are in contact with suppliers and contractors, and in particular those who are authorised to sign purchase orders, or place contracts for goods, materials or services, are expected to adhere to high professional standards.

EMPLOYEE BENEFITS

Headlam encourages and supports the financial security of its employees and offers a number of benefits including opportunities for participation in the Company's defined retirement benefit plans, 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.

Additionally, the Company operates a HM Revenue & Customs approved Save-As-You-Earn share option scheme ('SAYE'), a monthly savings scheme facilitating the purchase of shares in Headlam at a discount by eligible employees. The SAYE not only provides employees with a tax-efficient savings plan but additionally promotes a sense of ownership of the Company. During 2017, 941 eligible employees participated in the Company's SAYE schemes, equivalent to 44% of the UK workforce.

TRAINING AND DEVELOPMENT

All employees are actively encouraged to take advantage of training and development opportunities available to them, and which are considered an important part of the Company's strategy for success. In 2017, 247 UK employees attended training courses covering the areas of Health & Safety, People Management, Leadership, Communication and Selling and Influencing Skills. Additionally, the Company is proposing to launch a Sales Training Academy during 2018.

The Company utilises the services of an external driver training team for continuing professional competence training for its commercial vehicle drivers, and this team continues to deliver the Driver Certificate of Professional Competence ('CPC') training to all the Company's commercial vehicle drivers to ensure that the statutory requirement of 35 hours' CPC training for every driver over a five year period is achieved. In 2017, 408 drivers received CPC training via a course entitled 'The Professional Drivers Day'. The same trainer also delivered the Safe Urban Driving Course to 55 individuals from specific Company locations to assist in achieving further FORS Silver accreditations in the future (see Environment section on page 38). The training course for 2018 is designed to, among other things, raise understanding of vulnerable road users and how the industry and road schemes influence the safety of all road users.

The Company continues 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, transport managers and supervisors attended an Operator's Licence Awareness Training course and received refresher training on a broad range of transport compliance during 2017.

DIVERSITY

Further details on the Company's diversity policy as required by DTR 7.2.8AR is set out in the Corporate Governance statement on page 52. Headlam recognises and values highly the benefits of diversity in the workplace, and 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. Where existing employees become disabled, it is the Company's policy, wherever practicable, to provide continuing employment under normal terms and conditions and to provide training, career development and promotion wherever appropriate, and the Company gives full and fair consideration to applications for employment from disabled persons.

As at 31 December 2017, the Company had 2,427 employees of which 18% were female (2016: 17% female).

Table showing gender diversity:

Employees	Directors	Senior managers	Other	Total employees
Male	6	248	1,735	1,989
Female	–	30	408	438
Number of employees at 31 December 2017	6	278	2,143	2,427

During 2017, three females were appointed to the Senior Management Team, and post the year-end the Company appointed its first female Director to the Board.

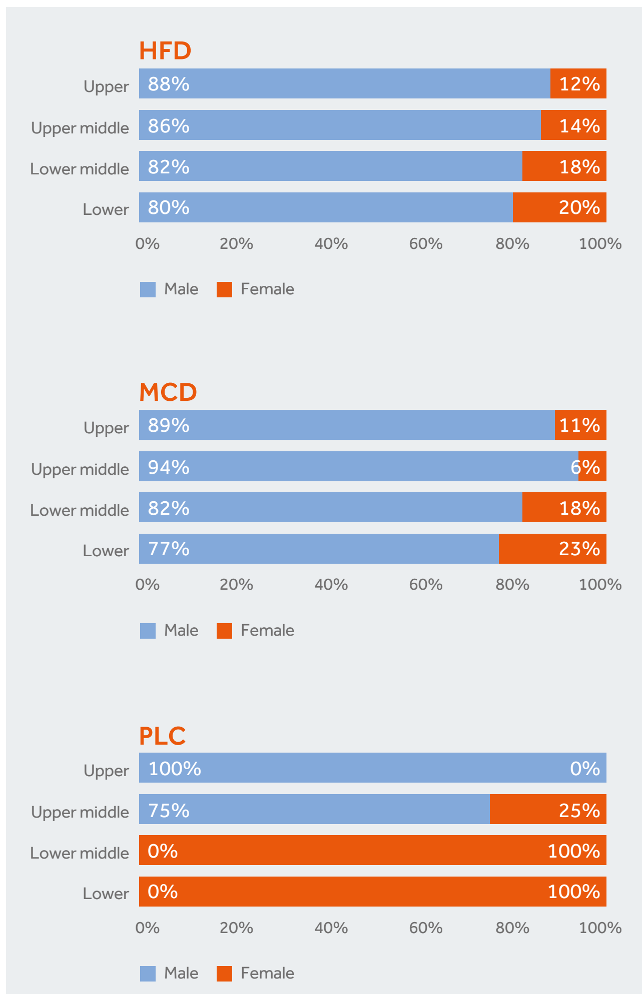
GENDER PAY GAP REPORT

In-line with the UK Government's regulations introducing mandatory gender pay gap reporting, the Company has published its Gender Pay Gap Report on the GOV.UK website (www.gov.uk) and its own website (www.headlam.com). The Report available on the two websites fully complies with the legislation but, by way of a summary, as at 5 April 2017 (the 'snapshot' date for all the data given) for the Company's two legal entities required to report under the legislation ('HFD' and 'MCD') and for the ultimate holding company ('PLC') not required to report:

- The Company's overall median pay gap was lower than the UK national average at 10.5%
- The proportion of men and women receiving bonuses:
  - HFD – men 97%, women 98%
  - MCD – men 97%, women 96%
  - PLC – men 67%, women 71%
- The bonus pay gap:

	Mean	Median
In **HFD** the bonus payment for a female is	**41.6%** lower than a male	**14.6%** lower than a male
In **MCD** the bonus payment for a female is	**44.0%** lower than a male	**24.5%** lower than a male
In **PLC** the bonus payment for a female is	**95.1%** lower than a male	**99.9%** lower than a male

- The proportion of men and women in each quartile of the Company's pay structure:

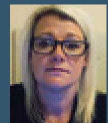


The Company is working to improve the male: female ratio across the whole Company and, as detailed above, appointed three females to the Senior Management Team during 2017 and post the year-end appointed its first female Director to the Board. In addition, it is committed to improving the balance of the workforce through both supporting the women who work for the Company moving into more senior positions and attracting more women to join.

GENERAL DATA PROTECTION REGULATION (GDPR)

The Company is in the process of ensuring that it will comply with the GDPR when it is implemented in May 2018. During the latter part of 2017 the Company identified the data processing activities in which it is engaged and is liaising with all third parties (be they customers, suppliers, employees or other third parties) involved in those data processing activities (or who may be the subject of data processing) to ensure that it will be compliant whether as data controller or data processor by the relevant time. The Company will also be putting in procedures to ensure the safety and security of the data it holds and/or processes as well as implementing new policies and providing training to employees who are engaged in roles which require them to process personal data.

Geraldine Cooney, Commercial Manager
C.K. Davie (Aberdeen)



In 1998, Geraldine began working as a contract cleaner for one of Headlam's Scottish businesses based in Glasgow. When the cleaning company Geraldine was working for went out of business, Headlam decided to employ her directly so she could continue in her cleaning role.

After 18 months, Geraldine was approached by the business asking if she would like to apply for an internal sales position as it was actively recruiting for sales people and given that Geraldine was a gregarious and well-liked member of the team, she was considered to be an ideal candidate. Having successfully applied, Geraldine began working on the sales desk during 2000 on a full-time basis and after eight years, was promoted to Sales Office Supervisor in 2008.

In 2012, Headlam acquired C.K. Davie, a business based in Aberdeen and Dundee, to enlarge its Scottish operations and Geraldine was asked if she would like to provide temporary cover to oversee the business during the weeks that followed the acquisition. After a few weeks in the cover role, Geraldine decided to ask if there was a permanent opening to manage C.K. Davie and if so, whether she could apply for the position.

To everyone's delight, Geraldine was subsequently appointed Commercial Manager of C.K Davie in 2013, which is a position she has made her own, has made successful and continues to hold to the current day.

Health & Safety

THE HEALTH AND SAFETY OF EMPLOYEES AND INDIVIDUALS LIKELY TO BE AFFECTED BY THE COMPANY'S OPERATIONS IS TREATED WITH THE UTMOST IMPORTANCE

INTRODUCTION

The health and safety of employees and individuals likely to be affected by the Company's operations is treated with the utmost importance. It is the Company's policy to ensure that operations are carried out at all times in compliance with the relevant health and safety guidance in the jurisdictions in which it operates.

Health & Safety ('H&S') is a standing agenda item at the Company's Board meetings, with an associated report submitted, and regular presentations are made to the Board and the Senior Management team. The report covers accident statistics, progress on initiatives, transport audits, assessment visits, updates on policies and procedures, and any changes in legislation that could affect the Company and its businesses. It is intended that a comprehensive review of existing policies and procedures will be undertaken during 2018 and presented to the Board for approval.

A Risk Committee (comprising the Chief Financial Officer, People Director, National Health & Safety Manager and Logistics & Compliance Director) serves as a governance body to provide oversight review and challenge of the risk management processes, and to confirm that appropriate and proportionate risk management procedures are in place. Investigations are carried out in respect of any accidents or matters warranting further detail.

Each of the Company's businesses occupying distribution facilities has a H&S Committee comprising representatives from the various business departments. These meet on a periodic basis and report quarterly to the National Health & Safety Manager. Management teams are encouraged to create a supportive H&S culture and recognise the value of employee participation.

KEY FOCUSES OF 2017

A focus of 2017 was the building of dedicated in-house H&S expertise. This will allow for more effective management of H&S, the implementation and tailoring of systems to meet the Company's specific needs, and ultimately ensure that H&S becomes embedded in the Company's culture and long-term practices. A National Health & Safety Manager and two Regional Health & Safety Advisers were appointed during 2017 and 2018 to effectively cover the Company's UK operating locations.

The new in-house team, working in conjunction with the existing outsourced provider, has already implemented a number of revised and improved policies and procedures. These include H&S compliance assessments being undertaken at all of the Company's locations on a quarterly basis at a minimum, and all business managers with responsibility for H&S completing the Institution of Occupational Safety and Health ('IOSH') 'Managing Safely' training course with periodic refresher training as necessary. During the beginning of 2018, 80 business managers completed the IOSH 'Managing Safely' course, with additionally 25 members of the Company's senior management completing the IOSH 'Leading Safely' course.

A new in-house Health & Safety Management System (that will ensure a consistent approach to risk assessments, safe systems of work, accident and near-miss reporting) is being launched in the first quarter of 2018 and implemented across the Company. It is well-recognised that reporting near-misses can significantly improve worker safety while enhancing an organisation's safety culture and induction procedures. The system will allow data to be immediately logged, analysed and any trends identified, with appropriate remedial action then taken.

80
Business managers completed the IOSH 'Managing Safely' course

25
Members of the Company's senior management completed the IOSH 'Leading Safely' course

36
AED units ('Automated External Defibrillators') were installed at the Company's larger depots in the UK in 2017

101
New commercial vehicles delivered with fall arrest systems in 2017

There were 25 reportable incidents in 2017, compared to 17 in 2016, none of which resulted in a serious injury or fatality. The uplift in reported incidents reflects the introduction of a more robust and enhanced reporting schedule in 2017. All reportable accidents are investigated and, in the infrequent 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.

In-line with a commitment outlined in the 2016 Annual Report, 101 new commercial vehicles were delivered in 2017 with fall arrest systems installed in the rear, and a further 109 are scheduled for delivery in 2018. The fall arrest system, in conjunction with the body harness worn by the driver, is designed to prevent falls by drivers unloading from the vehicle. The Company intends to continue rolling out this initiative across its whole fleet as the fleet is renewed.

Fire risk assessment is undertaken across the Company on an annual basis. During 2017, to improve activity in this area and ensure the highest level of compliance going forward, the Company undertook to enhance its processes and training in the area of fire compliance. As such, a Fire Risk Management course and training was undertaken at the end of 2017, with Diplomas in Fire Protection and Prevention to be run later in 2018.

In 2017, AED units ('Automated External Defibrillators') were installed at the Company's 36 larger depots in the UK, with people at each trained in their usage. These units are proven to be one of the most important tools in saving the life of someone suffering sudden cardiac arrest, and it is intended that units will be placed in the Company's larger Continental Europe premises currently without them during 2018.

Automated lone-working devices have recently been trialled at one site and will potentially be rolled out to other locations in 2018 where employees may be in a lone-working environment for a proportion of their time. The device provides a two-way communication with a monitoring station, with emergency assistance provided when necessary.

KEY PRIORITIES

With the aim of achieving excellence in H&S, and a clear vision for the future, the Company is undertaking a rigorous PDCA method ('plan-do-check-act') in 2018. Key priorities in the near to medium-term include continue growing the in-house expertise and systems, increase the regularity of visits to operating locations, and provide comprehensive ongoing training and support to all employees.

Environment

THE COMPANY IS COMMITTED TO IMPLEMENTING THE CORRECT POLICIES AND PROCEDURES RELATING TO THE SUSTAINABILITY OF THE ENVIRONMENT, AND MITIGATING ITS IMPACT ON THE ENVIRONMENT

INTRODUCTION

The Company is committed to implementing the correct policies and procedures relating to the sustainability of the environment, and mitigating its impact on the environment. The Company endeavours to lead by example and provides the managers of its businesses with guidance on waste reduction, recycling and consumption of utilities.

In general, and as part of its commitment to the environment, the Company is actively migrating away from paper-based systems to handheld paperless delivery and invoicing techniques.

RECYCLING & WASTE

The waste arising from the Company's operations is predominantly protective plastic packaging, cardboard poles and boxes, and wooden pallets. The cardboard poles from the centre of rolls and cut lengths of carpet and vinyl delivered to our customers are subsequently collected from their premises, with the Company providing a financial incentive to its drivers to do so. They are re-used until no longer fit for purpose and then recycled.

The Company continually seeks to increase the proportion of its waste it recycles, baling plastics and cardboard, and stacking unwanted pallets for dispatch to specialist reprocessing agents (when it is economic to do so), which has significantly reduced the quantity of waste going to landfill sites.

The Company makes a concerted effort to utilise recycled materials wherever possible in its operations. The packaging film used for broadloom at the Company's distribution hubs in Coleshill and Tamworth, and some other locations, is 100% recycled from used polyethylene. During 2018 more of the Company's locations will utilise the same material, machinery permitting.

Reflective of the Company's commitment to recycling, Headlam was awarded a trophy for 'Longstanding Support' at the Carpet Recycling UK Awards for Good Practice 2017. Carpet Recycling UK is a not-for-profit membership association working to increase the recycling of carpet waste across the UK, and Headlam is very proud to be a member and help increase awareness. According to Carpet Recycling UK, 168,000 tonnes of carpet was recovered in 2017 (for reuse, recycling or energy recovery) equivalent to a landfill diversion rate of 42%, a 7% increase on 2016 recovery, and showing strong progress towards their goal of 60% by 2020.

Within the UK, the Company seeks to ensure compliance with the Producer Obligations (Packaging Waste) Regulations 2007 (as amended). The Company is a member of an organisation called VALPACK. VALPACK provides compliance services to its members by analysing the packaging waste data submitted by each member organisation on an annual basis and comparing it with comparative data in order to be able to confirm to the Environment Agency that its members (including the Company) are continuing to meet UK recycling and recovery standards.

FLEET OPERATOR RECOGNITION SCHEME ('FORS')

The Fleet Operator Recognition Scheme (FORS) is a voluntary accreditation scheme that promotes best practice for commercial vehicle operators. FORS encompasses all aspects of safety, efficiency, and environmental protection by encouraging and training fleet operators to measure, monitor and improve performance. FORS operators demonstrate commitment to managing road risk, reducing environmental impact and improving operational efficiency, all of which improve overall fleet road safety and lessen the wider impacts of freight and fleet operations.

Six of the Company's businesses locations have achieved and hold FORS Bronze accreditation, with an additional business holding FORS Silver. It is the Company's ambition to add to this number of accreditations and progress up the membership levels as part of its commitment to achieving exemplary levels of best practice, and as FORS is rolled out nationwide beyond its original London focus.

FLEET

European emission standards define the acceptable limits for exhaust emissions of new vehicles sold in EU and EEA member states with the aim of improving air quality across the European Union. All the Company's new commercial and motor vehicles delivered since October 2014 have been compliant with the latest Euro 6 emission standards despite it having only become binding from September 2015. Currently 285 vehicles within the commercial fleet are Euro 6 compliant, and with another 75 commercial vehicles expected to be replaced during 2018, over 80% of the commercial fleet is expected to be Euro 6 compliant by the end of 2018.

The Company currently holds 12 operator licences, 11 of which have roadworthiness scores within the highest band (Green) under the Operator Compliance Risk Score ('OCRS') system developed by the Driver and Vehicle Standards Agency ('DVSA'). The OCRS roadworthiness score is concerned with the condition of a vehicle and is generated by roadside inspections that are carried out by the DVSA.

The Company is committed to assessing and improving the efficiency of its product delivery and limiting its vehicle emissions where possible.

PRODUCT SOURCING

As an importer of wood products from outside the EU, the Company has a procedure in place to comply with the requirements of the European Union Timber Regulations 2013. It applies a due diligence process to mitigate the risk of illegally sourced timber within the supply chain process and as a result is able to compile a document trail confirming that the wood products are sourced from authorised and renewable supplies. As part of this procedure, the Company also makes enquiries to ensure that the manufacturers dealt with do not use child labour or exploit children and treat their workforce fairly. The Company will always visit a factory prior to making purchases to check its operating standards and capabilities.

UTILITIES

Water, Electricity and Gas

The Company monitors greenhouse gases on a consistent basis with the aim of improving its 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.

While the Company recognises its business can have a direct and indirect effect upon the environment, owing to the nature of its operations and proactive approach when planning and developing any new facilities, the Company believes that its activities generally have a low impact on the environment. There were no environmental legal or compliance issues arising during the year.

Environment continued

Water

Water consumption arises predominantly in respect of employee welfare and commercial vehicle washing. The majority of water charges are in respect of water supplied and used. The Company encourages its drivers to keep the commercial vehicles clean and tidy and, to assist them, has a combination of jet wash machines and, at four of the largest distribution facilities, specialist truck washes. Each truck wash utilises 100% recycled water, helping with conservation, and environmentally friendly washing detergents.

The Company seeks 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.

Water consumption in 2017 of 32,112 cubic metres was consistent with 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 investing in new facilities or undertaking refurbishment or repair works.

Photovoltaic panels, installed on the roof of the Company's Coleshill distribution hub, generate an estimated 46,000 kWh of electricity. Future construction projects will similarly incorporate intelligent lighting systems and, where practical, renewable energy solutions. The Company is progressively installing more energy efficient LED units when undertaking lighting repairs and replacement.

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 hubs and centres. 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.

Electricity and gas supplies in the UK are purchased on a Company contract basis. The actual cost of electricity and gas in 2017 was comparable to prior years, and represented 0.13% of revenue.

CARBON REPORTING

The Company is 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.

	2017 CO_2 / tonnes	2016 CO_2 / tonnes	2015 CO_2 / tonnes
Electricity	**2,736**	3,457	4,348
Gas	**783**	1,052	1,010
Commercial vehicle fuel	**18,004**	19,597	18,153
Car fuel	**4,853**	4,780	4,603
Total	**26,376**	29,540	28,114
Tonnes per £1 million revenue	**37**	45	43

2017 electricity emissions decreased due in part to the continuance of the Company-wide initiative to install more LED units, as described above, in heavily trafficked areas such as the dispatch bays. In addition, the official government conversion factor for electricity has reduced from 0.41205 to 0.35156 kg CO_2 / kWh which in itself represents a 14% reduction. Electricity consumption across all Company sites (when aggregated) has reduced by 5.3%.

During 2017 an increased number of the Company's vehicles were Euro 6 compliant with Euro 6 more than halving the amount of nitrogen oxides that a diesel vehicle can emit with a cap of 80mg/km.

ENERGY SAVINGS OPPORTUNITY SCHEME ('ESOS')

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 to comply with the deadline of December 2015. Further audits are required every four years following and thus the next audit is not anticipated or required until December 2019. Due to the mix of energy, with the majority related to transport fuel, the assessment comprised an audit of the energy used by the Company's transport activities, there being no requirement to audit the energy consumed in respect of buildings and industrial processes.

Social Activities, Community and Charitable Donations

THE COMPANY IS COMMITTED TO HAVING A POSITIVE IMPACT ON THE COMMUNITIES IN WHICH ITS BUSINESSES OPERATE

The Company is committed to having a positive impact on the communities in which its businesses operate and looks to support its local communities through employment, becoming involved in local events and fundraising activities, charitable donations, sponsorships of local teams and donations of floorcovering products for specific projects. The Company encourages its businesses to support local charitable organisations, providing assistance to do so, and also has a policy in place to match individual's charity fundraisings under its Employee Donation Scheme and allow employees paid time off work to undertaken charitable duties.

Charitable donations made during the year in support of charitable causes in local communities, nationally, and those of interest to employees amounted to £33,483 (2016: £20,180). In addition, employees participated in a variety of fundraising activities and supported charities local to their businesses.

While the Company does not support a specific charity or community it has been a member of the Pennies from Heaven payroll giving scheme since 2011 and matches the charitable donation made by its employees under the scheme. In 2017, the Company made an overall contribution of £10,098.68 to Pennies from Heaven on behalf of itself and its employees.

