headlam
group plc

ANNUAL REPORT AND ACCOUNTS 2018

EUROPE'S LEADING FLOORCOVERINGS DISTRIBUTOR

Headlam Group plc is Europe's leading distributor of floorcoverings, providing the distribution channel between suppliers and trade customers

LEADING THROUGH...

SCALE

Leveraging an extensive distribution network and dense geographic coverage to service a broad and diverse customer base

Discover more on page 02

PARTNERS

Working in partnership with suppliers and customers to support their growth and development

Discover more on page 04

SERVICE

Providing the broadest product offering supported by next day delivery and additional marketing and other support

Discover more on page 06

EXPERTISE

Offering years of operating expertise supplemented by additional market segment knowledge via acquisition

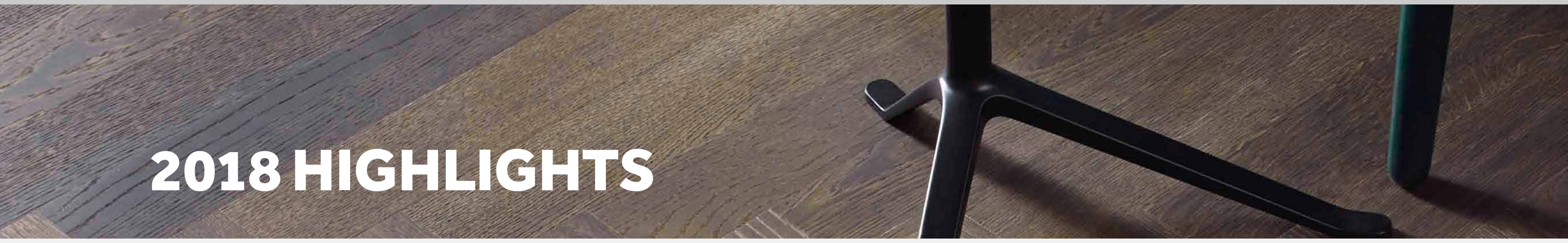
Discover more on page 08

OVERVIEW

STRATEGIC REPORT

GOVERNANCE

FINANCIAL STATEMENTS



2018 HIGHLIGHTS

Revenue* £million

£708.4m

+2.3% (2017: £692.5m)

2018	708.4
2017	692.5
2016	677.7
2015	639.3
2014	620.8

Underlying Operating Profit** £million

£44.3m

+1.1% (2017: £43.8m)

2018	44.3
2017	43.8
2016	41.1
2015	36.8
2014	31.5

2018 Statutory Operating Profit £41.3m (2017: £41.4m)

Underlying Profit before Tax** £million

£43.4m

+0.6% (2017: £43.1m)

2018	43.4
2017	43.1
2016	40.1
2015	35.6
2014	30.3

Basic Earnings Per Share pence

40.0p

+2.3% (2017: 39.1p)

2018	40.0
2017	39.1
2016	36.8
2015	33.8
2014	28.6

Total Ordinary Dividends (declared and proposed in respect of 2018) pence

25.0p

+0.8% (2017: 24.80p)

2018	25.0
2017	24.80
2016	22.55
2015	20.70
2014	17.50

Net Cash Position £million

£36.7m

+4.0% (2017: £35.3m)

2018	36.7
2017	35.3
2016	52.6
2015	43.9
2014	24.6

Statutory Profit before Tax £million

£40.4m

-0.7% (2017: £40.7m)

2018	40.4
2017	40.7
2016	38.2
2015	35.6
2014	30.3

* All prior year revenue numbers restated to present comparatives on a consistent basis due to the reclassification in 2018 of some items between revenue, cost of sales and operating expenses to better reflect their nature.

** Underlying is before non-underlying items which includes intangibles amortisation relating to businesses acquired, acquisition fees, contingent consideration movements, non-recurring pension costs in relation to guaranteed minimum pension ('GMP') equalisation and non-recurring costs relating to senior personnel changes.

Operational Highlights

- Ten efficiency initiatives focused on improving operational practices and financial performance, some earlier-stage ones beginning to contribute in 2018, with increasing benefits expected throughout 2019
- Five smaller strategic acquisitions completed in 2018, further enhancing and broadening the Company's industry and geographical position
- Planning approval received for the new regional distribution centre in Ipswich, with the land acquired post the year-end
- Board supplemented with a wealth of experience throughout the year, with several operational appointments bringing significant additional expertise into the business

LEADING THROUGH... SCALE

Leveraging an extensive distribution network and dense geographic coverage to service a broad and diverse customer base

+67 MILLION CUBIC FEET OF WAREHOUSE CAPACITY

67 BUSINESSES AND 4 COUNTRIES OF OPERATION

£102.0 MILLION PROPERTY, PLANT AND EQUIPMENT ASSETS

£50.0 MILLION CASH FROM OPERATIONS

£133.7 MILLION AVERAGE INVENTORY POSITION

All data stated for the financial year ended 31 December 2018 or as at 31 December 2018

LEADING THROUGH...

PARTNERS

Working in partnership with suppliers and customers to support their growth and development

199 SUPPLIERS WORLDWIDE

71,384 CUSTOMER ACCOUNTS

22
SUPPLIER COUNTRIES

35.0%
OF PRODUCT PURCHASES FROM UK SUPPLIERS*

+30,000
PRODUCT UNITS OFFERED TO UK CUSTOMERS

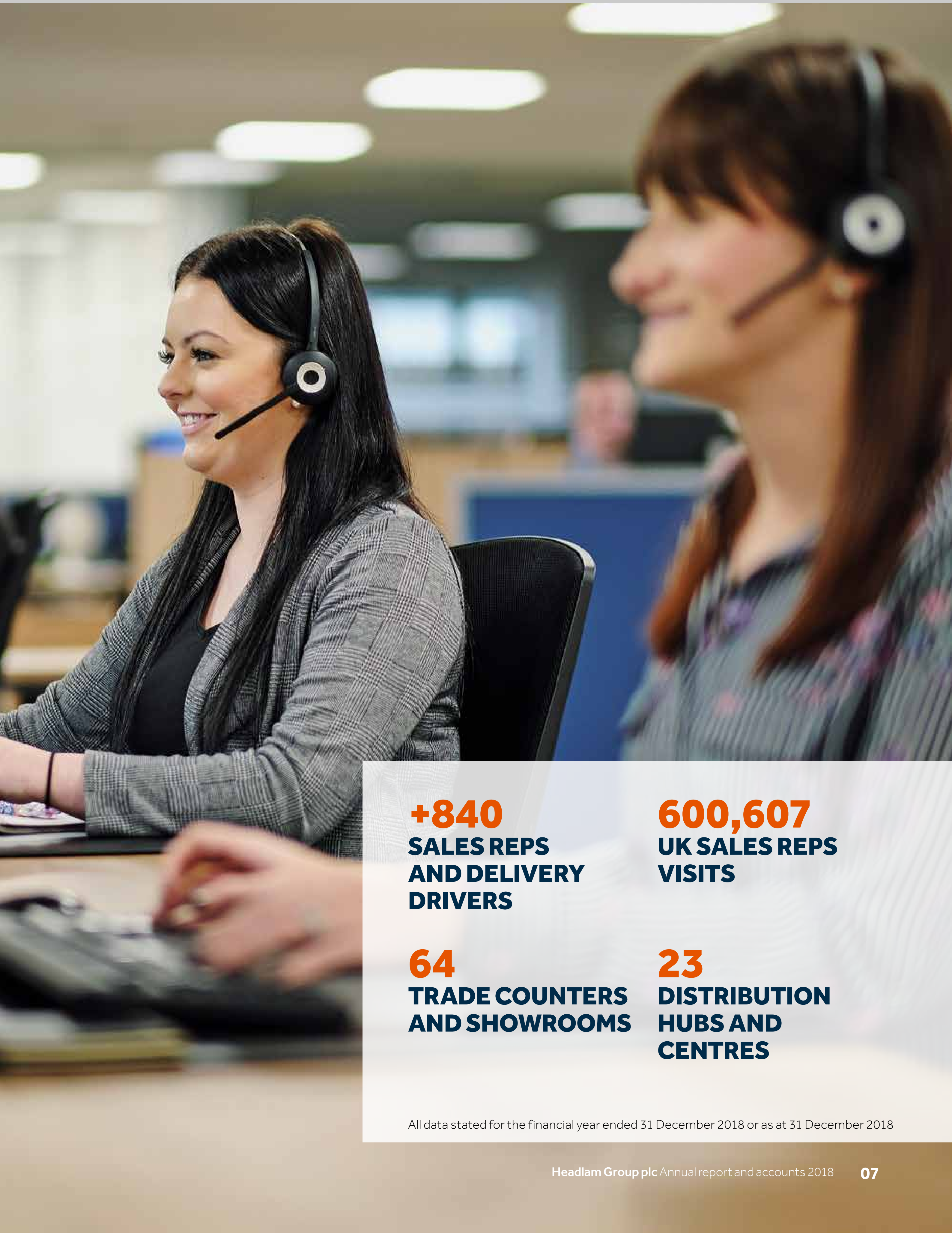
£133
AVERAGE ORDER SIZE**

* Based on actual purchase prices from suppliers
** Distribution businesses
All data stated for the financial year ended 31 December 2018 or as at 31 December 2018

LEADING THROUGH...
SERVICE

Providing the broadest product offering supported by next day delivery and additional marketing and other support

+5.3 MILLION ORDERS PROCESSED IN 2018



+840
SALES REPS AND DELIVERY DRIVERS

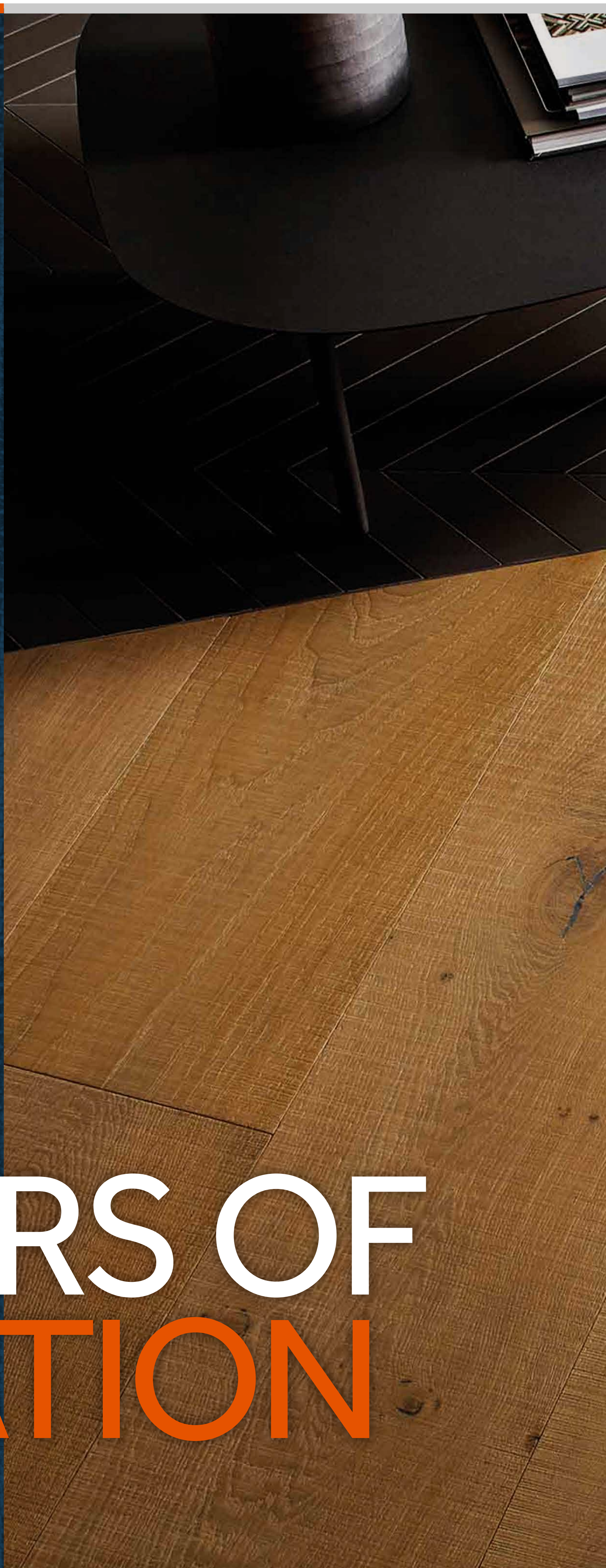
600,607
UK SALES REPS VISITS

64
TRADE COUNTERS AND SHOWROOMS

23
DISTRIBUTION HUBS AND CENTRES

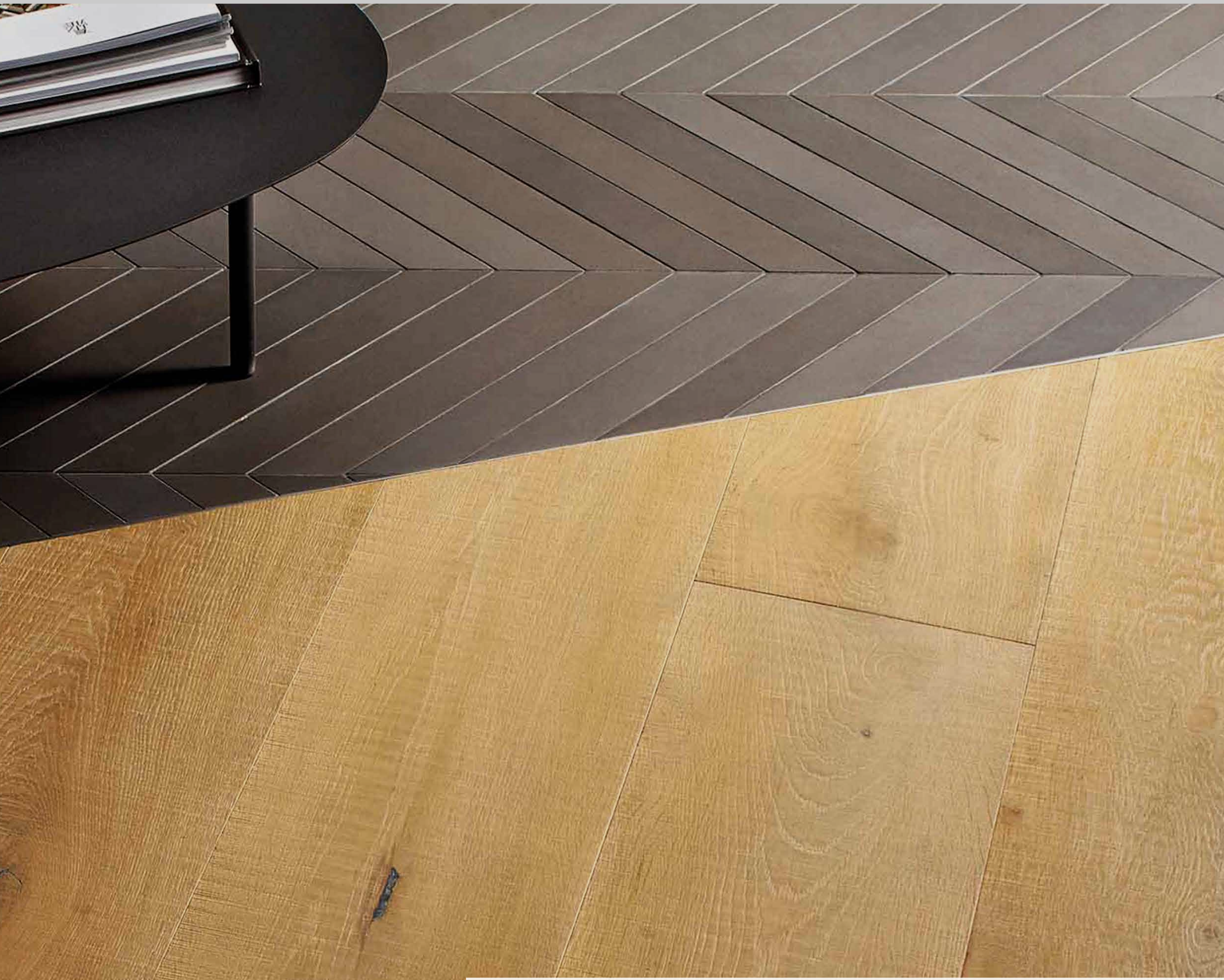
All data stated for the financial year ended 31 December 2018 or as at 31 December 2018

LEADING THROUGH... EXPERTISE



Offering years of operating expertise supplemented by additional market segment knowledge via acquisition

26 YEARS OF OPERATION



2,612
EMPLOYEES

10
PRIMARY PRODUCT CATEGORIES

31%
UK EMPLOYEES +10 YEARS WITH HEADLAM

332
MANAGERS

All data stated for the financial year ended 31 December 2018 or as at 31 December 2018

WHAT WE DO


SUPPLIERS


SALES

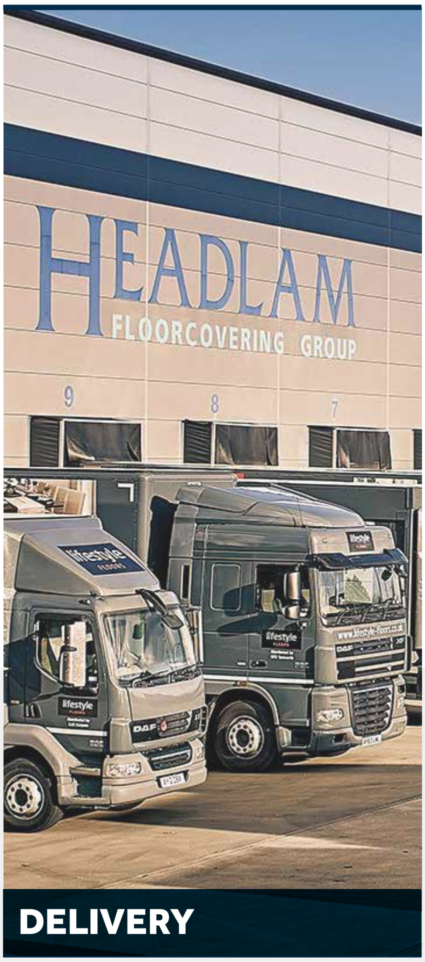

CUSTOMER SERVICE

Operating for 26 years and employing over 2,600 people, Headlam is Europe's leading distributor of floorcoverings.

Headlam provides the distribution channel between suppliers and trade customers of floorcoverings. Working in partnership with suppliers from 22 countries manufacturing a diverse range of floorcovering products and ancillary accessories, Headlam provides an unparalleled route to market for their products across the UK and certain Continental European territories.

The utilisation of an outsourced distribution channel enables manufacturers to focus on their core activities, incur reduced costs associated with distribution, and benefit from localised sales, marketing and distribution expertise that provides a more effective and greater route to market for their products.

To maximize customer and market penetration, Headlam comprises 67 individual businesses in the UK and Continental Europe (France, the Netherlands and Switzerland), each operating under their own unique trade brand and utilising individual sales teams.



Headlam's extensive customer base, operating within both the residential and commercial sectors and comprising principally independent retailers and flooring contractors, receives the broadest product offering supported by next day delivery as well as additional marketing and other support.

Headlam's offering is enabled through its unrivalled operating expertise, long-established supplier and customer relationships, and comprehensive distribution network.

Following years of considerable investment, Headlam's distribution network currently comprises four national distribution hubs, 19 regional distribution centres and a supporting network of smaller warehouse premises, trade counters, showrooms and specification centres.

In 2018, Headlam worked with 199 suppliers and fulfilled over 5.3 million customer orders.

CHAIRMAN'S WELCOME

I am pleased to present my first Annual Report and Accounts having succeeded Dick Peters as Chairman upon his retirement after last year's AGM.

Headlam is a market-leading business developed around an established business model and underpinned by strong operational cash generation and balance sheet strength. I am continually impressed by the commitment of our people, who I especially want to thank for their considerable efforts during 2018, in what was a demanding year due in the most part to the UK market weakness that prevailed throughout. Despite this backdrop, it is pleasing to report financial results marginally ahead of 2017 and an improved dividend for 2018 totalling 25.0 pence (subject to shareholders' approval at the AGM).

During the year we completed the planned succession and development of our Board by adding individuals with a wealth of new experience and expertise pertinent to the delivery of our strategic aims and future ambitions. As previously detailed, Amanda Aldridge was appointed a Non-Executive Director in February 2018 and assumed the role of Chair of the Audit Committee in June 2018 following my stepping down from the position after three years. Additionally, in conjunction with Andrew Eastgate's forthcoming retirement in May 2019 after nine years' service, Keith Edelman and Alison Littley were appointed Non-Executive Directors and assume the positions of Senior Independent Director and Chair of the Remuneration Committee respectively. I am delighted to welcome them to Headlam and their experience spanning the areas of supply chain management, consumer and customer-led service innovation, and commercial development mean their contributions will be invaluable. I also lastly wish to thank Andrew for his considerable service to the Company.

As announced earlier this year, 2019 is likely to present us with further general market weakness in the UK and an increased element of economic and political uncertainty. As previously announced, this is one of the factors contributing to our expectation that 2019 profits will be lower than 2018. This situation serves to reinforce our concerted commitment to pursuing multiple efficiency initiatives aimed at improving operational and financial performance, developing the business, and providing a more robust platform for future growth.

INVESTMENT CASE

Significant scale and longevity of operations underpinned by capital efficiency and progressive dividend policy

MARKET LEADER

- 26 years of operations and expertise
- Significant scale and dense coverage, with multiple businesses and touch-points
- Broadening overall industry position, with room for growth

RELATIONSHIPS

- Long-established supplier and customer relationships
- Partnerships with 199 suppliers in 22 countries
- Broad and diverse customer base, with 71,384 active accounts and over 5.3 million orders processed in 2018

All numbers given are for the financial year ended 31 December 2018

During 2019, I expect to see increasing momentum towards and contribution from these initiatives, aided by the enhanced Board and an expanded senior team following recent appointments bringing additional skills and expertise into the business.

Against this backdrop of confidence in our ability to deliver an improved future performance, the Board has reiterated its commitment to a progressive dividend policy, with the 2019 dividend currently intended to be maintained in-line with that of 2018.

I look forward to being able to update you on our progress during the year and within next year's Report.

Philip Lawrence
Non-Executive Chairman

6 March 2019

DISTRIBUTION NETWORK

- Significant warehousing network and inventory positions, supporting the customer service proposition
- Substantial time and resources required to replicate, creating a significant barrier to entry
- Largely freehold portfolio underpinning value, with property, plant and equipment assets totalling £102.0 million

FINANCIAL STRENGTH

- Strong balance sheet and operational cash generation
- Net cash of £36.7 million as at 31 December 2018, and included acquisition spend of £9.1 million during the year
- Strong cash generation, with cash generated from operations 121% of operating profit

EFFICIENCY INITIATIVES

- Gross margin improved 130 basis points to 32.3% over two years*, with focus on gradual improvement
- Multiple efficiency initiatives underway aimed at improving operating margin
- Initiatives at early roll-out phase and trialling to positively impact coming years

DIVIDEND

- Continued commitment to a progressive dividend policy
- Total ordinary dividend of 25.0 pence in 2018
- Intention to maintain 2019 dividend in-line with 2018 reflecting confidence despite lower profit guidance

* Gross margin for 2016 financial year restated to present comparatives on a consistent basis due to the reclassification in 2018 of some items between revenue, cost of sales and operating expenses to better reflect their nature.

CHIEF EXECUTIVE'S REVIEW

"Despite the generally softer trading backdrop that was evident throughout 2018, it was pleasing that total revenue increased by 2.3% in the year to £708.4 million (2017: £692.5 million)"*

Steve Wilson
Chief Executive

2018 Financial Performance

Despite the generally softer trading backdrop that was evident throughout 2018, it was pleasing that total revenue* increased by 2.3% in the year to £708.4 million (2017: £692.5 million). The Continental European businesses in aggregate outperformed this result, growing 5.3% and representing 14.7% of total revenue (2017: 14.3%), while the UK improved by 1.8% and accounted for 85.3% of total revenue (2017: 85.7%).