In conjunction with the first employee survey held in 2017, the Company donated £5 on behalf of each employee who completed it, raising a total of £5,430 for the chosen charities of Cancer Research UK, Make-A-Wish UK and Age UK.

In early 2018, a member of the Board and two of the Senior Management team became members of The Worshipful Company of Furniture Makers (referred to as The Furniture Makers' Company). The Furniture Makers' Company, incorporating the Furnishing Trades Benevolent Association and one of the Livery Companies of the City of London, aims to promote, encourage and foster the craft and industry of furnishing and furniture and its ancillary activities in the United Kingdom, advance education in the industry, and relieve financial hardship of present and past employees of the industry, their families, relatives and dependents.

During March 2018, the Company will donate flooring to Sebastian's Action Trust for their second purpose-built family respite facility being built in Berkshire. Sebastian's Action Trust supports families of life-limited and seriously ill children and through its facilities offers respite holidays to very sick children and their families, enabling precious time to be spent together.

MORE
CHOICE

“Looking back on my time as a Non-Executive Director of the Company, which has spanned twelve years, I am pleased to leave a legacy of a well-managed and forward-looking Board with sound systems in place. I consider that the Board is well-equipped to take the Company forward for the benefit of all of its stakeholders.”

Dick Peters
Non-Executive Chairman

Board of Directors and Senior Management Team

1. A J Aldridge | Non-Executive Director, Board | ● ■ ▲
Amanda was appointed a Non-Executive Director in February 2018. Amanda was a partner in KPMG LLP from 1996 until 2017, when she retired from the partnership, having joined the firm in 1984 and qualified as a chartered accountant in 1987. She has significant experience as an external auditor, working predominately with quoted clients in the retail and distribution sectors. Amanda has also advised quoted companies on corporate transactions and the assessment and remediation of internal controls. She is a Fellow of the Institute of Chartered Accountants in England and Wales.

2. C E Miles | Director of Communications
Catherine was appointed Director of Communications in January 2017. Catherine was previously Corporate Broking Director at the stockbroker Arden Partners, where she was an adviser to Headlam. Catherine worked in Corporate Broking for six years advising, and raising money for, a broad spectrum of public companies predominately in the small and mid-cap space. Prior to this she was Corporate Communications Director and Company Secretary at an AIM listed company, and initially worked in the Financial PR industry.

3. P J Lawrence | Non-Executive Director, Board | ● ■ ▲
Philip was appointed a Non-Executive Director in June 2015. 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.

4. A K Eastgate | Senior Independent Director, Board | ● ■ ▲
Andrew was appointed a Non-Executive Director in May 2010. He is the Chairman of the Remuneration and Nomination 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.

5. S G Wilson | Chief Executive, Board | ■
Steve was appointed Chief Executive in September 2016, having previously been the Group Finance Director, a position he had held since joining Headlam in 1991. Steve is a Non-Executive Director of Conviviality Plc, a UK wholesaler and distributor of alcohol and impulse products, and, until his retirement from their board in 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.

6. D A Price | Commercial Director
Darryl was appointed Commercial Director in September 2016 assuming operational responsibility for the majority of Headlam's UK businesses. Darryl joined the Company in February 1994 as Sales Office Manager at Thatcham before progressing to Operations Director. From 2003 to 2015, he was the Commercial Director responsible for the businesses in Coleshill. In November 2015 he was appointed to the Senior Management Team assuming operational responsibility for an increased number of the UK businesses. Darryl has 24 years' experience in the floorcoverings industry.

Committees
| ● Audit ■ Nomination ▲ Remuneration

7. R W Peters | Non-Executive Chairman, Board | ●

Dick was appointed Chairman in September 2013, having been appointed a Non-Executive Director in 2005. 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.

8. C R Payne | Chief Financial Officer, Board

Chris was appointed Chief Financial Officer in September 2017. Chris joined from Biffa plc, the UK integrated waste management company, where he was Group Commercial Finance Director with responsibilities including overseeing all the operational finance teams and divisional Finance Directors. Chris joined Biffa plc in 2013 and was previously at Mitie Group plc from 2008 to 2013 where he held two divisional Finance Director positions. He is a qualified Chartered Accountant having trained with KPMG and is a fellow of the Institute of Chartered Accountants in England and Wales.

9. S J LaVerne | People Director

Sue was appointed People Director in October 2017. Sue joined from E.ON where she worked between 2009 and 2017 carrying out various commercial and international HR leadership roles, latterly as HR Director of the global customer solutions division. Sue started her career in retail with commercial and HR appointments including at Marks and Spencer and Arcadia Group. Sue has broad experience in all areas of HR and has contributed to external bodies, including as Chair of the Department for Work and Pensions employers steering group focused on giving more disabled people access to work

10. S L Ward | Company Secretary and Legal Counsel

Sarah was appointed Company Secretary in October 2017. Sarah brings a wealth of experience in corporate transactions, leasing and landlord relationships, planning and construction projects, and is a qualified solicitor. Sarah qualified as a corporate lawyer spending a number of years at Eversheds. She was then a partner and head of the Corporate Department at a top 100 national firm before moving to Bicester Village where she managed the legal function. Sarah joined Headlam from UK Power Reserve where she was General Counsel.

11. A R Judge | Chief Operating Officer, Board

Tony Judge was appointed Chief Operating Officer in September 2016, and in March 2017 was appointed to the Board. Tony joined the Company in 1992 as 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, he was additionally appointed Managing Director of the Tamworth businesses and took operational responsibility for the Thatcham and Stockport businesses in 2012 and Gildersome in 2015. Tony has 36 years' experience in the floorcoverings industry.

Chairman’s Introduction to Governance

This has been a year of positive change at all of the senior levels of our business. At Board level, I am pleased that my own succession as Chairman has progressed smoothly, with Philip Lawrence taking over on 1 June 2018.

The Executive membership of the Board changed during the year with the appointment of Tony Judge, appointed in March 2017, as Chief Operating Officer and Chris Payne, appointed in September 2017, as Chief Financial Officer. We augmented the Board’s numbers following a search for a new independent Non-Executive Director which successfully concluded with the appointment of Amanda Aldridge on 1 February 2018. Amanda will take over from Philip Lawrence as chair of the Audit Committee from 1 June 2018. In addition, we intend to recruit a further Non-Executive Director during the early part of 2018.

During the year we added to the Senior Management team with the appointment of a new Director of Communications and People Director and filled our vacant Company Secretary position.

Against this backdrop of change, we have retained our view that good governance remains essential in order to deliver our strategic priorities, as well as supporting sustainable growth, an enhanced contribution to and from our stakeholders and ultimately protecting shareholder value. The Board’s commitment to this prioritisation has been reflected in the amount of time that it has supported the Executive Board members in their review of strategic, cultural and stakeholder issues (which are commented on further in this report).

Our Board evaluation this year was through an internal review process, further details of which are included on page 51. The Board is focused on the need to review and continue to develop its effectiveness, in order to support the Company in its ambitions.

During the year, the governance processes of the Company at executive level were overhauled, with the Executive Directors meeting with the Senior Management team more regularly and with a specific focus on vision and strategy and the instigation of processes designed to introduce and foster a winning culture among our employees. The section on the Board’s Activities in 2017 demonstrates the degree to which the Board has engaged in these developments and provided appropriate levels of input.

Together with the reports from each of the Nomination, Remuneration and Audit Committees, this section of the Annual Report provides an overview of our key governance activities and practices during the last year.

As I have mentioned above, I will be stepping down as Chairman of the Board on 31 May 2018. Looking back on my time as a Non-Executive Director of the Company, which has spanned twelve years, I am pleased to leave a legacy of a well-managed and forward-looking Board with sound systems in place. I consider that the Board is well-equipped to take the Group forward for the benefit of all of its stakeholders.

Dick Peters
Non-Executive Chairman

6 March 2018

The Board's Activities 2017

AN OVERVIEW OF SOME OF THE ACTIVITIES OF THE BOARD DURING 2017 IS SET OUT BELOW.

Those with an asterisk are new initiatives of the current enlarged and refreshed Board and Senior Management team. There is now greater breadth and communication at the senior levels of the business and this is reflected in the pro-active approach of the business to change. During the year, specific activities of the Board included the following:

BOARD AND SENIOR MANAGEMENT STRUCTURE

- Approving the promotion of Tony Judge to Chief Operating Officer and the appointment of Chris Payne as the new Chief Financial Officer
- Overseeing the induction process for new Board directors
- Overseeing the development of the Senior Management team with the appointments of Catherine Miles, Director of Communications, Sue LaVerne as People Director and Sarah Ward as Company Secretary
- Reviewing succession plans for all Directors and members of senior management
- Discussions on the relevant skills required on the Board and progression of the search for a new Non-Executive Director culminating with the successful appointment of Amanda Aldridge*

STRATEGY AND MANAGEMENT

- Requesting that the Executive Directors and Senior Management team undertake a wide strategic review of the business which has led to: the creation of a group vision; the start of a five-year strategic plan to include profit improvement, market consolidation and entry into parallel markets in order to expand the customer offer; and the development of 5 strategic pillars around growth, customers, dynamic model, margin improvement and culture and ethos
- Supporting the implementation of the five-year plan

INTERNAL CONTROLS AND RISK MANAGEMENT

- Undertaking a review of the Group's internal control and risk management systems and seeing progress in the establishment of a new Executive Risk Committee
- Support for an enhanced health and safety capability and focus*
- Support of the assessment of core IT and technology risks*
- Assessment of capital investment in property and acquisitions
- Receiving and considering reports on compliance with financial, regulatory, corporate responsibility and environmental commitments

GOVERNANCE AND STAKEHOLDER ENGAGEMENT

- Ongoing interaction with shareholders and the wider investment community
- Appointment of a dedicated Director of Communications to facilitate the interface with shareholders*

OPERATIONS AND MATERIAL TRANSACTIONS

- Review and approval of the Group's growth strategy and plans
- Approval of the acquisition of Mitchell Carpets Limited in February 2017*
- Approval of the acquisition of McMillan Flooring Limited in April 2017*
- Approval of the acquisition of Domus Group of Companies Limited in December 2017*
- Review of a pipeline of strategic acquisitions and growth of the Group's distribution network
- Programme of visits around the Group's operations and projects in the UK and continental Europe

FINANCIAL AND PERFORMANCE REPORTING

- Approval of the Group's annual and half-year results
- Review of the Group's ongoing capital management strategy
- Review and approval of the dividend policy and approval of the interim and final proposed dividend
- Reviews of the Group's performance against KPI's
- Reviews of the Group's operating and project performance
- Approval of the Group's 2018 budget

Corporate Governance Report

Our governance framework helps the Company in the delivery of its strategic priorities and ensures that its obligations to its shareholders and others are understood and met. The Non-Executive Directors are tasked with challenging the decisions of the Executive Directors and their mix of skills and backgrounds allow a range of deliberations to take place.

COMPLIANCE STATEMENT

This corporate governance statement, together with the Nomination Committee report on pages 52 to 53, the Audit Committee report on pages 54 to 59 and the Directors Remuneration Report on pages 60 to 73, provides a description of how the main principles of the 2016 edition of the UK Corporate Governance Code (the 'Code') have been applied within the Company during 2017. The Code is published by the Financial Reporting Council and is available on its website at www.frc.org.uk.

It is the Board's view that, throughout the financial year ended 31 December 2017, the Company complied with the relevant provisions set out in the Code.

This statement complies with Rule 7 of the Disclosure Rules and Transparency Rules of the Financial Conduct Authority with the information required to be disclosed by sub-section 2.6 of Rule 7 being shown on pages 74 to 77.

The Board is the Company's principal decision making body. The schedule of matters reserved for the Board, which was last reviewed on 6 April 2016, is available on the Governance section of our website, www.headlam.com. It includes matters relating to strategy, capital expenditure, acquisitions and risk management. An overview of the main duties, roles and responsibilities of the constituent members of the Board are set out below.

CHANGES TO THE BOARD

Amanda Aldridge was appointed to the Board as a Non-Executive Director on 1 February 2018. In accordance with the Articles of Association, Amanda will retire from the Board at the first AGM following her appointment and stand for election. The Directors consider her 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. Chris Payne was appointed Chief Financial Officer on 13 September 2017. In accordance with the Articles of Association, Chris 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.

The Directors consider that following the appointment of Amanda Aldridge as an additional Non-Executive Director, the size of the Board continues to be appropriate for the Company's size and listing. However, for the purposes of orderly succession and for expansion of the Board in line with the Company's growth aspirations, the Board will continue to look to recruit a further Non-Executive Director early in 2018.

ROLES, RESPONSIBILITIES AND DUTIES WITHIN THE BOARD – AT A GLANCE SUMMARY

The Board as a whole

- Collectively accountable for running the Group's affairs
- Responsible for promoting the success of the business of the Group
- Reviews key activities of the business on a monthly basis and at additional meetings when required
- Responsible for setting the strategy

Chairman

- Primary responsibility for leading the Board and ensuring its effectiveness
- Ensures other Directors make an effective contribution and, through the Company Secretary, that the Directors receive accurate and timely information
- Chairs Board meetings
- Role and responsibilities are clearly divided from those of the Chief Executive

Non-Executive Directors

- Particular responsibility for discussing and critically examining proposed strategies
- 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, participation in committees, questioning the delivery of strategic objectives and monitoring operational and financial performance

Executive Directors

- Responsible for implementing the strategy
- Organic growth and M & A – identifying opportunities and pursuing them to successful completion
- Have regard to employee interests, fostering of business relationships and impact of operations on the community and environment
- Approval of the annual operating plan and capital expenditure budget

Chief Executive

- The Chief Executive is responsible for leading the strategy and running the businesses in accordance with the policies and plans approved by the Board, leading the executive team, setting the culture and tone from the top for the Group and for communications with stakeholders and shareholders
- Matters that are not specifically reserved for the Board and its Committees under their terms of reference or for shareholders in general meetings are delegated to the Chief Executive

As at 31 December 2017 the Board comprised:

Non-Executive Chairman	Executive Directors	Independent Non-Executive Directors
Dick Peters	Steve Wilson, Chief Executive	Andrew Eastgate, Senior Independent Director
	Chris Payne, Chief Financial Officer	Philip Lawrence
	Tony Judge, Chief Operating Officer	Amanda Aldridge*

* On 1 February 2018 Amanda Aldridge was appointed as a Non-Executive Director of the Board.

Directors' attendance during the year at Board meetings is set out on page 50 with all Directors attending all meetings to which they were invited, and attendance at meetings of the Audit, Nomination 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. It is not considered that there is any conflict of interest or imbalance of duties by virtue of Steve Wilson holding this appointment.

The Board considers the balance achieved between Executive and Non-Executive Directors, following the recruitment of Chris Payne as Chief Financial Officer and Amanda Aldridge as Non-Executive Director as appropriate and effective for the control and direction of the business.

The Directors bring strong judgement to the Board's deliberations and the size and balance of skills and experience of the Board are considered appropriate for the requirements of the business and the size of the Company. The Board has considered the independence of the Non-Executive Directors and consider that all three (excluding the Chairman) 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 Chairman and 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.

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 Company, each of the Directors is required to retire by rotation at least once every three years. Chris Payne and Amanda Aldridge are seeking election and Steve Wilson and Philip Lawrence are seeking re-election at the forthcoming AGM.

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

Corporate Governance Report continued

BOARD MEETINGS AND ATTENDANCE

The Board met nine times in the year, at times that ensure the latest operating information is available for review or when key strategic decisions need to be made and when 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, Non-Executive Directors have substantial contact between meetings and endeavour to visit trading locations in order to maintain contact with the Group's wider employee base and review operations first-hand. 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	9/9
Tony Judge	7/7*
Chris Payne	4/4*
Dick Peters	9/9
Andrew Eastgate	9/9
Philip Lawrence	9/9

* Appointed to the Board part-way through the year, attended all eligible meetings. Amanda Aldridge was appointed as a Non-Executive Director on 1 February 2018

DIRECTORS' CONFLICTS OF INTEREST

Procedures are maintained by the Board whereby potential conflicts of interests are reviewed regularly. These procedures have been designed so that 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 Company's Articles of Association. The Board has not had to deal with any conflict during the period.

Directors holding significant commitments outside of the Company 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.

INDUCTION AND TRAINING AND DEVELOPMENT

When joining the Board, induction programmes are tailored for each individual Director. A comprehensive information pack is compiled which includes:

- background information about the Company;
- briefings on Directors' duties and responsibilities;
- information on Board meeting procedures;
- Board minutes;
- internal policies;
- structure charts;
- matters reserved for the Board;
- financial budgets;
- shareholder and other stakeholder feedback; and
- Committee terms of reference.

The information pack also includes an explanation of the Group's financing structure and relevant statutory and regulatory guidance notes, including the Code and the Company's share dealing policy.

An induction programme will include briefings on general strategy and other matters, site visits, and one-to-one meetings with all relevant colleagues, including other Directors and members of the Senior Management team as well as with advisers including the Company's Stockbrokers and Auditor.

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 Company's expense.

The Non-Executive Directors are encouraged to further their knowledge of the Company by spending time with the Executive Directors, the members of the Senior Management team and other senior managers on site visits. Non-Executive Directors are also encouraged to engage with people across the business to further enhance their understanding of the business.

PERFORMANCE EVALUATION 2017

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.

In 2017, an evaluation of the Board's effectiveness, including the effectiveness of the Board Committees, was undertaken internally. In 2018, an evaluation will be undertaken externally given the change process that the Board is currently within.

The 2017 evaluation concluded that the Board and its Committees continued to operate effectively, meeting the requirements and spirit of the Code. Since the evaluation, the Board has improved its functions and processes, including through:

- Provision of more comprehensive Board papers, additionally provided on an earlier basis;
- More in-depth financial evaluation of proposed capital expenditure projects and investments; and
- Introducing a greater breadth of skills and expertise to call upon for advice through appointments at the Board, Senior Management team and senior managerial level.

BOARD COMMITTEES

The Board has established Audit, Nomination 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 in the Governance section of the Company's website.

NOMINATION COMMITTEE

Information on the activities of the Nomination Committee is given in the Nomination Committee Report on pages 52 to 53 which should be read in conjunction with this report.

AUDIT COMMITTEE

Information on the activities of the Audit Committee is given in the Audit Committee Report on pages 54 to 59 which should be read in conjunction with this report.

REMUNERATION COMMITTEE

The Directors Remuneration Report is set out on pages 60 to73. The report also includes the Annual Report on Remuneration which is subject to an advisory vote at the 2018 AGM.

THE ANNUAL GENERAL MEETING

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 will 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 and in accordance with the Code a separate resolution on each substantially separate issue will be proposed. The Company 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 2018 AGM are set out in the circular to shareholders sent separately to this document and incorporating a Notice of Annual General Meeting.

Nomination Committee Report

I am pleased to present the Nomination Committee Report for 2017 which has seen both new Board appointments and appointments to the Senior Management team as follows:

- Catherine Miles as Director of Communications in January 2017
- Tony Judge as Chief Operating Officer in March 2017
- Chris Payne as Chief Financial Officer in September 2017
- Sarah Ward as Company Secretary in September 2017
- Sue LaVerne as People Director in October 2017
- Amanda Aldridge as Non-Executive Director (appointed in February 2018)

MEMBERSHIP AND ATTENDANCE AT MEETINGS HELD IN 2017

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

Members	Meetings attended	Eligible to attend
Dick Peters	3	3
Philip Lawrence	3	3
Andrew Eastgate	3	3
Steve Wilson	3	3

*Dick Peters will be resigning from the Nomination Committee on 31 May 2018. Amanda Aldridge was appointed on 1 February 2018.

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

PERFORMANCE EVALUATION AND SUCCESSION

Ahead of 2017'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.

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

2017 AND 2018 FOCUS

Board succession planning continued to be a key focus for the Nomination Committee in 2017. In 2018 the Nomination Committee will continue to pursue the recruitment of a further Non-Executive Director.

RE-ELECTION AND EVALUATION

As part of its role, the Nomination 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 Nomination Committee during the year to enable it to discharge its duties in accordance with its terms of reference included proposals to re-elect Steve Wilson and Philip Lawrence under the retirement by rotation provisions and Philip Lawrence's appointment as Chairman on 1 June 2018 in succession to Dick Peters.

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, 4, 5 and 6 at the 2018 AGM (which are the resolutions relating to Chris Payne, Amanda Aldridge, Steve Wilson and Philip Lawrence).

TERMS OF REFERENCE

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

BOARD DIVERSITY POLICY

The approach to Board diversity is unchanged. The Company continues to take note of the guidance provided and to make appointments on the basis of merit. However, it recognises the benefit that greater diversity can bring and takes into account such factors when considering any particular appointment. The Company has now appointed the first female director to the Board.

ADVICE

The Nomination Committee has access to such information and advice, both from within the Company and externally, at the cost of the Company, 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. The Company engaged PGC as a consultant in the recruitment of Chris Payne and Ridgeway Partners as a consultant in the recruitment of Amanda Aldridge. Neither PGC nor Ridgeway Partners is or has been connected in any other way with the Company.

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

Andrew Eastgate
Chairman of the Nomination Committee

6 March 2018

Audit Committee Report

As Chairman of the Audit Committee I am pleased to present the Audit Committee's Report for the year ended 31 December 2017. The Audit Committee has undertaken its work knowing that the Group has operated without a Chief Financial Officer until September 2017 but has taken assurance from knowing that there is an underlying risk management and control process, driven by detailed financial oversight from the head office and close operational knowledge from the Chief Executive and Chief Operations Officer. The additional capabilities within the new Senior Management team have enhanced the assessment and management of risk that would otherwise threaten the business model, future performance, solvency or liquidity of the Group.

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

The Audit Committee (as well as the Board as a whole) continues to monitor changes in the Group's key risks and welcomes the five pillar strategy that will help the Group to mitigate the risks presented from market demand, competitors, technology and people. The mitigation of risk within regulation, particularly relating to operational health and safety matters has been enhanced during the year. To ensure that it remains appropriate and provides a robust assessment of the principal risks, the Audit 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 Audit Committee has reviewed the proposed internal controls and the detailed audit plan for the next 12 months, both of which will assist the Group in achieving its strategic objectives by improving the effectiveness of risk management, control and governance processes.

PricewaterhouseCoopers ('PwC') were appointed as auditors in 2016 following a full tender exercise. The Audit Committee believes that PwC have to date provided an effective audit service in line with their proposal and commitments at the time of the audit tender and recommends their reappointment to shareholders at the forthcoming AGM.

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

From 1 June 2018 it is intended that Amanda Aldridge will be appointed as Chair of the Audit Committee when I take on the role of Chairman of the Board.

Philip Lawrence
Chairman of the Audit Committee

6 March 2018

AUDIT COMMITTEE

The Audit Committee has an agenda linked to events in the Company's financial calendar, normally meeting at least twice a year before the final and interim results announcements. The Audit Committee met three times in the year and attendance was as follows:

Members	Meetings attended	Eligible to attend
Philip Lawrence	3	3
Dick Peters	3	3
Andrew Eastgate	3	3

*Dick Peters will step down from the Audit Committee on 31 May 2018. Amanda Aldridge was appointed on 1 February 2018.

During the year the Audit Committee discharged its responsibilities as set out in the terms of reference and schedule of business for the year. Whilst only members of the Audit Committee are entitled to be present at meetings, the Auditor, Chief Executive and Chief Financial Officer may attend by invitation. The Audit 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 Company. The full terms of reference of the Audit Committee, which were reviewed during 2017, can be found in the governance section of the Company's website, www.headlam.com.

ROLE OF THE AUDIT COMMITTEE

The Audit 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 members of the Senior Management team on key financial control matters;
- the consistency of and any changes to the Group's accounting policies and the application of appropriate accounting standards and methods used to account for significant or unusual transactions;
- the appointment, reappointment or dismissal of the Auditor
- the integrity of the interim and annual financial statements, including a review of the significant financial reporting judgements contained therein;
- the effectiveness of the audit process;
- the Auditor's plan for the audit of the Group's accounts, confirmation of the 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 Auditor and management's response to any major audit recommendations;
- reports from management and the 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 application of the Board's policy on non-audit work performed by the Auditor together with the non-audit fees payable to the 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 AUDIT 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 Audit Committee has chosen to focus.

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

Internal controls and risk	Auditor	Financial Reporting
Considered reports from management and the 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 Auditor and their fees.	Reviewed the half year and annual financial statements and the significant financial reporting judgements.
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's half yearly and full year accounts on a going concern basis and reviewed the related disclosures in the annual report and accounts. Reviewed a viability statement that assesses the prospects of the Group over a three-year period. The Audit Committee considered that the Group's existing three-year financial planning view makes that time period the most appropriate.
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 Auditor and their effectiveness.	Reviewed reporting disclosures in relation to internal controls, risk management, principal risks and uncertainties and the work of the Audit Committee.

Audit Committee Report continued

Internal controls and risk	Auditor	Financial Reporting
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.

The Audit Committee has also considered during the year the impact of changes to accounting standards which are to be introduced and in particular IRFS 15 the new revenue recognition standard and IRFS 9 the new accounting standard which introduces a new classification approach for financial assets and liabilities, given that the comparative periods for these accounting standards commence from 1 January 2017. In addition, the Audit Committee has considered the timetable for adoption of IFRS 16 which sets out the principles for the recognition, measurement, presentation and disclosure of leases for annual periods beginning on or after 1 January 2019.

KEY ISSUES CONSIDERED BY THE AUDIT COMMITTEE

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

- acquisition accounting;
- supplier arrangements;
- inventory valuation; and
- valuation of employee benefit liabilities.

These issues were discussed with management during the year and with the Auditor at the time the Audit Committee reviewed and agreed the Auditor's Group audit plan and presented its findings at the conclusion of its year end audit.

ACQUISITION ACCOUNTING

The Group made a significant acquisition toward the end of 2017, which has resulted in the creation of goodwill, intangible assets and a judgment over the useful economic life of each category of intangible asset. The Audit Committee reviewed management's calculation of the consideration and the intangible assets, challenged the assumptions used in arriving at each category of asset and assessed the useful economic lives over which to amortise the assets. The Audit Committee is satisfied the values reflected for goodwill and intangible assets are based on appropriately robust assumptions and that the amortisation charge appropriately reflects the useful economic lives of the intangible assets.

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 Audit 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 Audit Committee challenged the assumptions used by management and reviewed the level of cash receipts or credit notes received after the year end. The Audit Committee is satisfied that the amounts recognised have been appropriately scrutinised and that the assumptions upon which the calculation was based are sufficiently robust.

INVENTORY VALUATION

As set out in the statement of financial position, inventory amounts to £131.5 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 may result in some inventory lines becoming slow-moving or obsolete, such that the recoverable amount is less than the carrying value.

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

VALUATION OF EMPLOYEE BENEFIT LIABILITIES

In the UK, the Company operates a defined benefit pension scheme (the 'Scheme'), further details of which are set out in note 20 to the financial statements. At 31 December 2017, the Scheme had assets of £116 million and liabilities, measured on an IAS 19 basis, of £126.3 million, with a net deficit of £9.7 million.

As set out in note 20 to the financial statements, the Scheme 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. Further, the liabilities for the Scheme were measured using both IAS 19 and the Trustees provisional Technical Provisions basis for the 31 March 2017 actuarial valuation date (as opposed to 31 December 2017). 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 Scheme. Management highlighted to the Audit Committee how they arrived at the key assumptions.

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

MISSTATEMENTS

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

After reviewing the presentations and reports from management and consulting, where necessary, with the Auditor, the Audit 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 Audit 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.

RISK MANAGEMENT AND INTERNAL CONTROL

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

- meets the needs of its customers;
- maintains proper relationships with suppliers and contractors;
- provides a safe and healthy workplace;
- 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 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 also allow for assurances to be provided at each level of management up 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 failings or weaknesses, which in any case 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 adversely 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 is 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 employee 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.

An Executive Risk Committee (comprising the Chief Financial Officer, People Director, Company Secretary, National Health and Safety Manager, and Logistics and Compliance Director) serves as a governance body to provide oversight, review and challenge of the risk management processes, and to confirm that appropriate and proportionate risk management procedures are in place. Investigations are carried out in respect of any accidents or matters warranting further detail. The work of the Executive Risk Committee will be reviewed by the Audit Committee going forward.

The Group promotes a high standard of health and safety management at all levels supported by training programmes at operating businesses. The Group's approach to Health & Safety is detailed on pages 36 to 37 of the Strategic Report.

Audit Committee Report continued

INTERNAL AUDIT

In accordance with the Code, the Audit Committee has undertaken an assessment of the need for a Group internal audit function. The Audit 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 Audit Committee will continue to review the need on an annual basis.

EXTERNAL AUDIT

The Audit Committee reviews annually the appointment and performance of the Auditor and considers their independence and objectivity taking into account all appropriate guidelines. Following a review of PwC's performance and independence in 2017, including compliance with rules on non-audit services, the Audit Committee was satisfied with the Auditor's effectiveness and independence.

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

The Audit Committee has the specific task of keeping the nature and extent of non-audit services provided by the Auditor under review in order to ensure that objectivity and independence are maintained. The Auditor has processes in place to ensure independence is maintained when providing non-audit services and has written to the Audit 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 Auditor were considered by the Audit Committee. The Audit Committee recognises that there are occasions when it is advantageous to use the Auditor to undertake non-audit services, where they are best placed to do so. Non-audit fees paid to the Auditor should not exceed 70% of the audit fee. The Chairman of the Audit 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. Non-audit fees of £91,000 were incurred in respect of financial due diligence services in relation to the acquisition by the Company of the entire issued share capital of The Domus Group of Companies Limited.

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

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 Auditor reviews the consistency between the narrative reporting and financial disclosures.

WHISTLEBLOWING POLICY

The Company has 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.

SUMMARY

The Audit 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 Audit Committee Chairman will be available at the AGM to answer any questions on the work of the Audit Committee.

ENGAGEMENT WITH SHAREHOLDERS

The Company places considerable importance on communication with shareholders. Ongoing engagement with shareholders and the wider investment community, including analysts and investors not currently holding shares in the Company, is essential to their understanding of the Company; their ability to appraise the performance and management of the Company; and consideration of the Company as an investment proposition.

As more fully detailed on page 31 of the Strategic Report, the Company offers its larger shareholders, either directly or via its broker, face-to-face meetings on a bi-annual basis at a minimum, to present and discuss performance and other matters, and obtain any feedback. These meetings are hosted by several of the Executive Directors and the Company's Director of Communications. The Company also retains a Financial PR and IR adviser (Buchanan) to facilitate interaction and support its communication with shareholders and other members of the investment community.

Meetings are also periodically held with shareholders at various Group locations to help illustrate the Group's operations and aid understanding. Non-Executive Directors, including the Chairman, attend certain events and briefings during the year in addition to the AGM where shareholders are present, and the Non-Executive Directors are committed to facilitating a direct channel of communication with the Group's larger shareholders to hear any views and concerns.

The Company actively seeks shareholder feedback, and feedback is collated by both the Company and its advisers, discussed at Board and Senior Management team level and considered in relation to all aspects of the Group which helps inform its written and verbal communications.

Directors Remuneration Report

THE CHAIRMAN'S ANNUAL STATEMENT

On behalf of the Board, I am pleased to present the Directors Remuneration Report for 2017, which features this statement and the Report on Remuneration for the year ended 31 December 2017. At the 2017 AGM, shareholders voted in favour of the adoption of the current remuneration policy with over 99% of the votes in support for both adoption of the policy and the Annual Report on Remuneration. The policy was designed to simplify the previous remuneration structure and encourage long term focus on sustained business improvement. Also, at the 2017 AGM, a new long-term incentive plan (the 'PSP' as defined below) was adopted with 97.26 % of the votes cast voting in favour of the PSP and additionally a deferred bonus plan (the 'DBP' also defined below) was adopted with 99.53 % of the votes cast voting in favour of the DBP.

As is noted elsewhere, the Company made a significant number of senior appointments during 2017, both internal and external.

I am pleased to say that our new policy has enabled and supported us in making appropriate changes to the Board in line with our succession plans. It has provided the Remuneration Committee with a simple framework focused on sustained business improvement. Key features are:

- Maximum bonus opportunity of 125% of base salary.
- The introduction of 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 the Deferred Bonus Plan ('DBP').
- A new Performance Share Plan ("PSP") with a maximum opportunity of 100% of salary, although awards in 2017 and 2018 have been set at 80% of salary. The PSP includes a two-year holding requirement after the awards vest.
- A maximum pension contribution (or cash allowance in lieu of pension) of up to 15% of salary for future hires.
- Clarity on our shareholding guidelines, which require that Executive Directors build up and maintain a shareholding in the Company equivalent in value to 200% of annual salary .

BUSINESS PERFORMANCE AND INCENTIVE OUT-TURN FOR 2017

The Company continued to grow in 2017 despite softer market conditions compared with 2016, showing a 2.0% growth in revenue and improvement in margins which resulted in reported 2017 underlying profit before tax of £43.1 million, an improvement of 7.5% on 2016. Bonus earned, based on this underlying profit before tax, was 65.82% of the maximum. Two thirds of this will be paid in cash and one third deferred into shares which must be held for a further two years from the date on which the annual bonus payout is determined.

DIRECTOR CHANGES

As explained in the Directors Remuneration Report last year, Tony Judge was appointed to the Board as Chief Operating Officer on 31 March 2017 and his salary was set at £425,000 reflecting the extension of his existing responsibilities and the scope of his new role. This rate of salary was payable with effect from 1 January 2017. Chris Payne joined the Board as Chief Financial Officer in September 2017 and his annual salary was set at £325,000 with an agreement that it would increase to £350,000 with effect from 1 March 2018, subject to performance (which will equate to £346,000 over the 12 months to 31 December 2018). Chris forfeited variable pay arrangements when he left his previous role and the Company therefore agreed to pay a bonus of £133,000. In addition, Chris was granted awards under the PSP equal to 80% of salary on joining the Company with the same performance conditions as for all other 2017 PSP participants.

Philip Lawrence will become Chairman of the Board from 1 June 2018. The Board considered what was an appropriate market competitive fee so that the Company could secure the best candidate for the role. Accordingly fees for the Chairman were set at £143,500 to take effect upon appointment.

PSP AWARDS IN 2017

Awards under the PSP were granted during 2017 to the Executive Directors (each such award equating to 80% of salary) using a share price of 536.8 pence. Further details of the awards and the performance conditions attaching are set out on page 67.

REMUNERATION FOR 2018

Other than in respect of Chris Payne whose annual salary increased from £325,000 per annum in 2017 to £350,000 per annum in 2018 with effect from 1 March 2018 (because his salary was set at a lower rate for the first six months of his employment and increased thereafter), none of the Executive Directors will receive any increase in base salary for 2018.

All aspects of variable pay will remain unchanged in 2018 with the same structure applying as the Remuneration Committee considers that this continues to be appropriate.

CONCLUSION

We believe that the combination of a holding period on the PSP, the deferral into shares under the annual bonus scheme, and the shareholding guidelines aligns Executive Director interests with the interests of shareholders and provides a beneficial long-term framework for our business.

We remain committed to a responsible approach to executive pay as I trust that this Directors Remuneration Report demonstrates. As always, I am happy to meet or speak with shareholders if there are any questions or feedback on our approach to executive remuneration.

Andrew Eastgate
Chairman of the Remuneration Committee

6 March 2018

KEY PRINCIPLES OF THE REMUNERATION POLICY

The table below sets out a summary of the policy for Executive Directors.

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.
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 Remuneration 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 Remuneration 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 ('SAYE')	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 continued

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 was 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 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 based on EPS performance and 20% 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 continued

MALUS AND CLAWBACK

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

For up to two years following the payment of an annual bonus award, the Remuneration 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 Remuneration 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 Executive's 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.

CONSIDERATION OF EMPLOYMENT CONDITIONS ELSEWHERE IN THE GROUP

The Remuneration 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.

NON-EXECUTIVE DIRECTORS

Purpose and link to strategy	Approach of the Company
Fees are set at a level that reflects market conditions and are sufficient to attract individuals with appropriate knowledge and experience.	Fees are normally reviewed annually and approved by the Board. Fees may include a basic fee and additional fees for further responsibilities (for example, chairmanship of committees or holding the office of Senior Independent Director). Fees are based on the level of fees paid at similar-sized UK listed companies and the time commitment and contribution expected for the role. Overall fees will remain within the limits set by the Articles of Association. Non-Executive Directors cannot participate in any of the Company'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 Remuneration 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 Remuneration Committee considers to be stretching performance.

For 2018, 100% of the annual bonus award will be based on underlying 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 2018 will be based on Earnings Per Share ('EPS') 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 Remuneration Committee does not consider it reflective of the overall financial performance of the Group over the performance period.

The Remuneration 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 Remuneration 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

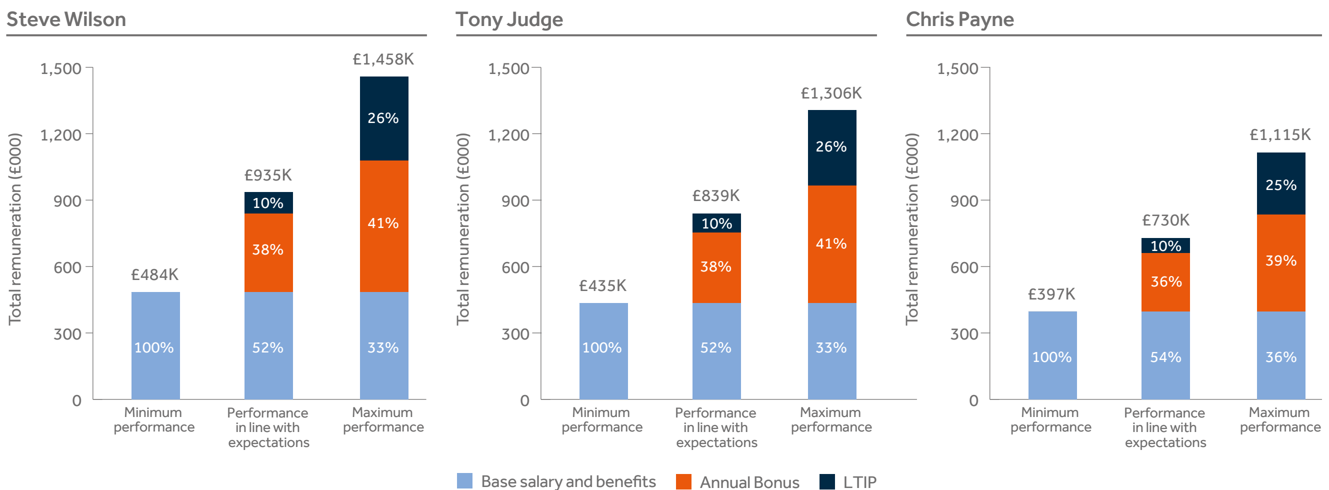
The Remuneration Committee retains the discretion to operate the Company's share plans in accordance with their terms, including the ability to adjust awards and options in the event of a variation of share capital, demerger, delisting, special dividend or other event that may affect the Company's share 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 charts below set out for the Chief Executive, Chief Operating Officer and Chief Financial Officer an illustration of the application for 2018 of the remuneration policy set out above. The charts show 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). As Chris Payne was only a Director from September 2017, his benefits figure has been assumed to be the same as for Steve Wilson.



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, benefits and pension.	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.

SERVICE AGREEMENTS

Executive Directors' service agreements are on a rolling basis and may be terminated on 12 months' notice by the Company or the Director. A new service agreement was entered into by Tony Judge on 31 March 2017 following his appointment as Chief Operating Officer and Executive Director of the Board effective from that date, having formerly been Commercial Director (not statutory) since 2012. Chris Payne entered into a service agreement with the Company on 13 September 2017 following his appointment as Chief Financial Officer and Executive Director of the Board effective from that date. Chris Payne is to be proposed for election at the 2018 AGM.

All Non-Executive Directors currently have fixed-term agreements by way of letters of appointment 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. Philip Lawrence will enter into a new fixed term agreement with regard to his appointment on 1 June 2018 as Chairman of the Board, subject to his re-election as a Director of the Company at the 2018 AGM. This agreement will be terminable by either party on three months' notice.

Amanda Aldridge was appointed to the Board as a Non-Executive Director on 1 February 2018 and entered into a fixed term agreement with the Company for a term of three years subject to earlier termination by either party on three months' notice.

Directors Remuneration Report continued

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 Remuneration Committee seeks to ensure that arrangements are in the best interests of the Group and not to pay more than is appropriate.

The Remuneration 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 Remuneration Committee will typically align the remuneration package with the above policy. The Remuneration 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 Remuneration 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 Company's policy to allow reasonable relocation, travel and subsistence payments. Any such payments will be at the discretion of the Remuneration Committee.
- The Remuneration Committee may also alter the performance measures, performance period, vesting period, deferral period and holding period of the annual bonus or PSP, if the Remuneration 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 Company'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 Remuneration 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 Remuneration 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 Remuneration 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.

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

Non-Executive Director	Date of appointment	Expiry of current term
Dick Peters	1 December 2005	31 May 2018*
Andrew Eastgate	17 May 2010	May 2019**
Philip Lawrence	1 June 2015	31 May 2018***
Amanda Aldridge	1 February 2018	31 Jan 2021****

* Mr Peters is due to step down from the Board on 31 May 2018 after 12 years as a member of the Board and will not therefore be standing for re-election.

** Mr Eastgate was re-elected at the 2017 AGM.

*** It is intended that Mr Lawrence will be appointed as Chairman of the Board on 31 May 2018. Mr Lawrence is to be proposed for re-election as a Director at the 2018 AGM. The fee payable to Mr Lawrence from 1 June 2018 has been set at £143,500 per annum which the Remuneration Committee considered to be an appropriate rate and which was market competitive to secure Mr Lawrence's services as Chairman.

**** Amanda Aldridge was appointed to the Board on 1 February 2018 and will be proposed for election at the AGM.

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 2017 and 2016.