Disappointingly, like-for-like** revenue declined in both the UK and Continental Europe, 4.2% and 1.8% respectively. This was a reflection of the generally softer markets, more keenly felt in the UK, with a noticeable weakness in the UK residential sector where the Company's distribution business is more heavily weighted. This particular weakness resulted in the percentage of total revenue attributable to the residential sector declining to 64.6% in the year (2017: 67.9%).

The UK like-for-like performance did, however, show an improvement in the second half of the year compared with the first (H1 2018: -5.5%; H2 2018: -3.5%). The commercial sector reversed a small decline in the first half to end the year up 0.6%, and the full-year residential sector decline of 6.2% represented an uplift on the first half (H1 2018: -7.6%; H2 2018: -5.1%). Pleasingly, the month of September was comparatively strong, recording a good like-for-like uplift on the previous year in both the residential and commercial sectors, with September noteworthy for being when the majority of the educational refurbishment activity completes.

In contrast to the UK, the second half performance in Continental Europe was weaker than the first, moving from a modest positive like-for-like position to a decline (H1 2018: +1.7%; H2 2018: -4.5%), and the residential sector was positive for the year (FY 2018: +2.8%) while the commercial sector declined (FY 2018: -6.9%).

Gross margin* increased by 80 basis points during the year, from 31.5% in 2017 to 32.3%, an historic high. The improvement in the year was due in the most part to an increased contribution from the higher-margin specification business area, as well as the benefits from early settlement discount on trade creditors and ongoing pricing discipline implemented across the Company since late 2016.

Due to year-on-year inflationary cost increases and the expanded specification business area having a higher overhead percentage when compared with revenue, total underlying*** distribution expenses and administration costs increased to 26.1% as a percentage of revenue (2017: 25.2%). This 90 basis points increase offset the gross margin improvement leading to the year's underlying operating margin declining by 10 basis points from 6.3% to 6.2%.

Underlying profit before tax increased by £0.3 million during the year to £43.4 million compared with £43.1 million for the previous year, and statutory profit before tax of £40.4 million was marginally down on the prior year (2017: £40.7 million).

The net cash position increased year-on-year, being £36.7 million as at 31 December 2018 (2017: £35.3 million), and included acquisition spend during the year of £9.1 million on five smaller businesses to further enhance and broaden the Company's industry and geographical position.

Efficiency Initiatives

Ten efficiency initiatives currently being pursued are focused on improving operational practices and financial performance, and are collectively aimed at improving the Company's operating margin. Whilst most of these initiatives are at an early-stage in their implementation, we have previously highlighted the initiative focused on the streamlining of processes and pricing discipline implemented since late 2016. This initiative has contributed to gross margin improving by 130 basis points since 2016 and reaching an historic high in 2018. Other initiatives which began to contribute to the financial performance in 2018 included the work completed in connection with a revised group procurement approach to Goods Not for Resale ('GNFR') and changes to our vehicle leasing contracts.

Additionally, we are making progress with our trials in relation to inventory management and more effective utilisation of the delivery fleet. Thus far, the inventory management trial at Coleshill, our largest distribution hub, has resulted in improved customer service through a meaningful reduction in the number of stock-outs, whilst creating surplus warehouse capacity of approximately 10%. This increased capacity has helped support the Company's investment in additional inventory across its fastest-moving products in 2019 to partially mitigate potential disruption and maintain levels of customer service in the event of a hard Brexit.

STRATEGIC FOCUS:
EFFICIENCY INITIATIVES TO IMPROVE PERFORMANCE

Ten efficiency initiatives currently being pursued are focused on improving operational practices and financial performance, and are collectively aimed at improving the Company's operating margin. Whilst most of these initiatives are at an early-stage in their implementation, we have previously highlighted the initiative focused on the streamlining of processes and pricing discipline implemented since late 2016. This initiative has contributed to gross margin improving by 130 basis points since 2016 and reaching an historic high in 2018.

See more on page 18

10 MAIN INITIATIVES

MOSTLY EARLY-STAGE

The review around the more effective utilisation of our delivery fleet incorporates two separate initiatives both currently being trialled, these being dynamic route planning and the aggregation and consolidation of geographic specific deliveries. The latter deliveries initiative, whereby deliveries destined for the same customers or geographic location by different Headlam businesses are consolidated at, and delivered from, the nearest warehouse location, is currently being trialled in South Wales. The proposed benefits of improved customer service levels, reduction in the cost to serve and reduced carbon footprint are beginning to materialise. There is potential to extend this trial across a number of the Company's other locations.

As each of the ten initiatives continues to be progressed, we will see increasing benefits throughout 2019 and a more meaningful impact on financial and operational performance in 2020 and beyond. It is our aim to expedite activity as much as possible while ensuring there is no disruption to the business and customer service levels, which ultimately influences the pace of implementation.

Continental Europe

In Continental Europe, following investment in people and an acquisition during 2018, the emphasis has been on revenue improvement and restoring their collective profitability, with additional focus on higher margin products and certain market segments. In the Netherlands, against a positive market backdrop, there has been investment in new product ranges, particularly luxury vinyl tile ('LVT'), and progress towards extracting operating synergies following the acquisition of Dersimo BV in March 2018, which enlarged the Company's Dutch footprint.

In Switzerland, following continued investment in the specification-focused sales team and showrooms, there have been positive developments in terms of product mix and associated higher margin revenue.

A strategic review has been completed at the French business following the appointment of a new Managing Director in 2018 to address the previous decline in performance. Areas now being focused on, in association with an improved sales team, include specification and higher-margin own-branded products, and leveraging of the business's position as the only national distributor. Progress to date in 2019 has been encouraging.

Acquisitions

We completed five smaller strategic acquisitions in 2018, spending a total of £9.1 million during the year. Ashmount Flooring Supplies Limited, Rackhams Limited and Garrod Bros Ltd expanded our footprint in Greater London, an area where we have historically been underrepresented. Dersimo BV increased our presence and geographical coverage in the Netherlands, and CECO (Flooring) Limited based in Carryduff, south of Belfast, extended our position in the specification area which provides an opportunity to broaden our overall position in the industry. We are delighted to welcome the businesses and their employees to Headlam, and to be able to provide support for their future growth and development through our financial and centralised resources.

Whilst we are a leading business in aggregate, there are a number of market segments and product categories where we hold underweight positions, and this provides scope for growth whether organically or through further strategic acquisitions. While our present overarching focus is the improvement of performance of the existing business portfolio and network, we continue to monitor a deliberately reduced pipeline of acquisitions, and remain responsive to further opportunity.

Investments and Capital Expenditure

In-line with our focus on improvement, during 2019 investment and capital expenditure will primarily be focused on the development of our new regional distribution centre in Ipswich which will enable greater network optimisation and provide improved support to our surrounding businesses and customers in the South East of England. In October 2018 we received planning approval for the centre and as of last month acquired the land at a cost of £4.0 million. Ground-work preparation will start in the second quarter of this year to enable the project to move to the construction phase by the second half of 2019. The current timetable indicates that the centre, which is estimated to cost a total of approximately £26 million, should be operational in mid-2020.

In addition to ongoing maintenance capital expenditure of typically £3-4 million per annum in connection with the running of our operations in a largely freehold property portfolio, there has been recent investment in people and expertise. Some of this investment is specifically to support the timely delivery of our efficiency initiatives.

People

As detailed in the Chairman's Welcome, the Board has been supplemented with a wealth of experience and expertise. Additionally, we have made several operational appointments, the most senior being the UK Operations Director who will join the Company and Senior Management Team shortly. I believe we now have all the appropriate people in place to fulfil our ambitions.

Dividends

We are committed to providing improving returns to shareholders and a progressive dividend policy****. The Board seeks to protect dividend payments against short-term fluctuations in profit resulting from temporary adverse trading conditions. This commitment is enabled by the strength of our balance sheet, and additionally reflects our confidence in the ability to improve profitability and maintain a strong balance sheet and operational cash generation going forward.

The Board has proposed a final ordinary dividend of 17.45 pence (2017: 17.25 pence), payable on 1 July 2019 to shareholders on the register as at 7 June 2019. This brings the total ordinary dividend declared and proposed in respect of 2018 to 25.0 pence, a slight increase on the 24.8 pence in 2017.

Current Trading and Outlook

As advised in January 2019, we have taken a prudent view of 2019 and expect revenue to be in-line with 2018 due to the anticipated further general weakness in the UK market, and as a consequence it is anticipated that underlying profit before tax will be lower than 2018 due to a number of factors. These include the anticipated movement in revenue mix and associated margin, the year-on-year inflationary pressure on distribution costs and administrative expenses, and the efficiency initiatives being predominately at an early stage and not yet sufficiently material in their contribution to offset the current weak market backdrop and increases in overheads.

It is gratifying that despite being an established and leading business with considerable financial strength, there remain multiple initiatives and measures under our control which should enable improvement in performance going forward. This position provides the confidence to support our current intention to maintain the 2019 dividend in-line with that of 2018.

We have had a positive start to the year, with both the UK and Continental Europe up on a like-for-like revenue basis for the year-to-date. I would like to thank all our people for their hard work and dedication in 2018, and delivery of an improved financial performance in a somewhat challenging year. I believe that with the improvements we are putting in place and the evolution of our business firmly underway, 2019 will be a year of progress towards our objectives.

Steve Wilson
Chief Executive

6 March 2019

* All prior year revenue, like-for-like revenue and gross margin numbers are restated to present comparatives on a consistent basis with 2018. This follows the reclassification in 2018 of some items between revenue, cost of sales and operating expenses to better reflect their nature.

** Like-for-like revenue is calculated based on constant currency from activities and businesses that made a full contribution in both the 2018 and 2017 periods and is adjusted for any variances in working days.

*** Underlying is before non-underlying items which includes intangibles amortisation relating to businesses acquired, acquisition fees, contingent consideration movements, non-recurring pension costs in relation to guaranteed minimum pension ('GMP') equalisation and non-recurring costs relating to senior personnel changes.

**** A progressive dividend policy is one where the dividend is expected to rise at least in-line with increases in earnings per share, and if earnings per share falls, the dividend will not be reduced.


lifestyle

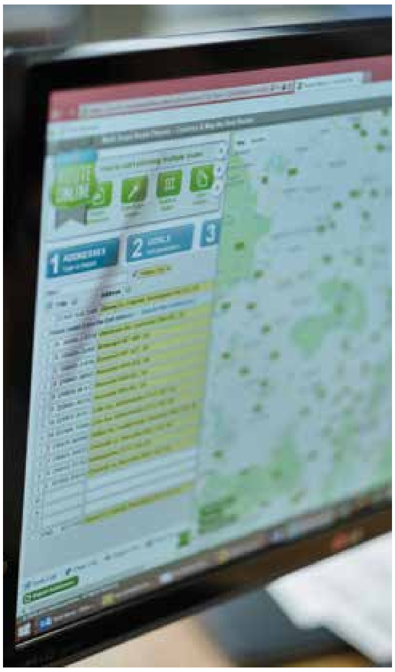
IMPROVING PERFORMANCE

A number of efficiency initiatives aimed at lowering the breakeven point and improving operating margin are at the early roll-out phase or trialling. They will yield increasing benefits as 2019 progresses and have a more meaningful impact in 2020 and beyond. An overview of the ten main initiatives are given in the table below.

Initiative	Description	Status
1. Inventory Management	A stock reordering and management algorithm to i) improve stock-turn and increase warehouse capacity; ii) reduce stock-outs and improve customer service; iii) focus working capital investment on fastest-moving products; and iv) enable improved supplier production scheduling.	2018: Trialled 2019: Roll-out phase
2. Dynamic Route Planning	A dynamic route planning software system to improve usage and efficiency of the commercial fleet. Giving rise to better vehicle load-fill, and associated cost savings through reduced fleet number and fuel consumption.	2018: Trialled 2019: Larger scale trials
3. Delivery Fleet Utilisation	Consolidation of geographic specific deliveries, whereby deliveries from different Headlam businesses to the same customer are consolidated into a delivery from the nearest warehouse location. Leading to enhanced customer service and improved operating efficiencies through reducing the cost to serve (via fleet and fuel consumption) whilst also reducing carbon footprint.	2018: Initial trialling 2019: Potential trial roll-out to additional geographical locations
4. Vehicle Leasing	Extend the life of the vehicle leasing contracts across both the commercial vehicle and company car fleet. Delivers reduced lease costs and other associated cost savings, including costs connected to renewal and replacement.	2018: Commercial vehicle fleet migrated to new contract 2019: Company car fleet initiated
5. Goods Not For Resale (GNFR)	Review and leverage group purchasing (group procurement) to deliver cost savings and service improvements in relation to GNFR. Introduction of aligned group practices also aimed at reducing costs. Categories to include: Print; Consumables; Promotional Items; Continuous Stationery; Mobile Telecommunications; and Packaging.	2018: Tenders and contracts entered into 2019: Further tenders and actions initiated

Initiative	Description	Status
6. Administrative Expenses	Examine all components within Administrative Expenses with the objective of arresting the growing percentage of revenue it accounts for year-on-year, and ultimately improve operating margin.	2018: Analysis 2019: Review and planning, initial implementation 2020
7. Cloud Migration	Migration of all business servers to the Cloud to increase security and resilience, speed up processes with associated efficiencies, and allow a more flexible response to support future growth and expansion.	2018: Successful migration of first site 2019: Full migration completed
8. Distribution Network Configuration	Proposed new regional distribution centre in Ipswich, UK, to support businesses in the wider area, provide growth capacity, and enable greater network optimisation.	2018: Planning permission granted and construction consultants engaged 2019: Land acquisition and construction commence
9. Streamlining of Processes	Elimination of inconsistent pricing practices across the group, coupled with a move towards a more disciplined pricing policy and focus on higher margin and exclusive products. Objective of improving and maintaining gross margin above historic levels.	2018: Gross margin improvement of 80 basis points* 2019: Maintain improvement
10. Data Management and Analytics	Introduce a business data management and analytics software solution to provide improved visibility of key performance metrics across the group. Enabling better identification of inefficiencies, and improved operational decision making and cost control.	2018: Software identified 2019: Implementation

* Gross margin for 2017 financial year restated to present comparatives on a consistent basis due to the reclassification in 2018 of some items between revenue, cost of sales and operating expenses to better reflect their nature.



EVERY ROOM HAS A FLOOR

Almost all need a covering

Introduction
It might seem like an obvious statement, but every room has a floor and almost all require some form of covering.

The marketplace for floorcoverings can be divided into residential and commercial sector usage, with the total UK floorcoverings market valued at £2.05 billion in 2018*. Supporting this value is a residential sector comprising 27.2 million households with an estimated 146.9 million rooms** and a commercial sector spanning, amongst others, buildings within the health, education, leisure, retail, office and hospitality industries.

Market Dynamics
The residential and commercial sectors have largely differing demand drivers and product requirements in terms of functionality, design characteristics and size of area to be covered.

Demand in the residential sector is mainly driven by refreshment or refurbishment of a single room or several rooms at a time and, as such, typically tends to be a non-essential, discretionary purchase. This is much less true of the commercial sector, which operates on a far greater scale and where a replacement requirement is a key driver. Health and safety and the provision of a safe, clean and comfortable working environment are key drivers of replacement demand particularly within the areas of office, health and education. Demand from the hospitality, retail and leisure industries is also influenced to a greater degree by innovation and design trends, with an aspiration to update furnishings to keep them current.

Due to the differing dynamics behind the demand for product, the residential sector tends to be more susceptible, at least in the short-term, to a weaker economic environment than the commercial sector which tends to operate on less discretionary spend parameters, larger budgets and longer planning timelines.

One of Headlam's strategic aims (detailed on page 24) is to broaden its position within the overall industry; expanding its revenue streams, customer base and presence in certain market segments and sectors. During 2018, Headlam increased its presence in the specification segment of the marketplace, which is predominately focused around longer-term project work with a greater weighting towards the commercial sector than Headlam's core distribution businesses (see 'Market Segment Focus' box on page 21).

Manufacturers & Product
Manufacturers of floorcoverings are focused on constant technical innovation and the development of improved materials and floorcovering solutions. Significant investment has been made in technology and manufacturing processes leading to a broadening range of products with improved functionality available in the marketplace. This in turn helps create ongoing customer demand and support the growth of the market. Due to the technical advancements made by the manufacturers, certain product categories have outperformed in recent years including luxury vinyl tile ('LVT') and the associated floor preparation materials.

£2.05 BILLION
UK MARKET VALUE*

146.9 MILLION
UK RESIDENTIAL ROOMS**

£133
HEADLAM'S AVERAGE ORDER SIZE***

* Source: AMA Research, December 2018 (estimate), and expressed by reference to manufacturer's selling price
** Source: ONS
*** The Company's distribution businesses, for the financial year ended 31 December 2018

Image from Domus

MARKET SEGMENT FOCUS: SPECIFICATION

The specification consultant's key relationships are with professionals who act as the 'specifier' on projects requiring floor and wallcovering products. 'Specifiers' are principally architects, designers, developers and end-users who determine the materials and products to be used in a particular project having defined the preferred product characteristics and design. This information is then passed to the 'buyer', typically a contractor, who makes the final purchasing decision and places the order with the specification consultant who then supplies the products.

The specification consultant's sales teams utilise their relationships with specifiers to identify, target and track projects through the concept and planning stage, and ultimately get their products specified and ordered following a tender process.

Successful specification is reliant on the relationships with both specifiers and buyers, quality of service levels, technical expertise, and ability to provide a compelling and typically exclusive product range which caters to the specifier's emphasis on design as well as functionality. Due to the design-led nature of the business, specifiers often look to specification consultants for inspiration and advice as well as guidance on trends.

Projects span the commercial and residential sectors, ranging from residential homes to office, and other commercial categories including healthcare, education, retail, leisure, hospitality and transportation. The sales and order process can cover a few months to well over a year dependent on the size and complexity of the project, and specification consultants typically have extensive pipelines of project opportunities and long-term order books.

CECO

During 2018, Headlam acquired CECO (Flooring) Ltd, a leading specification consultant based in Carryduff, south of Belfast, to expand its presence in the specification marketplace. Established in 1978, CECO has partnerships and exclusive distribution rights with a number of leading manufacturers of tiles, carpet tiles and architectural stone products enabling it to offer an unrivalled portfolio of floor finishes and wall solutions to retail and commercial customers. Covering all sectors of the market, CECO has been involved in many prestigious projects including high-profile office fit-out work for global names such as Google and Facebook. Recent and upcoming projects include the new mental health facility at Belfast City Hospital, HM Prison Maghaberry and HMRC's new headquarters in Belfast.


Image from CECO

The utilisation of an outsourced distribution channel enables manufacturers to focus on their core activities, incur reduced costs associated with distribution, and benefit from localised sales, marketing and distribution expertise that provides a more effective and broader route to market for their products.

As stated within Our Strategy on page 24, Headlam continually engages with manufacturers around the world to partner in bringing a broad range of innovative and sometimes exclusive products to market, and enhance the product range it can offer its customer base.

Customers & Processing

Within the trade segment of the marketplace, the customer base includes independent retailers, flooring contractors, specialist multiples, non-specialist multiples, architects, interior designers and housebuilders.

Supporting sales and marketing activities and order characteristics vary markedly between the customer groups. Independent retailers, for example, have frequent interaction with sales representatives at their premises and place regular, smaller orders reflecting the end-consumer's refurbishment of a single room or several rooms at a time.

The interaction with flooring contractors is also mainly conducted by sale representatives, but due to the focus on the commercial sector there is greater consideration of the technical requirements of products and therefore more support provided in terms of technical advice and product options, and orders are much larger and less frequent.

Customers' orders will on the whole require some form of preparation or processing prior to delivery. This includes rolls of carpet or vinyl and boxes of palletised goods such as engineered wood and ceramic being cut to length or broken-down to meet the customer's specific order size. Specialised equipment required to process orders includes cutting tables, sortation units and specially adapted handling equipment, with a large degree of material handling expertise required.

Headlam has developed its footprint and operations to cater to the differing needs of its customer base. The trade counter network is designed to support the local flooring contractor who typically doesn't have premises with warehousing capacity and prefers to collect orders, while next day delivery particularly benefits the independent retailer who tends to have a limited ability to hold stock due to small premises and prefers delivery just-in-time for end-consumer installation.

CREATING VALUE FOR OUR STAKEHOLDERS

INPUTS AND SOURCES OF COMPETITIVE ADVANTAGE

- 26 years of industry expertise and knowledge
- Market-leading position
- Extensive distribution network
- Partnerships with a global supplier base
- Unparalleled product offering
- Longstanding customer relationships
- Broad customer base
- Commitment to customer service
- Considerable investment over many years
- Financial strength and centralised support
- Expanding route to market

WHAT WE DO

Europe's leading distributor of floorcoverings, providing the distribution channel between suppliers and trade customers. Provides suppliers with an unparalleled route to market for their products, and customers with the broadest product offering supported by comprehensive customer service and next day delivery.

Years of operation

+26

HOW WE OPERATE

Suppliers & Products

Work closely with a global manufacturing supply base to offer over 30,000 product units to customers covering all principal product categories. Build on supplier relationships to continue expanding product offering to customers.

Suppliers

+110

Businesses & Extensive Network

Comprise 67 businesses in the UK and Continental Europe, each operating under their own unique trade brand and utilising individual sales teams to maximise customer and market penetration. Each business supported by centralised and financial resources and extensive distribution network.

Sales reps

+360

REINVESTMENT

UNDERPINNED BY

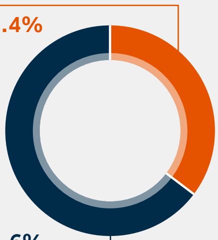
Clear strategy

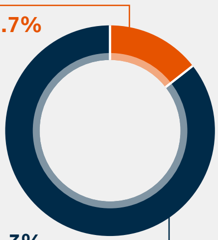
Read more on page 24

Robust governance

Read more on page 52

Revenue





Customers & Sectors

Customers span both the residential and commercial sectors, and comprise principally independent retailers and flooring contractors. Focused on supporting customers and their growth through sales and marketing support, credit and next day delivery.

Active customer accounts in 2018

+71,000

Expanded Industry Position

Extend position within the industry, and customer base, through focus in other market segments, including specification, working principally with interior designers, architects and building developers on projects.

Specification projects in 2018

+2,750

Informed risk management

Read more on page 34

Empowering culture

Read more on page 40

BENEFITS FOR STAKEHOLDERS

Employees

- Stability and security, and sense of ownership
- Long-standing relationships with other stakeholders
- Benefits including employee share-save schemes and performance based rewards
- Feedback actively encouraged, with a commitment to fostering an open and positive working environment

Suppliers

- Unparalleled route to market for products
- Able to supply large volumes
- Extensive market and customer insight, and feedback on sales potential and positioning of product
- Marketing support

Customers

- Broadest product offering, including exclusive lines
- Next day delivery satisfying end-consumer demand, and minimising need to hold stock
- Market awareness of new product lines and trends
- Point-of-sale materials, new product training and provision of credit

Shareholders

- Commitment to the highest level of corporate governance
- Focused on long-term sustainable growth
- Strong cash generation and balance sheet
- Progressive dividend policy

SUSTAINABLE LONG-TERM VALUE

Our strategy is based upon building a successful company delivering sustainable long-term value

Strategic Area	Strategic Objective
DEVELOP AND BROADEN	‣ Continue developing the market-leading distribution business ‣ Broaden position within the overall industry to expand revenue streams and customer base ‣ Grow in identified product categories and market segments
NETWORK UTILISATION	‣ Improve performance through better utilisation of the network and collaboration amongst the group ‣ Review existing configuration to remove inefficiencies, improve capacity and customer service ‣ Leverage the network and be the intermediary of choice for suppliers and customers
PERFORMANCE AND MODERNISATION	‣ Pursue multiple efficiency initiatives to improve operational and financial performance ‣ Update existing operational processes and business practices ‣ Build the business reflecting market and industry evolution
CULTURE AND PEOPLE	‣ Invest in people through training, support and creating a positive working environment ‣ Focus on culture and opportunity to attract and retain the best talent ‣ Extend a collaborative culture and common purpose to deliver success
SUPPLIERS	‣ Maintain and build upon the basis of a true partnership ‣ Provide a cost efficient and most effective route to market for products ‣ Engage further with suppliers to develop product categories and overall offering
CUSTOMERS	‣ Maintain commitment to achieving the highest level of customer service and support ‣ Continue building customer base through service quality, product diversity and market segment expansion ‣ Respond to evolving customer demands and industry trends

25.0 PENCE
TOTAL ORDINARY DIVIDEND FOR 2018

1.7
FREE CASH FLOW COVER RATIO

FINANCIAL REVIEW

"The total dividend payable in respect of 2018 equates to an earnings per share cover ratio of 1.6, cash outflow of £21.0 million, and reflects a free cash flow cover ratio of 1.7"

Chris Payne
Chief Financial Officer

2017 Income Statement Restatement

As disclosed in the 2018 Interim Report, the Income Statement for 2017 has been restated due to the reclassification, in 2018, of some items between revenue, cost of sales and operating expenses to better reflect their nature. The 2017 restated results are presented in a consistent manner with 2018 and all references to year-on-year movements are on a restated basis.