Executive Directors remuneration as a single figure – 2017 (audited)

Executive Directors	Base salary/ fees 2017 £000	Non-salary benefits 2017 £000	Annual performance bonus 2017 £000	Share-based incentive schemes 2017 £000	Pension related benefits 2017 £000	Other 2017 £000	Total 2017 £000
Steve Wilson	**475**	**9**	**391**	**245**	**–**	**–**	**1,120**
Tony Judge*	**319**	**10**	**350**	**218**	**–**	**–**	**897**
Chris Payne**	**95**	**8**	**–**	**–**	**11**	**133**	**247**
	889	**27**	**741**	**463**	**11**	**133**	**2,264**

* Tony Judge was appointed as an Executive Director on 31 March 2017 and his annual salary was set at £425,000 although this was effective from 1 January 2017. The table above reflects the pro-rata amount of salary received since his appointment but 100% of annual bonus and amount in respect of share based incentive schemes.

** Chris Payne was appointed as an Executive Director on 13 September 2017 on an initial salary of £325,000. The figures above for Chris Payne reflect the pro-rata amounts received since his appointment. Chris Payne forfeited variable pay arrangements when he left his previous role and the Company therefore agreed to pay a bonus of £133,000 when he commenced his employment with the Company.

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

Executive Directors	Base salary/ 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
Steve Wilson	403	15	386	263	–	–	1,067
Tony Brewer	393	16	–	328	–	1,143	1,880
	796	31	386	591	–	1,143	2,947

* Tony Brewer resigned as a Director on 14 September 2016.

* Steve Wilson was appointed as Chief Executive on 14 September 2016 although his salary was not increased to reflect his new appointment until 1 January 2017.

* Share based incentives vested in respect of performance to the year ended 31 December 2016 in the form of Co-Investment Plan ("CIP") awards. These CIP awards granted on 1 April 2014 vested on 1 April 2017. The mid-market closing share price on 3 April 2017 was 623 pence and this is the share price that has been used to calculate the values above.

The table below reports the total remuneration receivable in respect of qualifying services by each of the Non-Executive Directors for the years 2017 and 2016.

Non-Executive Directors remuneration as a single figure – 2017 (audited)

Non-Executive Directors	Base fees 2017 £000	Non-salary benefits 2017 £000	Annual performance bonus 2017 £000	Share-based incentive schemes 2017 £000	Pension related benefits 2017 £000	Total 2017 £000
Andrew Eastgate	**55**	**–**	**–**	**–**	**–**	**55**
Philip Lawrence*	**45**	**–**	**–**	**–**	**–**	**45**
Dick Peters	**110**	**–**	**–**	**–**	**–**	**110**
	210	**–**	**–**	**–**	**–**	**210**

* Philip Lawrence's fees during 2017 were paid to the Coal Authority, which releases him to perform his duties as a Non-Executive Director.

Directors Remuneration Report continued

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

Non-Executive Directors	Base/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*	45	–	–	–	–	45
Dick Peters	110	–	–	–	–	110
	210	–	–	–	–	210

* Philip Lawrence's fees during 2016 were 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 2016 and £55,000 per annum during 2017 which he retained.

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 and from the date of appointment, respectively, for each of Tony Judge and Chris Payne).
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 and from the date of appointment, respectively, for each of Tony Judge and Chris Payne). These are car 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 in respect of duties as an Executive Director including the value attributable to shares awarded under the DBP as part of the bonus earned that year.
Pension related benefits	The amount of employer contribution to a scheme based on a fixed percentage of base salary.
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.

Base salaries and fees

The Executive Directors received no increase to their base salary in 2017. A cost of living increase of 2% of base salary was otherwise awarded in 2017 to all UK employees of the Group earning less than £42,500 per annum.

No changes were made to Chairman or Non-Executive Directors fees in 2017.

		2017 £000	2016 £000	Increase %
Chairman fee		**110**	110	0%
Base fee		**40**	40	0%
Additional fee for	– Chairmanship of the Remuneration Committee	**5**	5	0%
	– Chairmanship of the Audit Committee	**5**	5	0%
	– Senior Independent Director	**10**	10	0%

Annual performance bonus

For 2017, the Executive Directors were awarded a maximum annual bonus opportunity equal to 125% of salary. The bonus was assessed against a Group underlying Profit Before Tax performance metric. The following table sets out the bonus earned by the Executive Directors for 2017 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%	£37.1m	£41.9m	£50.28m	£43.118m	65.82%

The bonus paid to Chris Payne formed part of his take on arrangements under which he was compensated for bonus and incentives foregone from his previous employment. Under this arrangement it was agreed that his bonus for 2017 would be £133,000 paid in cash.

Share based payments vesting in respect of the financial period

Awards granted under the CIP in 2015 vested in respect of the performance year ended 31 December 2017. The awards were subject to two performance conditions, based on EPS growth (80% of the award) and relative TSR (20% of the award). The performance outcome and consequent vesting was as follows:

EPS growth	EPS CAGR over three years	TSR Relative performance against FTSE Small Cap
Threshold: 0:6 : 1 match	3% + RPI	Median
Maximum: 2: 1 match	6% + RPI	Upper quartile
Outcome	10.8%	Ranked 78th
Vesting	100% of EPS element	87.58% of TSR element
Proportion of award vesting	80%	17.5%

	Shares granted	Shares vesting	Value of shares vesting
Steve Wilson	44,124	43,028	£244,614
Tony Judge	39,326	38,349	£218,014
Tony Brewer	34,667	33,806	£192,187

Value is based on the average share price for the final quarter of the financial year which was 568.5p based on the mid-market closing share price. The awards for Tony Brewer are pro-rated to reflect the terms of his exit under which he retained his CIP shares.

PSP awards granted during the financial period

PSP awards were granted to the Executive Directors in 2017 subject to EPS and TSR metrics.

	Number of shares under option	Value of Award £000	% of salary	Date of Grant	Holding period
Steve Wilson	70,789	380	80	5 July 2017	2 years
Tony Judge	63,338	340	80	5 July 2017	2 years
Chis Payne	48,435	260	80	25 September 2017	2 years
	182,562	980			

The share price used to determine the number of shares under the PSP was 536.8 pence, being the average mid-market closing share price for the five business days prior to the date of Steve Wilson and Tony Judge's award. The same share price was used to determine the number of shares under Chris Payne's award.

There are two performance conditions attaching to the PSP award: an EPS condition which accounts for 80% of the award and a TSR condition which accounts for 20% of the award.

The EPS target required for maximum vesting was set at 8% annual growth over the three years to 31 December 2019. This is above current consensus market expectations and above the internal business plan and at a level which the Remuneration Committee considers to be appropriate given the level of stretch within the forecast numbers. Threshold performance at which 25% of the award vests is EPS growth of 5% per annum. The Remuneration Committee is satisfied that the EPS target range appropriately reflects business risks and uncertainties.

The amount of the award which vests is also based on a TSR condition. The TSR for the period of three financial years commencing with the financial year in which the award is granted is calculated for both the Company and a comparator group. The comparator group is constituted from the companies making up the FTSE SmallCap Index (excluding investment trusts) at the start of the relevant period of three financial years. If the Company's TSR is below the median TSR for the comparative group then none of the award is vested. If the Company's TSR is equal to the median of the TSR of the comparator's group then 25% of the award shall vest. If the Company's TSR is between the median and upper quartile of the TSR of the comparator's group then between 25% and 100% of the award shall vest on a straight-line basis. If the Company's TSR is above the upper quartile of the TSR of the comparators group then 100% of the award shall vest.

Directors Remuneration Report continued

Dilution

The Remuneration Committee supports the Investment Association ('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 Company's usage of shares against the limits detailed above in respect of the all employee schemes was 0.84% of the issued share capital (excluding treasury shares) and in respect of grants under discretionary plans was 0% of issued capital (excluding treasury shares). It is the Remuneration Committee's intention that options exercised under the SAYE scheme will continue to be satisfied by shares held in treasury.

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

Pension related benefits

No Executive Director received any pension benefit during the financial period other than Chris Payne who received pension contributions from the Company equivalent to 11% of his base salary from the date of his appointment

Payments to past Directors

No payments were made to past Directors during the financial period other than in respect of Tony Brewer who resigned as a Director on 14 September 2016. Tony Brewer was permitted to retain his CIP awards under the terms of the plan rules and the 2014 policy and the awards made to him under the 2014 CIP vested pro-rated for time served at the normal vesting date subject to the outcome of the relevant performance metrics. Under the 2014 CIP granted on 1 April 2014 Tony Brewer was granted an award over 59,222 ordinary shares of which a proportionate award of 53,386 ordinary shares vested. Similarly, Tony Brewer was permitted to retain CIP awards awarded in 2015 and 2016 and these awards will also vest pro-rated subject to the outcome of the relevant performance metrics.

Statement of Directors' shareholding and share interests (audited)

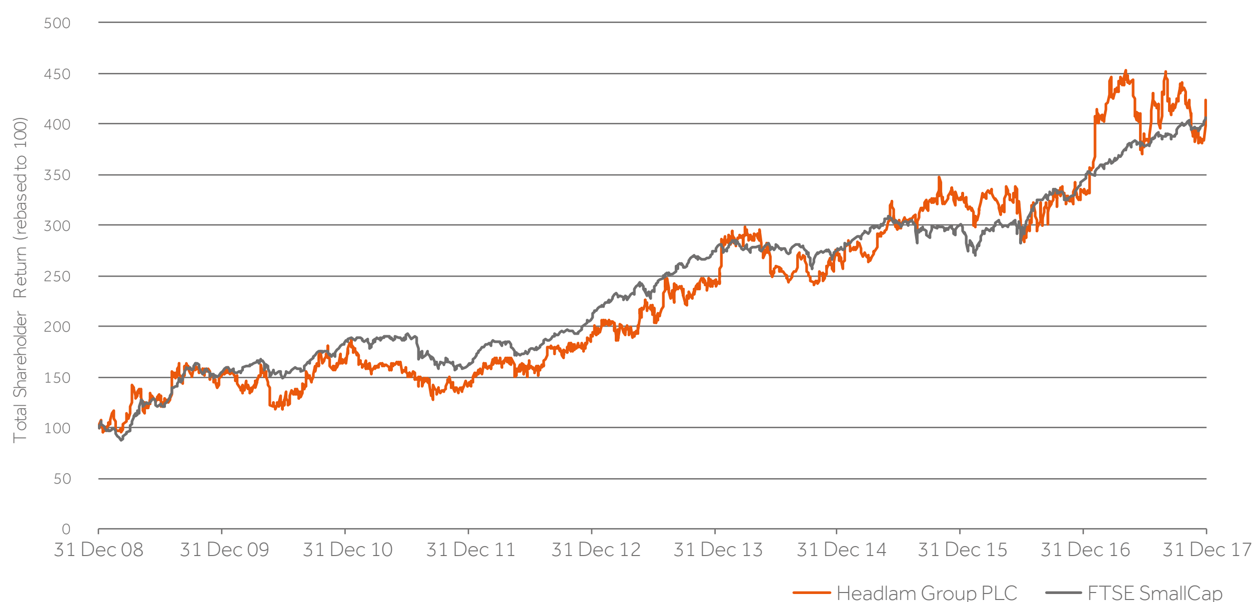
In order to align the interests of the Executive Directors with those of the Company's shareholders, the Remuneration Committee is keen to encourage Executive Directors to increase their shareholdings in the Company. The Executive Directors are required to have a beneficial interest (including family) in the ordinary shares of the Company 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 Company's share plans until the guideline is met.

The interests of Directors and their connected persons in the Company's ordinary shares as at 31 December 2017 were as set out below. So far as the Company is aware there have been no changes to those interests between 31 December 2017 and the date of signing of these financial statements and reports.

	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 2017
Steve Wilson	Ordinary Shares	–	–	–	614,244	–	–	–	614,244*
Steve Wilson	PSP Shares	5 July 2017	Nil	536p	–	70,789	–	March 2020	70,789
	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 SAYE	8 May 2014	381p	476p	–	–	7,874	July 2019	7,874
Tony Judge	Ordinary Shares	–	–	–	115,696	–	–	–	115,696
	PSP Shares	5 July 2017	Nil	536p	–	63,338	–	March 2020	63,338
	2016 CIP	6 May 2016	Nil	477p	–	36,567	–	May 2019	36,567
	2015 CIP	1 May 2015	Nil	466p	–	39,326	–	May 2018	39,326
	2015 SAYE	5 May 2015	400.2p	461p	–	–	8,823	July 2020	8,823
Chris Payne	PSP Shares	25 Sept 2017	Nil	536p	–	48,435	–	March 2020	48,435
Andrew Eastgate	Ordinary Shares	–	–	–	1,000	–	–	–	1,000
Philip Lawrence	Ordinary Shares	–	–	–	–	–	–	–	–
Dick Peters	Ordinary Shares	–	–	–	5,000	–	–	–	5,000

* Steve Wilson as at 31 December 2017 held shares in excess of the shareholding guideline (based on the Company's closing mid-market share price on 31 December 2017).

The graph below shows the value at 31 December 2017 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 Company being a constituent member within the Household Goods & Home Construction sector. This allows comparison of the Company's performance against the performance of the Index as a whole.

Chief Executive remuneration table

The table below sets out the remuneration of the Chief Executive for the previous nine 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 %
2017	Steve Wilson	1,120	65.82	97.5
2016	Steve Wilson	1,067*	76.8	98.6
	Tony Brewer	737**	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 Company's employees as a whole between the financial periods 2017 and 2016.

Percentage increase/(decrease) in remuneration in 2017 compared with 2016	Chief Executive*	Total Employees
Salary and fees	15.2%	2%
All taxable benefits	0%	0%
Annual bonuses	1.2%	(13 %)

* The increase in Steve Wilson's remuneration between the financial periods 2017 and 2016 is reflective of his promotion to Chief Executive.

Directors Remuneration Report continued

Relative importance of spend on pay

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

	2017 £000	2016 £000	% change
Dividends	**25,729**	22,464	14.5%
Overall expenditure on pay	**94,204**	96,772	(2.65%)

Statement of implementation of remuneration policy in 2018

Details of how the Company will operate the remuneration policy in 2018 is provided below (subject to shareholder approval of the Directors Remuneration Report for the year ended 31 December 2017).

Base salaries and fees for 2018

Other than in respect of Chris Payne whose annual salary increased from £325,000 per annum in 2017 to £350,000 per annum in 2018 with effect from 1 March 2018 (equating to £346,000 over the 12 months ending 31 December 2018) because his salary was set at a lower rate for the first six months of his employment and increased thereafter, none of the Executive Directors will receive any increase in base salary for 2018.

	2018 £000	2017 £000	Increase %
Steve Wilson	**475**	475	0
Tony Judge	**425**	425	0
Chris Payne	**346**	325	6

There are no increases to Non-Executive Director fees for 2018 save in respect of the appointment of Philip Lawrence as Non-Executive Chairman who will receive a fee of £143,500 per annum upon his appointment as Non-Executive Chairman from 1 June 2018. In addition, Amanda Aldridge who joined the Board as Non-Executive Director with effect from 1 February 2018 will be paid a fee of £45,000 per annum rising to £52,500 per annum on 1 June 2018 when she assumes the role of chair of the Audit Committee.

Annual bonus

The maximum annual bonus opportunity for 2018 will remain at 125% of salary. The bonus will be subject to the Company's underlying Profit Before Tax performance. 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

Awards in respect of 2018 will be granted in the form of nil cost options over ordinary shares at the level of 80% of salary, subject to EPS and TSR metrics as described below:

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.

Remuneration Committee activity

The Board approved the terms of reference delegating certain responsibilities to the Remuneration Committee. The terms of reference are reviewed periodically, most recently in April 2016, and are available on the Group's website within the Governance section at www.headlam.com. The Remuneration Committee comprises the Chairman and each of the other Non-Executive Directors and attendance was as follows:

Members	Meetings attended	Eligible to attend
Philip Lawrence	5	5
Dick Peters*	5	5
Andrew Eastgate	5	5

* Dick Peters will step down from the Remuneration Committee on 31 May 2018. Amanda Aldridge was appointed to the Remuneration Committee with effect from 1 February 2018.

Other Directors may attend Remuneration Committee meetings by invitation but no one attending a Remuneration Committee meeting may participate in discussions relating to their own terms and conditions of service or remuneration.

The Remuneration Committee 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 the Senior Management team.
- Approving the design and operation of the Company's short-term and long-term incentive arrangements. This includes agreeing the targets that are applied to awards made to Executive Directors and the Senior Management team.
- Administering share plans as required.

Matters discussed at the five meetings of the Remuneration Committee were as follows:

Meeting Date	Key agenda items
16 January 2017	Approval of letter to substantial shareholders consulting on proposed new remuneration policy Approval of new form of service agreement for Executive Directors
1 March 2017	Approval of documents for SAYE
31 March 2017	Feedback from consultation on new remuneration policy from substantial shareholders Approval of remuneration package for Tony Judge on his appointment to the Board Approval of deferred bonus rules and PSP rules for submission to AGM CIP vesting Annual bonus targets for 2017
8 June 2017	Implementation of the PSP and grant of the first award
20 Sept 2017	Grant of a PSP award to Chris Payne

Advisers

Deloitte LLP were appointed as advisers to the Remuneration Committee in October 2016 to advise on the new remuneration policy and on an ongoing basis. Deloitte's fees in respect of advice to the Remuneration Committee during the period ended 31 December 2017 were £16,750 excluding VAT 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 Company 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 Remuneration Committee is satisfied that all advice received was objective and independent.

The Remuneration Committee also receives input and advice from the Company Secretary and the People Director.

Statement of shareholders' votes

The following table sets out the results of the advisory vote on the 2016 Annual Report on remuneration at the 2017 AGM and binding vote on the remuneration policy at the 2017 AGM. The table also sets out the votes cast in favour of adopting each of the Performance Share Plan and the Deferred Bonus Plan.

	For %	Against %	Withheld
2016 Directors Remuneration Report	99.51	0.49	310,202
2017 Remuneration Policy	99.34	0.66	160,202
2017 Deferred Bonus Plan	99.53	0.47	3,899
2017 Performance Share Plan	97.26	2.74	122,728

This report has been approved by the Board of Directors and signed on its behalf by Andrew Eastgate, Chairman of the Remuneration Committee.

Andrew Eastgate
Chairman of the Remuneration Committee

6 March 2018

Other Statutory Disclosures

The Directors present their report, together with the audited financial statements, for the year ended 31 December 2017. This report, which has been prepared solely for the Company'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 46 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 acquisition of the entire issued share capital of Domus Group of Companies Limited ('Domus') on 7 December 2017 significantly increased the Company's presence in the commercial specification market to supplement and complement the Company's core activities. Domus is the UK's leading specification consultant and supplier of hard surfaces for premium construction and refurbishment projects. The principal activity of the Company is that of a holding company and its subsidiaries are listed on page 128. Further details of the Group's activities and future plans are set out in the Strategic Report on pages 9 to 41.

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 2006 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 41, which is 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 48 and is incorporated into this report by reference.

ACQUISITIONS AND POST BALANCE SHEET EVENTS

Details of the Domus acquisition and other acquisitions made in 2017 and post the balance sheet date are given in note 24 to the financial statements, which should be treated as forming part of this report.

RESULTS AND ORDINARY DIVIDENDS

The results for the year and financial position at 31 December 2017 are shown in the Consolidated Income Statement on page 84 and Statements of Financial Position on page 86.

An interim ordinary dividend of 7.55p per share (2016: 6.70p) was paid on 1 January 2018 to shareholders on the register at the close of business on 1 December 2017. The Directors propose a final ordinary dividend of 17.25p per ordinary share (2016: 15.85p), to be paid on 6 July 2018 to shareholders on the register of members at the close of business on 1 June 2018, the associated ex-dividend date being 31 May 2018.

This would bring the total ordinary dividend for the year to 24.80p per ordinary share (2016: 22.55p). The payment of the final ordinary dividend is subject to shareholder approval at the Annual General Meeting ('AGM').

SHARE CAPITAL

As at 31 December 2017, the issued share capital of the Company comprised a single class of ordinary shares of 5p each.

The Company's ordinary shares are listed on the Main Market of the London Stock Exchange. No ordinary shares were issued during the year and there were no additions to treasury shares. The reduction in treasury shares related to transfers in connection with the SAYE scheme. The balance of shares in treasury stock following the transfers during 2017 was 512,230 ordinary shares of 5p each.

Details of the Company'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 of Associate and the Companies Act 2006, shares may be issued with such rights or restrictions as the Company may by ordinary resolution determine or, if the Company has not so determined, as the Directors may decide. There are, however, no restrictions on the transfer of securities in the Company, 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'), and the Market Abuse Regulation, whereby certain employees require the approval of the Company to deal in the Company's shares.

On a show of hands at a general meeting of the Company 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 Company's website after the meeting. The holders of ordinary shares are entitled to receive the Annual Report and Accounts, to attend and speak at general meetings of the Company, to appoint proxies and to exercise voting rights. The Company is not aware of any agreements between holders of securities that may result in restrictions on voting rights. Further shareholder information is available in the Notice of AGM which contains explanations as to the resolutions proposed..

Subject to certain limits, at the AGM on 25 May 2017, the Directors were granted general authority to allot shares in the Company together with an authority to allot shares in the Company in connection with a rights issue and in respect of cash without first offering them to existing shareholders. 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 which is contained in a separate circular to shareholders.

At the AGM on 25 May 2017, the Company was given the authority to purchase shares in the Company up to 10% of the issued share capital.

Whilst no shares have been purchased under the buyback authority by the Company during the year, the Directors will be seeking to renew this authority for the Company to purchase its ordinary shares at the forthcoming AGM.

Further details are set out in the Notice of AGM sent in a circular to shareholders.

DIRECTORS

Biographies of Directors currently serving on the Board are set out on pages 44 and 45.

Changes to the Board during the period are set out in the Corporate Governance Report on page 48. Details of Directors' service agreements are set out below and in the Directors Remuneration Report on page 65.

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

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/ service agreement	Effective date of current letter of appointment/ service agreement	Next due for re-election
Executive Directors				
Steve Wilson	December 1991	n/a	3 March 2017	May 2018
Tony Judge	31 March 2017	n/a	31 March 2017	May 2020
Chris Payne	13 September 2017	n/a	13 September 2017	May 2018
Non-Executive Directors				
Dick Peters*	1 December 2005	1 December 2005	10 March 2015	n/a
Andrew Eastgate	17 May 2010	27 April 2010	17 May 2014	n/a
Philip Lawrence	1 June 2015	18 June 2015	1 June 2015	May 2018
Amanda Aldridge	1 February 2018	12 January 2018	12 January 2018	May 2018

* Due to retire on 31 May 2018

CHANGE OF CONTROL

The Group has entered into certain agreements that may take effect, alter or terminate upon a change of control of the Company 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 Company following a takeover taking place.

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

SUBSTANTIAL INTERESTS IN VOTING RIGHTS

Notifications of the following voting interests in the Company's ordinary share capital had been received by the Company (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 Company was notified; however, notification of any change is not required until the next notifiable threshold is crossed.

Other Statutory Disclosures continued

The table below reflects the notifications received by the Company up to 1 March 2018 (being the latest practical date prior to the date of this report).

ORDINARY SHARES OF 5 PENCE EACH

	1 March 2018 aggregate total voting rights	% of total voting rights at 1 March 2018	Indirect/direct
Franklin Templeton Institutional, LLC	13,532,822	15.95	indirect
Heronbridge Investment Management LLP	4,209,552	5.04	direct
BlackRock Inc	n/a	below 5%	indirect
Ruffer LLP	4,217,009	4.97	direct
Rathbone Brothers plc	4,070,078	4.87	indirect
Aggregate of Standard Life Aberdeen plc affiliated management entities	4,290,191	5.05	indirect
Investec Asset Management Limited	4,213,538	4.97	indirect
Canaccord Genuity Group Inc	2,770,314	3.27	indirect

Pursuant to DTR 5.1.2 a person must notify the issuer of the percentage of the voting rights he holds as shareholder or holds or is deemed to hold through his direct or indirect holding of financial instruments (or a combination of such holdings) if the percentage of those voting rights reaches, exceeds or falls below 3%, 4%, 5%, 6%, 7%, 8%, 9%, 10% and each 1% threshold thereafter up to 100%.

RIGHTS UNDER EMPLOYEES' SHARE SCHEMES

As at 31 December 2017, 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'), which was approved by shareholders on 20 June 2008, held 341,891 shares, approximately 0.4% of the issued share capital of the Company, 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 512,330 shares, approximately 0.6% of the issued share capital of the Company, 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 Company carrying special rights with regard to control of the Company.

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 Company or any of its subsidiary undertakings, other than service agreements between each Executive Director and the Company. In addition, the Company 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 Company's Articles of Association. This provision extends to include the Directors of Headlam Group Pension Trustees Limited, a corporate trustee of the Scheme, 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 agreements, and interests in the shares of the Company are set out in the Directors Remuneration Report.

MODERN SLAVERY STATEMENT

We support the aims of the Modern Slavery Act and have published our disclosure on our website. Following further investigations of our supply chain we will be updating our disclosure.

ENVIRONMENTAL POLICY AND MANDATORY GREENHOUSE GAS EMISSIONS REPORTING

Our environmental policy is included within the Strategic Report. 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 treatment of 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 Accounts is given on page 78 and a statement by the Auditor on their responsibilities is given on page 83.

POLITICAL DONATIONS AND EXPENDITURE

The Company'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 Company nor its subsidiaries made any political donations or incurred political expenditure in the financial period under review (2016: £nil).

CHARITABLE CONTRIBUTIONS

Details are given on page 41 of the Corporate Responsibility section of the Strategic Report.

AMENDMENT OF ARTICLES OF ASSOCIATION

The Company's Articles of Association 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 119 to 124.

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 12. In addition, note 23 to the financial statements on pages 119 to 124 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.

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 84 to 129 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 2018 AGM.

AGM

This year's AGM will be held at the Company's distribution facility in Coleshill on Thursday, 24 May 2018 at 10.00 am. The notice convening this meeting is in a separate document to this Annual Report and Accounts along with the explanatory notes regarding the resolutions that will be proposed at the meeting.

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

Sarah Ward
Company Secretary

6 March 2018

Company registration number: 460129

Statement of Directors Responsibilities

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 and Parent Company financial statements, both 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 the Company and of the profit or loss of the Group and the 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 have been followed for the Group financial statements and for the Company's 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 a going concern basis unless it is inappropriate to presume that the Group and the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group and the Company's transactions and such that they disclose with reasonable accuracy at any time the financial position of the Group and the Company. Adequate accounting records enable the Directors 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 the 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 Company's website at www.headlam.com. 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 the 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 Company's financial statements, which have been prepared in accordance with IFRSs, 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, 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 the 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 Corporate Governance Report is approved:

- so far as the Director is aware, there is no relevant audit information of which the 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 Auditor is aware of that information.

Independent auditors' report to the members of Headlam Group plc

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

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 the Parent Company's affairs as at 31 December 2017 and of the Group's profit and the Group's and the Parent Company's cash flows for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union and, as regards the Parent Company's financial statements, as applied in accordance with the provisions of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements, included within the Annual Report and Accounts (the "Annual Report"), which comprise: the Group and Company Statements of Financial Position as at 31 December 2017; the Consolidated Income Statement and Consolidated Statement of Comprehensive Income, the Group and Company Cash Flow Statements, and the Group and Company Statements of Changes in Equity for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

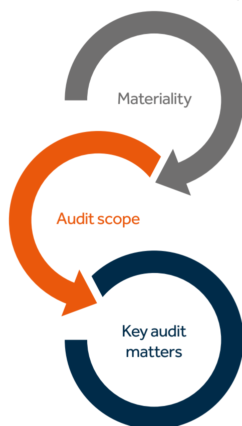
We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

Other than those disclosed in note 3 to the financial statements, we have provided no non-audit services to the Group or the Parent Company in the period from 1 January 2017 to 31 December 2017.



OUR AUDIT APPROACH

Overview

- Overall Group materiality: £2 million (2016: £1.91 million), based on 5% of profit before tax.
- Overall Parent Company materiality: £1.9 million (2016: £1.8 million), based on 0.8% of total assets.

- 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 86% of consolidated revenue and 97% of consolidated operating profit.
- In addition, limited scope audit procedures were performed on three further reporting companies based in the UK, France and Switzerland for group reporting purposes.

- Supplier arrangements.
- Acquisition accounting for Domus – fair value of acquired assets and liabilities

The scope of our audit

As part of designing our audit, we determined materiality and assessed 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.

We gained an understanding of the legal and regulatory framework applicable to the Group and the industry in which it operates, and considered the risk of acts by the Group which were contrary to applicable laws and regulations, including fraud. We designed audit procedures at group and significant component level to respond to the risk, recognising that the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. We focused on laws and regulations that could give rise to a material misstatement in the Group and Parent Company financial statements, including, but not limited to, Companies Act 2006, the Listing Rules, Pensions legislation and UK tax legislation. Our tests included, but were not limited to, review of the financial statement disclosures to underlying supporting documentation and enquiries of management, component teams and professional advisors. There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it.

We did not identify any key audit matters relating to irregularities, including fraud. As in all of our audits we also addressed the risk of management override of internal controls, including testing journals and evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

Independent auditors' report to the members of Headlam Group plc continued

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.

Key audit matter	How our audit addressed the key audit matter
Supplier arrangements Refer to the Audit Committee Report on page 56 and the use of estimates and judgements in the Accounting Policies on page 91. 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 co-terminus 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 requesting confirmations from the counterparty. For those balances where no counterparty confirmation was received, we recalculated the amount due based on the supporting purchase agreements and tested the calculation inputs back to underlying financial records. 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 balances accrued at the previous year end. No material inconsistencies or exceptions were noted.
Acquisition accounting for Domus– fair value of acquired assets and liabilities Refer to the Audit Committee Report on page 56 and the use of estimates and judgements in the Accounting Policies on page 91. On 7 December 2017, Headlam Group plc acquired 100% of the share capital of Domus Group Limited and its subsidiary entities for consideration of £29.1m. Headlam Group plc has also made two smaller acquisitions during the year, but we have focused our work on the largest acquisition due to its relative size and significance to the Group as a whole and the relative immateriality of the other acquisitions. We focused our work on this area as the accounting for the acquisition is inherently judgmental as it requires the directors to exercise judgement and use estimates in order to value consideration, identify and value intangible assets, and assess the fair value of other assets and liabilities, as well as the calculation of associated goodwill.	We read the sale and purchase agreement in order to understand the nature of the transaction and ensure that relevant clauses that impact the accounting had been considered by the directors. We tested the fair values ascribed to intangible assets by understanding the assumptions adopted in the valuation model, which include the forecast attrition rate in relation to existing customers, the expected longevity of the customer relationships, royalty revenue rates and the financial forecasts. We evaluated the assumptions, utilising the work of valuation experts where appropriate, and confirmed that the directors have adopted reasonable assumptions in each circumstance. For the remaining fair values of other assets and liabilities, we evaluated the assessment and calculation of material assets and provisions to check that they are accurate and reflect information that was known in relation to events that existed at the transaction date. We reviewed the basis of the deferred and contingent consideration and verified the expected future performance to the directors' forecasts and the underlying agreements to conclude that the basis of recognition was reasonable. We consider the directors' assessment of the provisional fair value of the opening balance sheet to be supportable.

We determined that there were no key audit matters applicable to the parent company to communicate in our report.

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 structure of the Group and the Parent Company, the accounting processes and controls, and the industry in which they operate.

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 Limited and Headlam Group plc (the Company). These reporting companies were audited by the group engagement team. We also conducted a limited scope audit over three insignificant reporting companies, based in France, Switzerland and the UK. The France and Switzerland limited scope audits were conducted by a PwC network firm in their respective countries as component auditors, and in the UK was performed by Grant Thornton UK LLP 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 six 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 in aggregate on the financial statements as a whole.

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

	Group financial statements	Parent Company financial statements
Overall materiality	£2 million (2016: £1.91 million).	£1.9 million (2016: £1.8 million).
How we determined it	5% of profit before tax.	0.8% of total assets.
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.	We believe that total assets is the primary measure used by the shareholders in assessing the performance of the Parent Company, and is a generally accepted auditing benchmark.

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. The range of materiality allocated across components was between £112,000 and £1,900,000. Certain components were audited to a local statutory audit materiality that was also less than our overall group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £100,000 (Group audit) (2016: £65,000) and £100,000 (Parent Company audit) (2016: £65,000) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Going concern

In accordance with ISAs (UK) we report as follows:

Reporting obligation	Outcome
We are required to report if we have anything material to add or draw attention to in respect of the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the directors' identification of any material uncertainties to the group's and the parent company's ability to continue as a going concern over a period of at least twelve months from the date of approval of the financial statements.	We have nothing material to add or to draw attention to. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's and Parent Company's ability to continue as a going concern.
We are required to report if the directors' statement relating to Going Concern in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.	We have nothing to report.

Independent auditors' report to the members of Headlam Group plc continued

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' Report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, the Companies Act 2006, (CA06), ISAs (UK) and the Listing Rules of the Financial Conduct Authority (FCA) require us also to report certain opinions and matters as described below (required by ISAs (UK) unless otherwise stated).

Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 31 December 2017 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report. (CA06)

The directors' assessment of the prospects of the group and of the principal risks that would threaten the solvency or liquidity of the Group
We have nothing material to add or draw attention to regarding:

- The directors' confirmation on page 26 of the Annual Report 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.
- The disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.
- The directors' explanation on page 27 of the Annual Report 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 to report having performed a review of the directors' statement that they have carried out a robust assessment of the principal risks facing the group and 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 UK Corporate Governance Code (the "Code"); and considering whether the statements are consistent with the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit. (Listing Rules).

Other Code Provisions

We have nothing to report in respect of our responsibility to report when:

- The statement given by the directors, on page 58, that they consider the Annual Report taken as a whole to be fair, balanced and understandable, and provides the information necessary for the 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 obtained in the course of performing our audit.
- The section of the Annual Report on page 56 describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.
- The directors' statement relating to the parent company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified, under the Listing Rules, for review by the auditors.
- Directors Remuneration

In our opinion, the part of the Directors Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006. (CA06)

RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS AND THE AUDIT

Responsibilities of the directors for the financial statements

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 in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditors' responsibilities for the audit of the financial statements

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

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

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.

OTHER REQUIRED REPORTING

Companies Act 2006 exception reporting

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
- certain disclosures of Directors remuneration specified by law are not made; 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.

Appointment

Following the recommendation of the Audit Committee, we were appointed by the members on 20 May 2016 to audit the financial statements for the year ended 31 December 2016 and subsequent financial periods. The period of total uninterrupted engagement is 2 years, covering the years ended 31 December 2016 to 31 December 2017.

Mark Smith
(Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Birmingham

6 March 2018

Consolidated Income Statement

for the year ended 31 December 2017

	Note	Underlying 2017 £000	Non-underlying 2017 £000	Total 2017 £000	Underlying 2016 £000	Non-underlying 2016 £000	Total 2016 £000
Revenue	2	**707,764**	**–**	**707,764**	693,572	–	693,572
Cost of sales		**(487,683)**	**–**	**(487,683)**	(481,068)	–	(481,068)
Gross profit		**220,081**	**–**	**220,081**	212,504	–	212,504
Distribution costs		**(130,476)**	**–**	**(130,476)**	(127,982)	–	(127,982)
Administrative expenses	3	**(45,822)**	**(2,399)**	**(48,221)**	(43,450)	(1,927)	(45,377)
Operating profit	2	**43,783**	**(2,399)**	**41,384**	41,072	(1,927)	39,145
Finance income	6	**578**	**–**	**578**	756	–	756
Finance expenses	6	**(1,243)**	**–**	**(1,243)**	(1,722)	–	(1,722)
Net finance costs		**(665)**	**–**	**(665)**	(966)	–	(966)
Profit before tax	3	**43,118**	**(2,399)**	**40,719**	40,106	(1,927)	38,179
Taxation	7	**(7,976)**	**179**	**(7,797)**	(7,601)	385	(7,216)
Profit for the year attributable to the equity shareholders		**35,142**	**(2,220)**	**32,922**	32,505	(1,542)	30,963
Earnings per share							
Basic	9	**41.7p**		**39.1p**	38.7p		36.8p
Diluted	9	**41.5p**		**38.9p**	38.5p		36.6p
Ordinary dividend per share							
Interim dividend proposed for the financial year	22			**7.55p**			6.70p
Final dividend proposed for the financial year	22			**17.25p**			15.85p
Special dividend proposed for the financial year	22			**–**			8.00p

All Group operations during the financial years were continuing operations.

Consolidated Statement of Comprehensive Income

for the year ended 31 December 2017

	Note	2017 £000	2016 £000
Profit for the year attributable to the equity shareholders		**32,922**	30,963
Other comprehensive income:			
Items that will never be reclassified to profit or loss			
Remeasurement of defined benefit plans	20	**9,127**	(4,336)
Related tax		**(1,729)**	961
Impact of change in UK tax rates on deferred tax		**–**	(183)
		7,398	(3,558)
Items that are or may be reclassified to profit or loss			
Foreign exchange translation differences arising on translation of overseas operations		**(277)**	1,707
Effective portion of changes in fair value of cash flow hedges		**(154)**	572
Transfers to profit or loss on cash flow hedges		**(77)**	175
Related tax		**43**	(148)
Impact of change in UK tax rates on deferred tax		**–**	(3)
		(465)	2,303
Other comprehensive income/(expense) for the year		**6,933**	(1,255)
Total comprehensive income attributable to the equity shareholders for the year		**39,855**	29,708

Statements of Financial Position

at 31 December 2017

	Note	Group		Company	
		2017 £000	2016 £000	**2017 £000**	2016 £000
Assets					
Non-current assets					
Property, plant and equipment	10	**101,631**	102,934	**2**	36
Investment properties	10	**–**	–	**83,143**	84,835
Intangible assets	11	**44,662**	10,388	**–**	–
Investments in subsidiary undertakings	12	**–**	–	**120,640**	90,707
Deferred tax assets	13	**648**	1,138	**–**	–
		146,941	114,460	**203,785**	175,578
Current assets					
Inventories	14	**131,566**	126,037	**–**	–
Trade and other receivables	15	**127,976**	128,934	**21,320**	17,351
Cash and cash equivalents	16	**42,030**	59,343	**16,646**	28,171
		301,572	314,314	**37,966**	45,522
Total assets		**448,513**	428,774	**241,751**	221,100
Liabilities					
Current liabilities					
Bank overdraft	16	**–**	(4)	**–**	–
Other interest-bearing loans and borrowings	17	**(233)**	(224)	**–**	–
Trade and other payables	18	**(190,299)**	(183,304)	**(41,780)**	(38,143)
Employee benefits	20	**(2,235)**	(2,169)	**(2,235)**	(2,169)
Income tax payable	8	**(6,339)**	(6,824)	**(1,329)**	(2,147)
		(199,106)	(192,525)	**(45,344)**	(42,459)
Non-current liabilities					
Other interest-bearing loans and borrowings	17	**(6,519)**	(6,493)	**–**	–
Trade and other payables	18	**(4,938)**	–	**(4,938)**	–
Provisions	19	**(2,048)**	(1,531)	**–**	–
Deferred tax liabilities	13	**(6,847)**	(4,077)	**(4,438)**	(3,239)
Employee benefits	20	**(10,481)**	(20,781)	**(7,513)**	(16,113)
		(30,833)	(32,882)	**(16,889)**	(19,352)
Total liabilities		**(229,939)**	(225,407)	**(62,233)**	(61,811)
Net assets		**218,574**	203,367	**179,518**	159,289
Equity attributable to equity holders of the parent					
Share capital	22	**4,268**	4,268	**4,268**	4,268
Share premium		**53,512**	53,512	**53,512**	53,512
Other reserves	22	**2,891**	2,272	**16,610**	15,714
Retained earnings		**157,903**	143,315	**105,128**	85,795
Total equity		**218,574**	203,367	**179,518**	159,289

The notes on pages 90 to 129 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 £38,981,000.

These financial statements were approved by the Board of Directors on 6 March 2018 and were signed on its behalf by

Steve Wilson
Director

Chris Payne
Director

Company Number: 460129

Statement of Changes in Equity – Group

for the year ended 31 December 2017

	Share capital £000	Share premium £000	Capital redemption reserve £000	Translation reserve £000	Cash flow hedging reserve £000	Treasury reserve £000	Retained earnings £000	Total equity £000
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/(expense)	–	–	–	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
Balance at 1 January 2017	**4,268**	**53,512**	**88**	**7,136**	**231**	**(5,183)**	**143,315**	**203,367**
Profit for the year attributable to the equity shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**32,922**	**32,922**
Other comprehensive income	**–**	**–**	**–**	**(277)**	**(231)**	**–**	**7,441**	**6,933**
Total comprehensive income/(expense) for the year	**–**	**–**	**–**	**(277)**	**(231)**	**–**	**40,363**	**39,855**
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**1,218**	**1,218**
Share options exercised by employees	**–**	**–**	**–**	**–**	**–**	**2,307**	**(1,504)**	**803**
Consideration for purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(1,180)**	**–**	**(1,180)**
Current tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**102**	**102**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**138**	**138**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(25,729)**	**(25,729)**
Total contributions by and distributions to equity shareholders	**–**	**–**	**–**	**–**	**–**	**1,127**	**(25,775)**	**(24,648)**
Balance at 31 December 2017	**4,268**	**53,512**	**88**	**6,859**	**–**	**(4,056)**	**157,903**	**218,574**

Statement of Changes in Equity – Company

for the year ended 31 December 2017

	Share capital £000	Share premium £000	Capital redemption reserve £000	Special reserve £000	Cash flow hedging reserve £000	Treasury reserve £000	Retained earnings £000	Total equity £000
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
Balance at 1 January 2017	**4,268**	**53,512**	**88**	**20,578**	**231**	**(5,183)**	**85,795**	**159,289**
Profit for the year attributable to the equity shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**38,981**	**38,981**
Other comprehensive income	**–**	**–**	**–**	**–**	**(231)**	**–**	**6,312**	**6,081**
Total comprehensive income/(expense) for the year	**–**	**–**	**–**	**–**	**(231)**	**–**	**45,293**	**45,062**
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**1,218**	**1,218**
Share options exercised by employees	**–**	**–**	**–**	**–**	**–**	**2,307**	**(1,504)**	**803**
Consideration for purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(1,180)**	**–**	**(1,180)**
Current tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**19**	**19**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**36**	**36**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(25,729)**	**(25,729)**
Total contributions by and distributions to equity shareholders	**–**	**–**	**–**	**–**	**–**	**1,127**	**(25,960)**	**(24,833)**
Balance at 31 December 2017	**4,268**	**53,512**	**88**	**20,578**	**–**	**(4,056)**	**105,128**	**179,518**

Cash Flow Statements

for the year ended 31 December 2017

	Note	Group		Company	
		2017 £000	2016 £000	**2017 £000**	2016 £000
Cash flows from operating activities					
Profit before tax for the year		**40,719**	38,179	**38,706**	33,732
Adjustments for:					
Depreciation, amortisation and impairment		**5,845**	5,276	**1,697**	1,718
Finance income	6	**(578)**	(756)	**(496)**	(763)
Finance expense	6	**1,243**	1,722	**747**	1,178
(Profit)/loss on sale of property, plant and equipment		**(45)**	(15)	**–**	5
Share-based payments	21	**1,218**	1,239	**403**	338
Operating cash flows before changes in working capital and other payables		**48,402**	45,645	**41,057**	36,208
Change in inventories		**(2,210)**	(5,895)	**–**	–
Change in trade and other receivables		**7,564**	(6,467)	**(338)**	(782)
Change in trade and other payables		**754**	10,365	**364**	5,062
Cash generated from the operations		**54,510**	43,648	**41,083**	40,488
Interest paid		**(761)**	(1,133)	**(246)**	(565)
Tax paid		**(8,388)**	(7,703)	**(229)**	(339)
Additional contributions to defined benefit plan	20	**(2,164)**	(2,171)	**(2,164)**	(2,171)
Net cash flow from operating activities		**43,197**	32,641	**38,444**	37,413
Cash flows from investing activities					
Proceeds from sale of property, plant and equipment		**190**	401	**29**	327
Interest received		**576**	752	**288**	400
Acquisition of subsidiaries, net of cash acquired	24	**(24,763)**	–	**(24,180)**	–
Repayment of acquired borrowings on acquisition		**(7,042)**	–	**–**	–
Acquisition of property, plant and equipment	10	**(3,058)**	(2,963)	**–**	(282)
Net cash flow from investing activities		**(34,097)**	(1,810)	**(23,863)**	445
Cash flows from financing activities					
Proceeds from the issue of treasury shares		**803**	423	**803**	423
Payment to acquire own shares		**(1,180)**	(647)	**(1,180)**	(647)
Drawdown of borrowings		**25,000**	6,456	**25,000**	–
Repayment of borrowings		**(25,230)**	(20,000)	**(25,000)**	(20,000)
Dividends paid	22	**(25,729)**	(22,464)	**(25,729)**	(22,464)
Net cash flow from financing activities		**(26,336)**	(36,232)	**(26,106)**	(42,688)
Net (decrease)/increase in cash and cash equivalents		**(17,236)**	(5,401)	**(11,525)**	(4,830)
Cash and cash equivalents at 1 January		**59,339**	63,932	**28,171**	33,001
Effect of exchange rate fluctuations on cash held		**(73)**	808	**–**	–
Cash and cash equivalents at 31 December	16	**42,030**	59,339	**16,646**	28,171

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 6 March 2018.