Revenue

During the year, total revenue improved by 2.3% from £692.5 million to £708.4 million, an increase of £15.9 million. Like-for-like* revenue declined in both the UK and Continental Europe, by 4.2% and 1.8% respectively.

UK

The Company's UK revenue performance was marginally up on 2017 at £604.2 million (2017: £593.5 million), reflecting a weak market backdrop throughout the year compared with 2017, particularly in the residential sector, offset by contributions from acquisitions. Year-on-year revenue from acquired businesses during the year amounted to £33.1 million while like-for-like revenue declined by £24.7 million.

The residential sector represented 66.3% of UK revenue in 2018 (2017: 70.4%), a reduction of 4.1% and 6.2% on an absolute and like-for-like basis respectively.

	£000	%	£000	%
Revenue for the year ended 31 December 2017 (restated)				
UK	593,476	85.7		
Continental Europe	99,064	14.3		
			692,540	100.0
Incremental items during the 12-month period to 31 December 2018				
UK:				
Like-for-like*	(24,651)	(4.2)		
One additional working day	2,275	0.4		
Acquisitions	33,050	5.6		
			10,674	1.8
Continental Europe:				
Like-for-like*	(1,791)	(1.8)		
Changes in working days	112	0.1		
Acquisitions	6,648	6.7		
Translation effect	240	0.2		
			5,209	5.3
Total movement			15,883	2.3
Revenue for the year ended 31 December 2018				
UK	604,150	85.3		
Continental Europe	104,273	14.7		
			708,423	**100.0**

* Like-for-like revenue is calculated based on constant currency from activities and businesses that made a full contribution in both the 2018 and 2017 periods and is adjusted for any variances in working days.

As a consequence, there was a slight shift in the business mix towards the commercial sector, now representing 33.7% of UK revenue in 2018 (2017: 29.6%), although the year-on-year movement was almost flat on a like-for-like basis, up 0.6%.

Continental Europe

The Continental European businesses delivered a 5.3% increase in revenue to £104.3 million, with this growth, driven by an acquisition in the Netherlands during the year, being slightly offset by the 1.8% decline in like-for-like revenue.

Continental Europe accounted for 14.7% of total revenue in 2018, up from 14.3% in 2017. In contrast to the UK, the weighting between the residential and commercial sector revenue showed a slight movement towards residential compared with 2017, accounting for 54.7% of revenue (2017: 52.6%).

Gross Margin

Gross margin increased by 80 basis points in the year from 31.5% to 32.3% predominately as a result of the positive impact of higher margin acquisitions (55 basis points), with the balance largely due to the benefit arising from anticipated early settlement discount on trade creditors and the ongoing focus on pricing discipline since late 2016.

Expenses

Combined distribution costs and administrative expenses increased by 6.2% up £11.0 million to £187.7 million. On an underlying basis, and after adjusting for the impact of the acquisitions during the year, total costs actually decreased by £3.3 million which was largely driven by a reduction in performance-related bonus payments offsetting the 2% cost of living award given to all UK employees bar the Executive Directors and Senior Management Team.

Underlying distribution costs and administrative expenses expressed as a proportion of total revenue increased from 25.2% in 2017 to 26.1% in 2018. This was predominately as a consequence of the expansion into the specification business area which typically has a higher fixed cost base compared with the Company's distribution businesses.

The relative proportions of distribution costs and administrative expenses as a percentage of total expenses for 2018 remained largely consistent at 72.7% and 27.3% respectively (2017: 72.9% and 27.1%).

After adjusting for the effect of the acquisitions during the year, the annual movement in other expenses was relatively modest, with the next largest item being the £3.2 million decrease in people costs reflecting the reduction in performance-related bonus payments offset by the aforementioned 2% cost of living award.

Items totalling £2.9 million (net) have been treated as non-underlying in 2018 (2017: £2.4 million). These non-underlying items related to amortisation of acquired intangible assets (£1.8 million), acquisition related fees for the five acquisitions made in 2018 (£0.5 million), non-recurring people costs (£0.8 million), pension equalisation costs associated with past service liabilities (£1.2 million) and a credit from the release of contingent consideration accrued for the Domus acquisition in 2017 (£1.4 million). These are discussed in detail in note 3 to the Financial Statements.

	Total expenses		Distribution		Administration	
	£000	%	£000	%	£000	%
Expenses for 2017	176,720		127,145	71.9	49,575	28.1
Significant movements in 2018:						
People cost	(3,170)	(29.0)	(339)	(4.8)	(2,831)	(74.3)
Vehicle expenses	244	2.2	238	3.4	6	0.1
Carriage and packaging costs	(205)	(1.9)	(205)	(2.8)	–	–
Sampling investment	(387)	(3.5)	(387)	(5.5)	–	–
Legal and professional fees	(543)	(5.0)	–	–	(543)	(14.3)
Effect of acquisitions	13,765	126.1	7,795	109.7	5,970	156.6
Other	669	6.1	2	0.0	667	17.6
Underlying sub total	10,373	95.0	7,104	100.0	3,269	85.7
Non-underlying	543	5.0	–	–	543	14.3
Total before currency translation	10,916	100.0	7,104	100.0	3,812	100.0
Currency translation	107		67		40	
Expenses for 2018	**187,743**		**134,316**	**71.5**	**53,427**	**28.5**

Operating Profit

Underlying operating profit was marginally up on 2017 at £44.3 million (2017: £43.8 million), however, the underlying operating margin was slightly reduced at 6.2% (2017: 6.3%). The underlying operating margin was almost maintained despite the £7.6 million loss of gross profit from a reduction in like-for like-revenue. This was due to the positive contribution from acquisitions of £2.8 million, improvement in pricing, a reduction in cost of sales for the anticipated early settlement discount received from the year-end trade creditors, reduction in performance-related bonus payments, and ongoing operating cost mitigations.

One of the key areas of strategic focus is improving the Company's operating efficiency. The Company has a rolling programme of margin improvement initiatives, most of which are at an early-stage of implementation with some earlier ones having been commenced in 2017 or 2018. Some of these started to deliver initial benefits in 2018, with more meaningful contributions to come. These primarily were achieved by operating a group procurement function in relation to a number of goods not for resale and an extension of commercial vehicle and car leasing contracts. Commenced in 2018, these changes will deliver an accumulated cost saving of over £1.0 million per annum once fully deployed following the full fleet replacement cycle over the next few years and as supply contracts come up for renewal.

	Underlying £000	Non-underlying £000	Total £000
Operating profit 2017	43,783	(2,399)	41,384
Gross margin improvement in 2018:			
Volume reduction	(7,570)	–	(7,570)
Pricing benefit	954	–	954
Anticipated trade creditor settlement discount	1,049	–	1,049
Effect of acquisitions	16,537	–	16,537
	10,970	–	10,970
Expense changes			
Distribution	624	–	624
Administration	2,661	(543)	2,118
Effect of acquisitions	(13,765)	–	(13,765)
Total increase	(10,480)	(543)	(11,023)
Operating profit 2018	**44,273**	**(2,942)**	**41,331**

Tax

The underlying effective tax rate for 2018 was 17.9% (2017: 18.5%) which is lower than the headline rate of corporation tax in the UK of 19.0%. This difference is largely due to an adjustment in prevailing overseas tax rates and a release in creditors for uncertain tax positions following the ongoing review of tax risks in the Company. The full effective rate of tax in 2018 was lower at 17.2% (2017: 19.1%) due to non-underlying tax credits.

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'.

Ordinary Dividends and Earnings Per Share

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

The total dividend payable in respect of 2018 equates to an earnings per share cover ratio of 1.6 (2017: 1.6), cash outflow of £21.0 million, and reflects a free cash flow (cash from operating activities less capital equipment spend) cover ratio of 1.7 (2017: 1.9).

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

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

Acquisitions, Related Goodwill and Other Intangible Assets

The Board has a methodology for calculating the value of acquired intangible assets and the period over which intangible assets are amortised for each acquired business.

In arriving at values for goodwill and the associated intangible assets, the Board has taken a judgment on the discounted fair value of any contingent consideration which is payable after completion of the acquisition. Similarly, the Company has taken judgments over attributing values for the intangible assets of order book, brand value, any non-compete arrangements with sellers and customer relationships together with a useful economic life over which to amortise the assets. After evaluating the above, this leaves the Company with residual goodwill value which reflects the overall value to the Company as a result of having a more diverse product range and broader route to market.

The carrying value of contingent consideration and goodwill for acquired businesses is then reviewed at the end of each financial year.

As an illustration, the impact of each of the five acquired businesses in 2018 are shown in the table below, together with the current value and amortisation charge in the Income Statement (although it is worth noting that the Garrod Bros intangible asset was fully written down in 2018). Further information is contained in note 24 to the Financial Statements.

Businesses acquired in 2018	Consideration £ million	Residual goodwill £ million	Intangible assets £ million	Amortisation costs in 2018 £000
Dersimo	3.7	1.3	1.2	82
CECO	5.6	2.2	1.4	113
Ashmount	2.4	0.5	0.4	50
Rackhams*	0.7	0.4	0.4	23
Garrod Bros*	0.6	-	0.2	219
Total	13.0	4.4	3.6	487

* Both Rackhams and Garrod Bros are currently subject to a merger inquiry by the Competition and Markets Authority ('CMA').

Retirement Benefits

The Company operates two defined benefit pension schemes in the UK and in Switzerland, the assets and liabilities of which are dominated by the UK scheme which is closed to new members.

The net liability attaching to employee benefits is as follows:

	2018 £000	2017 £000
Current liabilities	**–**	2,235
Non-current liabilities	**5,888**	10,481
Total	**5,888**	12,716

The year-on-year decrease in the net liability amounts to £6.8 million, which reflects the elimination of the short-term deficit contributions which ceased to be paid by the Company during 2018 following the most recent triennial valuation. This was mainly caused by the changes in financial assumptions, where annual salary increases are assumed to rise in-line with RPI rather than at a 1.5% uplift to RPI as previously the case and an increase in the discount rate to 2.7% (0.3% increase), offset by negative changes in the returns on asset performance.

Following recent pension case law, the UK scheme liabilities have increased to reflect gender equalisation of benefits for past service. This has resulted in a one-off £1.2 million cost in the Income Statement for 2018, categorized within the non-underlying items.

Capital Allocation, Investment Decisions and Return on Capital

The Board is committed to ensuring the efficient allocation of capital, with a clear strategy for sustainable growth, with controls in place to govern capital expenditure and working capital.

The Board routinely reviews organic growth opportunities and associated investment, value enhancing acquisitions, and shareholder returns to ensure the Company deploys an optimal capital structure. Such investment opportunities are subject to both internal rate of return and cash flow payback criteria, regularly reviewed by the Company to ensure consistency of assessment.

Return on Capital Employed (measured as earnings before interest and taxes ('EBIT') as % of capital employed) in 2018 was 23.2% (2017: 26.2%).

Capital Expenditure

The Company incurred a replacement level of capital expenditure on its land and buildings of £0.4 million during the year (2017: £0.2 million), and capital expenditure on plant and machinery of £3.5 million (2017: £2.8 million).

Activity in relation to the new Ipswich regional distribution centre is now meaningfully underway. Total capital expenditure is estimated to be in the region of £26.0 million, with £0.5 million spend incurred in 2018, approximately £16.0 million expected in 2019 (including land acquisition cost of £4.0 million), and the balance in 2020.

New Accounting Standard not yet applied – IFRS16 Leases

This new standard is effective for financial periods beginning after 1 January 2019 and eliminates the classification between operating and finance leases over 12 months in length. Full information, including an evaluation of the impact on the Company's financial statements, is detailed in note 1 to the Financial Statements. While adoption of the new standard will have a material impact on the presentation of the Group Statement of Financial Position, the Group expects that the impact on the Income Statement for 2019 will be a reduction in the net profit before tax by approximately £0.5 million.

Cash Flows

Net Cash Flow from Operating Activities

During the year, net cash flow from operating activities was £40.0 million (2017: £43.2 million) with the key drivers behind this positive cash flow generation shown below.

	2018 £000	2017 £000
Cash flows from operating activities		
Profit before tax for the year	**40,447**	40,719
Depreciation, amortisation and impairment	**7,038**	5,845
Profit on sale of property, plant and equipment	**(50)**	(45)
Net finance cost	**884**	665
EBITDA	**48,319**	47,184
Share-based payments	**1,478**	1,218
Working capital changes	**209**	6,108
Cash generated from the operations	**50,006**	54,510
Interest paid	**(1,426)**	(761)
Tax paid	**(7,789)**	(8,388)
Additional pension contributions	**(747)**	(2,164)
Net cash from operating activities	**40,044**	**43,197**

Cash generated from operations remained strong in the year despite the weaker trading backdrop, being 121% of operating profit (2017: 132%).

Cash Flows from Investing and Financing Activities

The table below summarises the cash flow movements arising from investing and financing activities during the year. The overall net cash outflow from the two activities was £38.5 million, with the main factors being the payment of dividends, acquisition consideration (net of cash acquired), investment in capital equipment, and an increase in shares acquired reflecting payments to acquire own shares for treasury to satisfy future obligations under the Company's employee share schemes. In 2018, there was a £4.8 million reduction in dividends paid owing to an additional special dividend being paid in relation to 2017.

	2017 £000	2016 £000
Cash flows from investing activities		
Proceeds from sale of property, plant and equipment	**403**	190
Interest received	**601**	576
Acquisition of subsidiaries, net of cash and debt acquired and repaid	**(9,576)**	(31,805)
Acquisition of property, plant and equipment	**(4,384)**	(3,058)
Net cash from investing activities	**(12,956)**	(34,097)
Cash flows from financing activities		
Shares acquired (net of treasury shares issued)	**(4,764)**	(377)
Net movement on borrowings	**211**	(230)
Dividends paid	**(20,969)**	(25,729)
Net cash from financing activities	**(25,522)**	**(26,336)**

Net Funds

Net funds at the year-end increased slightly to £36.7 million from £35.3 million in 2017 as a result of the net cash outflows arising from operating, investing and financing activities outlined above.

In both 2017 and 2018, the Company drew-down on its banking facilities during the year in-line with the normal swings in working capital. Average net debt in 2018 was £16.9 million (2017: £9.2 million net funds).

	At 1 January 2018 £'000	Cash flows including acquisitions £'000	Translation differences £'000	At 31 December 2018 £'000
Cash at bank and in hand	42,030	**1,784**	**191**	**44,005**
Bank overdraft	–	**(218)**	**(3)**	**(221)**
Debt due within one year	(233)	**–**	**(3)**	**(236)**
Debt due after one year	(6,519)	**(211)**	**(75)**	**(6,805)**
	35,278	**1,355**	**110**	**36,743**

Funding and Going Concern

The Company increased its committed UK banking facilities in 2017 to £72.5 million (Sterling denominated) and €8.6 million (Euro denominated) all with end dates of December 2021. 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 £7.6 million in Continental Europe.

The Company maintains sufficient banking facilities to fund its operations and investments, and as at 31 December 2018, 93.6% of the total facilities were undrawn as shown below.

	Drawn £'000	Undrawn £'000	Total facility £'000
Less than one year	**457**	**32,116**	**32,573**
Over one year and less than five years	**6,805**	**73,401**	**80,206**
	7,262	**105,517**	**112,779**

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 Statements.

Chris Payne
Chief Financial Officer

6 March 2019

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 strategy.

	Measurement	Why it's important	Performance (3 years)	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	2018 3.8 2017 1.1 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	2018 32.3 2017 31.5 2016 31.0 ***	Pricing discipline and product expansion
Underlying operating profit margin**	Measured as a % of revenue	Shows the effectiveness of sustainable operating profit generation from revenue	2018 6.2 2017 6.3 2016 6.1 ***	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	2018 40.0 2017 39.1 2016 36.8	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	2018 23.2 2017 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	2018 97.5 2017 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	2018 26.1 2017 25.2 2016 24.7 ***	Maintain cost control to ensure increases remain below revenue growth

	Measurement	Why it's important	Performance (3 years)	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	2018 3.6x 2017 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	2018 76.0 2017 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	2018 18 2017 25 2016 17	Increase frequency of in-house H&S compliance assessments to identify and limit failures in compliance
Recycled packaging	Use of recycled polythene for protective plastic packaging needs across the Company's UK locations. Measured as % of the Company's total UK volume per annum	Protective plastic packaging is one of the main areas of waste arising from the Company's operations. By utilising recycled polythene, the Company mitigates its impact on the environment	2018 68.8% (new KPI for 2018)	Group procurement initiative in place for every UK location to be using regranulated polythene packaging manufactured from 100% recycled polythene by end of 2019 (machinery permitting)

* Like-for-like revenue is calculated based on constant currency from activities and businesses that made a full contribution in both the 2018 and 2017 periods and is adjusted for any variances in working days.

** Underlying is before non-underlying items which includes intangibles amortisation relating to businesses acquired, acquisition fees and contingent consideration movements, non-recurring pension costs in relation to guaranteed minimum pension ('GMP') equalisation and non-recurring costs relating to senior personnel changes.

*** Prior year numbers restated to present comparatives on a consistent basis due to the reclassification in 2018 of some items between revenue, cost of sales and operating expenses to better reflect their nature.

Risk Governance

The Board is responsible for the adequacy and effectiveness of the Company's internal control system and risk management framework.

The Group Executive team has been delegated ownership and responsibility from the Board for day to day risk management and control. The Company's Chief Financial Officer chairs a risk committee, established in 2018, whose purpose it is to discharge this delegated authority with a more granular review of business risks from a cross function of business leaders which are then reported back to the Board on a quarterly basis.

This allocation of responsibilities is best described by the Group's risk governance framework summarised on page 35.

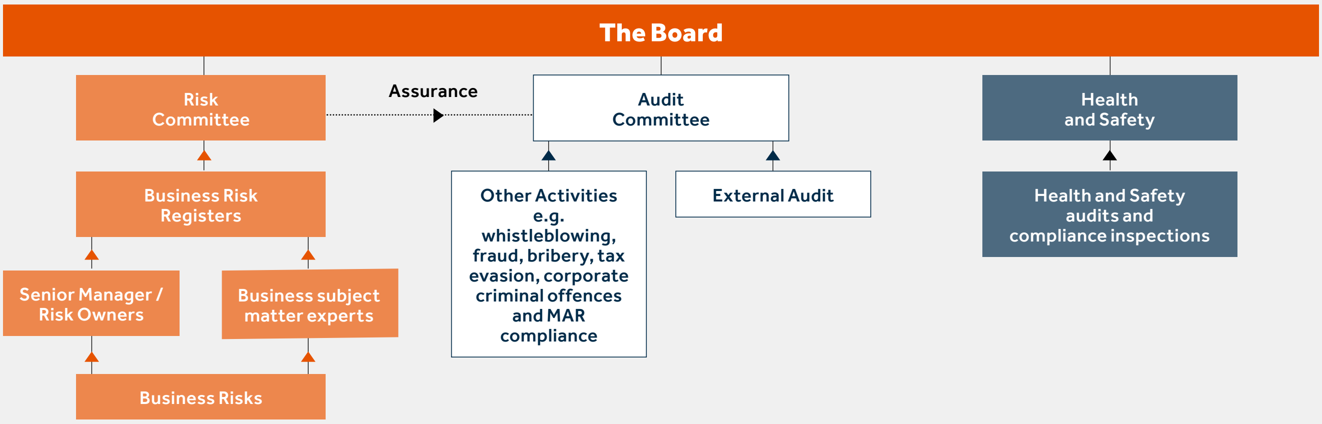
Risk Assessment

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.

Summarised below are the key risks, not in order of significance, which the Board considers could have a material impact on the Company's reputation, operations or financial performance. These include, but are not limited to, risks that are directly managed by the Board and therefore may be informed by more detailed risk management processes in place via the Risk Committee or the Audit Committee.

Area of risk	Description	Potential Impact	Mitigating Actions
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 or market disruptor 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.
IT resilience and cyber security	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. The theft, destruction or loss of sensitive and or confidential information could adversely affect business performance and reputation.	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. Third party IT provision enables network software to be kept up to date.
People	The Company's ability to deliver ongoing success is dependent upon its ability to attract, retain and develop its people.	An inadequate pool of suitably qualified and motivated people can disrupt business development, customer delivery and undermine the Company's ability to deliver on its strategy.	The Company is committed to driving employee engagement through direct communication, listening groups and employee champion forums. 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.

Risk Management Framework



Area of risk	Description	Potential Impact	Mitigating Actions
Health and safety	The Company's operations and business model carry inherent health and safety risks to our people, customers and the wider public.	If the Company were to breach health and safety law and/or regulations it could have a material adverse effect on reputation, overall business performance and the welfare of our people.	The Company employs a health and safety function reporting directly to the Board. Active and regular engagement by the senior and local management in prioritising health and safety procedures. There are embedded common processes and controls in place across the UK businesses which are supported by regular independent reviews and checks.
Brexit	The Company operates an international supply chain, with purchases made across EU borders. A hard Brexit is likely to result in cost increases and extended supply chain timelines.	Any tariffs or other increases in costs will affect the whole market and result in higher prices. Delays in supply chain deliveries may affect our ability to service customers in a timely manner, particularly during a period of adjustment to post-Brexit conditions.	The Company maintains strong relationships with its suppliers enabling an open dialogue to secure supply. The Company's business model creates a significant level of UK stock holding which buffers supply disruption. The Company has invested in additional stock holding for fast moving products to protect customer service.
Legislation and regulation	The Company's operations are regulated by a variety of laws and regulations, the principal ones relating to 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 policies and procedures and, where appropriate, engages the services of competent third-party advisers.

Background

Provision C2.2 of the 2014 revision of the UK Corporate Governance Code requires the Board to assess the prospects of the Company over a period in excess of the twelve months required by the 'Going Concern' provision. This section sets out, in overview, that assessment.

After analysing various options, a period of three years, to 31 December 2021, was chosen for the purpose of the viability assessment, as this represents the period focussed on by the Board during strategic planning. This period also allows for modelling of capital investments planned during the timeframe. 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.

Sensitivity Analysis

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 as given in the Risk Management and Principal Risks & Uncertainties section on pages 34 and 35.

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

In respect of market demand, the key risk relates to periods of economic recession that create reduced consumer confidence or contraction in the construction industry, both of which could result in a significant reduction in demand for the Company's products. As a result, two alternative plausible downside scenarios have been modelled which have a potential to threaten the viability of the Company.

Scenario A – Sustained Recessionary Environment

Scenario A is modelled on the basis that there is a sustained recessionary environment in both the UK and Continental Europe such that revenues decline in 2020 and 2021 whilst there are ongoing inflationary fixed cost pressures.