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.

(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.

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 9 and Chief Executive's Review on pages 10 and 11.

The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Finance Review on pages 12 to 17. 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.

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 to increase its existing facilities, this was to maintain sufficient headroom throughout the year whilst allowing funds for the Groups acquisition and investment initiatives. The Group has maintained two separate agreements with Barclays Bank PLC and HSBC Bank Plc and these include both Sterling and Euro term facilities. The Group's additional funding, increase the level of Sterling committed facilities from £47.5 million to £72.5 million, alongside its Euro facilities of €8.6 million. The Group also has short term uncommitted facilities which continue at £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

Estimates

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:

- *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.

1 ACCOUNTING POLICIES CONTINUED

- *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.
- *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.
- *Supplier arrangements*
  The group has a 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 co-terminus 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.
- *Acquisition accounting*
  IFRS 3 'Business Combinations' requires that the consideration for an acquisition is recorded at fair value. Where contingent consideration is part of the acquisition cost then management have estimated the fair value of the amount payable. Contingent consideration is revalued each reporting period according to the latest forecasts of the acquired business based on the terms of the earn-out arrangement. Where deferred consideration is part of the acquisition cost then it is recorded, discounted back to the present value and held on the balance sheet.

Judgements

Judgements made by the Directors, in the application of these accounting policies that have significant effect on the financial statements have been:

- *Acquisition accounting*
  Assets and liabilities must also be recognised at fair value on acquisition. The identification and measurement of contingent liabilities and intangible assets are key areas of judgement.
  The Group acquired Domus Group of Companies Limited during the year. As part of the acquisition the Group has performed a purchase price allocation review and has assessed the fair value of the assets acquired. Using valuations experts and assumptions regarding the performance of the acquired entities management have identified additional intangibles relating to brand names, customer relationships and order book which have been recognised and either defined as indefinite lived or amortised over their expected useful economic life. Key assumptions in valuing the intangibles were royalty rates, discount rates, and future cash flows which have been assessed by the directors and where appropriate bench marked against the market. Any excess of the purchase consideration over the estimated fair values of acquired net identified assets is recorded as goodwill in the balance sheet and is allocated to an appropriate business segment. Any changes in the underlying assumptions or life of the determined assets would alter the goodwill and amortisation charges included within the financial statements. More details on the Domus Group of Companies Limited are set out in note 24.

(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 2017.

(d) IFRS not yet applied

The following standards and interpretations, which were not effective as at 31 December 2017 and have not been early adopted by the Group, will be adopted in future accounting periods:

- International Financial Reporting Standard (IFRS) 9 'Financial instruments' (effective 1 January 2018, replacing IAS 39).
- International Financial Reporting Standard (IFRS) 15 'Revenue from contracts with customers' (effective 1 January 2018, replacing IAS 18 and IAS 11).
- International Financial Reporting Standard (IFRS) 16 'Leases' (effective 1 January 2019, replacing IAS 17).
- 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.

Whilst some of the standards above are not expected to have an impact on the Group the ones discussed further below will potentially have an impact.

IFRS 9 – Financial Instruments

This introduces new rules for hedge accounting and a new impairment model for financial assets, it also addresses the classification, measurement and de-recognition of financial assets and liabilities.
A detailed assessment of the impact of the new standard is currently underway. It is currently not possible to quantify the impact of the new standard but it is not expected to be significant.

Notes to the Financial Statements continued

1 ACCOUNTING POLICIES CONTINUED

IFRS 15 – Revenue from Contracts with Customers

This standard uses a five-step model to be applied to all sales contracts. The key principle of the standard is that revenue is recognised when control of the goods or services passes to customers at an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services.

A detailed assessment of the impact of the new standard is currently ongoing and initial findings are that there wouldn't be a significant impact on revenue for the Group.

IFRS 16 – Leases

This new standard eliminates the classification of leases over 12 months in length as either operating or finance leases and introduces a single lessee accounting model whereby all leases are accounted for as finance leases, unless of low-value. The standard will therefore require that the Group's leased assets are recorded within property, plant and equipment as 'right of use assets' with a corresponding lease liability which is based on the discounted value of the cash payments required under each lease. The income statement will be affected by the replacement of the operating lease expense with a depreciation charge and a financing expense.

The Standard is effective for periods beginning after 1 January 2019 and it will therefore be effective in the consolidated financial statements for the Group for 31 December 2019. The Group has collated information on leases held at the 31 December 2017 for an evaluation of the impact of IFRS 16 and this work is still being assessed.

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.

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.

1 ACCOUNTING POLICIES CONTINUED

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.

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.

Notes to the Financial Statements continued

1 ACCOUNTING POLICIES CONTINUED

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 and is split over the estimated useful lives of each separately identifiable intangible asset unless such lives are indefinite. Amortisation occurs on brand names, order book and customer relationships and is charged to administrative expenses in the income statement. The estimated useful lives are assessed to be:

Brand names	– 10 – 15 years
Order book – one month	– 36 months
Customer relationships	– 5 – 10 years

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.

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.

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.

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.

Notes to the Financial Statements continued

1 ACCOUNTING POLICIES CONTINUED

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 60 to 73.

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 floorcoverings 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 floorcoverings 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.

Supplier arrangements

Rebates received from suppliers comprise volume related rebates on the purchase of inventories. Volume related discounts are accrued as units are purchased based on the percentage rebate applicable to the forecast total purchases over the rebate period, where it is probable the rebates will be received and the amounts can be estimated reliably. Rebates relating to inventories purchased but still held at the balance sheet date are deducted from the carrying value so that the cost of inventories is recorded net of applicable rebates.

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.

Notes to the Financial Statements continued

2 SEGMENT REPORTING

On 31 December 2017, the Group had 59 operating segments in the UK and three operating segments in Continental Europe. 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	
	2017 £000	2016 £000	**2017 £000**	2016 £000	**2017 £000**	2016 £000
Revenue						
External revenues	**607,234**	602,104	**100,530**	91,468	**707,764**	693,572
Reportable segment underlying operating profit	**44,765**	40,944	**1,271**	793	**46,036**	41,737
Reportable segment assets	**297,325**	263,968	**44,515**	44,516	**341,840**	308,484
Reportable segment liabilities	**(179,016)**	(167,754)	**(25,021)**	(23,801)	**(204,037)**	(191,555)

During the year there were no inter-segment revenues for the reportable segments (2016: £nil).

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

	2017 £000	2016 £000
Profit for the year		
Total profit for reportable segments	**46,036**	41,737
Non-underlying items	**(2,399)**	(1,927)
Unallocated expense	**(2,253)**	(665)
Operating profit	**41,384**	39,145
Finance income	**578**	756
Finance expense	**(1,243)**	(1,722)
Profit before taxation	**40,719**	38,179
Taxation	**(7,797)**	(7,216)
Profit for the year	**32,922**	30,963

2 SEGMENT REPORTING CONTINUED

	2017 £000	2016 £000
Assets		
Total assets for reportable segments	**341,840**	308,484
Unallocated assets:		
Properties, plant and equipment	**89,379**	90,981
Deferred tax assets	**648**	1,138
Cash and cash equivalents	**16,646**	28,171
Total assets	**448,513**	428,774
Liabilities		
Total liabilities for reportable segments	**(204,037)**	(191,555)
Unallocated liabilities:		
Employee benefits	**(12,716)**	(22,951)
Income tax payable	**(6,339)**	(6,824)
Deferred tax liabilities	**(6,847)**	(4,077)
Total liabilities	**(229,939)**	(225,407)

	UK £000	Continental Europe £000	Reportable segment total £000	Unallocated £000	Consolidated total £000
Other material items 2017					
Capital expenditure	**2,443**	**615**	**3,058**	**–**	**3,058**
Depreciation	**1,933**	**690**	**2,623**	**2,291**	**4,914**
Non-underlying items	**1,722**	**677**	**2,399**	**–**	**2,399**
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

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	
	2017 £000	2016 £000	**2017 £000**	2016 £000	**2017 £000**	2016 £000
Revenue						
Residential	**427,484**	422,048	**52,920**	46,337	**480,404**	468,385
Commercial	**179,750**	180,056	**47,610**	45,131	**227,360**	225,187
	607,234	602,104	**100,530**	91,468	**707,764**	693,572

Notes to the Financial Statements continued

3 PROFIT BEFORE TAX

The following are included in profit before tax:

	2017 £000	2016 £000
Depreciation on property, plant and equipment	**4,914**	5,276
Amortisation of intangible assets	**931**	–
Profit on sale of property, plant and equipment	**(45)**	(15)
Operating lease rentals		
Plant and machinery	**11,014**	10,972
Land and buildings	**2,197**	2,548

Non-underlying items of £2,399,000 relate to intangibles amortisation relating to businesses acquired, acquisitions fees and non-recurring costs relating to personnel changes, and the related tax of £179,000 on these costs, see table below.

	2017 £000	2016 £000
Non-recurring people costs	**677**	1,927
Amortisation of acquired intangibles	**931**	–
Acquisitions fees	**791**	–
	2,399	1,927

Auditor's remuneration:

	2017 £000	2016 £000
Audit of these financial statements	**87**	78
Amounts received by the Auditor and their associates in respect of:		
Audit of financial statements of subsidiaries of the Company	**175**	172
Other tax advisory services	**–**	–
Corporate finance services	**91**	–
	353	250

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	
	2017	2016	2017	2016
By sector:				
Floorcoverings	**2,430**	2,337	**–**	–
Central operations	**19**	11	**19**	11
	2,449	2,348	**19**	11
By function:				
Sales and distribution	**2,276**	2,200	**–**	–
Administration	**173**	148	**19**	11
	2,449	2,348	**19**	11

The aggregate payroll costs were as follows:

	Group		Company	
	2017 £000	2016 £000	2017 £000	2016 £000
Wages and salaries	**80,961**	80,336	**3,383**	3,245
Equity settled share-based payment expense (note 21)	**1,218**	1,239	**403**	338
Social security costs	**10,402**	10,213	**538**	460
Pension costs (note 20)	**5,126**	4,984	**883**	343
	97,707	96,772	**5,207**	4,386

5 EMOLUMENTS OF KEY MANAGEMENT PERSONNEL

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

	2017 £000	2016 £000
Short-term employee benefits	**2,474**	3,157
Equity settled share-based payment expense	**507**	304
	2,981	3,461

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 67.

6 FINANCE INCOME AND EXPENSE

	2017 £000	2016 £000
Interest income:		
Bank interest	**540**	756
Other	**38**	–
Finance income	**578**	756
Interest expense:		
Bank loans, overdrafts and other financial expenses	**(770)**	(1,062)
Net change in fair value of cash flow hedges transferred from equity	**–**	(23)
Net interest on defined benefit plan obligations (note 20)	**(473)**	(566)
Other	**–**	(71)
Finance expenses	**(1,243)**	(1,722)

7 TAXATION

Recognised in the income statement

	2017 £000	2016 £000
Current tax expense:		
Current year	**8,548**	8,434
Adjustments for prior years	**(567)**	(878)
	7,981	7,556
Deferred tax expense:		
Origination and reversal of temporary differences	**(39)**	(202)
Effect of change in tax rates	**(27)**	(104)
Adjustments for prior years	**(118)**	(34)
	(184)	(340)
Total tax in income statement	**(7,797)**	7,216

	2017 £000	2016 £000
Tax relating to items (charged)/credited to equity		
Current tax on:		
Income and expenses recognised directly in equity	**(150)**	(2)
Deferred tax on:		
Share options	**(138)**	21
Income and expenses recognised directly in equity	**(18)**	–
Deferred tax on other comprehensive income:		
Defined benefit plans	**1,729**	(778)
Cash flow hedge	**(43)**	132
Total tax reported directly in reserves	**1,380**	(627)

Notes to the Financial Statements continued

7 TAXATION CONTINUED

Factors that may affect future current and total tax charges

The UK headline corporation tax rate for the period was 19.25% (2016: 20%). The UK Budget on 16 March 2016 included a rate reduction to 17% from 1 April 2020 which was enacted during the prior year. The majority of the deferred tax balance in respect of UK entities has therefore been calculated at 17% (2016: 17%) on the basis that most of the balances will materially reverse after 1 April 2020.

In addition, a further reduction in the French corporation tax rate to 25% by 2022 was enacted in December 2017 which has also been taken into account in the calculation of the related deferred tax balance.

Reconciliation of effective tax rate

	2017		2016	
	%	£000	%	£000
Profit before tax		**40,719**		38,179
Tax using the UK corporation tax rate	**19.3**	**7,836**	20.0	7,636
Effect of change in UK tax rate	**(0.1)**	**(30)**	(0.1)	(42)
Effect of change in overseas tax rate	**(0.1)**	**(27)**	(0.2)	(58)
Non-deductible expenses	**1.6**	**646**	1.5	588
Effect of tax rates in foreign jurisdictions	**0.1**	**57**	0.0	4
Adjustments in respect of prior years	**(1.7)**	**(685)**	(2.3)	(912)
Total tax in income statement	**19.1**	**7,797**	18.9	7,216

8 CURRENT TAX LIABILITIES

The Group's current tax liability of £6,339,000 (2016: £6,824,000) 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 £1,329,000 (2016: £2,147,000) represents the amount of income tax payable in respect of current and prior year periods which exceed any amounts recoverable.

9 EARNINGS PER SHARE

	2017 £000	2016 £000
Earnings		
Earnings for underlying basic and underlying diluted earnings per share	**35,142**	32,505
Earnings for basic and diluted earnings per share	**32,922**	30,963

	2017	2016
Number of shares		
Issued ordinary shares at 31 December	**85,363,743**	85,363,743
Effect of weighted average and shares held in treasury	**(1,183,451)**	(1,330,339)
Weighted average number of ordinary shares for the purposes of basic earnings per share	**84,180,292**	84,033,404
Effect of diluted potential ordinary shares:		
Weighted average number of ordinary shares at 31 December	**84,180,292**	84,033,404
Dilutive effect of share options	**549,488**	458,697
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**84,729,780**	84,492,101

At 31 December 2017, the Company held 856,458 (2016: 1,123,060) 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

	Land and buildings £000	Plant and equipment £000	Under construction £000	Total £000
Cost				
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
Balance at 1 January 2017	**118,436**	**36,046**	**–**	**154,482**
Acquisitions	**451**	**418**	**–**	**869**
Additions	**204**	**2,762**	**92**	**3,058**
Disposals	**(23)**	**(1,257)**	**–**	**(1,280)**
Reclassification	**928**	**(928)**	**–**	**–**
Effect of movements in foreign exchange	**(129)**	**97**	**(3)**	**(35)**
Balance at 31 December 2017	**119,867**	**37,138**	**89**	**157,094**
Depreciation and impairment				
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	26,269	–	51,548
Balance at 1 January 2017	**25,279**	**26,269**	**–**	**51,548**
Depreciation charge for the year	**2,284**	**2,630**	**–**	**4,914**
Disposals	**(23)**	**(1,113)**	**–**	**(1,136)**
Reclassification	**205**	**(205)**	**–**	**–**
Effect of movements in foreign exchange	**8**	**129**	**–**	**137**
Balance at 31 December 2017	**27,753**	**27,710**	**–**	**55,463**
Net book value				
At 1 January 2016	94,424	10,229	24	104,677
At 31 December 2016 and 1 January 2017	93,157	9,777	–	102,934
At 31 December 2017	**92,114**	**9,428**	**89**	**101,631**

At 31 December 2017 the cost less accumulated depreciation of long leasehold property held by the Group was £7,430,000 (2016: £7,611,000).

Notes to the Financial Statements continued

10 PROPERTY, PLANT AND EQUIPMENT CONTINUED
Company investment properties and plant and equipment

	Investment properties £000	Plant and equipment £000	Under construction £000	Total £000
Cost				
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
Balance at 1 January 2017	**103,396**	**72**	**–**	**72**
Disposals	**–**	**(62)**	**–**	**(62)**
Balance at 31 December 2017	**103,396**	**10**	**–**	**10**
Depreciation				
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
Balance at 1 January 2017	**18,561**	**36**	**–**	**36**
Depreciation charge for the year	**1,692**	**5**	**–**	**5**
Disposals	**–**	**(33)**	**–**	**(33)**
Balance at 31 December 2017	**20,253**	**8**	**–**	**8**
Net book value				
At 1 January 2016	86,529	85	24	109
At 31 December 2016 and 1 January 2017	84,835	36	–	36
At 31 December 2017	**83,143**	**2**	**–**	**2**

At 31 December 2017 the cost less accumulated depreciation of long leasehold property held by the Company was £7,430,000 (2016: £7,611,000).

11 INTANGIBLE ASSETS – GROUP

	Goodwill £000	Order book £000	Customer relationships £000	Brand names £000	Total £000
Cost					
Balance at 1 January 2016 and 31 December 2016	13,585	4,832	–	–	18,417
Balance at 1 January 2017	**13,585**	**4,832**	**–**	**–**	**18,417**
Addition (note 24)	**23,396**	**1,370**	**5,443**	**4,996**	**35,205**
Balance at 31 December 2017	**36,981**	**6,202**	**5,443**	**4,996**	**53,622**
Amortisation					
Balance at 1 January 2016 and 31 December 2016	3,197	4,832	–	–	8,029
Balance at 1 January 2017	**3,197**	**4,832**	**–**	**–**	**8,029**
Charge for the year	**–**	**858**	**45**	**28**	**931**
Balance at 31 December 2017	**3,197**	**5,690**	**45**	**28**	**8,960**
Net book value					
At 1 January 2016 and 31 December 2016	10,388	–	–	–	10,388
At 31 December 2017	**33,784**	**512**	**5,398**	**4,968**	**44,662**

Cumulative impairment losses recognised in relation to goodwill is £3,197,000 (2016: £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.

11 INTANGIBLE ASSETS – GROUP CONTINUED

The aggregate carrying amounts of goodwill allocated to each CGU are as follows:

	Reported segment	2017 £000	2016 £000
Joseph, Hamilton & Seaton	UK	4,348	4,348
Crucial Trading	UK	1,369	1,369
Belcolor AG	Continental Europe	3,342	3,342
Domus Group Limited	UK	22,955	–
Mitchell Carpets Limited	UK	345	–
McMillan Flooring	UK	96	–
Other	UK	1,329	1,329
		33,784	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 (2016: 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 2016, and applying the following key assumptions.

Key assumptions

Cash flows were projected based on actual operating results, the approved 2018 business plan and management's assessment of planned performance in the period to 2022. For the purpose of impairment testing the cash flows were assumed to grow into perpetuity at a rate of 2.5% beyond 2022.

The main assumptions within the operating cash flows used for 2018 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 10.4% (2016: 10.6%) has been used for impairment testing adjusted to 11.3% (2016: 11.5%) 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.

Notes to the Financial Statements continued

12 INVESTMENTS IN SUBSIDIARIES

Summary information on investments in subsidiary undertakings is as follows:

	£000
Cost	
Balance at 1 January 2016	89,806
Share options granted to employees of subsidiary undertakings	901
Balance at 31 December 2016	90,707
Balance at 1 January 2017	**90,707**
Share options granted to employees of subsidiary undertakings	**815**
Acquisitions *(note 24)*	**29,118**
Balance at 31 December 2017	**120,640**
Carrying value	
At 1 January 2016	89,806
At 31 December 2016	90,707
At 31 December 2017	**120,640**

A full list of the Group's subsidiaries are listed on page 128. There were no impairments recognised on the Company's investments in subsidiaries in the year ended 31 December 2017.

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	
	2017 £000	2016 £000	**2017 £000**	2016 £000	**2017 £000**	2016 £000
Property, plant and equipment	**–**	–	**(7,552)**	(7,871)	**(7,552)**	(7,871)
Intangible assets	**–**	–	**(2,097)**	(180)	**(2,097)**	(180)
Employee benefits	**2,892**	4,792	**–**	–	**2,892**	4,792
Hedging	**–**	–	**–**	(40)	**–**	(40)
Other items	**558**	360	**–**	–	**558**	360
Tax assets/(liabilities)	**3,450**	5,152	**(9,649)**	(8,091)	**(6,199)**	(2,939)
Set-off of tax	**(2,802)**	(4,014)	**2,802**	4,014	**–**	–
	648	1,138	**(6,847)**	(4,077)	**(6,199)**	(2,939)

Movement in deferred tax during the year

	1 January 2017 £000	**Brought in on acquisition £000**	**Recognised in income £000**	**Recognised in equity £000**	**31 December 2017 £000**
Property, plant and equipment	**(7,871)**	**–**	**255**	**64**	**(7,552)**
Intangible assets	**(180)**	**(2,078)**	**161**	**–**	**(2,097)**
Employee benefits	**4,792**	**–**	**(266)**	**(1,634)**	**2,892**
Hedging	**(40)**	**–**	**–**	**40**	**–**
Other items	**360**	**164**	**34**	**–**	**558**
	(2,939)	**(1,914)**	**184**	**(1,530)**	**(6,199)**

Movement in deferred tax during the prior year

	1 January 2016 £000	Brought in on acquisition £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	4,061	–	(25)	756	4,792
Hedging	92	–	–	(132)	(40)
Other items	416	–	(57)	1	360
	(3,904)	–	340	625	(2,939)

Unrecognised deferred tax assets and liabilities

At the Statement of Financial Position date the Group has unused capital losses of £10,797,000 (2016: £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.

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	
	2017 £000	2016 £000	**2017 £000**	2016 £000	**2017 £000**	2016 £000
Property, plant and equipment	**–**	–	**(6,287)**	(6,571)	**(6,287)**	(6,571)
Employee benefits	**1,795**	3,324	**–**	–	**1,795**	3,324
Hedging	**–**	–	**–**	(40)	**–**	(40)
Other items	**54**	48	**–**	–	**54**	48
Tax assets/(liabilities)	**1,849**	3,372	**(6,287)**	(6,611)	**(4,438)**	(3,239)
Set-off of tax	**(1,849)**	(3,372)	**1,849**	3,372	**–**	–
	–	–	**(4,438)**	(3,239)	**(4,438)**	(3,239)

Movement in deferred tax during the year

	1 January 2017 £000	**Recognised in income £000**	**Recognised in equity £000**	**31 December 2017 £000**
Property, plant and equipment	**(6,571)**	**284**	**–**	**(6,287)**
Employee benefits	**3,324**	**(279)**	**(1,250)**	**1,795**
Hedging	**(40)**	**–**	**40**	**–**
Other items	**48**	**6**	**–**	**54**
	(3,239)	**11**	**(1,210)**	**(4,438)**

Movement in deferred tax during the prior year

	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)

Unrecognised deferred tax assets and liabilities

At the Statement of Financial Position date the Company has unused capital losses of £10,797,000 (2016: £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		Company	
Goods for resale	**2017 £000**	2016 £000	**2017 £000**	2016 £000
Balance as at 31 December	**131,566**	126,037	**–**	–

Cost of sales consists of the following:

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Material cost	**485,455**	478,046	**–**	–
Processing cost	**2,228**	3,022	**–**	–
	487,683	481,068	**–**	–

The cost of inventories within cost of sales stated above includes movements in the provision for obsolete inventory of £727,000 release (2016: £245,000 release).

Notes to the Financial Statements continued

15 TRADE AND OTHER RECEIVABLES

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Trade receivables	**94,652**	97,589	**–**	–
Prepayments and accrued income	**5,105**	4,483	**392**	530
Other receivables	**28,211**	26,630	**468**	297
Derivative assets used for economic hedging:				
Other derivatives at fair value	**8**	232	**–**	232
Amounts due from subsidiary undertakings	**–**	–	**20,460**	16,292
	127,976	128,934	**21,320**	17,351

Other receivables include balances totalling £120,000 that fall due after more than 1 year (2016: £nil).

£1,198,000 (2016: £849,000) 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:

	2017 £000	2016 £000
UK	**995**	734
Continental Europe	**203**	115
	1,198	849

16 CASH AND CASH EQUIVALENTS

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Cash	**42,030**	59,343	**16,646**	28,171
Bank overdrafts	**–**	(4)	**–**	–
Cash and cash equivalents per Statement of Financial Position	**42,030**	59,339	**16,646**	28,171

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.

On 7 December 2017, the Group completed a refinancing to increase its existing facilities; this was to maintain sufficient headroom throughout the year whilst allowing funds for the Groups acquisition and investment initiatives. The Group has maintained two separate agreements with Barclays Bank PLC and HSBC Bank Plc and these include both Sterling and Euro term facilities. The Group's additional funding, increase the level of Sterling committed facilities from £47.5 million to £72.5 million, alongside its Euro facilities of €8.6 million. The Group's new banking arrangements run to 7 December 2021. The Group also has short term uncommitted facilities which continue at £25 million, and are renewable on an annual basis. The total banking facilities available to the Group at 31 December 2017 were £112,464,000 (2016: £87,651,000).

For more information about the Group's and Company's exposure to interest rate and foreign currency risk, see note 23.

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Current liabilities				
Interest-bearing loan	**233**	224	**–**	–
	233	224	**–**	–
Non-current liabilities				
Interest-bearing loans	**6,519**	6,493	**–**	–
	6,519	6,493	**–**	–

The Group has undrawn borrowing facilities at 31 December 2017, which amounted to £105,712,000 (2016: £80,931,000). 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 2017 and there were no breaches.

17 OTHER INTEREST-BEARING LOANS AND BORROWINGS CONTINUED

The undrawn borrowing facilities are as follows:

	Interest rate %	2017 £000	Interest rate %	2016 £000
UK	**1.57**	**97,500**	1.32	72,500
Netherlands	**2.03**	**1,313**	2.13	1,466
France	**1.30**	**3,107**	1.15	2,984
Switzerland	**1.65**	**3,792**	2.20	3,981
		105,712		80,931

All the borrowing facilities above bear interest at floating rates. The Swiss facility may be drawn as an overdraft or fixed rate loan with different rates depending on the term and amount.

Changes in net funds

	At 1 January 2017 £000	Cash flows £000	Acquisitions £000	Foreign exchange movements £000	At 31 December 2017 £000
Cash at bank and in hand	59,339	**(19,407)**	**2,171**	**(73)**	**42,030**
Debt due within one year	(224)	**–**	**–**	**(9)**	**(233)**
Debt due after one year	(6,493)	**7,272**	**(7,042)**	**(256)**	**(6,519)**
	52,622	**(12,135)**	**(4,871)**	**(338)**	**35,278**

18 TRADE AND OTHER PAYABLES

	Group		Company	
Current	2017 £000	2016 £000	2017 £000	2016 £000
Trade payables	**149,594**	141,999	**1,343**	578
Taxation and social security	**17,954**	16,617	**2,112**	2,172
Non-trade payables and accrued expenses	**22,751**	24,658	**3,519**	3,507
Amounts due to subsidiary undertakings	**–**	–	**34,806**	31,886
Derivative liabilities used for economic hedging:				
Other derivatives at fair value	**–**	30	**–**	–
	190,299	183,304	**41,780**	38,143

Included within current non-trade payables and accrued expenses is an amount of £nil for accrued interest on unsecured bank loans (2016: £nil).

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 23.

	Group		Company	
Non-current	2017 £000	2016 £000	2017 £000	2016 £000
Non-trade payables and accrued expenses	**4,938**	–	**4,938**	–
	4,938	–	**4,938**	–

Non-current non-trade payables and accrued expenses relate to discounted deferred consideration for Domus Group of Companies Limited.

19 PROVISIONS

	Property	
	2017 £000	2016 £000
Balance at 1 January	**1,531**	1,087
Acquired on acquisition	**195**	–
Charged/(credited) to the income statement:		
Additional provisions	**322**	444
Balance at 31 December	**2,048**	1,531

The property provisions relate to property dilapidations.

Notes to the Financial Statements continued

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.

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 2017.

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. A scheme funding valuation of the plan as at 31 March 2017 is currently ongoing and the preliminary results of this valuation reported a reduction in deficit from £10,883,000 to £2,388,000. The main factors that have combined to produce this change in the position since the last formal valuation are shown in the following table:

	£m
Deficit as at 31 March 2014	(10.9)
Interest on deficit	(1.6)
Gain on investments	26.7
Contributions paid to repair the deficit	8.4
Change in market conditions	(31.3)
Changes in mortality assumptions	4.2
Other factors	2.1
Preliminary deficit as at 31 March 2017	**(2.4)**

The main annual rate assumptions used by the actuary in the 2014 valuation were: increase in salaries 4.80%; increase of pensions in payment 3.30%; discount rate before retirement 5.46%; discount rate after retirement 3.71%; and inflation 3.30%. Assets were taken at their market value at the valuation date.

20 EMPLOYEE BENEFITS CONTINUED

Under the recovery plan dated 26 March 2015 the Company is due to pay contributions of £186,741 per month form 1 January 2018, increasing by 3.3% each subsequent 1 January, with the view to eliminating the shortfall by 30 April 2019. However the scheme funding valuation as at 31 March 2017 is currently ongoing and a new recovery plan may come into place, which may affect the level of payments made to the Plan.

The main annual rate assumptions used by the actuary to produce the preliminary 2017 valuation results were: increase in salaries 4.69%; increase of pensions in payment 3.19%; discount rate before retirement 3.66%; discount rate after retirement 1.91%; and inflation 3.19%.

In accordance with the recovery plan dated 26 March 2015, payments were made to the plan during 2017 of £2,164,000 towards the deficit. The Company is expected to pay contributions of £3,122,000 over the next accounting period. This includes £2,235,000 for payments under the recovery plan and £887,000 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 21 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.

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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 5.2% 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 2017.

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 2017 revealed a funding deficit of £2,591,000 (2016: £4,325,000). The Group is expected to pay £334,000 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 20.0 years.

Notes to the Financial Statements continued

20 EMPLOYEE BENEFITS CONTINUED

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	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Present value of funded defined benefit obligations	**(139,048)**	(141,947)	**(126,308)**	(128,002)
Fair value of plan assets	**126,709**	119,339	**116,560**	109,719
Net obligations	**(12,339)**	(22,608)	**(9,748)**	(18,283)
Other long-term employee benefits	**(377)**	(343)	**–**	–
Total employee benefits	**(12,716)**	(22,951)	**(9,748)**	(18,283)
Analysed as:				
Current liabilities	**(2,235)**	(2,169)	**(2,235)**	(2,169)
Non-current liabilities	**(10,481)**	(20,781)	**(7,513)**	(16,114)
Total employee benefits	**(12,716)**	(22,951)	**(9,748)**	(18,283)

Movements in present value of defined benefit obligation

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
At 1 January	**141,947**	115,849	**128,002**	102,766
Current service cost	**2,488**	2,061	**1,628**	1,329
Past service costs	**(511)**	–	**–**	–
Interest cost	**3,479**	3,863	**3,410**	3,734
Net remeasurement losses/(gains) – financial	**6,827**	26,825	**7,527**	25,640
Net remeasurement (gains)/losses – demographic	**(4,598)**	(358)	**(4,598)**	–
Net remeasurement (gains)/losses – experience	**(6,552)**	(571)	**(6,221)**	(535)
Benefits paid	**(3,740)**	(5,675)	**(3,592)**	(5,103)
Settlement	**–**	(2,587)	**–**	–
Contributions by members	**384**	392	**152**	171
Effect of movements in foreign exchange	**(676)**	2,148	**–**	–
At 31 December	**139,048**	141,947	**126,308**	128,002

Movements in fair value of plan assets

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
At 1 January	**119,339**	97,167	**109,719**	86,601
Interest income on plan assets	**3,006**	3,297	**2,957**	3,194
Return on assets, excluding interest income	**4,804**	21,560	**4,265**	21,673
Contributions by employer:				
Future service contributions	**1,222**	1,336	**895**	1,012
Past service deficit contributions	**2,164**	2,171	**2,164**	2,171
Contributions by members	**384**	392	**152**	171
Benefits paid	**(3,740)**	(5,675)	**(3,592)**	(5,103)
Settlement	**–**	(2,587)	**–**	–
Effect of movements in foreign exchange	**(470)**	1,678	**–**	–
At 31 December	**126,709**	119,339	**116,560**	109,719

20 EMPLOYEE BENEFITS CONTINUED

The fair value of the plan assets were as follows:

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Equities	**58,062**	38,672	**55,194**	36,357
Government debt	**14,760**	21,220	**14,760**	21,220
Corporate bonds	**29,630**	32,514	**25,415**	27,566
Annuities	**5,074**	5,442	**5,074**	5,442
Hedge funds	**2,918**	699	**2,918**	699
Other	**16,265**	20,792	**13,199**	18,435
	126,709	119,339	**116,560**	109,719

Expense recognised in the income statement relating to defined benefit obligation

	Group	
	2017 £000	2016 £000
Service cost	**1,977**	2,061
Net interest on the net defined benefit liability (note 6)	**473**	566
Total	**2,450**	2,627

The expenses recognised in the following line items in the Consolidated Income Statement are:

	Group	
	2017 £000	2016 £000
Administrative expenses	**1,977**	2,061
Net financing income (note 6)	**473**	566
	2,450	2,627

Remeasurement of the net defined benefit liability in the Statement of Comprehensive Income:

	Group	
	2017 £000	2016 £000
Net remeasurement – financial	**6,827**	26,825
Net remeasurement – demographic	**(4,598)**	(358)
Net remeasurement – experience	**(6,552)**	(571)
Return on assets, excluding interest income	**(4,804)**	(21,560)
	(9,127)	4,336

Notes to the Financial Statements continued

20 EMPLOYEE BENEFITS CONTINUED

Principal actuarial assumptions are as follows:

	UK		Swiss	
	2017 %	2016 %	**2017 %**	2016 %
Discount rate	**2.4**	2.7	**0.8**	0.5
Future salary increases	**4.9**	4.9	**2.0**	2.0
Future pension increases	**3.4**	3.4	**–**	–
Inflation rate	**3.4**	3.4	**2.0**	2.0
Mortality table assumptions: UK pre-retirement	**AC00 (Ultimate) table**	AC00 (Ultimate) table	**–**	–
UK post-retirement – future pensioners	**96%(M)/98%(F) of the S1PA tables with future improvements from 2007 in line with the CMI mortality projections model CMI_2016 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.		
UK post-retirement – current pensioners	**96%(M)/98%(F) of the S1PA tables with future improvements from 2007 in line with the CMI mortality projections model CMI_2016 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 2015

The mortality assumption implies the expected future lifetime from age 65 is as follows:

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Non-pensioner male	**24.3**	25.2	**24.3**	25.2
Pensioner male	**22.5**	22.9	**22.5**	22.9
Non-pensioner female	**26.1**	27.1	**26.1**	27.1
Pensioner female	**24.2**	24.8	**24.2**	24.8

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.

20 EMPLOYEE BENEFITS CONTINUED

UK defined benefit plan

Effect in £millions	Change in assumption	Impact on scheme liabilities 2017		Impact on scheme liabilities 2016	
		Increase	**Decrease**	Increase	Decrease
Discount rate	0.25% movement	**(6.3)**	**6.8**	(6.8)	7.3
Rate of inflation (RPI)*	0.25% movement	**5.7**	**(5.3)**	6.2	(5.8)
Salary increases	0.25% movement	**1.3**	**(1.3)**	1.6	(1.6)
Assumed life expectancy	one year movement	**6.1**	**(6.2)**	5.8	(6.0)

* With corresponding changes to the salary and pension increase assumptions.

The figures in the table as at 31 December 2017 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 2016 have been calculated by applying the same percentage increase or decrease as at 31 December 2017.

Extrapolation of the sensitivity analysis beyond the ranges shown may not be appropriate.

Swiss defined benefit plan

Effect in £millions	Change in assumption	Impact on scheme liabilities 2017		Impact on scheme liabilities 2016	
		Increase	**Decrease**	Increase	Decrease
Discount rate	0.25% movement	**(0.6)**	**0.7**	(0.7)	0.8
Rate of inflation (RPI)*	0.25% movement	**0.5**	**–**	0.5	–
Salary increases	0.25% movement	**0.1**	**(0.1)**	0.1	(0.1)
Assumed life expectancy	one year movement	**0.1**	**(0.1)**	0.2	(0.1)

* With corresponding changes to the salary and pension increase assumptions.

The figures in the table as at 31 December 2017 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 2016 have been calculated by applying the same percentage increase or decrease as at 31 December 2017.

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	**2017 £000**	2016 £000	2015 £000	2014 £000	2013 £000
Present value of defined benefit obligation	**(139,048)**	(141,947)	(115,849)	(117,639)	(97,085)
Fair value of plan assets	**126,709**	119,339	97,167	96,190	82,263
Deficit	**(12,339)**	(22,608)	(18,682)	(21,449)	(14,822)

Company	**2017 £000**	2016 £000	2015 £000	2014 £000	2013 £000
Present value of defined benefit obligation	**(126,308)**	(128,002)	(102,766)	(106,297)	(87,111)
Fair value of plan assets	**116,560**	109,719	86,601	86,907	73,704
Deficit	**(9,748)**	(18,283)	(16,165)	(19,390)	(13,407)

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 2017 is £377,000 (2016: £343,000). 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 £3,149,000 (2016: £2,922,000). Contributions amounting to £180,000 (2016: £176,000) in respect of the December 2017 payroll were paid in January 2018.

The total Group cost of operating the plans during the year was £5,126,000 (2016: £4,984,000) and, at 31 December 2017, there was an amount of £316,000 (2016: £319,000) owed to the plans, being employer and employee contributions due for December 2017, which was paid in January 2018.

Notes to the Financial Statements continued

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 3 May 2017 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 60 to 73.

The terms and conditions of the grants are as follows, whereby all options are settled by physical delivery of shares:

	Number of instruments			
Grant date/employees entitled	**2017**	2016	Vesting conditions	Contractual life of options
Five-year Sharesave scheme granted to other employees 11 May 2012	**–**	49,400	Continuous service	01/07/17 – 01/01/18
Three-year Sharesave scheme granted to other employees 10 May 2013	**–**	656	Continuous service	01/07/16 – 01/01/17
Five-year Sharesave scheme granted to other employees 10 May 2013	**36,662**	42,136	Continuous service	01/07/18 – 01/01/19
Headlam Group Co-Investment Plan 2008 granted to key management 1 April 2014*	**–**	243,585	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	Continuous service	01/07/17 – 01/01/18
Five-year Sharesave scheme granted to other employees 8 May 2014	**52,661**	58,959	Continuous service	01/07/19 – 01/01/20
Headlam Group Co-Investment Plan 2008 granted to key management 1 May 2015*	**225,874**	225,874	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	**296,593**	342,107	Continuous service	01/07/18 – 01/01/19
Five-year Sharesave scheme granted to other employees 5 May 2015	**204,855**	211,736	Continuous service	01/07/20 – 01/01/21
Headlam Group Co-Investment Plan 2008 granted to key management 6 May 2016*	**162,647**	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	**219,801**	248,631	Continuous service	01/07/19 – 01/01/20
Five-year Sharesave scheme granted to other employees 4 May 2016	**47,044**	48,167	Continuous service	01/07/21 – 01/01/22
Headlam Group Performance Share Plan 2008 granted to key management 5 July 2017*	**239,045**	–	Awards will vest between 25% and 100% for performance between 'threshold' performance and 'maximum' performance	06/07/20 – 06/07/27
Three-year Sharesave scheme granted to other employees 3 May 2017	**216,906**	–	Continuous service	01/07/20 – 01/01/21
Five-year Sharesave scheme granted to other employees 3 May 2017	**34,725**	–	Continuous service	01/07/22 – 01/01/23
Total share options	**1,736,812**	1,794,868		

* Further details are provided on pages 60 to 73 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 2017	**Number of options 2017**	Weighted average exercise price 2016	Number of options 2016
Outstanding at the beginning of the year	**230.9**	**1,794,868**	225.4	1,606,790
Exercised during the year	**172.2**	**(466,602)**	(266.7)	(158,532)
Granted during the year	**261.8**	**502,931**	231.9	539,281
Lapsed during the year	**346.9**	**(94,385)**	(158.9)	(192,671)
Outstanding at the end of the year	**249.3**	**1,736,812**	230.9	1,794,868
Exercisable at the end of the year	**–**	**–**	274.0	656

The weighted average share price for options exercised during the year was 591.0p (2016: 434.5p).