In this scenario, even in the absence of any significant mitigating actions, the Company continues to operate within its current banking facilities and the covenant restrictions set out therein.

Scenario B – Economic Environment

Scenario B is modelled on the basis that there is a similar economic crisis to that observed in 2008, where revenues decreased sharply in 2009 with modest growth thereafter through to 2014.

In this scenario, the Company continues to operate within its current banking facilities and the covenant restrictions set out therein, although, the covenant headroom is significantly reduced and this position requires swift and pro-active management of the cost base.

Based on the consolidated financial impact of the scenarios analysed 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 existing UK bank facilities, running to 7 December 2021, continue in existence.

Confirmation of Longer-Term Viability

Based on the results from these two scenarios, and having considered the available mitigating actions, the Board can have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the three-year period of this assessment. This longer-term assessment process supports the Board's statements on both viability and Going Concern.

The Strategic Report was approved by the Board on 6 March 2019:

Steve Wilson
Chief Executive

Chris Payne
Chief Financial Officer


HFD

OUR COMMITMENT

The relationships with our stakeholders are of the uppermost importance

We remain committed to managing our Company in a socially responsible way, continually reviewing our performance in all areas of Corporate Responsibility. We utilize the feedback and recommendations from the agencies, consultancies and voting bodies who undertake reviews of environmental, social and governance ('ESG') issues to enhance our practices going forward. During 2018, we were delighted to remain a constituent of the FTSE4Good Index, an Index launched to identify companies that demonstrate strong ESG practices as measured against globally recognised standards.

A key constituent of our Corporate Responsibility is the relationships with our stakeholders, encompassing our people; suppliers; customers; investors; and the communities in which we operate. These relationships, many of which span the 26 years we have been operating, are of the uppermost importance. They are pivotal to our performance and delivery of our Strategy (as detailed on page 24) 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, working in partnership with them, 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.

Our ambition is to embed Corporate Responsibility within the Company's culture and uphold the highest standards. Pages 39 to 49 of this Strategic Report detail our considerable efforts in this regard during 2018, particularly in relation to employee engagement, and our further endeavours for 2019.

Philip Lawrence
Non-Executive Chairman

Steve Wilson
Chief Executive

6 March 2019

FTSE4Good

STAKEHOLDER ENGAGEMENT

The Company aims to have a positive impact on all its stakeholders through its interaction with them, working in partnership to create value and a positive contribution which benefits all. The Company places particular importance on directly engaging and communicating with its stakeholders in the areas of operational and financial performance, strategy, corporate values, and policies and procedures including health and safety.

The main methods of engagement with each of the Company's stakeholders are given below:

Stakeholder	Engagement
EMPLOYEES	Conducted at both the Company and individual business level, and including all departments and levels of seniority, engagement is undertaken via meetings (formal and informal), presentations, training, emails, bulletins, and the corporate website and intranet. Specific activities include: • Employee surveys, and follow-up workshops and planning meetings to take appropriate actions • Senior manager events at head office, including to discuss performance and strategy • Visits to all operating locations by the Chief Executive, Chief Financial Officer and Commercial Director, and associated meetings with the local management teams
SUPPLIERS AND OTHER PROVIDERS	Conducted primarily by the delegated buyers within the Company, and supported by regular interaction with the Company's executive team, activities include: • Meetings on a regular basis at manufacturing facilities and/or showrooms, including to discuss product development and production scheduling • Trade shows, and collaborative events/presentations to enhance the sales potential of products • Questionnaires and reviews of practices, including with the aim of ensuring a supply-chain free from slavery and human trafficking
CUSTOMERS AND LOCAL COMMUNITIES	Conducted primarily by sales representatives' visits, delivery drivers and telephonically with the customer service team, the Company provides the widest interaction possible for the customer to ensure the service proposition is upheld. Additional activities include: • Open-house or trade days at the Company's business locations to educate about products and/or promotions • One-to-one meetings with managers / directors to garner feedback and ensure the level of service received • Customer surveys to be conducted to gauge levels of satisfaction and analyse buying habits
SHAREHOLDERS AND WIDER INVESTMENT COMMUNITY	Conducted primarily via meetings following the publication of the Company's interim and final results, and at the time of the AGM. The Company seeks to provide regular corporate updates, and increased direct interaction through: • Briefings for analysts and other members of the investment community to coincide with the Company's bi-annual results • Meetings hosted at the Company's main operating locations to enable first-hand review of operations and meet additional members of the team • Group events, including those aimed at increasing the understanding of a specific area of the business or marketplace

OUR PEOPLE

At the heart of the Company's approach to people management is the provision of a safe and environmentally sound workplace where everyone can fulfil their potential. Having further invested in the HR team, 2018 saw progress with the continuing development of people practices to build on the Company's history and which will help shape its future.

Employee Engagement

The Company undertook its second employee survey during 2018 with the aim of enabling employees to express their views on a confidential basis and identify areas for improvement. The survey was enlarged to include both UK and Dutch employees, and a much improved response rate of 73% (2017: 53%) presented a broader and more in-depth insight into the views of an increased number of employees across all departments. Pleasingly, while capturing an enlarged representation of opinion, the overall engagement score of 75% stayed broadly in-line with the previous year's score of 77% and provides a positive foundation to continue developing a positive workplace. The next survey will take place during 2020, with the Company's Swiss employees participating and the Company's French business continuing to operate a survey specific to them.

2018 Employee Initiatives

- Second Employee Survey
- Enhanced Maternity Policy
- Enhanced Occupational Health Service
- Inclusion and Respect at Work Policy

Throughout 2018, senior managers of the Company's businesses continued to work with the champions from their different departments to discuss ideas and concerns specific to their businesses as well as the Company as a whole, and undertake actions as a result.

To increase employee involvement further and ensure that employees have a greater opportunity to communicate their views, the Company is launching an Employee Forum in 2019 which will be comprised of elected employees from across the Company's businesses in the UK and Continental Europe. The Forum, to be held quarterly, will be chaired by the Company's Chief Executive and act as a communication platform, enabling employees to voice their ideas, opinions and concerns and allow them to participate more actively in the future direction of the Company.

During 2018, three events were held for the senior managers of the Company's businesses to discuss the financial and operational performance of the collective group as well as engage with them on the delivery of the Company's vision, strategy and initiatives to deliver improved performance. These events will continue throughout 2019.

75%
EMPLOYEE ENGAGEMENT SCORE

76%
EMPLOYEE RETENTION

All data stated is for the financial year ended 31 December 2018 or as at 31 December 2018

Positive Workplace Culture

In order to continue creating a positive working environment and culture, a number of policies and working practices were reviewed and additionally launched during 2018, including:

- **Maternity Policy** – An enhanced maternity policy was introduced aimed at providing greater support for families and encouraging women to continue their career after motherhood. During 2018 10 women benefitted from the enhanced policy;
- **Drugs and Alcohol** – To further support the policies and processes in place to ensure a safe workplace for all, 'For cause' drugs and alcohol testing was introduced; and
- **Inclusion and Respect at Work** – The launch of this policy, accompanied by training for all managers, reflects the Company's commitment to providing equality of opportunity for all in an environment which is free from discrimination, victimisation and harassment, and in which everyone is treated with dignity and respect.

Employee Support

Following its introduction in November 2017, the Employee Assistance Programme ('EAP') ran for its first full year in 2018. The EAP, delivered via an independent company called LifeWorks, is a confidential telephone, internet, app-based service available to all employees and their immediate families providing advice, information and support on issues spanning work, health, life, family and money. During 2018, 26 people benefitted from individual support provided.

During 2018 an enhanced Occupational Health service was introduced via an independent company called MediGold Health to further support employee wellbeing. The service assists the HR team in supporting employees with complex medical conditions via early intervention and their appropriate return to work.

OUR PEOPLE CONTINUED

Recruitment and Tenure

The Company actively recruited in all departments throughout 2018 and the total number of employees grew year-on-year to 2,612 as at 31 December 2018 (2017: 2,427). The focus on supporting and encouraging internal moves resulted in 30 vacancies being filled by internal candidates. The Company's commitment to retaining talent and experience is additionally reflected in the tenure of its employees, with 31% of UK employees having been with the Company over 10 years as at 31 December 2018 and 132 people since operations began in 1992.

As detailed within the Key Performance Indicators section on page 33, employee retention improved during 2018 to 76.0% (2017: 74.0%).

Training and Development

The Company actively encourages all its employees to participate in the training opportunities available to them. In 2018, and in addition to the training outlined within the Health & Safety and Environment sections of the Strategic Report:

- 35 newly appointed managers attended a 'Step into Management' course designed to equip first-time managers with the skills needed to lead people; and
- 51 sales representatives attended the Sales Induction Programme which is designed to induct them in all aspects of the role.

As detailed below, the Company has begun in 2019 to utilise its apprenticeship levy to fund apprenticeship training schemes.

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 2018, the Company elected to award a cost of living increase of 2% to base salary for all UK employees with the exception of the Board and Senior Management Team who elected not to receive it. For 2019 the Company has awarded an increase of 2% to all UK employees. For the Company's employees in Continental Europe, local market practice was followed in 2018 and for 2019.

Employee Benefits

The Company encourages and supports the financial security of its employees and offers a number of benefits including opportunities for participation in the Company's Pension Plan and the Government auto-enrolment National Employee Savings Trust, and 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 2018, 608 eligible employees participated in the Company's SAYE schemes, equivalent to 33% of the UK workforce.

Diversity and Equal Opportunities

The Company 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. The Company gives full and fair consideration to applications for employment from disabled persons.

As at 31 December 2018, the Company had 2,612 employees of which 20% were female, a marked improvement on 2017 (2017: 18% female).

The table below shows the Company's gender diversity:

Employees	Executive Directors	Senior Management	Managers	Other	Total
Male	2	1	286	1,793	2,082
Female	0	2	46	482	530
Number of employees as at 31 December 2018	2	3	332	2,275	2,612

As of the date of the report, the Board (including the Non-Executive Directors) and Senior Management Team, who attend all Board Meetings, comprised 5 females and 6 males, equivalent to a 45% female representation. This will increase to 50% upon Andrew Eastgate's retirement from the Board on 31 May 2019.

The Company is working to improve the male: female ratio across the whole Company which stood at 4:1 as at 31 December 2018. Actions and initiatives being launched include:

- Enhance Maternity Policy (as detailed above)
- Paternity and Shared Paternity Leave policies (to be launched in 2019)
- Flexible Working Policy and practices (to be launched in 2019)
- Reward frameworks and policies (to be launched in 2020)

Gender Pay Gap Report

In-line with the UK Government's regulations which introduced gender pay gap reporting, the Company has published its most recent report dated 5 April 2018 on the GOV.UK website and its own website. The report fully complies with the legislation and an abridged summary is given below which includes the Company's two legal entities required to report ('HFD' and 'MCD') and additionally the ultimate holding company ('PLC') not required to report.

- The Company's overall median pay gap was lower than the UK national average at 10.1%
- The proportion of men and women eligible to receive bonuses:
  - HFD - men 97%, women 98%
  - MCD - men 98%, women 98%
  - PLC - men 100%, women 100%

Modern Slavery and Human Rights

The Company is committed to improving its practices to combat slavery and human trafficking, and the Company's Slavery and Human Trafficking Statement detailing its policies, processes and actions is available on its website www.headlam.com.

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, which is detailed on the Company's website www.headlam.com, 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.

2019 Activity

New activity for 2019, in addition to the Employee Forum and policies detailed above, includes a development programme for senior managers and the launch and roll-out of apprenticeship schemes. The apprenticeship schemes have been launched to capitalise on the levy payable under the Government's Apprenticeship Levy programme to fund new apprenticeships and increase investment in human capital. Since the beginning of the year the Company has piloted two cohorts in the area of sales, and will roll-out the schemes across other job functions as the year progresses.

To help provide ongoing support to the wider workforce, the Company will continue to offer guaranteed interviews to employees from local companies who face redundancy as a result of closures or job cuts and who have appropriate experience.

Right to Work and Brexit

The Company is ensuring that it is fully compliant with the legal requirement to carry out checks with existing and prospective employees to ensure that they have the legal right to work in the UK. The Company has 134 identified EU and EEA nationals working in the UK and has commenced a communication plan which will provide ongoing support and guidance for employees applying for pre-settled or settled status to remain in the UK after it leaves the EU ('Brexit').

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. 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.

Introduction

The Company is committed to promoting a positive Health & Safety ('H&S') culture and high standard of H&S management throughout the Company. 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 regular basis and formally report to the National Health & Safety Manager quarterly.

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.

A Risk Committee (as detailed on page 34) 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 Company's H&S capacity has been much enhanced since 2017 following the introduction of a new in-house H&S team, and a comprehensive review of the Company's policies and procedures was undertaken by them and the Risk Committee during 2018.

2018 Key Activities

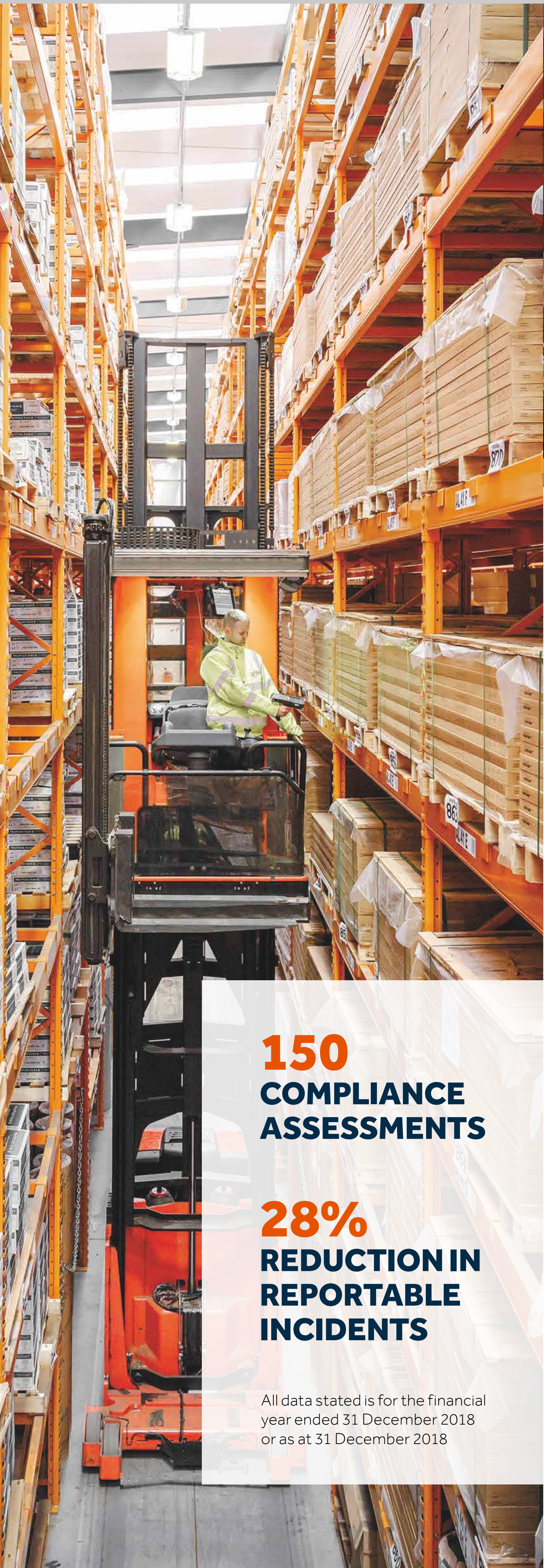
During 2018, a new in-house Health & Safety Management System was launched and rolled-out across the Company to ensure a standardised approach to risk assessments, safe systems of work, accident and near-miss reporting. The System allows data to be immediately logged, analysed and any trends identified, with appropriate remedial action then taken. In addition to being a centralised portal containing all general policies, procedures and pictorial aids, the System contains specific information tailored to each operating location and has an employee feedback facility.

Various in-house and external training programmes were undertaken during the year. All business managers responsible for H&S completed the Institution of Occupational Safety and Health ('IOSH') 'Managing Safely' training course, and in-house training courses tailored to the specific requirements of the Company focused on Fire Risk Management, First Aid and Accident Investigation.

The Company continued the installation of fall arrest systems across its commercial fleet, with a further 62 systems installed in the rear of vehicles and trailers to prevent falls by drivers unloading. In-line with its fleet renewal schedule, a further 70 installations are anticipated for 2019. Additionally, 'creep speed' mode was fully implemented across the forklift fleet adding enhanced control when handling loads at high elevations.

Over 150 H&S compliance assessments were undertaken at the Company's 69 UK locations by the in-house H&S team in 2018, far exceeding historic numbers, with this level of local assessment anticipated to increase going forward.

There were 18 reportable incidents in 2018, down from 25 in 2017, none of which resulted in a serious injury. All reportable accidents are investigated and, in the infrequent instances where improvement is required, remedial actions to prevent reoccurrence are implemented in a timely manner. There were no prosecutions for breaches of health and safety or enforcement actions in the year.



150
COMPLIANCE ASSESSMENTS

28%
REDUCTION IN REPORTABLE INCIDENTS

All data stated is for the financial year ended 31 December 2018 or as at 31 December 2018

2019 Key Priorities

A key priority for 2019 is the commencement of work towards achieving ISO 45001 accreditation across the Company's main UK operating sites. The ISO 45001 Occupational Health and Safety Management Systems is a new international standard introduced in 2018 with the aim of reducing occupational injuries, and provides a single benchmark for the management of occupational health and safety. Accreditation would provide validation that the Company is operating at the highest standard with regard to H&S, and a series of independent audits will commence in 2019 and progress through 2020 and 2021.

And Lastly

The Company would like to congratulate Leigh Holdsworth, National Health & Safety Manager, who was admitted as a Chartered Member to the Institution of Occupational Safety in December 2018. Chartered Members are recognised within the H&S profession as meeting the highest standards of skills and knowledge.

ENVIRONMENT

The Company is committed to 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 continues to actively migrate away from paper-based systems to handheld paperless delivery and invoicing techniques.

Three of the efficiency initiatives being pursued by the Company, detailed on page 18 of the Strategic Report, will lead to improvements in the Company's environmental impact and are referred to below. In addition, a KPI in relation to recycled packaging has been introduced this year to better measure the Company's progress in this important area (page 33).

Recycling & Waste

The waste arising from the Company's operations is predominantly protective plastic packaging, cardboard poles and wooden pallets. The cardboard poles from the centre of rolls and cut lengths of carpet and vinyl delivered to customers are subsequently collected from their premises by the Company's drivers, 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. All pallets are reused for goods going out and when not needed are dispatched to specialist reprocessing agents when it is economic to do so.

For several years the Company's main UK distribution hubs, and some other locations with appropriate machinery, have been utilising recycled polythene for their protective plastic packaging needs. Packaging has been identified as one of the key areas targeted for review as part of the Company's group procurement efficiency initiative aimed at delivering cost-savings and other benefits. As a result of this initiative, by the end of 2019, machinery permitting, every Company UK location will be using regranulated polythene packaging manufactured from 100% recycled polythene.

The Company is a core funder member of Carpet Recycling UK, a not-for-profit membership association working to increase the recycling of carpet waste across the UK. Core funder members are deemed industry leaders in developing voluntary responsibility for carpet recycling throughout their lifecycle. Per Carpet Recycling UK, 175,252 tonnes of carpet was diverted from landfill in the UK in 2018 (being reused, recycled or recovered for energy generation). This represented a diversion rate of 44%, and a 2% increase on 2017. The Company does not send any floorcovering products or plastic packaging to landfill.

The Company is a member of Valpak, the leading provider of environmental compliance, data and resource management services. Valpak provides compliance services to its members by analysing the packaging waste data submitted by each member on an annual basis and comparing it with comparative data in order to confirm to the Environment Agency that its members are continuing to meet UK recycling and recovery standards.

Fleet Operator Recognition Scheme ('FORS')

FORS is a voluntary accreditation scheme that promotes best practice for commercial vehicle operators, including in relation to reducing environmental impact and improving operational efficiency. The Company is committed to achieving and maintaining FORS accreditations. 10 of the Company's businesses' locations now hold FORS Bronze accreditation, up from six last year, with an additional business holding FORS Silver. Further accreditations will be applied for in 2019.

Fleet

European emission standards define the acceptable limits for exhaust emissions of new vehicles sold in the European Union and European Economic Area member states with the aim of improving air quality. Currently 87% of the Company's commercial fleet is compliant with the latest Euro 6 emission standards, up from 74% last year. This will rise to almost 100% following the delivering of new vehicles in 2019.

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 Company is working towards the remaining licence achieving a Green score.

The Company is committed to improving the efficiency of its deliveries and limiting its vehicle emissions where possible. Further progress in this area will be achieved in 2019 and beyond via two efficiency initiatives that are currently being pursued by the Company, namely dynamic route planning and more effective delivery fleet utilisation. If successfully deployed, both initiatives will result in a reduced fleet size and fuel consumption.

87%
COMMERCIAL FLEET EURO 6 COMPLIANT

100%
RECYCLED POLYTHENE PACKAGING IN 2019

All data stated is for the financial year ended 31 December 2018 or as at 31 December 2018

Wood Sourcing

As an importer of wood products from outside the EU, the Company has procedures in place to comply with the requirements of the European Union Timber Regulation 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.

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.

While the Company recognises its business has a direct and indirect effect on the environment, it believes that owing to its proactive approach, its activities generally have a low impact on the environment. There were no environmental legal or compliance issues arising during 2018.

Water

Water consumption arises predominantly in respect of employee welfare and commercial vehicle washing, and was 42,246 cubic metres in 2018. The Company is committed to commercial vehicles being kept clean and a pleasant environment in which its drivers operate, and operates jet wash machines and specialist truck washes throughout its network. Each truck wash utilises 100% recycled water and environmentally-friendly washing detergents.

The Company continually seeks to reduce water consumption and charges through analysing invoices received, the installation of water meters, and by reducing consumption through repair, renewal or installation of equipment to improve efficiency.

ENVIRONMENT
CONTINUED

Electricity
Electricity consumption is predominantly in relation to: forklift truck battery charging; operation of specialist cutting tables; associated mechanical handling and compressed air equipment; and warehouse and office lighting and equipment. Modern and energy-efficient construction techniques and products are incorporated when investing in new facilities or undertaking refurbishment or repair works. Energy-efficient LED lighting units have now been installed across the vast majority of the network, and photovoltaic panels installed on the roof of the Company's Coleshill distribution hub generate an estimated 46,000 kWh of electricity. Similar panels are currently in scope for the Company's proposed new distribution centre in the Ipswich area, where all the most energy-efficient and cost-saving appliances will be considered.

Gas
Gas is consumed predominantly in respect of office heating and a very limited number of localised radiant heating above work stations on cutting tables located within 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. It is intended that such a system will be installed at the new Ipswich distribution centre.

Electricity and gas supplies in the UK are purchased on a Company contract basis. The actual cost of electricity and gas in 2018 was comparable to prior years, and represented 0.14% of UK revenue (2017: 0.13%).

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.

	2018 CO_2/ tonnes	2017 CO_2/ tonnes	2016 CO_2/ tonnes
Electricity	2,080	2,736	3,457
Gas	866	783	1,052
Commercial vehicle fuel	19,400	19,475	19,597
Car fuel	5,498	4,853	4,780
Total	27,844	27,847	29,540
Tonnes per £1 million revenue	39	40	45

The total 27,844 tonnes CO_2 for the financial year ended 31 December 2018 was in-line with that of the prior year despite the expansion in the number of businesses within the Company.

Energy Savings Opportunity Scheme ('ESOS')
ESOS is a mandatory energy assessment scheme for large organisations in the UK. External audits are required to be carried out every four years following the previous audit, and the Company's next audit is therefore not anticipated before December 2019.

SOCIAL ACTIVITIES, COMMUNITY & CHARITABLE DONATIONS

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, involvement 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 £24,172 (2017: £33,483). 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 2018, the Company made an overall contribution of £5,482.07 to Pennies from Heaven on behalf of itself and its employees (2017: £10,098.68).

During 2018, the Company held its second employee survey, again donating £5 on behalf of each employee who completed it. Due to the much-improved response rate in 2018, a greater total of £8,190 was raised for the chosen charities of Cancer Research UK, Make-A-Wish UK and Age UK. (2017: £5,430).

In 2018, the Company became a corporate member of The Furniture Makers' Company, the City of London livery company and charity for the furnishing industry. The Furniture Makers' Company aims to promote, encourage and foster the craft and industry of furnishing and furniture and its ancillary activities, advance education in the industry, and relieve financial hardship of present and past employees of the industry, their families, relatives and dependents. In 2018, Headlam made a donation to their charitable fund, and one of its businesses, Florco, participated in their charitable football tournament.

The Company and its individual businesses donate floorcovering products to many deserving causes during the year. During 2018, these included:

- Coleshill-based businesses donating to Sebastian's Action Trust, for their new purpose-built respite facility which provides support to families of seriously ill children
- Headlam Newcastle donating to BAY Foodbank, for their office space in support of their work providing emergency food provision to those experiencing financial crisis
- Mercado Leeds donating to DIY SOS, to provide assistance in a home rebuild project in support of a disadvantaged family

Other activities in support of both local communities and furthering education included the sponsorship of a junior football club local to the Company's head office, the presentation to summer school students as part of an educational trip, and providing work experience at several of the Company's locations.

Headlam is proud to have been able to be supportive of all the incredibly worthwhile causes and activities detailed above.

BOARD OF DIRECTORS

Philip Lawrence
Non-Executive Chairman

Philip was appointed a Non-Executive Director in June 2015 and became Non-Executive Chairman on 1 June 2018. Philip is currently Chairman of private equity backed Airband Community Internet Limited and a member of the advisory board for the Offshore Petroleum Regulator for Environment and Decommissioning, part of the Department for Business, Energy and Industrial Strategy ('BEIS'). Philip is the former Chief Executive of the Coal Authority, an arm's-length body of BEIS. He stepped down as Chief Executive of the Coal Authority in May 2018 after 11 years, and prior to this, he held significant roles with Marconi plc and Deloitte LLP. He is an Associate of the Institute of Chartered Accountants in England and Wales.

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Steve Wilson
Chief Executive

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 in England and Wales.

Steve is the Executive Director with lead oversight of People and Health & Safety matters as part of the Company's commitment to Corporate Responsibility.

■

Chris Payne
Chief Financial Officer

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.

Chris is the Executive Director with lead oversight of Environment and Social & Community matters as part of the Company's commitment to Corporate Responsibility.

Amanda Aldridge
Independent Non-Executive Director

Amanda was appointed a Non-Executive Director in February 2018 and appointed Chair of the Audit Committee on 1 June 2018. Amanda is currently a Non-Executive Director of Impact Health REIT plc. 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, and held a number of strategic and line management roles during her 32 years with KPMG LLP. She is a Fellow of the Institute of Chartered Accountants in England and Wales.

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Andrew Eastgate
Independent Non-Executive Director

Andrew was appointed a Non-Executive Director in May 2010. He is the Chairman of the Remuneration and Nomination Committees and was previously the Senior Independent Director until Keith Edelman's appointment in January 2019. 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 Non-Executive Chairman of Epwin Group Plc, the AIM listed manufacturer of low maintenance building products, and a Non-Executive Director of Castings PLC, an iron casting and machining group based in the UK. He is also an experienced commercial mediator.

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Key to Committees:
- ● Audit
- ■ Nomination
- ▲ Remuneration
- ▬ Chairman of Committee

SENIOR MANAGEMENT TEAM

Keith Edelman
Senior Independent Director

Keith was appointed a Non-Executive Director in October 2018 and was appointed Senior Independent Director on 1 January 2019. Keith is currently Chairman of Revolution Bars Group Plc and Pennpetro Energy Plc and a Non-Executive Director of the London Legacy Development Corporation and Altitude Group plc. In his executive career he was a director of consumer, retail and leisure companies including Ladbroke Group Plc, Carlton Communications Plc and Storehouse Plc. His last executive appointment, which ended in 2009, was Managing Director of Arsenal Holdings Plc where he was responsible for the move from Highbury to Emirates Stadium. Since 2009, Keith has held a number of non-executive roles including Superdry Plc, Safestore Plc, Goals Soccer Centres plc, JE Beale Plc and Thorntons Plc.

Catherine 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.

Darryl 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 25 years' experience in the floorcoverings industry.

Alison Littley
Independent Non-Executive Director

Alison was appointed a Non-Executive Director in January 2019 and will be appointed Chair of the Remuneration and Nomination Committees on 1 June 2019. Alison has substantial experience in multinational manufacturing and supply chain operations, and a strong international leadership background of building effective management teams and third-party relationships gained through a variety of senior management positions in Diageo plc and Mars Inc and an Agency to HM Treasury where she was Chief Executive Officer. She is currently a Non-Executive Director at James Hardie Industries Plc, an industrial building materials company headquartered in Ireland and listed on the Australian Securities Exchange, Eakin Healthcare Limited, Weightmans LLP, and Geoffrey Osborne Group.

Sue 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.

Karen Atterbury
Company Secretary

Karen was appointed Company Secretary in January 2019. Karen was previously Deputy Company Secretary of Barratt Developments PLC. Prior to this, she held various company secretarial roles including Company Secretary of Dixons Carphone PLC and Deputy Company Secretary of Dixons Retail. She is an Associate of the Institute of Chartered Secretaries and Administrators.

CHAIRMAN'S INTRODUCTION TO THE CORPORATE GOVERNANCE REPORT

I am pleased to present this, my first governance report since becoming Headlam's Chairman on 1 June 2018. I extend my and the Board's gratitude to my predecessor Dick Peters for his leadership these past years, and I look forward to maintaining the highest levels of corporate governance as the Company moves forward.

My priorities in 2018 have been to provide succession for Non-Executive Directors, improve the diversity of skills and experience on the Board, and ensure we continuously improve on all areas of corporate governance including risk management and addressing the requirements of the new UK Corporate Governance Code 2018 (the 'New Code').

The succession planning and evolution of the Board continued during the year with two new Independent Non-Executive Director appointments, and another just post the year-end on 1 January 2019. These appointments in part reflect Andrew Eastgate's forthcoming retirement from the Board on 31 May 2019 after nine years as a Non-Executive Director, and his roles as Chairman of the Remuneration Committee, Chairman of the Nomination Committee, and the Company's Senior Independent Director subsequently being divided between two of the recently appointed Non-Executive Directors.

Amanda Aldridge joined the Board on 1 February 2018 as a Non-Executive Director and became Chair of the Audit Committee on 1 June 2018. Amanda has significant experience as an external auditor from her 32 years with KPMG LLP, working predominately with quoted companies in the retail and distribution sectors.

Keith Edelman joined the Board on 1 October 2018 as a Non-Executive Director and was appointed Senior Independent Director on 1 January 2019. Keith brings extensive commercial experience coupled with a background in consumer facing businesses.

Alison Littley joined the Board on 1 January 2019 as a Non-Executive Director and will become Chair of both the Remuneration and Nomination Committees on 1 June 2019. Alison has substantial experience in multinational manufacturing and supply chain operations and a strong international leadership background of building effective management teams and third-party relationships.

I believe we have developed an effective Board which comprises the key strengths, experience and vision to uphold the highest levels of corporate governance and evaluate and continue to develop the Company's strategy (as detailed on page 24). Our Board considers that good governance underpins the delivery of our strategic priorities and future success of the business for the benefit of all stakeholders. The New Code took effect from 1 January 2019, and applies to accounting periods beginning on or after 1 January 2019. The application of the principles articulated in the New Code goes to the heart of good governance, and the Board has carefully considered and analysed the Company's position in relation to these principles and accompanying guidance which will apply to the Company's 2019 financial year. Being mindful of the New Code as well as the Company's continual endeavour to improve and evolve, the Company has initiated a number of actions and changes which will lead to full compliance with the New Code. Compliance with the New Code will be reflected in the next corporate governance report to be included in the annual report and accounts for the year ending 31 December 2019.

At the heart of the New Code is an emphasis on stakeholder relations and a company's culture. A key component for us will be the establishment of an Employee Forum this year, as outlined in detail on page 40 of the Strategic Report.

In last year's annual report, we stated that we intended to run an externally facilitated Board evaluation in 2018. Due to the considerable evolution of the Board, as detailed above, it was thought more beneficial to delay this external evaluation until 2019 when all the new Directors had joined the Board and could fully participate in the exercise. Instead we conducted an internal evaluation towards the end of 2018. Details of this evaluation are set out on page 55, and an external evaluation will be carried out in 2019 to adhere to best practice, despite there being no requirement for the Company to do so at this time.

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.

Philip Lawrence
Non-Executive Chairman

6 March 2019

CORPORATE GOVERNANCE REPORT

Our governance framework helps the Company in the delivery of its strategic priorities and ensures that its obligations to its stakeholders are understood and met. The Board consists of the Chairman, two Executive Directors and four Non-Executive Directors, with this reducing to three following the AGM in May 2019. The Executive Directors in conjunction with the members of the Senior Management Team, who also attend Board meetings, are responsible for the implementation of the decisions of the Board. The Non-Executive Directors are responsible for evaluating and challenging the proposals of the wider executive team, and their mix of skills and experience bring a broader perspective to the Board's dialogue and decision-making process.

Compliance statement

This corporate governance statement, together with the Nomination Committee report on pages 57 to 58, the Audit Committee report on pages 59 to 63 and the Directors Remuneration Report on pages 64 to 72 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 2018. The Code, as well as the New Code to be applied to accounting periods beginning 1 January 2019 onwards, 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 2018, 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 73 to 77.

The Board's Activities in 2018

Overview

The following sections outline the key activities of the Board during 2018. During the year, the Board took a number of steps to refresh and develop its role and remit, and the approach that it takes to governance in general. Specific activities of the Board included the following (with new initiatives marked with an asterisk):

Board and senior management structure:

- Review of succession plans and identifying required skills for all Directors and Senior Management Team;
- Discussions on the relevant skills required on the Board, including those that would help mitigate the risks specific to the Company, and the successful appointment of Amanda Aldridge, Keith Edelman and Alison Littley;
- Overseeing the induction process for new Directors; and
- Agreeing the appointment of a new Company Secretary.

Strategy and management:

- Review and approval of the Company's strategy and development plans;
- Greater interaction with senior managers of the Company's businesses on strategy and development plans, with particular emphasis on the People Strategy 2019-2021 prepared during the year*;
- Consideration of proposed cost control, margin and efficiency initiatives; and
- Review of the Company's acquisition strategy.

Internal controls and risk management

- Establishment of a new executive Risk Committee, and review of the Company's internal control and risk management systems*;
- Support for an enhanced Health & Safety capability and focus*;
- Review of reports on the Company's core IT, cyber security and technology risks and management's response plan*;
- Review of steps taken to ensure compliance with the General Data Protection Regulation (GDPR)*;
- Assessment of capital investment in property and acquisitions;
- Review and approval of an updated Whistleblowing policy;
- Advised on the updating of the Company's Anti-Corruption and Bribery policy, procedures on gifts & hospitality, and Fraud and Anti-money Laundering policy for Board approval in January 2019; and
- 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, with the Chairman attending a number of shareholder meetings;
- Participation in and review of the results of an internally facilitated Board and Committee evaluation exercise;
- A review of compliance against the New Code to determine the actions required to comply with its principles for the year ending 31 December 2019, including revisions to the Schedule of Matters reserved to the Board, Statement of the Responsibilities of the Chairman, Chief Executive and Senior Independent Director and terms of reference of the Board Committees*;
- Approval of a proposal to provide a forum for employees to engage with the Chief Executive and other Directors as appropriate, the key driver being the desire to improve communications with employees and create a positive working culture across the Company*;
- Consideration of the results of the 2018 Employee Engagement Survey*;
- Commissioning a supplier survey for implementation in the first half of 2019*;
- Approval of a Customer Insight exercise in the first half of 2019*; and
- Approval of the Modern Slavery Act Statement;

Operations and material transactions

- Review of a presentation on BREXIT by KPMG, and an action plan in preparation for operational issues that might arise on the UK leaving the European Union*;
- Review of the planning and subsequent trailing of stock re-ordering and dynamic route planning initiatives*;
- Approval of the acquisitions of Dersimo, CECO, Ashmount, Rackhams and Garrod Bros (see page 129 for full details of the transactions);
- Continuous assessment of potential acquisitions, cognisant of market and general economic background, with the objective of delivering strategic benefits to the Company and building upon certain product lines and/or market segments;
- Reviews of management structures in the Company's Continental Europe businesses; and
- Approval of the proposed acquisition of land for the development of a new distribution centre in Ipswich, UK*.

Financial and performance reporting

- Approval of the Company's annual and half-year results, and trading updates;
- Reviews of the Company's ongoing capital management strategy;
- Approval of share purchases;
- Reviews and approvals of the Company's investment programme;
- Review and approval of the Company's dividend policy, and approval of the interim and proposed final dividend;
- Approval of the UK Tax Strategy;
- Reviews of the Company's performance against KPIs;
- Reviews of the Company's operating and project performance; and
- Review of the Company's draft budget relating to 2019.

Leadership

The Board is the Company's principal decision-making body. The schedule of matters reserved for the Board, as approved by the Board on 21 September 2018, is available on the Governance section of the Company's website, www.headlam.com. It includes matters relating to strategy, capital expenditure, acquisitions and risk management. The Board also reviewed the roles and responsibilities of the Chairman, Chief Executive and the Senior Independent Director during the year. An overview of the main duties, roles and responsibilities of the Board are available on the Company's website. The Statement of the Responsibilities of the Chairman, Chief Executive and Senior Independent Director were reviewed during the year and the latest version is also available on the Company's website.

The Board has long-established Audit, Nomination and Remuneration Committees to oversee and debate important issues of policy and assist in attending to its responsibilities. Terms of reference for each have been updated during 2018 to ensure that they comply with the provisions of the New Code, and are available on 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 57 to 58 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 59 to 63 which should be read in conjunction with this report.

Remuneration Committee

The Directors Remuneration Report is set out on pages 64 to 72. The report also includes the Annual Report on Remuneration which is subject to an advisory vote at the 2019 AGM.

Effectiveness

Composition

As at 31 December 2018, the Board comprised:

Non-Executive Chairman	Executive Directors	Independent Non-Executive Directors[4]
Philip Lawrence	Steve Wilson, Chief Executive	Andrew Eastgate[1], Senior Independent Director
	Chris Payne, Chief Financial Officer	Amanda Aldridge[2], Non-Executive Director
		Keith Edelman[3], Non-Executive Director

[1] Stepped down as Senior Independent Director on 1 January 2019
[2] Appointed 1 February 2018
[3] Appointed 1 October 2018, and as Senior Independent Director on 1 January 2019
[4] Alison Littley was appointed after the year-end on 1 January 2019

Directors' attendance during the year at Board meetings is set out on page 55. 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.

The Board considers the balance achieved between Executive and Non-Executive Directors as appropriate and effective for the control and direction of the business going forward.

The Directors bring strong judgement to the Board's deliberations, and the size and balance of skills and experience of the Board is 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 four (excluding the Chairman, and including Alison Littley who was appointed a Non-Executive Director on 1 January 2019) 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.

The Senior Independent Director is available to shareholders if they have concerns which are not resolved through the normal channels of the Chairman, Chief Executive or Chief Financial Officer, or for which such contact is inappropriate.

The Non-Executive Chairman and Non-Executive Directors do not participate in any bonus, share option or pension scheme of the Company. They are initially appointed for a three-year term and, subject to review and re-election by shareholders, can serve up to a maximum of three such terms. However, in-line with governance best practice, all Board members (with the exception of Andrew Eastgate who will step down from the Board on 31 May 2019) will stand for election or re-election, as appropriate, by shareholders at the 2019 AGM and subsequent AGMs.

Commitment

The Board met 12 times during the year, to discuss the latest operating and financial information, key strategic items and other topics requiring discussion or decision. The Board meeting agenda is structured to ensure that sufficient time is given to each item 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 also endeavour to regularly visit operating locations to review operations first-hand and meet with the wider employee base.

A record of Directors' attendance at Board meetings held during the year is set out below. Committee meeting attendance is given in the relevant Committee reports.

	Meetings attended	Eligible to attend
Philip Lawrence	12	12
Dick Peters (stepped down 31/5/18)	5	5
Steve Wilson	12	12
Chris Payne	12	12
Tony Judge (stepped down 14/9/18)[1]	7	8
Andrew Eastgate	12	12
Amanda Aldridge (appointed 1/2/18)	11	11
Keith Edelman (appointed 1/10/18)	3	3

1 Tony Judge was unable to attend one Board meeting due to personal reasons

Training and Development

When joining, each new Director receives a tailored induction programme relevant to their experience, expertise and committees. Particular emphasis is placed on the new Director visiting several operating locations and businesses and meeting the associated senior managers.

A comprehensive information pack is provided which includes (but is not limited to):
- Background information about the Company;
- Briefings on Directors' duties and responsibilities;
- Information on Board meeting procedures;
- Board minutes;
- Internal and external policies;
- Matters reserved for the Board;
- Financial budgets;
- Shareholder and other stakeholder feedback;
- Sell-side analyst research notes;
- Relevant industry reports; and
- Committee terms of reference.

The new Director is also provided with an explanation of the Company's financing structure and relevant statutory and regulatory guidance notes, including the Code and New Code.

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 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 Company 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 Senior Management Team and senior managers of the Company's businesses on site visits. Non-Executive Directors are also encouraged to engage with all people across the Company to further enhance their understanding of the business.

Evaluation

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 three years. Under the Code and New Code, companies outside the FTSE 350 Index are not required to consider the use of externally facilitated Board evaluations. The Company was not a constituent of the FTSE 350 Index during 2018, nor as of the date of this Report.

As detailed above, in last year's annual report it was stated that the Company intended to run an externally facilitated Board evaluation in 2018. However, due to the considerable evolution of the Board it was thought more beneficial to delay this until 2019 when all new Directors referred to in this Report would be able to fully participate. An internal evaluation was instead conducted by the Company Secretary in conjunction with the Chairman towards the end of 2018. A comprehensive questionnaire was issued to each member of the Board and the responses were analysed by the Company Secretary and the Chairman, with the results reported to the Board. The evaluation concluded that the Board and its committees continued to operate effectively. Areas considered for improvement, and actions arising from this evaluation, were as follows:

	Board Decisions	Succession Planning	Board Meetings	Risk Management
2018 Outcomes	To continue to ensure that Board decisions are reviewed following their implementation.	Further enhance the succession planning for the Board and senior management roles.	Maintain and develop disciplines surrounding Board processes and ensure that an appropriate balance exists between the Board's discussions on short-term and long-term issues.	Further evolve the approach to risk management.
Actions for 2019	Broaden the use of post-implementation reviews.	Enhance succession plans for Executive Directors and other senior managers.	Make further progress in developing Board and Committee agendas and packs to assist the Board in its analysis of items presented for discussion.	Review approach to risk appetite.

Re-election of Directors

The Company's current Articles of Association provide that each Director shall retire from office and shall be eligible for reappointment at the third annual general meeting after the general meeting at which he or she was appointed or last reappointed. The Board has agreed that, with effect from and including at the 2019 AGM, all Directors will be subject to annual re-election, in compliance with the New Code. The Notice of AGM sets out the specific reasons why the Board considers the contribution of each Director to be important to the Company's long-term sustainable success and recommends their appointment or re-appointment.

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.

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 Company 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 conflicts of interest during the year.

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 Company's 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 Company to discharge their responsibilities effectively. This is reviewed annually by the Chairman.

Relations with shareholders

The Board places considerable importance on communication with shareholders. The Board considers that ongoing engagement with shareholders and the wider investment community, including analysts and investors not currently shareholders in the Company, is essential to shareholders' understanding of the Company and their ability to appraise the performance and management of the Company and consider the Company as an investment proposition.

The Company offers its larger shareholders, either directly or via its stockbrokers, face-to-face meetings on a bi-annual basis at a minimum, to present and discuss performance and other matters, and obtain feedback. These meetings are typically hosted by the two Executive Directors and the Company's Director of Communications. The Company also retains a Financial PR and IR adviser to further facilitate interaction and support its communication with the investment community.

Meetings are also periodically offered to and held with shareholders at various Company locations to help illustrate the Company's operations and aid understanding. Non-Executive Directors, including the Chairman, attend certain meetings, 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 Company's larger shareholders to hear any views and concerns.

The Company actively seeks shareholder feedback. 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 whilst also helping to inform its future communications.

All shareholders have the opportunity to communicate directly with the Board at the AGM. Shareholders are invited to ask questions during the meeting, followed by an opportunity to meet with the Directors after the formal business of the meeting. The Senior Management Team also attend the AGM and meet with shareholders before and after the meeting, and can provide operational tours to interested parties. All of the Directors attend the AGM, and the Chairman of the Board and the Chairs of 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 releases the results of voting, including proxy votes on each resolution, on its website on the next business day after the AGM and announces them through a regulatory news service. Details of the 2019 AGM are set out in the Notice of Annual General Meeting circular sent to shareholders as a separate document to this Report, and which is also available on the website.

NOMINATION COMMITTEE REPORT

Dear Shareholder

On behalf of the Board, I am pleased to present the Nomination Committee report for the year ended 31 December 2018.

The Nomination Committee has responsibility for reviewing the structure, size and composition of the Board and recommending to the Board any changes required for succession planning and for identifying and nominating for the approval of the Board candidates to fill vacancies as and when they arise. The Committee is also responsible for reviewing the results of any Board performance evaluation process and making recommendations to the Board concerning the Board's Committees and the re-election of Directors at the AGM.

I am pleased to present the Nomination Committee Report for 2018 which has seen the following new Board appointments:
- Amanda Aldridge as Non-Executive Director (appointed 1 February 2018 as reported in last year's Report);
- Keith Edelman as Non-Executive Director (appointed 1 October 2018); and
- Alison Littley as Non-Executive Director (appointed 1 January 2019).

We reported on Amanda Aldridge's appointment in the 2017 Annual Report and Accounts. Keith Edelman and Alison Littley's appointments followed a rigorous and independent selection process conducted in accordance with the Code. Further information on this is included in the report below.

Following my retirement from the Board on 31 May 2019, Alison Littley will become Chair of the Nomination Committee on 1 June 2019 having been a member of the Committee since her appointment. She is well placed to continue the Committee's work.

Andrew Eastgate
Chair of the Nomination Committee

6 March 2019

Board changes

Dick Peters, the Company's Non-Executive Chairman, stepped down from the Board on 31 May 2018. Philip Lawrence, a Non-Executive Director since June 2015 was appointed Non-Executive Chairman on 1 June 2018 following his re-election to the Board at the AGM on 24 May 2018. Philip continued as a member of all Committees, until stepping down as a member of the Audit Committee on 19 October 2018 of which he had previously been Chairman. Amanda Aldridge, whose appointment to the Board on 1 February 2018 was reported in the 2017 Annual Report, assumed the Chair of the Audit Committee on 1 June 2018.

Tony Judge, the Company's Chief Operating Officer, stepped down from the Board in September 2018 ahead of leaving the Company in March 2019. The Company initiated a search process at the end of 2018 for a UK Operations Director, a non-Board position, to assume a number of the Chief Operating Officer's responsibilities. Following this search process, a new UK Operations Director will join the Company, and the Senior Management Team, shortly.

Keith Edelman was appointed to the Board as a Non-Executive Director on 1 October 2018. In accordance with the Articles of Association, Keith will retire from the Board at the first AGM following his appointment and stand for election at the AGM in May 2019. 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 Company announced on 22 August 2018 that Alison Littley would be appointed as a Non-Executive Director with effect from 1 January 2019. In accordance with the Articles of Association, Alison will retire from the Board at the first AGM following her appointment and stand for election at the AGM in May 2019. 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.