The options outstanding at the year end have an exercise price in the range of 0.0p to 499.0p and a weighted average contractual life of 2.2 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 2017 are shown below:

2017		**Three-year Performance Share Plan 2008**	**Three-year Sharesave scheme**	**Five-year Sharesave scheme**
Number of options		**239,045**	**228,260**	**35,626**
Fair value at measurement date:				
No performance conditions		**–**	**184.2p**	**169.2p**
Performance conditions	EPS 80% & TSR 20%	**471.9p**	**–**	**–**
Share price at 31 December		**536.8p**	**600.0p**	**600.0p**
Exercise price		**–**	**499.0p**	**499.0p**
Expected volatility		**47.7%**	**47.7%**	**39.2%**
Option life		**three years**	**three years**	**five years**
Dividend yield		**4.3% p.a.**	**3.9% p.a.**	**3.9% p.a.**
Risk-free rate of interest		**0.4% p.a.**	**0.2% p.a.**	**0.5% p.a.**

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 continued

21 SHARE-BASED PAYMENTS CONTINUED

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

	Group		Company		Subsidiaries	
	2017 £000	2016 £000	2017 £000	2016 £000	2017 £000	2016 £000
Share options granted in 2011 under the SAYE five-year scheme	–	6	–	–	–	6
Share options granted in 2012 under the SAYE five-year scheme	5	14	–	–	5	14
Share options granted in 2013 under the SAYE three-year scheme	–	10	–	–	–	10
Share options granted in 2013 under the SAYE five-year scheme	7	7	–	–	7	7
Headlam Group Co-Investment Plan 2008 (awarded 2014)	104	408	35	137	69	271
Share options granted in 2014 under the SAYE three-year scheme	27	76	1	1	26	75
Share options granted in 2014 under the SAYE five-year scheme	39	39	6	5	33	34
Headlam Group Co-Investment Plan 2008 (awarded 2015)	315	284	140	126	175	158
Share options granted in 2015 under the SAYE three-year scheme	138	138	3	6	135	132
Share options granted in 2015 under the SAYE five-year scheme	52	52	–	–	52	52
Headlam Group Co-Investment Plan 2008 (awarded 2016)	204	138	93	63	111	75
Share options granted in 2016 under the SAYE three-year scheme	90	59	–	–	90	59
Share options granted in 2016 under the SAYE five-year scheme	11	8	–	–	11	8
Share options granted in 2017 under the SAYE three-year scheme	75	–	1	–	74	–
Share options granted in 2017 under the SAYE five-year scheme	6	–	–	–	6	–
Headlam Group Performance Share Plan 2016 (awarded 2017)	145	–	124	–	21	–
Total expense recognised	1,218	1,239	403	338	815	901

22 CAPITAL AND RESERVES

Share capital

	Ordinary shares	
	2017	2016
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

	2017 £000	2016 £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 2017, the Company held 856,458 (2016: 1,123,060) 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 1.0% (2016: 1.3%) of the issued share capital with a nominal value of £42,823 (2016: £56,153).

In the period from 31 December 2017 to 6 March 2018 no shares have been purchased by the Company.

22 CAPITAL AND RESERVES CONTINUED

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

	2017 £000	2016 £000
Interim dividend for 2016 of 6.70p paid 3 January 2017	**5,637**	–
Special dividend for 2016 of 8.00p paid 24 April 2017	**6,732**	–
Final dividend for 2016 of 15.85p paid 1 July 2017	**13,360**	–
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
	25,729	22,464

Interim dividends of 7.55p per share (2016: 6.70p per share) are provided for when the dividend is paid. The dividend was paid on 3 January 2018 and totalled £6,372,000.

The final proposed dividend of 17.25p per share (2016: 15.85p 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 2017 is £20,932,000 (2016: £18,997,000) excluding special dividend.

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.

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.

Notes to the Financial Statements continued

23 FINANCIAL INSTRUMENTS CONTINUED

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	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Trade and other receivables (note 15)	**122,863**	124,219	**20,928**	16,589
Derivative assets (note 15)	**8**	232	**–**	232
Cash and cash equivalents (note 16)	**42,030**	59,339	**16,646**	28,171
	164,901	183,790	**37,574**	44,992

The fair values of the above financial assets at both 31 December 2017 and 2016, 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	
	2017 £000	2016 £000	**2017 £000**	2016 £000
UK	**81,989**	85,207	**–**	–
Continental Europe	**12,663**	12,382	**–**	–
	94,652	97,589	**–**	–

The ageing of trade receivables at the Statement of Financial Position date was:

	2017		2016	
Group	**Gross £000**	**Impairment £000**	Gross £000	Impairment £000
Not past due	**85,038**	**–**	87,384	–
Past due 0–30 days	**8,330**	**(415)**	8,382	(234)
Past due 31–120 days	**3,972**	**(2,273)**	4,192	(2,135)
	97,340	**(2,688)**	99,958	(2,369)

All other receivables and derivative financial assets are not past due (2016: not past due).

The Company had trade receivables of £nil (2016: £nil).

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Balance at 1 January	**2,369**	2,588	**–**	–
Amounts acquired	**125**	–	**–**	–
Amounts provided	**1,198**	849	**–**	–
Amounts utilised	**(1,017)**	(1,205)	**–**	–
Effect of movements in foreign exchange	**13**	137	**–**	–
Balance at 31 December	**2,688**	2,369	**–**	–

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 0.17% (2016: 0.12%).

23 FINANCIAL INSTRUMENTS CONTINUED

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 2017 cash and cash equivalents covered the amounts of borrowings maturing in the next 12 months with a net positive liquidity of £41,797,000 (2016: £59,115,000). Details of the total facilities that the Group has access to are given in note 17.

The following are the contractual maturities of financial liabilities:

31 December 2017 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	**6,752**	**(7,033)**	**(307)**	**(305)**	**(6,421)**	**–**
Trade and other payables	**172,345**	**(172,345)**	**(167,407)**	**(1,489)**	**(3,449)**	**–**
	179,097	**(179,378)**	**(167,714)**	**(1,794)**	**(9,870)**	**–**

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 2017 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	**39,668**	**(39,668)**	**(39,668)**	**–**	**–**

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)	–	–

The value of the Group's and Company's financial liabilities as detailed above at 31 December 2017 and 2016 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 2017 and 2016.

31 December 2017	**Available for sale £000**	**Other derivatives at fair value £000**	**Amortised cost £000**	**Total carrying value £000**
Cash and cash equivalents	**–**	**–**	**42,030**	**42,030**
Borrowings due within one year	**–**	**–**	**(233)**	**(233)**
Borrowings due after one year	**–**	**–**	**(6,519)**	**(6,519)**
Trade payables	**–**	**–**	**(149,594)**	**(149,594)**
Non-trade payables	**–**	**–**	**(27,689)**	**(27,689)**
Trade receivables	**–**	**–**	**94,652**	**94,652**
Other receivables	**–**	**–**	**28,211**	**28,211**
Provisions	**–**	**–**	**(2,048)**	**(2,048)**
Derivative assets	**–**	**8**	**–**	**8**
	–	**8**	**(21,190)**	**(21,182)**

Notes to the Financial Statements continued

23 FINANCIAL INSTRUMENTS CONTINUED

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
Cash and cash equivalents	–	202	8,653	8,855

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.

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	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Variable rate instruments				
Financial assets	**42,030**	59,343	**16,646**	28,171
Financial liabilities	**(6,752)**	(6,721)	**–**	–
	35,278	52,622	**16,646**	28,171

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 2016.

	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 2017								
Variable rate instruments	**353**	**(353)**	**–**	**–**	**166**	**(166)**	**–**	**–**
31 December 2016								
Variable rate instruments	526	(526)	–	–	282	(282)	–	–

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 was a two-year commodity transaction swap. The risk hedged was the diesel fuel price risk, being the change in fuel price payments on the specified diesel consumption. The notional amount was 6,768 metric tons, under which a fixed diesel price of £348.25 per metric ton was paid monthly and the floating price according to Platts European was received.

The fair value of this diesel commodity swap is £nil in the Statement of Financial Position as at 31 December 2017, it having terminated on 31 October 2017 (2016: £232,000 asset).

On 31 December 2017 there were no commodity transaction swaps entered into by the Group.

23 FINANCIAL INSTRUMENTS CONTINUED

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 2016.

	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 2017								
Variable rate instruments	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
31 December 2016								
Variable rate instruments	2	(2)	–	–	2	(2)	–	–

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 an asset at 31 December 2017 amounted to £8,000 (2016: liability of £30,000).

For the 12-month period to 31 December 2017, 3.1% (2016: 2.0%) of the Group's operating profit was derived from overseas subsidiaries and at 31 December 2017, 18.8% (2016: 17.7%) 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**		
2017	**Euro amount £000**	**Other amount £000**	**Total £000**	**Euro amount £000**	**Other amount £000**	**Total £000**
Trade and other receivables	**109**	**133**	**242**	**–**	**–**	**–**
Cash and cash equivalents	**364**	**109**	**473**	**49**	**–**	**49**
Trade and other payables	**(5,483)**	**(1,496)**	**(6,979)**	**–**	**–**	**–**
	(5,010)	**(1,254)**	**(6,264)**	**49**	**–**	**49**

	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

Notes to the Financial Statements continued

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 2016.

	Group		Company	
	2017 £000	2016 £000	**2017 £000**	2016 £000
Euro	**(501)**	(99)	**5**	18
Other	**(125)**	(142)	**–**	–

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 had a diesel commodity swap used for hedging which was fair valued in accordance with level 2 for the year ended 31 December 2017 (2016: level 2) and forward currency contracts which were fair valued in accordance with level 2 (2016: 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.

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 7 December 2017, the Group completed a refinancing of its banking facilities to maintain headroom whilst also providing funds for the Groups acquisition and investment strategy. The new facilities comprise a £72.5 million sterling committed facility, a €8.6 million euro committed facility and a £25 million sterling uncommitted facility. This represents an increase in total available facilities of £25 million.

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 2017 and 31 December 2016.

24 ACQUISITIONS

On 28 February 2017, a subsidiary company of Headlam Group plc entered into an agreement to acquire Mitchell Carpets Limited. The company is a distributor of floorcovering in the south east of England.

On 28 April 2017, a subsidiary company of Headlam Group plc entered into an agreement to acquire the business and certain assets of McMillan Flooring. McMillan Flooring is a distributor of contract floorcovering in Scotland.

On 7 December 2017, Headlam Group plc entered into an agreement to acquire Domus Group of Companies Limited and its subsidiary entities. The Domus Group is the UK's leading specification consultant and supplier of hard surfaces for premium construction and refurbishment projects.

The acquired businesses contributed revenues of £4.5 million and an operating loss of £0.1 million to the Group for the year ended 31 December 2017. If the acquisitions had occurred on 1 January 2017, pro-forma revenue and operating profit for the year ended 31 December 2017 would have increased by £33.9 million and £3.1 million respectively.

Details of the acquisitions are provisional and are shown in aggregate below:

	Acquiree's book value £000	Fair value adjustments £000	Acquisition amounts £000
Acquiree's provisional net assets at the acquisition date:			
Intangible assets	–	11,809	11,809
Acquired goodwill	8,778	(8,778)	–
Tangible fixed assets	870	–	870
Inventories	3,893	(747)	3,146
Trade and other receivables	6,192	375	6,567
Cash at bank and in hand	2,171	–	2,171
Trade and other payables	(7,190)	254	(6,936)
Borrowings	(6,643)	(399)	(7,042)
Provisions	–	(195)	(195)
Deferred tax	–	(1,914)	(1,914)
Net identifiable assets and liabilities	8,071	405	8,476
Goodwill on acquisition		23,396	23,396
Consideration			31,872
Satisfied by:			
Cash			26,934
Deferred and contingent consideration			4,938
			31,872
Analysis of cash flows:			
On completion			26,934
Cash acquired			(2,171)
Borrowing repayment			7,042
Costs of acquisition			869
			32,674

Professional fees of £0.9 million were incurred on the acquisitions 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 £23.4 million arose on the acquisitions, there were also intangible assets on acquisition of £11.8 million which were attributed to brand names, order book and customer relationships as shown in note 11. During the year £0.9 million of intangibles have been amortised to the income statement.

The residual goodwill reflects the significant benefit the acquisitions will have on the Group by bringing further geographic coverage, offering an expanded product range, developing a more sophisticated customer route to market, providing an additional avenue for growth and a different order profile. The Domus acquisition is complementary to the Group's market-leading core business which supplies a high volume of small orders into both the residential and commercial sectors and has minimal overlap in terms of current product lines, suppliers and customer base. Domus diversifies and broadens Headlam's overall position in the floorcoverings market with entry into ceramics and an increased weighting in engineered wood, LVT and laminate, incorporating product lines that continue to achieve ongoing growth in the market.

In addition, Domus significantly increases the Group's presence in the commercial specification market and brings considerable expertise into the Group, providing a platform to pursue further domestic and international growth opportunities.

Notes to the Financial Statements continued

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.

Deferred and contingent consideration

The acquisition of Domus Group of Companies Limited was financed by initial cash consideration of £24.2 million paid on completion and satisfied by the Group's existing cash and debt facilities; a deferred consideration of £3.3 million, payable in cash and Ordinary shares of 5 pence each in the capital of the Company ('Ordinary Shares'), of which £1.6 million is payable on 7 December 2019 and £1.7 million is payable on 7 December 2020; and a further maximum contingent consideration of £2.7 million, payable in cash based on Domus achieving certain EBITDA targets over the three-year period ending 31 December 2020.

The deferred and contingent consideration have been discounted back and reported at present value, and contingent consideration has been recognised based on management's assessment of the probability of it being paid

There were no acquisitions made by the Group during the year ended 31 December 2016.

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:

	2017			2016		
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	**3,243**	**9,569**	**12,812**	1,879	9,855	11,734
Between one and five years	**7,341**	**16,796**	**24,137**	3,993	15,348	19,341
More than five years	**4,478**	**641**	**5,119**	2,989	169	3,158
	15,062	**27,006**	**42,068**	8,861	25,372	34,233

	2017			2016		
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**	**10**	**115**	105	3	108
More than five years	**1,802**	**–**	**1,802**	1,828	–	1,828
	1,933	**18**	**1,951**	1,959	11	1,970

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 2017, total operating lease expense of £13,211,000 was recognised in the Consolidated Income Statement (2016: £13,520,000).

26 CAPITAL COMMITMENTS

Group

During the year ended 31 December 2017, the Group entered into commitments to purchase property, plant and equipment for £358,000 (2016: £663,000). These commitments are expected to be settled in the following financial year.

Company

At the year ended 31 December 2017, the Company had no commitments to purchase property, plant and equipment (2016: £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 44 and 45.

As at 31 December 2017, Directors of the Company and their immediate relatives controlled 0.8% of the voting shares of the Company (2016: 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 £507,000 (2016: £304,000).

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 2017 £000	Highest during the year £000	Balance at 31 December 2016 £000
Amounts due from subsidiaries	**20,460**	**20,460**	**16,292**	**16,292**
Amounts due to subsidiaries	**(34,806)**	**(34,806)**	**(31,886)**	**(31,886)**

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 2017 £000	For year ended 31 December 2016 £000
Rental income	**7,971**	7,971
Dividends received	**38,378**	31,522
Recharge of operating expenses	**3,140**	2,576
Interest income	**163**	163

Notes to the Financial Statements continued

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 Dersimo BV. On 2 March 2018, Headlam Holdings BV, a group subsidiary company acquired 100% of the issued share capital of Dersimo BV, a floorcovering distribution business based in The Netherlands, for a consideration of €4.1 million, subject to finalising the net assets position.

GROUP SUBSIDIARIES

Company	Type	Place of incorporation
HFD Limited	Trading	Great Britain*
MCD Group Limited	Trading	Great Britain*
Domus Tiles Limited	Trading	Great Britain*
Headlam BV	Trading	Netherlands**
LMS SA	Trading	France***
Belcolor AG	Trading	Switzerland****
Headlam (European) Limited	Holding Company	Great Britain*
Headlam Holdings BV	Holding Company	Netherlands**
Headlam SAS	Holding Company	France***
Yourfloors Plc	Holding Company	Great Britain*
Domus Group of Companies Limited	Holding Company	Great Britain*
Tileco (2012) Bidco Ltd	Holding Company	Great Britain*
Tileco Group (2007) Ltd	Holding Company	Great Britain*
Tileco Group Limited	Holding Company	Great Britain*
Crossforge Limited	Dormant	Great Britain*
Gorsey Eleven Limited	Dormant	Great Britain*
Headlam Group Employee Trust Company Limited	Dormant	Great Britain*
Headlam Group Pension Trustees Limited	Dormant	Great Britain*
Mercado Group Limited	Dormant	Great Britain*
NCT (International) Limited	Dormant	Great Britain*
Mitchell Carpets Limited	Dormant	Great Britain*
Tileright Limited	Dormant	Great Britain*
Tileco Limited	Dormant	Great Britain*
Domus Stone Limited	Dormant	Great Britain*
Surface Tiles Limited	Dormant	Great Britain*
Tile Solutions Limited	Dormant	Great Britain*

The ordinary share capital of 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

	2017 £000	2016 £000	Restated* 2015 £000	Restated* 2014 £000	Restated** 2013 £000
Trading results					
Revenue	**707,764**	693,572	654,078	635,242	603,051
Gross profit	**220,081**	212,504	200,510	190,540	181,255
Overheads	**(176,298)**	(171,432)	(163,733)	(159,078)	(153,575)
Underlying profit before net financing costs	**43,783**	41,072	36,777	31,462	27,680
Net financing costs	**(665)**	(966)	(1,153)	(1,162)	(1,241)
Underlying profit on ordinary activities before tax	**43,118**	40,106	35,624	30,300	26,439
Taxation	**(7,976)**	(7,601)	(7,213)	(6,515)	(6,146)
Underlying profit on ordinary activities after taxation	**35,142**	30,963	28,411	23,785	20,293
Profit before tax	**40,719**	38,179	35,624	30,300	21,087
Shareholder value					
Paid interim and final dividend per share	**22.55p**	20.70p	17.50p	15.30p	14.85p
Paid special dividend per share	**8.00p**	6.00p	–	–	–
Proposed dividend per share	**25.25p**	22.55p	20.70p	17.50p	15.30p
Earnings per share	**39.1p**	36.8p	33.8p	28.6p	18.0p
Underlying earnings per share	**41.7p**	38.7p	33.8p	28.6p	24.5p
Net assets					
Non-current assets					
Property, plant and equipment	**101,631**	102,934	104,677	106,875	106,493
Intangible assets	**44,662**	10,388	10,388	10,013	10,013
Deferred tax assets	**648**	1,138	629	515	354
	146,941	114,460	115,694	117,403	116,860
Current assets					
Inventories	**131,566**	126,037	118,165	115,591	114,700
Trade and other receivables	**127,976**	128,934	120,300	118,962	119,634
Cash and cash equivalents	**42,030**	59,343	63,932	47,589	47,477
	301,572	314,314	302,397	282,142	281,811
Total assets	**448,513**	428,774	418,091	399,545	398,671
Current liabilities					
Bank overdraft	**–**	(4)	–	–	–
Other interest-bearing loans and borrowings	**(233)**	(224)	–	(204)	(218)
Trade and other payables	**(190,299)**	(183,304)	(171,375)	(165,240)	(164,856)
Employee benefits	**(2,235)**	(2,169)	(2,171)	(2,933)	(2,842)
Income tax payable	**(6,339)**	(6,824)	(6,974)	(6,073)	(7,022)
	(199,106)	(192,525)	(180,520)	(174,450)	(174,938)
Non-current liabilities					
Other interest-bearing loans and borrowings	**(6,519)**	(6,493)	(20,000)	(22,818)	(33,239)
Trade and other payables	**(4,938)**	–	–	–	–
Provisions	**(2,048)**	(1,531)	(1,087)	(787)	(790)
Deferred tax liabilities	**(6,847)**	(4,077)	(4,533)	(3,931)	(2,742)
Employee benefits	**(10,481)**	(20,781)	(16,843)	(18,803)	(12,780)
	(30,833)	(32,882)	(42,463)	(46,339)	(49,551)
Total liabilities	**(229,939)**	(225,407)	(222,983)	(220,789)	(224,489)
Net assets	**218,574**	203,367	195,108	178,756	174,182

* The balance sheets for 2015, 2014 and 2013 were 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 subsequent years. This is fully described in the Annual Report and Accounts for the year ended 31 December 2016.

** Restated to reflect the changes for revised IAS 19 and also * shown above.

Notes

Notes

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FINANCIAL CALENDAR

Statutory Announcements

Annual General Meeting	24 May 2018
Interim results announced	22 August 2018
Final results announced	March 2019

Dividend Dates

Final dividend for 2017, if approved, payable to qualifying shareholders on the register as at 1 June 2018	6 July 2018
Interim dividend for 2018 declared	22 August 2018
Interim dividend for 2018 payable	2 January 2019

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