Andrew Eastgate will step-down from the Board on 31 May 2019 following nine years as a Non-Executive Director of the Company at that time and will not be standing for re-election at the AGM in May 2019.

The Directors consider that following the appointment of Keith Edelman and Alison Littley as additional Non-Executive Directors, the size of the Board continues to be appropriate for the Company's size and listing.

Membership and attendance at meetings held in 2018

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 (stepped down 31/5/18)	2	2
Philip Lawrence	3	3
Andrew Eastgate	3	3
Amanda Aldridge (appointed to the Committee 1/2/18)	3	3
Keith Edelman (appointed to the Committee 19/10/2018)	0	0
Steve Wilson	3	3

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.

Appointment of Non-Executive Directors

In anticipation of Andrew Eastgate's retirement from the Board in May 2019 as announced within the interim results on 22 August 2018, the Nominations Committee undertook a skills review and succession planning exercise to ensure the Board comprises the skills required for the Company to deliver on its strategy. The Nomination Committee decided that two Non-Executive Directors would be recruited to assume separately the Senior Independent Director role and Remuneration Committee Chair thus providing an optimal balance on the Board. The Committee also re-affirmed its commitment to developing a diverse Board when considering candidates.

The skills review identified that the Board would benefit from additional expertise and experience in the following areas:

- Supply chain management;
- Change and cultural development;
- Commercial development and growth, both in the UK and Continental Europe;
- Customer-led service innovation; and
- Digital development.

The Nomination Committee appointed Ridgeway Partners, an independent search and recruitment consultancy with no other connection to the Company or its Directors, to carry out a full market appraisal of suitable candidates in-line with a comprehensive candidate brief developed by the Committee.

The Committee oversaw a rigorous and structured recruitment and interview process which concluded that Keith Edelman and Alison Littley were qualified to perform the roles for which they had applied. Keith Edelman and Alison Littley were subsequently appointed to the Board in October 2018 and January 2019 respectively.

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 in doing so, 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 Board continues to keep its diversity policy under review.

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.

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
Chair of the Nomination Committee

6 March 2019

AUDIT COMMITTEE REPORT

Dear Shareholder

As the new Chair of the Audit Committee, I am delighted to present the Committee's report for the year ended 31 December 2018 and to thank Philip Lawrence for his previous leadership of the Committee. Philip stepped down as Chair of the Committee following his appointment as Chairman of the Board in June and from the Committee in October. I am pleased to welcome to the Committee Keith Edelman and Alison Littley, who joined in October 2018 and January 2019, respectively.

The Audit Committee is given its authority by the Board and we act in accordance with our written terms of reference. An important part of our role is to monitor the integrity of the Group's financial reporting and management. In performing this role, we scrutinise the full and half yearly financial statements and review in detail, the work of the external auditor ('the Auditor') and any significant financial judgements made by management to ensure they are appropriate. Another important part of our role is to review the risk management and internal control framework operating across the Group to ensure that risks are being carefully identified and assessed and that sound systems of internal control are in place. During the year this has included reviewing reports from third parties in relation to cyber risk and strengthening the Group's IT infrastructure as well as the results from the Group's accounting team's reviews of accounting controls at each business (which are similar to those which might be undertaken by an internal audit function).

The Committee reviewed its terms of reference in September 2018, taking into account the requirements of the UK Corporate Governance Code issued on 18 July 2018 and applicable to the Group from 1 January 2019. We have also continued to oversee the Group's processes and reporting to ensure that it is compliant with the requirements of IFRS 15 'Revenue from Contracts with Customers' and IFRS 9 'Financial Instruments' this year and that it will be compliant with the requirements of IFRS 16 'Leases' when it becomes applicable for the year ending 31 December 2019.

In this report, we share some of the Committee's discussions from the year including details of the significant accounting matters and issues in relation to the Group's financial statements that the Committee has assessed and we explain why the issues were considered significant, which provides context for understanding the Group's accounting policies and financial statements for the year.

When drafting our annual Audit Committee calendar, we take into account the external environment, internal operations of the business and any planned accounting and regulatory changes to ensure that all of the areas we need to prioritise are included. In 2019 we will continue to focus on internal financial controls and risk assurance, particularly in respect of the performance improvement initiatives which are being trialled and implemented across the Group which are described on pages 18 and 19 and the principal risks and uncertainties outlined on pages 34 and 35 and to ensure that the links between the Board, Executive Risk Committee and Audit Committee processes are effectively managed.

I will be available at the AGM to answer any questions about our work.

Amanda Aldridge
Chair of the Audit Committee

6 March 2019

Audit Committee membership and meeting attendance

The Audit Committee has a meeting agenda linked to events in the Company's financial calendar, meeting as a minimum twice a year before the final and interim results announcements and subsequent publication of the respective reports. The Audit Committee met four times in the year and attendance was as follows:

Members	Meetings attended	Eligible to attend
Amanda Aldridge (appointed to the Committee 1/2/18, Chair of Committee from 1/6/18)	4	4
Philip Lawrence (Chair of Committee until 31/5/18, stepped down from Committee 19/10/18)	3	3
Andrew Eastgate	4	4
Keith Edelman (appointed to the Committee 19/10/18)	1	1
Dick Peters (stepped down 31/5/18)	1	1

All members are independent Non-Executive Directors. The Committee structure requires that at least one member has recent and relevant financial experience. This requirement was fulfilled by Philip Lawrence (from 1 January 2018 until 19 October 2018) and by Amanda Aldridge from 1 February 2018. All members of the Committee are financially literate and have expertise relevant to the Company's sector, gained through a variety of corporate and professional appointments as required by the UK Corporate Governance Code (see biographies on pages 50 and 51).

The Chief Executive, Chief Financial Officer and the Auditor also attended the Committee's meetings at the invitation of the Committee as did the Chairman from 19 October when he stepped down from the Committee. Meetings of the Committee with the Auditor without the presence of management were also held during the year. The role of Secretary to the Committee is performed by the Company Secretary.

As well as attending the Audit Committee meetings, the Committee members met with operational and finance team members during the year.

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 key activities of the Audit Committee during the year in discharging its principal areas of responsibility were:

Area of responsibility	Key Activities
Financial Reporting	▸ Reviewed the half year and annual financial statements and reports and the significant financial reporting estimates and judgements. ▸ 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 the Viability Statement included in the annual report and accounts in the context of the Group's three-year financial plan which had previously been considered by the Board. ▸ Reviewed and considered whether the annual report and accounts is fair, balanced and understandable, and provides information necessary for stakeholders to assess the Group's performance, business model and strategy. ▸ Assessed the impact of the new accounting standards (IFRS 9, 15, and 16).
External Audit	▸ Considered and approved the audit approach and scope of the audit work to be undertaken by the Auditor and the audit fee. ▸ Reviewed reports on audit findings. ▸ Considered the independence of the Auditor. ▸ Considered the effectiveness of the external audit.
Internal Controls and Risk	▸ Considered reports from management, the Auditor and other third parties on their assessment of the control environment. ▸ Assessed the effectiveness of the Group's internal control environment and the need for an internal audit function. ▸ Reviewed output from the Executive Risk Committee, and considered the systems and processes for identifying, managing and mitigating those risks. ▸ Reviewed reporting disclosures in relation to internal controls, risk management, principal risks and uncertainties and the work of the Audit Committee. ▸ Reviewed the Whistleblowing Policy and recommended its update.

Significant financial reporting issues and areas of estimate and judgement

A key responsibility of the Committee is to consider the significant areas of complexity, management judgement and estimation that have been applied in the preparation of the financial statements. The Committee has received reports and recommendations from management and the Auditor setting out the significant areas. These areas of judgement and estimation 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 when the Auditor presented its findings at the conclusion of its year-end audit. Set out below is a description of how the Committee concluded that such judgements and estimates were appropriate.

Acquisition Accounting

The Company made five small acquisitions during 2018 – details are set out on page 129. For each of these acquisitions, management carried out an assessment of the fair value of the consideration and the assets and liabilities on acquisition, and performed individual purchase price allocation reviews which involved exercise of judgement. Management were also required to review the provisional fair values attributed to the assets and liabilities of Domus in 2017 and to reassess their estimate of the deferred contingent consideration likely to be payable in respect of this acquisition.

The Audit Committee reviewed the accounting for each of the 2018 transactions, focusing on the calculation of the fair value of consideration and the intangible assets, challenged the assumptions used in arriving at each category of asset and considered the useful lives over which the assets would be amortised. Following this review and discussion with the Auditor, the Audit Committee was satisfied with the purchase price allocation and that the amortization charge appropriately reflects the useful economic lives of the assets.

The Committee discussed with management the basis of their conclusion that no adjustments to the provisional fair values of Domus' assets and liabilities was required and their calculation of the deferred contingent consideration which led to a release of £1.4m of the provision established on acquisition. Based on this and review of the Auditor's findings, the Committee was satisfied that the approach adopted by management was robust and that the assumptions made were reasonable.

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 had not been received 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 £132.7 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 entails close monitoring of inventory levels, review of relevant supplier rebates and overheads which are absorbed into the cost of inventory, review of the ageing profile and consideration of inventory sold for less than its carrying value.

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 2018, the Scheme had assets of £109 million and liabilities, measured on an IAS 19 basis, of £112 million, with a net deficit of £2.6 million, after taking account of a past service cost of £1.2m in respect of GMP equalisation. 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. 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. Management also took advice from the Group's external actuary in assessment of the Group's GMP liability.

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

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.

Non-underlying items

The Group accounting policy for non-underlying items states that performance measures will be presented which exclude items which 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. Management must exercise judgements in deciding whether items should be treated as non-underlying by reference to this policy.

The Committee considered the presentation of non-underlying items in accordance with the Group accounting policy. The Committee received reports from management and the Auditor, outlining the judgements applied. The most significant items treated as non-underlying are in respect of the amortisation of acquired intangible assets, the release of the provision for variable consideration for Domus (described above) and the past pension service cost arising on GMP equalization (described above). The Committee concluded that the disclosure of the non-underlying items was sufficient for the user of the accounts to understand the nature of the items and reason for their treatment as non-underlying.

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 had been found in the course of the audit work and no material amounts remain unadjusted. The Audit Committee confirmed that it was satisfied that the Auditor's responsibilities had been fulfilled with diligence and professional scepticism.

Risk management and internal control

The Board has ultimate responsibility for effective management of risk for the Group including determining its risk appetite and identifying key strategic and emerging risks. An overview of the risk management process and the principal risks and uncertainties identified is set out on pages 34 to 35. The Executive Risk Committee 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. The work of the Executive Risk Committee is reviewed by the Board. The role of the Audit Committee in risk management is to monitor and review assurance provided via the Executive Risk Committee, including over any non-financial internal controls and management systems requested by the Board.

In supporting the Board to assess the effectiveness of risk management and internal control processes, the Audit Committee relies on a number of different sources including reports provided by management and the assurance provided by the Auditor and other third parties in specific risk areas. Additionally, the Audit Committee receives reports from the Auditor on matters identified in the course of its statutory audit work. The Audit Committee also takes into account the resources within the finance team including the structure of the team, and the qualifications, experience and competence of the people within it.

During the year the Committee received reports on and/or considered the following:

(i) Management's follow up on control recommendations raised by the Auditor.
(ii) Monitoring progress with implementation of recommendations made by third parties for strengthening the IT infrastructure and reducing risk of cyber-attack.
(iii) Internal control review work undertaken by the finance team at each location in the Group.
(iv) Structure, qualifications, competence and experience of the finance team.

The Group's control framework has developed over many years and is intended to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. The control framework is evolving in-line with the strategic objectives outlined on page 24 and monitoring this will be a key element of the Committee's focus in 2019.

The Audit Committee was satisfied that the reporting disclosures in respect of internal controls and risk management are a fair representation of the Group's position.

Internal audit

During the year, the Audit Committee undertook an assessment of the need for a Group internal audit function including consideration of the various reports by management and assurance reporting from third parties referred to above in relation to risk and control. 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.

External Auditor

Each year the Audit Committee reviews the appointment and performance of the Auditor and considers their independence and objectivity, taking into account all appropriate guidelines.

PwC was appointed as Auditor in 2016 following a full tender exercise. Mark Smith has been the lead audit partner since PwC's appointment and accordingly this is his third year in that role. In accordance with the current professional standards the lead audit partner responsible for the audit will change every five years. Under current FRC guidance the Company is not due to retender its audit until 2026, however the Audit Committee will continue to monitor the performance of the External Auditor during this time and make recommendations accordingly.

The Auditor has processes in place to ensure that independence is maintained and has written to the Audit Committee confirming that, in its opinion, they remain independent within the meaning of the relevant regulations on this matter and their professional standards.

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 Audit Committee recognises that there are occasions when it is advantageous to use the Auditor to undertake non-audit services, as it may improve the quality of the audit and reduce cost and complexity for the Company. Per the EU Audit Directive, 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. The Auditor did not perform any non-audit work for the Group during 2018. A breakdown of audit and non-audit fees is provided in note 3 to the Financial Statements.

The scope of the external audit for the 2018 Annual Report was presented by the Auditor to the Committee in October 2018. The Committee had the opportunity to discuss and challenge the audit plan to gain a good understanding of the key elements.

The Committee assesses the effectiveness of the Auditor during the year on the basis of meetings with management and carries out a formal review of its performance after the year-end audit is completed. In undertaking this assessment, the Audit Committee considers a number of factors which include the experience and tenure of the audit partner, the completion of the agreed audit plan, the professional scepticism, robustness and perceptiveness of the Auditor in handling of key accounting judgements and the interaction between management and the Auditor.

The Audit Committee has independent access to the Auditor and the Auditor has direct access to the Chair 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.

The Audit Committee is satisfied with the independence, objectivity and effectiveness of the Auditor and recommends PwC to be reappointed by the shareholders at the forthcoming AGM.

Interaction with the FRC

Company can confirm that during the year under review it had no interaction with the FRC's Corporate Reporting Team or its Audit Quality Review Team.

Fair, balanced and understandable statements

The Audit Committee undertook a detailed review of the drafting and preparation process of the Annual Report and Accounts to support its deliberations on whether the 2018 Annual Report and Accounts were fair, balanced and understandable. The drafting and preparation process involved various teams and individuals within the Group including Executive Directors, Finance Team, Director of Communications, Senior Managers of the businesses and Company Secretary working together with support and advice from the Company's advisers. This collaborative approach helped to ensure a consistent and detailed approach between the Strategic Report, the Governance section and the Financial Statements. At its meeting in March 2019, the Audit Committee deliberated on whether the 2018 Annual Report and Accounts were fair, balanced and understandable. Following detailed consideration of all sections, the Audit Committee concluded that the 2018 Annual Report and Accounts contained an accurate reflection of the Company's performance and business model, correctly reflected its strategy, and included consistent messaging throughout. It, therefore, recommended to the Board that the 2018 Report and Accounts were, fair, balanced and understandable and contained sufficient information for shareholders to assess the Company's position, performance, business model and strategy.

Viability statement

The Audit Committee assessed the Group's resilience to the principal risks and uncertainties by consideration of a paper which included stress testing forecasts through the application of adverse scenarios. These scenarios included (A) a reduction in market demand whilst there is ongoing inflationary fixed cost pressure and (B) an economic crisis similar to that experienced in 2008, both modelled over a three-year period. The testing indicated that the Group would be able to operate within its current facilities and meet its financial covenants, however the scenario based on a severe economic environment did require management to take swift action to manage the cost base in mitigation. The Audit Committee was therefore comfortable that the Group would maintain resilience in the event such scenarios occurred and concluded that there was a reasonable expectation that the Group would continue to operate and meet its liabilities over a three-year period. The Audit Committee agreed that the long-term viability assessment should continue to be performed over a three-year timespan. This conclusion was communicated and recommended to the Board for approval.

The long-term viability statement is shown on page 36.

Whistleblowing policy, fraud and the Bribery Act

The Group has in place a whistleblowing policy that sets out the formal process by which an employee of the business may, in confidence, raise concerns about possible improprieties in financial reporting or other matters. During the year, the Audit Committee and the Board reviewed and updated the Whistleblowing Policy.

The Group also has in place a procedure for detecting fraud and systems in place to prevent a breach of anti-bribery legislation. The Group is committed to a zero-tolerance position with regard to bribery. The Anti-corruption and Bribery, and Fraud and anti-money laundering policies were considered by the Committee during the year and approved by the Board in January 2019.

Committee effectiveness review

The effectiveness of the Audit Committee was evaluated this year as part of the Board evaluation process. Details of this can be found on page 55. The review found that the committee is operating effectively and that its role and remit remained appropriate for the current needs of the business. The Committee discussed the findings of the evaluation to identify opportunities for further improvement.

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.

Amanda Aldridge
Chair of the Audit Committee

6 March 2019

THE CHAIRMAN'S ANNUAL STATEMENT

Dear shareholder

On behalf of the Board, I am pleased to present the Directors' Remuneration Report for 2018, which features this statement and the Annual Report on Remuneration for the financial year ended 31 December 2018. At the 2018 AGM, shareholders endorsed the 2017 Annual Report on Remuneration, with 98.62% of votes cast being in favour. The Remuneration Policy, as required to be put to shareholders every three years, was approved at the 2017 AGM and is designed to simplify the previous remuneration structure and encourage a long-term focus on the performance of the business.

The key features of the remuneration structure for Executive Directors are:

- Base salary;
- Maximum bonus opportunity of 125% of base salary;
- One-third of any amount earned under the bonus is deferred into ordinary shares in the Company for two years;
- This deferral element is delivered under the terms of the Deferred Bonus Plan ('DBP');
- A Performance Share Plan ('PSP') with a maximum opportunity of 100% of base salary and a two-year holding requirement after the awards vest. For the financial years 2017, 2018 and 2019, the opportunity has been set at 80% of base salary;
- A maximum pension contribution (or cash allowance in lieu of pension) of up to 15% of salary, although only the Chief Financial Officer currently participates in any pension arrangement and this is at a contribution level of 11%; and
- Shareholding guidelines requiring that Executive Directors build-up and maintain a shareholding in the Company equivalent in value to 200% of annual base salary.

Director changes

During the year, Amanda Aldridge and Keith Edelman joined the Board and were appointed as members of the Remuneration Committee. Alison Littley joined the Board on 1 January 2019 and will take over as Chair of the Remuneration Committee on 1 June 2019 following my retirement from the Board on 31 May 2019 after nine years.

On 14 September 2018, Tony Judge, the Company's Chief Operating Officer, stepped down from the Board ahead of leaving the Company on 14 March 2019. The termination arrangements in relation to Tony Judge, are detailed on page 68.

Remuneration for 2018

As disclosed in last year's Annual Report, the annual salary of Chris Payne, who joined the Board as Chief Financial Officer in September 2017, was set at £325,000 with an agreement that it would increase to £350,000 with effect from 1 March 2018 subject to performance. The increase was confirmed following an assessment of his performance by the Committee. There was no other increase in base salary for Executive Directors during 2018, with the Executive Directors waiving a base salary increase of 2.0% for 2018 which was awarded to the Company's UK employees with effect from 1 January 2018.

Awards under the PSP were granted during April 2018 to the three Executive Directors at that time (each award equating to 80% of salary). Further details of the awards and the performance conditions attached are set out on page 68. Bonus details and vesting outcomes for the long-term incentive plans are explained below.

During the year, three new Non-Executive Directors were appointed to the Board. The search process instigated a review of fees required to find the right calibre of candidate. Fees for Non-Executive Directors were increased by £5,000 in respect of the basic fee and additionally £2,500 for Committee chairmanship (excluding Nomination Committee chairmanship) during 2018. My own fees remained unchanged recognising that I shall be stepping down from the Board in May 2019. As noted last year, the Chairman's fees were increased to £143,500 on appointment of Philip Lawrence in June 2018 to better reflect the duties of the role.

Business performance and incentive out-turn for 2018

For 2018, the Executive Directors had a maximum annual bonus opportunity equal to 125% of base salary, with the bonus assessed against the Company's underlying profit before tax performance metric as shown in the table on page 67. Threshold performance was not achieved in respect of the underlying Profit Before Tax performance metric and, therefore, the Executive Directors will not receive an annual bonus payment in respect of the financial year ended 31 December 2018.

Awards granted under the CIP in 2016 vest with respect to performance for the financial year ended 31 December 2018. The awards were subject to two performance conditions, based on EPS growth (80% of the award) and relative TSR (20% of the award). The combined assessment of the two performance conditions means that 53.5% of the awards will vest, as shown on page 67.

Remuneration for 2019

The Executive Directors received an increase in base salary of 2.0% effective 1 January 2019, in-line with the 2019 2.0% pay award to all UK employees. All aspects of variable pay remained unchanged against that of 2018, with the same structure applying, except that the Remuneration Committee will, in-line with the terms of the Remuneration Policy, adjust the annual bonus metrics so that in 2019 75% will be based on financial performance with 25% on achievement of non-financial strategic/personal objectives. This is to further align the annual bonus to the Company's strategy which comprises both financial and non-financial targets. The combination of a holding period requirement under the PSP, the deferral into shares under the annual bonus scheme and the shareholding guidelines is considered to appropriately align Executive Director interests with the interests of shareholders and provides a beneficial long-term framework for our business and delivery of the strategy.

Conclusion

I would like to welcome Alison Littley who will be assuming the Chair of the Committee on 1 June 2019. Alison brings extensive supply chain and procurement experience and currently holds a number of Non-Executive Director appointments, including James Hardie Industries plc where she sits on the Compensation Committee and Weightmans LLP where she sits on the Remuneration Committee. She therefore brings significant experience to her new role as Chair of this Committee. One of her first tasks will be to conduct a review of our remuneration policy, as this will be required to be put to a shareholder vote at the 2020 AGM. In addition, working closely with the Board, she will be reviewing any changes required by the New Code from a remuneration perspective and we will be reporting in full on these in the 2019 Annual Report.

We remain committed to a responsible approach to executive pay, as I trust 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 2019

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 2018 and 2017.

Executive Directors' remuneration as a single figure – 2018 (audited)

Executive Directors	Base salary/ fees 2018 £000	Non-salary benefits[2] 2018 £000	Annual performance bonus 2018 £000	Share-based incentive schemes[3,4] 2018 £000	Pension related benefits 2018 £000	Other 2018 £000	Total 2018 £000
Steve Wilson	**475**	**16**	**–**	**97**	**–**	**–**	**588**
Tony Judge (stepped down 14/9/18)[1]	**301**	**10**	**–**	**86**	**–**	**–**	**397**
Chris Payne	**346**	**19**	**–**	**4**	**38**	**–**	**407**
	1,122	**45**	**–**	**187**	**38**	**–**	**1,392**

[1] Salary and benefits for Tony Judge relate to amounts earned during the year to the date of stepping down from the Board on 14 September 2018.
[2] Non-salary benefits include the provision of a company car or car allowance, private medical insurance and some fuel costs.
[3] Performance conditions for the CIP were tested after 31 December 2018 and approximately 53.5% of the award is due to vest in May 2019. The market price of the shares has been calculated based on an average market value over three months to 31 December 2018 (£4.423). The figure shown for Chris Payne relates solely to the grant of options under the Sharesave Scheme.
[4] Includes the grant of options under the Sharesave Scheme on 3 May 2018, calculated on an intrinsic value basis.

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[3] 2017 £000	Pension related benefits 2017 £000	Other 2017 £000	Total 2017 £000
Steve Wilson	475	16	391	187	–	–	1,069
Tony Judge (appointed 31/3/17)[1]	319	10	350	167	–	–	846
Chris Payne (appointed 13/9/17)[2]	95	8	–	–	11	133	247
	889	27	741	354	11	133	2,155

[1] Tony Judge was appointed as an Executive Director on 31 March 2017 with his annual base salary increased to £425,000 at that time. The table above reflects the pro-rata amount of salary received in the period after his appointment but 100% of annual bonus and an amount in respect of share-based incentive scheme.
[2] Chris Payne was appointed as an Executive Director on 13 September 2017 on an initial annual base salary of £325,000. The figures reflect the pro-rata amounts received in the period after 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, with this figure included in the 'Other' column.
[3] Share based incentives vested in respect of the performance to the year ended 31 December 2017 in the form of Co-Investment Plan ('CIP') awards. These CIP awards, granted on 1 May 2015, vested on 1 May 2018 and 97.5% of the matching award became due to the participants. The long-term incentives figure for the year ended 31 December 2017 has been restated to reflect the market value of the shares on the date of vesting (£4.355).

The table on page 66 reports the total remuneration receivable in respect of qualifying services by each of the Non-Executive Directors for the years 2018 and 2017.

Non-Executive Directors' remuneration as a single figure – 2018 (audited)

Non-Executive Directors	Fees[1] 2018 £000	Non-salary benefits 2018 £000	Annual performance bonus 2018 £000	Share-based incentive schemes 2018 £000	Pension related benefits 2018 £000	Total 2018 £000
Andrew Eastgate	**55**	**–**	**–**	**–**	**–**	**55**
Philip Lawrence (appointed Chairman 1/6/18)[2]	**102**	**–**	**–**	**–**	**–**	**102**
Amanda Aldridge (appointed 1/2/18)	**46**	**–**	**–**	**–**	**–**	**46**
Keith Edelman (appointed 1/10/18)	**11**	**–**	**–**	**–**	**–**	**11**
Dick Peters (stepped down 31/5/18)	**46**	**–**	**–**	**–**	**–**	**46**
	260	**–**	**–**	**–**	**–**	**260**

1 The fees above reflect the pro-rated amounts received since appointment or to the date of stepping down from the Board.
2 Philip Lawrence's fees until 31 May 2018 were paid to the Coal Authority which released him to perform his duties as a Non-Executive Director. Philip resigned from the Coal Authority with effect from 31 May 2018 upon assuming his appointment as Chairman on 1 June 2018. Fees from 1 June 2018 were paid to him directly.

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

Non-Executive Directors	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[1]	45	–	–	–	–	45
Dick Peters	110	–	–	–	–	110
	210	–	–	–	–	210

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

Executive Directors' external appointments

Steve Wilson is currently a Non-Executive Director of Conviviality plc, and in respect of the financial year ended 31 December 2018, received a fee of £12,500 in relation to the appointment. No other Executive Director holds any external appointments as of the date of this report.

Individual elements of remuneration

The figures in the single figure tables above are derived from the following:

Base salary and fees	The amount of salary/fees received during the financial period for service on the Board.
Non-salary benefits	The taxable value of benefits received in the financial period for service on the Board for each Director. 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 or paid as cash in lieu of retirement benefits 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. The last award made under the CIP occurred in 2016 with the final vesting included in the 2018 single figure table. From 2017, share-based incentives were made under the PSP.

Base salaries and fees for 2018

Other than in respect of Chris Payne whose annual base salary increased from £325,000 per annum in 2017 to £350,000 per annum in 2018 with effect from 1 March 2018 (as detailed above), none of the Executive Directors received an increase in annual base salary for 2018. A cost of living pay increase of 2.0% of base salary was awarded to all UK employees in 2018, with the exception of the Executive Directors and Senior Management Team who elected not to receive it.

	2018 £000	2017 £000	Increase %
Steve Wilson	**475**	475	0
Tony Judge	**425**	425	0
Chris Payne	**350**	325	6

Changes were made to Non-Executive Directors fees as set out in the table below.

		2018 £000	2017 £000	Increase %
Chairman fee		**143.5**	110	30.4%
Non-Executive Director fee[2]		**45.0**	40	12.5%
Additional fee for	– Chairmanship of the Remuneration Committee	**7.5**	5	50.0%
	– Chairmanship of the Audit Committee	**7.5**	5	50.0%
	– Senior Independent Director	**10.0**	10	0.0%

[1] The Chairman's fee was increased from when Philip Lawrence was appointed Chairman on 1 June 2018.
[2] The general increase in fees for Non-Executive Directors was implemented for new appointments and responsibilities on or after 1 January 2018. Andrew Eastgate's fees remained unchanged as he will be stepping down from the Board on 31 May 2019.

Annual performance bonus

For 2018, the Executive Directors were awarded a maximum annual bonus opportunity equal to 125% of base salary. The bonus was assessed against the Company's underlying Profit Before Tax performance metric as shown in the table below. Threshold performance was not achieved and, therefore, the Executive Directors will not receive an annual bonus payment in respect of the financial year ended 31 December 2018.

Performance metric	Proportion of bonus determined by metric	Threshold performance	Target performance	Maximum performance	Actual performance	Bonus earned (% max)
Underlying Profit Before Tax	100%	£42.62m	£47.3m	£56.66m	£42.4m[1]	0%

[1] Reported underlying profit before tax of £43.4m less £1.0m reflecting a reduction in cost of sales for the anticipated early settlement discount received from the year-end trade creditors.

In accordance with our remuneration policy, one-third of any bonus earned would have been deferred into shares for a two-year period.

Share based payments vesting in the financial year

Awards granted under the CIP in 2016 vest with respect to performance for the financial year ended 31 December 2018. 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 SmallCap Index
Threshold: 0:6:1 match	3% + RPI	Median
Maximum: 2:1 match	6% + RPI	Upper quartile
Outcome	4.58% + RPI	Ranked 74th
Vesting	66.83%	0%
Proportion of award vesting	53.46%	0%

	Shares granted	Shares vesting	Value of shares vesting
Steve Wilson	40,886	21,860	£96,687
Tony Judge	36,567	19,550	£86,470

Value is based on the average share price for the final quarter of the financial year which was 442.3 pence based on the mid-market closing share price. Tony Judge was not an Executive Director at the time of grant and his award was in-line with other members of the Senior Management Team.

PSP awards granted during the financial period

PSP awards were granted to Executive Directors in 2018 as follows:

	Number of ordinary shares over which award granted	Value of Award £000	% of salary	Date of Grant	Holding period
Steve Wilson	86,187	380	80	9 April 2018	2 years
Tony Judge	77,114	340	80	9 April 2018	2 years
Chris Payne	63,506	280	80	9 April 2018	2 years
	226,807	1,000			

The share price used to determine the number of shares under the PSP was 440.9 pence, being the average mid-market closing share price for the five business days prior to the date of 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% compound annual growth over the three years to 31 December 2020. This was above consensus market expectations at the date of the grant and above the Company's internal business plan, and at a level which the Remuneration Committee considered 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.

Dilution

The Remuneration Committee supports the Investment Association ('IA') guidelines regarding dilution and regularly monitors compliance with these requirements. The Company's 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 3.71% of the issued share capital (excluding treasury shares) and in respect of grants under discretionary plans was 0% of the issued share 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

The only Executive Director to receive any pension benefit during the year was Chris Payne, who received pension contributions from the Company equivalent to 11% of his base salary which is in-line with pension payments to members of the Company's senior management.

Payment for loss of office

No payments for loss of office were made to past Directors during the financial period other than in respect of Tony Judge who stepped down as an Executive Director on 14 September 2018. Tony Judge remained employed by the Company until 14 March 2019 and continued to receive his base salary and normal benefits during this time. For the period between 14 September 2018 and 14 March 2019 the payment to Tony Judge relating to his salary and benefits was £217,277. The Company also made a contribution of £12,000 plus VAT in respect of Tony's legal fees incurred in relation to his leaving arrangements. A maximum payment of £212,500 in lieu of notice will be made in respect of the six months from 14 March 2019 in equal instalments and subject to mitigation. As with the other Executive Directors, Tony Judge will not receive an annual bonus payment in respect of the financial year ended 31 December 2018. As he was employed for the whole of the relevant performance period in respect of the 2016 awards under the CIP, the awards granted in 2016 vested as set out above.

In recognition of Tony Judge's long service with the Company, having been with the business for 26 years, it was agreed that awards made under the PSP in 2017 and 2018 will vest to the extent that performance measures are met and subject to pro-rating for time employed. Malus and clawback provisions apply under the terms of the rules and all such vested shares will be released in April 2021. Awards made under the DBP (in respect of the deferred element of the 2017 annual bonus) will vest on their normal vesting date, subject to malus and clawback.

Payments to past Directors

As outlined on page 70 of the 2017 Annual Report and Accounts, Tony Brewer was permitted to retain his 2015 and 2016 CIP awards. The 2015 CIP award vested on 1 May 2018. Accordingly, 33,805 shares vested following the application of pro-rating for his period in office and performance conditions. The 2016 CIP award is due to vest on the 6 May 2019. Following the application of time pro-rating and performance conditions, 7,123 shares will be issued to Tony Brewer on vesting.

No further payments to former Directors have been made in the 2018 financial year and up to the date of this Report except those disclosed above.

Statement of Directors' shareholding and share interests (audited)

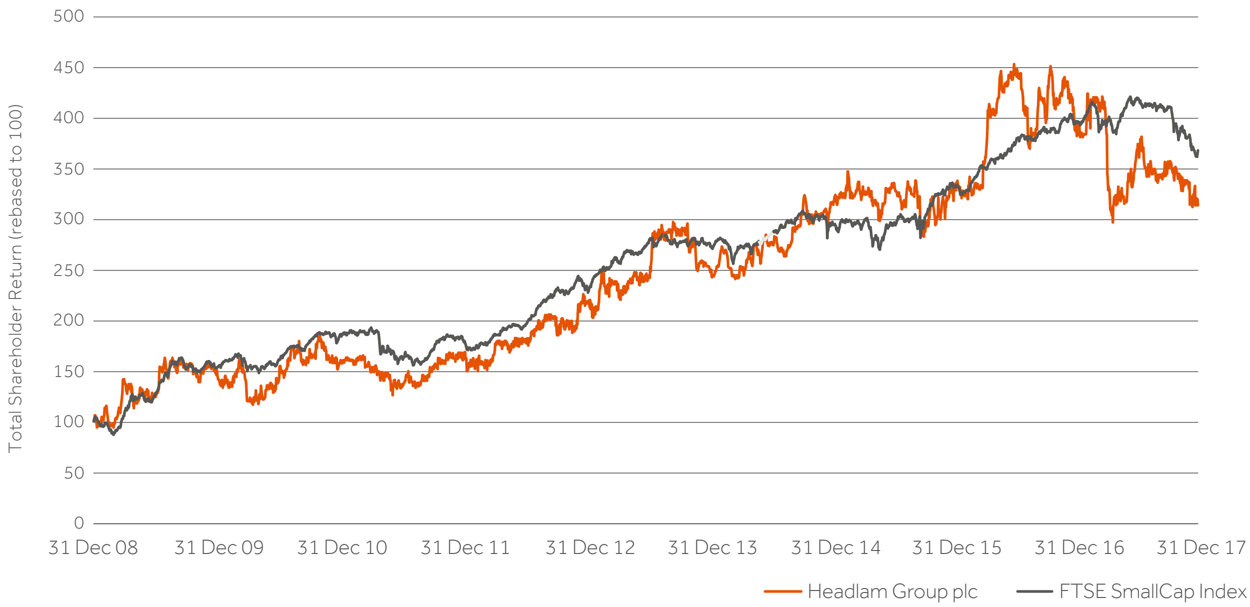
In order to align the interests of the Executive Directors with those of the Company's shareholders, the Remuneration Committee encourages Executive Directors to increase their shareholdings in the Company. The Executive Directors are required to build up and maintain a beneficial interest (including interests of connected persons) 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 the CIP, PSP and DBP until the guideline is met.

The interests of Directors and their connected persons in the Company's ordinary shares as at 31 December 2018 were as set out below. There have been no changes to those interests between 31 December 2018 and the date of signing of these financial statements and reports.

	Type	Grant date	Option price	Share price at grant[3]	Owned outright	Unvested and subject to performance conditions	Unvested and not subject to performance conditions	Vesting date	Total as at 31 December 2018
Steve Wilson	Ordinary Shares	–	–	–	657,272	–	–	–	657,272[1]
	PSP Shares	9 April 2018	Nil	441p	–	86,187	–	March 2021	86,187
	DBP Shares	9 April 2018	Nil	441p	–	–	29,514	March 2020	29,514
	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
	2014 SAYE	8 May 2014	381p	476p	–	–	7,874	July 2019	7,874
Tony Judge[2]	Ordinary Shares	–	–	–	129,045	–	–	–	129,045
	PSP Shares	9 April 2018	Nil	441p	–	77,114	–	March 2021	77,114
	DBP Shares	9 April 2018	Nil	441p	–	–	26,408	March 2020	26,408
	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 SAYE	5 May 2015	340p	461p	–	–	8,823	July 2020	8,823
Chris Payne	PSP Shares	9 April 2018	Nil	441p	–	63,506	–	March 2021	63,506
	PSP Shares	25 Sept 2017	Nil	536p	–	48,435	–	March 2020	48,435
	2018 SAYE	3 May 2018	353p	442p	–	–	5,084	July 2021	5,084
Amanda Aldridge	Ordinary Shares	–	–	–	–	–	–	–	–
Andrew Eastgate	Ordinary Shares	–	–	–	1,000	–	–	–	1,000
Keith Edelman	Ordinary Shares	–	–	–	–	–	–	–	–
Philip Lawrence	Ordinary Shares	–	–	–	–	–	–	–	–
Dick Peters[2]	Ordinary Shares	–	–	–	5,000	–	–	–	5,000

1 Steve Wilson as at 31 December 2018 held shares in excess of the shareholding guideline (based on the Company's closing mid-market share price on 31 December 2018).
2 The interests are shown to the date when Tony Judge and Dick Peters stepped down from the Board.
3 Share price shown to the nearest pence if applicable.

The graph below shows the value at 31 December 2018 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 (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 ten financial periods.

Period		Chief Executive single figure of total remuneration £000	Annual bonus (% of maximum opportunity)	Long-term incentive vesting rates against maximum opportunity %
2018	Steve Wilson	588	0.0	53.5
2017	Steve Wilson	1,069	65.82	97.5
2016	Steve Wilson	1,067[1]	76.8	98.6
	Tony Brewer	737[2]	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

1 This remuneration is for the full year and incorporates his remuneration as Group Finance Director from 1 January 2016 until 14 September 2016 when he became Chief Executive

2 Tony Brewer stepped down as Chief Executive and a Director on 14 September 2016. The 2016 figures reflect his remuneration earned from the start of 2016 until the date of his resignation as a Director. 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 2018 and 2017.

Percentage increase/(decrease) in remuneration in 2018 compared with 2017	Chief Executive	Total Employees
Salary and fees	0.0%	2.0%
All taxable benefits	0.0%	0.0%
Annual bonuses	(100.0%)	(35.1%)

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.

	2018 £000	2017 £000	% change
Dividends	**20,969**	25,729	(18.5%)
Pay	**103,329**	97,707	5.8%

Statement of implementation of remuneration policy in 2019
Details of how the Company will operate the Remuneration Policy in 2019 is provided below.

Base salaries and fees for 2019
The Executive Directors received an increase in base salary of 2.0% for 2019 in-line with the pay award to all UK employees, effective 1 January 2019.

In-line with the additional fees associated with Chairmanship of the Remuneration Committee and Senior Independent Director (as detailed on page 67), in January 2019 Keith Edelman's fee increased from £45,000 to £55,000 when he assumed the role of Senior Independent Director, and Alison Littley's fee will increase from £45,000 to £52,500 when she becomes Chair of the Remuneration Committee in June 2019 having been appointed a Non-Executive Director on 1 January 2019.

Annual bonus
The maximum annual bonus opportunity for 2019 will remain at 125% of base salary. As referenced above, the Remuneration Committee will, in-line with the terms of the Remuneration Policy, adjust the annual bonus metrics so that in 2019 75% will be based on financial performance with 25% on achievement of non-financial strategic/personal objectives. The achievement of these objectives would further align the achievement of annual bonus to the Company's strategy which comprises both financial and non-financial targets. Full disclosure of all objectives and targets, both financial and non-financial, will be provided in the 2019 Annual Report and Accounts. As previously stated, 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 2019 will be granted in the form of nil cost options over ordinary shares in the Company 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, and 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, most recently on 21 September 2018. The terms of reference are reviewed periodically and are available on the Company'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 at scheduled meetings of the Committee during the year was as follows:

Members	Meetings attended	Eligible to attend
Philip Lawrence	4	4
Dick Peters (stepped down 31/5/18)	2	2
Keith Edelman (appointed 1/10/18)	1	1
Amanda Aldridge (appointed 1/2/18)	4	4
Andrew Eastgate	4	4

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.
- Setting 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 four meetings of the Remuneration Committee were as follows:

Meeting Date	Key agenda items
1 March 2018	Approval of 2017 annual bonus and setting 2018 annual bonus
29 March 2018	Grant of awards under the DBP and PSP
21 September 2018	Review of Executive Director and Senior Management Team remuneration; review of terms of reference and Committee programme in anticipation of the New Code
18 December 2018	Pay increases for Executive Directors and Senior Management Team and review of bonus arrangements against anticipated performance (as detail in base salaries and fees for 2019 section on page 71)

Advisers

Deloitte LLP were appointed as advisers to the Remuneration Committee in October 2016 to advise on the Remuneration Policy, and on an ongoing basis. Deloitte's fees in respect of advice to the Remuneration Committee during the period ended 31 December 2018 were £18,108 (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 2017 Annual Report on remuneration at the 2018 AGM and binding vote on the remuneration policy at the 2017 AGM.

	% of votes cast For	% of votes cast Against	Number of shares Withheld
2017 Directors' Remuneration Report	98.62	1.38	2,379,028
2017 Remuneration Policy	99.34	0.66	160,202

Key Principles of the Remuneration Policy

The key principles of the Remuneration Policy are as set out in the 2016 Annual Report and Accounts on pages 52 to 62, and can be found on the Company's website www.headlam.com.

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 2019

OTHER STATUTORY DISCLOSURES

The Directors present their report, together with the audited financial statements, for the year ended 31 December 2018. This report 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 12 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 the sales, marketing, supply and distribution of floorcoverings and certain other ancillary products in the UK and Continental Europe. The principal activity of the Company is that of a holding company and its subsidiaries are listed on page 133. Further details of the Group's activities and future plans are set out in the Strategic Report on pages 10 to 49.

Headlam Group plc is a company incorporated and domiciled in the UK, company number 00460129. 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 49, which is incorporated in this report by reference. The Strategic Report includes certain disclosures required to be contained in the Directors Report as follows: approach to diversity (page 42), employee engagement (page 42), equal opportunities and employment of disabled people (page 42), an indication of likely future developments (page 14, Chief Executive's Review), and the approach to risk management (page 34 to 35).

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 53 and is incorporated into this report by reference.

Acquisitions

On 2 March 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of Dersimo BV ('Dersimo') located in the western Netherlands. Dersimo is a full service distributor of both soft and hard floors from a combination of well-known manufacturer brands as well as its own carpet and vinyl designs which are manufactured as a private label. The Dersimo acquisition is complementary to the Company's market-leading core business which supplies a high volume of small orders into both the residential and commercial sectors, and increases the Company's presence and geographical coverage in the Netherlands.

On 30 March 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of BETU Holdings Limited (a non-trading holding company), the parent company of CECO (Flooring) Limited ('CECO'). CECO is a leading provider of flooring and wallcovering products to retail and commercial customers throughout Northern Ireland and the Republic of Ireland. The CECO acquisition diversifies and broadens the Company's overall position in the commercial specification market.

On 1 July 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of Ashmount Flooring Supplies Limited ('Ashmount'), a floorcovering distribution business based in Tottenham, North London. The Ashmount acquisition expands the Company's presence in commercial products in Greater London, a geographic area in which the Company has historically had a low market share.

On 28 September 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of Rackhams Limited ('Rackhams') located in Highams Park, East London. Established in 1935, Rackhams is a leading provider of retail and commercial products to customers in Greater London and the surrounding counties with a strong Rackhams 'brand' having been developed in recent years. The Rackhams acquisition expands the Company's presence in Greater London, a geographic area in which the Company has historically had a low market share.

On 26 October 2018, a subsidiary company of Headlam Group plc completed the acquisition of all the trade and assets of Garrod Bros Limited ('Garrod Bros') located in Enfield, North London. Established in 1827, Garrod Bros is a leading provider of commercial flooring products and accessories to customers in Greater London. The Garrod Bros acquisition expands the Company's presence in commercial products in Greater London, a geographic area in which the Company has historically had a low market share.

Both the Rackhams and Garrod Bros acquisitions are currently subject to a merger inquiry by the Competition and Markets Authority ('CMA').

Post-balance sheet events

No post-balance sheet events have taken place since 31 December 2018 and up until the date of this report.

Financial results and ordinary dividends

The results for the year and financial position at 31 December 2018 are shown in the Consolidated Income Statement on page 84 and Statements of Financial Position on page 86.

A 2018 interim dividend of 7.55p per ordinary share (2017: 7.55p) was paid on 2 January 2019 to shareholders on the register at the close of business on 30 November 2018. The Directors propose a final dividend of 17.45p per ordinary share (2017: 17.25p), to be paid on 1 July 2019 to shareholders on the register of members at the close of business on 7 June 2019, the associated ex-dividend date being 6 June 2019.

This would bring the total dividend for the year to 25.0p per ordinary share (2017: 24.8p). The payment of the final dividend is subject to shareholder approval at the AGM in May 2019.

Share capital

As at 31 December 2018, the issued share capital of the Company comprised a single class of ordinary shares of 5p each ('Ordinary Shares').

The Company's Ordinary Shares are listed on the Main Market of the London Stock Exchange. No Ordinary Shares were issued during the year, with the Company's total issued share capital consisting of 85,363,743 Ordinary Shares as at 31 December 2018. During the year, the Company purchased into treasury 562,192 Ordinary Shares, in accordance with the authority granted by shareholders at the Company's Annual General Meeting on 24 May 2018, at an average price of 489.62p per Ordinary Share. The highest price paid was 490.00p per Ordinary Share and the lowest price paid was 485.96p per Ordinary Share. The Ordinary Shares were purchased on the open market to be held in treasury for the purpose of satisfying future share options and share awards under the Company's employee share schemes.

A total of 318,670 Ordinary Shares were transferred from treasury stock during 2018 in connection with the Company's employee share schemes, and the balance of shares in treasury stock following these transfers was 758,089 Ordinary Shares as at 31 December 2018.

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 Association 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 by the next business day 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 24 May 2018, 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 24 May 2018, the Company was given the authority to purchase shares in the Company up to 10% of the issued share capital. Under this authority and as detailed above, the Company purchased into treasury 562,192 Ordinary Shares between that date and the 31 December 2018 for the purpose of satisfying future share options and share awards under the Company's employee share schemes. No further shares have been purchased into treasury since 1 January 2019 and to the date of signing of this report. The Directors will be seeking to renew the authority at the forthcoming AGM. For the avoidance of doubt, the Company does not currently intend to use the authority in relation to share buyback and cancellation of Ordinary Shares. Further explanation and details are set out in the Notice of AGM sent in a separate circular to shareholders and which is also available on the Company's website, www.headlam.com.

Directors

Biographies of Directors currently serving on the Board are set out on pages 50 and 51.

Changes to the Board during the period are set out on page 57. Details of the Directors' service agreements are set out below:

	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 2019
Chris Payne	13 September 2017	n/a	13 September 2017	May 2019
Non-Executive Directors				
Philip Lawrence	1 June 2015	18 June 2015	26 October 2017	May 2019
Andrew Eastgate[1]	17 May 2010	27 April 2010	17 May 2014	n/a
Amanda Aldridge	1 February 2018	12 January 2018	12 January 2018	May 2019
Keith Edelman	1 October 2018	15 August 2018	15 August 2018	May 2019
Alison Littley	1 January 2019	15 August 2018	15 August 2018	May 2019

[1] Stepping down from the Board on 31 May 2019.

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.

As noted elsewhere in this report, with effect from the 2019 AGM, all Directors will be subject to annual election.

Directors' Powers

Subject to the Company's Articles of Association, the Act and any directions given by the Company by special resolution, the business of the Company will be managed by the Board which may exercise all the powers of the Company, whether relating to the management of the business of the Company or otherwise. The matters reserved for the Board are detailed in a specific schedule, which is reviewed annually and is available on the Company's website, www.headlam.com.

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 successful 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.

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), with the information received from the discloser stated to be correct at the time of disclosure.

As at and up to 31 December 2018, the persons set out in the table below have notified the Company, pursuant to DTR 5.1, of their interests in the voting rights in the Company's issued share capital.

Ordinary shares of 5p each

	Aggregate total voting rights[1]	% of total voting rights[2]	Indirect/direct
Franklin Templeton Institutional, LLC	12,192,708	14.45	indirect
Heronbridge Investment Management LLP	4,209,552	5.04	direct
Investec Asset Management Limited	4,248,163	5.02	indirect
Ruffer LLP	4,225,172	below 5%	direct
BlackRock, inc	below 5%	below 5%	indirect
Aggregate of Standard Life Aberdeen plc affiliated management entities	4,189,429	4.95	indirect
Rathbone Brothers plc	4,070,078	4.87	indirect
Canaccord Genuity Group Inc	2,770,314	3.27	indirect

1 Represents the number of voting rights last notified to the Company by the respective shareholder in accordance with DTR 5.1.
2 Based on the Total Voting Rights in the Company as at the notification date.

As at 6 March 2019, the last practical date prior to the printing of this Report, no change in these holdings had been notified and no further notifications of a disclosable interest had been received.

Rights under employees' share schemes

As at 31 December 2018, Kleinwort Hambros, as trustee of the Headlam Group Employee Trust Company Limited ('Trust') held 765,281 shares, approximately 0.9% of the issued share capital of the Company for the purpose of satisfying options and awards under the various employee share schemes operated by the Company. Kleinwort Hambros waives dividends due on all but 0.01p per share of their total holding.

Details of employee share schemes are set out in note 21 to the Financial Statements. Details of long-term incentive schemes for the Directors are shown in the Remuneration Report on pages 64 to 72.

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

During the year, no Director held any 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 Act

The Board fully supports the aims of the Modern Slavery Act, and an annual statement is published on the Company's website detailing the actions undertaken to prevent slavery and human trafficking in both the Company's organisation and supply chain.

Environmental policy and mandatory greenhouse gas emissions reporting

The Company's policy towards environmental issues can be found within the Strategic Report on pages 46 to 48. The Board recognises that a responsible approach to the environment 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 Corporate Responsibility section of the Strategic Report on page 46 to 48.

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 79.

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 (2017: £nil).

Charitable donations
Details are given on page 49 of the Corporate Responsibility section of the Strategic Report.

Amendments to the 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 123 to 129.

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 in the Financial Review on page 26. In addition, note 23 to the financial statements on pages 123 to 129 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 134 have been prepared on the going concern basis.

External auditor
PwC 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 2019 AGM.

AGM
This year's AGM will be held at the Company's distribution hub in Coleshill on Friday, 24 May 2019 at 10.00am. 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:

Karen Atterbury
Company Secretary

6 March 2019

Company registration number: 00460129

STATEMENT OF DIRECTORS' RESPONSIBILITIES
IN RESPECT OF THE FINANCIAL STATEMENTS

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group financial statements in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the European Union and parent company financial statements in accordance with IFRSs as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and parent company and of the profit or loss of the group and parent company for that period. In preparing the financial statements, the directors are required to:

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

The directors are also responsible for safeguarding the assets of the group and parent company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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

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

Directors' confirmations

The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the group and parent company's position and performance, business model and strategy.

Each of the directors, whose names and functions are listed in Annual report and accounts confirm that, to the best of their knowledge:

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

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

- so far as the director is aware, there is no relevant audit information of which the group and parent company's auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the group and parent company's auditors are aware of that information.

For and on behalf of the Board

Steve Wilson	**Chris Payne**
Director	*Director*

6 March 2019

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 company financial statements (the 'financial statements'):

- give a true and fair view of the state of the group's and of the company's affairs as at 31 December 2018 and of the group's profit and the group's and the company's cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the 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 2018 (the 'Annual Report'), which comprise: the Group and Company statements of financial position as at 31 December 2018; 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 company.

We have provided no non-audit services to the group or the company in the period from 1 January 2018 to 31 December 2018.

Our audit approach

Overview

- Overall group materiality: £2.0 million (2017: £2.0 million), based on 5% of profit before tax.
- Overall company materiality: £1.9 million (2017: £1.9 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 five UK reporting components: HFD Limited, MCD Limited, Domus Group of Companies, Headlam (European) Limited and Headlam Group plc (the Company) due to their size and risk characteristics. These UK reporting components comprise 85% of consolidated revenue and 90% of consolidated operating profit.
- In addition, we performed analytical procedures on insignificant trading components for group reporting purposes.

- Supplier arrangements.
- Acquisition accounting.

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.

Capability of the audit in detecting irregularities, including fraud

Based on our understanding of the group and industry, we identified that the principal risks of non-compliance with laws and regulations related to the listing Rules, tax legislation, pensions legislation, employment regulation, and health and safety legislation, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries. Audit procedures performed by the engagement team included:

- Discussions with management, including consideration of known or suspected instances of non-compliance with laws and regulations, and fraud;

- Reading key correspondence with regulatory authorities, such as the Competition and Markets Authority (CMA);
- Review of correspondence with legal advisors;
- Challenging assumptions and judgements made by management in their significant accounting estimates; and
- Review of unusual account combinations with journals to revenue, rebates and cash, as well as unusual journal descriptions.

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. Also, 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.

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 61 and the use of estimates and judgements in the Accounting Policies on page 90. 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 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 rebates 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 Refer to the Audit Committee Report on page 61 and the use of estimates and judgements in the Accounting Policies on page 90 and note 24 to the financial statements on page 130. The Group has made five acquisitions during 2018, for total consideration of £13.0m. In the prior year the Group acquired the share capital of Domus Group of Companies Limited and its subsidiaries ('Domus Group') for consideration of £29.1m. In relation to the acquisitions in 2018, our work focused on the acquisition accounting which is inherently judgemental 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 agreements for the five acquisitions in 2018 to understand the nature of the transactions 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 models, which include forecast attrition rates 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 confirm 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 underlying agreements to conclude that the basis of recognition was reasonable.

Acquisition accounting continued	
The Directors are also required to reconfirm the provisional fair values attributed in the prior year to the Domus Group, and estimate the level of deferred contingent consideration that is likely to be payable under the terms of the acquisition agreement.	The directors reviewed the acquisition accounting for the Domus Group and concluded that no adjustments to the provisional fair values determined in 2017 were necessary. We have considered the results of our current year audit of the Domus Group, including reviewing key estimates and judgements reached as part of the acquisition, and concluded that there is no evidence that material re-measurement is required. We reviewed the directors' calculation of the deferred contingent consideration for the Domus Group and have concluded that the release of £1.4m of the provision that was established in December 2017, during the course of 2018, as a non-underlying credit is reasonable.

We determined that there were no key audit matters applicable to the 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 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 five UK reporting components which, in our view, required an audit of their complete financial information both due to their size and risk characteristics: HFD Limited, MCD Limited, Domus Group of Companies, Headlam (European) Limited and Headlam Group plc (the Company). These reporting companies were audited by the group engagement team. In addition, we performed analytical procedures on insignificant trading components for group reporting purposes.

The work on these five components, 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	Company financial statements
Overall materiality	£2.0 million (2017: £2.0 million).	£1.9 million (2017: £1.9 million).
How we determined it	5% of profit before tax.	0.8% of total assets.
Rationale for benchmark applied	Based on the benchmarks used in the annual report, 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 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 £1,919,000. 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) (2017: £100,000) and £100,000 (Company audit) (2017: £100,000) 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 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 company's ability to continue as a going concern. For example, the terms on which the United Kingdom may withdraw from the European Union, which is currently due to occur on 29 March 2019, are not clear, and it is difficult to evaluate all of the potential implications on the group's trade, customers, suppliers and the wider economy.
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.

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 2018 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 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 62 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 36 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 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 78 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 company's position and performance, business model and strategy is materially inconsistent with our knowledge of the group and company obtained in the course of performing our audit.
- The section of the Annual Report on page 60 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 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 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 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 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 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 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 3 years, covering the years ended 31 December 2016 to 31 December 2018.

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

6 March 2019

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	Underlying 2018 £000	Non-underlying (Note 3) 2018 £000	Total 2018 £000	Underlying 2017 £000	Non-underlying (Note 3) 2017 £000	Restated* Total 2017 £000
Revenue	2	**708,423**	**–**	**708,423**	692,540	–	692,540
Cost of sales		**(479,349)**	**–**	**(479,349)**	(474,436)	–	(474,436)
Gross profit		**229,074**	**–**	**229,074**	218,104	–	218,104
Distribution costs		**(134,316)**	**–**	**(134,316)**	(127,145)	–	(127,145)
Administrative expenses	3	**(50,485)**	**(2,942)**	**(53,427)**	(47,176)	(2,399)	(49,575)
Operating profit	2	**44,273**	**(2,942)**	**41,331**	43,783	(2,399)	41,384
Finance income	6	**709**	**–**	**709**	578	–	578
Finance expenses	6	**(1,593)**	**–**	**(1,593)**	(1,243)	–	(1,243)
Net finance costs		**(884)**	**–**	**(884)**	(665)	–	(665)
Profit before tax	3	**43,389**	**(2,942)**	**40,447**	43,118	(2,399)	40,719
Taxation	7	**(7,750)**	**807**	**(6,943)**	(7,976)	179	(7,797)
Profit for the year attributable to the equity shareholders		**35,639**	**(2,135)**	**33,504**	35,142	(2,220)	32,922
Earnings per share							
Basic	9	**42.5p**		**40.0p**	41.7p		39.1p
Diluted	9	**42.2p**		**39.6p**	41.5p		38.9p
Ordinary dividend per share							
Interim dividend for the financial year	22			**7.55p**			7.55p
Final dividend proposed for the financial year	22			**17.45p**			17.25p

* The results for the year ended 31 December 2017 have been restated to reflect changes made for the year ended 31 December 2018 as reported in note 1.

All Group operations during the financial years were continuing operations.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018 £000	2017 £000
Profit for the year attributable to the equity shareholders		**33,504**	32,922
Other comprehensive income/(expense):			
Items that will never be reclassified to profit or loss			
Remeasurement of defined benefit plans	20	**8,562**	9,127
Related tax		**(1,628)**	(1,729)
		6,934	7,398
Items that are or may be reclassified to profit or loss			
Foreign exchange translation differences arising on translation of overseas operations		**540**	(277)
Effective portion of changes in fair value of cash flow hedges		**–**	(154)
Transfers to profit or loss on cash flow hedges		**–**	(77)
Related tax		**–**	43
		540	(465)
Other comprehensive income for the year		**7,474**	6,933
Total comprehensive income attributable to the equity shareholders for the year		**40,978**	39,855

STATEMENTS OF FINANCIAL POSITION
AT 31 DECEMBER 2018

	Note	Group 2018 £000	Group 2017 £000	Company 2018 £000	Company 2017 £000
Assets					
Non-current assets					
Property, plant and equipment	10	**102,048**	101,631	**476**	2
Investment properties	10	**–**	–	**81,647**	83,143
Intangible assets	11	**50,924**	44,662	**–**	–
Investments in subsidiary undertakings	12	**–**	–	**121,380**	120,640
Deferred tax assets	13	**516**	648	**–**	–
		153,488	146,941	**203,503**	203,785
Current assets					
Inventories	14	**132,704**	131,566	**–**	–
Trade and other receivables	15	**119,007**	127,976	**23,491**	21,320
Cash and cash equivalents	16	**44,005**	42,030	**12,573**	16,646
		295,716	301,572	**36,064**	37,966
Total assets		**449,204**	448,513	**239,567**	241,751
Liabilities					
Current liabilities					
Bank overdraft	16	**(221)**	–	**–**	–
Other interest-bearing loans and borrowings	17	**(236)**	(233)	**–**	–
Trade and other payables	18	**(181,300)**	(190,299)	**(34,226)**	(41,780)
Employee benefits	20	**–**	(2,235)	**–**	(2,235)
Income tax payable	8	**(6,730)**	(6,339)	**(394)**	(1,329)
		(188,487)	(199,106)	**(34,620)**	(45,344)
Non-current liabilities					
Other interest-bearing loans and borrowings	17	**(6,805)**	(6,519)	**–**	–
Trade and other payables	18	**(2,592)**	(4,938)	**(2,007)**	(4,938)
Provisions	19	**(2,249)**	(2,048)	**–**	–
Deferred tax liabilities	13	**(8,063)**	(6,847)	**(5,487)**	(4,438)
Employee benefits	20	**(5,888)**	(10,481)	**(2,561)**	(7,513)
		(25,597)	(30,833)	**(10,055)**	(16,889)
Total liabilities		**(214,084)**	(229,939)	**(44,675)**	(62,233)
Net assets		**235,120**	218,574	**194,892**	179,518
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	**185**	2,891	**13,364**	16,610
Retained earnings		**177,155**	157,903	**123,748**	105,128
Total equity		**235,120**	218,574	**194,892**	179,518

The notes on pages 90 to 133 are an integral part of these consolidated financial statements.

The Company is taking advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement, however the profit for the year attributable to the equity shareholders is £34,350,000.

These financial statements were approved by the Board of Directors on 6 March 2019 and were signed on its behalf by

Steve Wilson
Director

Chris Payne
Director

Company Number: 00460129

STATEMENT OF CHANGES IN EQUITY – GROUP
FOR THE YEAR ENDED 31 DECEMBER 2018

	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 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 (expense)/income	–	–	–	(277)	(231)	–	7,441	6,933
Total comprehensive (expense)/income 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
Balance at 1 January 2018	**4,268**	**53,512**	**88**	**6,859**	**–**	**(4,056)**	**157,903**	**218,574**
Profit for the year attributable to the equity shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**33,504**	**33,504**
Other comprehensive income	**–**	**–**	**–**	**540**	**–**	**–**	**6,934**	**7,474**
Total comprehensive income for the year	**–**	**–**	**–**	**540**	**–**	**–**	**40,438**	**40,978**
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**1,478**	**1,478**
Share options exercised by employees	**–**	**–**	**–**	**–**	**–**	**2,579**	**(1,518)**	**1,061**
Consideration for purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(5,825)**	**–**	**(5,825)**
Current tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**38**	**38**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**(169)**	**(169)**
Deferred tax on income and expenses recognised directly in equity	**–**	**–**	**–**	**–**	**–**	**–**	**(46)**	**(46)**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(20,969)**	**(20,969)**
Total contributions by and distributions to equity shareholders	**–**	**–**	**–**	**–**	**–**	**(3,246)**	**(21,186)**	**(24,432)**
Balance at 31 December 2018	**4,268**	**53,512**	**88**	**7,399**	**–**	**(7,302)**	**177,155**	**235,120**

STATEMENT OF CHANGES IN EQUITY – COMPANY
FOR THE YEAR ENDED 31 DECEMBER 2018

	Share capital £000	Share premium £000	Capital redemption reserve £000	Special reserve £000	Cash flow hedging reserve £000	Treasury reserve £000	Restated* Retained earnings £000	Restated* Total equity £000
Balance at 1 January 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 (expense)/income	–	–	–	–	(231)	–	6,312	6,081
Total comprehensive (expense)/income 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
Balance at 1 January 2018	**4,268**	**53,512**	**88**	**20,578**	**–**	**(4,056)**	**105,128**	**179,518**
Restatement for discounting on inter-company receivable	**–**	**–**	**–**	**–**	**–**	**–**	**(1,601)**	**(1,601)**
Restated balance at 1 January 2018	**4,268**	**53,512**	**88**	**20,578**	**–**	**(4,056)**	**103,527**	**(177,917)**
Profit for the year attributable to the equity shareholders	**–**	**–**	**–**	**–**	**–**	**–**	**34,350**	**34,350**
Other comprehensive income	**–**	**–**	**–**	**–**	**–**	**–**	**6,887**	**6,887**
Total comprehensive income for the year	**–**	**–**	**–**	**–**	**–**	**–**	**41,237**	**41,237**
Transactions with equity shareholders, recorded directly in equity								
Share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**1,478**	**1,478**
Share options exercised by employees	**–**	**–**	**–**	**–**	**–**	**2,579**	**(1,518)**	**1,061**
Consideration for purchase of own shares	**–**	**–**	**–**	**–**	**–**	**(5,825)**	**–**	**(5,825)**
Current tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**29**	**29**
Deferred tax on share options	**–**	**–**	**–**	**–**	**–**	**–**	**(36)**	**(36)**
Dividends to equity holders	**–**	**–**	**–**	**–**	**–**	**–**	**(20,969)**	**(20,969)**
Total contributions by and distributions to equity shareholders	**–**	**–**	**–**	**–**	**–**	**(3,246)**	**(21,016)**	**(24,262)**
Balance at 31 December 2018	**4,268**	**53,512**	**88**	**20,578**	**–**	**(7,302)**	**123,748**	**194,892**

* Retained earnings for the Company were restated when an inter-company loan was discounted in accordance with IFRS 9 see note 1.

CASH FLOW STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018

		Group		Company	
	Note	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Cash flows from operating activities					
Profit before tax for the year		**40,447**	40,719	**33,977**	38,706
Adjustments for:					
Depreciation, amortisation and impairment	3	**7,038**	5,845	**1,688**	1,697
Finance income	6	**(709)**	(578)	**(691)**	(496)
Finance expense	6	**1,593**	1,243	**985**	747
Profit on sale of property, plant and equipment	3	**(50)**	(45)	**–**	–
Share-based payments	21	**1,478**	1,218	**739**	403
Operating cash flows before changes in working capital and other payables		**49,797**	48,402	**36,698**	41,057
Change in inventories		**1,563**	(2,210)	**–**	–
Change in trade and other receivables		**12,524**	7,564	**(2,170)**	(338)
Change in trade and other payables		**(13,878)**	754	**(10,357)**	364
Cash generated from the operations		**50,006**	54,510	**24,171**	41,083
Interest paid		**(1,426)**	(761)	**(765)**	(246)
Tax paid		**(7,789)**	(8,388)	**(590)**	(229)
Additional contributions to defined benefit plan	20	**(747)**	(2,164)	**(747)**	(2,164)
Net cash flow from operating activities		**40,044**	43,197	**22,069**	38,444
Cash flows from investing activities					
Proceeds from sale of property, plant and equipment		**403**	190	**–**	29
Interest received		**601**	576	**258**	288
Acquisition of subsidiaries, net of cash acquired	24	**(9,141)**	(24,763)	**–**	(24,180)
Repayment of acquired borrowings on acquisition		**(435)**	(7,042)	**–**	–
Acquisition of property, plant and equipment	10	**(4,384)**	(3,058)	**(667)**	–
Net cash flow from investing activities		**(12,956)**	(34,097)	**(409)**	(23,863)
Cash flows from financing activities					
Proceeds from the issue of treasury shares		**1,061**	803	**1,061**	803
Payment to acquire own shares		**(5,825)**	(1,180)	**(5,825)**	(1,180)
Drawdown of borrowings		**45,443**	25,000	**45,000**	25,000
Repayment of borrowings		**(45,232)**	(25,230)	**(45,000)**	(25,000)
Dividends paid	22	**(20,969)**	(25,729)	**(20,969)**	(25,729)
Net cash flow from financing activities		**(25,522)**	(26,336)	**(25,733)**	(26,106)
Net increase/(decrease) in cash and cash equivalents		**1,566**	(17,236)	**(4,073)**	(11,525)
Cash and cash equivalents at 1 January		**42,030**	59,339	**16,646**	28,171
Effect of exchange rate fluctuations on cash held		**188**	(73)	**–**	–
Cash and cash equivalents at 31 December	16	**43,784**	42,030	**12,573**	16,646

1 Presentation of the Financial Statements and 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 2019.

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 a 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 financial statements.

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 12 and Chief Executive's Review on pages 14 to 16.

The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Financial Review on pages 26 to 31. 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 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 Sterling committed facilities are £72.5 million and its Euro facilities are €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 financial statements. 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

- *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.

- *Taxation*
  Provision is made for any uncertain tax positions that the Group may be exposed to at the Statement of Financial Position date. Deferred tax assets are recognised at the Statement of Financial Position date based on the assumption that there is a high expectation that the asset will be realised in due course. This assumption is dependent on the Group's ability to generate sufficient future taxable profits.

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

  Provisions to write down stock to its net realisable value are 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.

  Guaranteed Minimum Pension (GMP) equalization
  In-line with the recent Lloyds judgement which has ruled that GMPs must be equalised across males and females, we have added 1.1% to the liabilities as at 31 December 2018. This is an approximate scheme-specific allowance calculated by the schemes actuaries which takes into account high-level summary data of the Scheme. This is detailed further in note 20.

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 made five acquisitions during the year which are detailed in note 24. As part of these acquisitions the Group has performed individual purchase price allocation reviews and has assessed the fair value of the assets and liabilities acquired. Using assumptions regarding the performance of the acquired entities, management have identified additional intangibles relating to brand names, customer relationships, non-compete clauses and order book which have been recognised and either defined as indefinite lived or amortised over their expected useful economic life. The fair value of intangibles at the date of acquisition are calculated by reference to the net present value of future benefits accruing to the Group from the utilisation of the asset, discounted at the appropriate discount rate. 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 and liabilities would alter the goodwill and amortisation charges included within the financial statements.

1 Accounting policies continued

- *Impairment of goodwill*
  The Group determines whether goodwill is impaired on an annual basis unless there is an indication of impairment at an earlier date. This requires an estimation of the value in use of the cash generating units to which they are allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. Further detail on the assumptions used in determining the value in use calculations is provided in note 11

(c) Income Statement Restatement

The Consolidated Income Statement for the year ended 31 December 2017 has been restated to reclassify a number of rebates and prompt payment discounts between revenue, cost of sales, distribution costs and operating expenses in order to more appropriately reflect their nature. Consequently, these adjustments mean the prior year comparatives are now presented in a consistent manner with the current year.

	31 December 2018 £000	31 December 2017 As originally presented £000	Adjustment £000	Restated Year ended 31 December 2017 £000
Revenue	**708,423**	707,764	(15,224)	692,540
Cost of sales	**(479,349)**	(487,683)	13,247	(474,436)
Gross profit	**229,074**	220,081	(1,977)	218,104
Distribution costs	**(134,316)**	(130,476)	3,331	(127,145)
Administrative expenses	**(53,427)**	(48,221)	(1,354)	(49,575)
Operating profit	**41,331**	41,384	–	41,384

d) Impact of newly adopted accounting standards

The Group and Company has adopted two new accounting standards in 2018 and these are detailed below:

IFRS 9 – Financial Instruments

IFRS 9 replaces the provisions of IAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting. The adoption of IFRS 9 Financial Instruments from 1 January 2018 resulted in changes in accounting policies but did not have a significant impact on the financial statements. The new accounting policies are set out in note 1 below. In accordance with the transitional provisions in IFRS 9(7.2.15) and (7.2.26), comparative figures have not been restated.

There was no material impact on the group's retained earnings as at 1 January 2018 arising from the transition but the Company's retained earnings were affected as follows:

In accordance with IFRS 9 the value of inter-company receivables were reviewed as at 31 December 2018. Headlam Group plc has an inter-company balance with Headlam (European) Limited, which is supported by Headlam (European) Limited's investment in the Group's French entities. The inter-company loan is due on demand and it has been valued by reference to the net present value of the future cash flows accruing to Headlam (European) Limited from its investment in the French entities and discounted at an appropriate discount rate.

	Restated 1 January 2018 £000
Retained earnings	105,128
Restatement due to discounting	(1,601)
Restated retained earnings	103,527

IFRS 15 – Revenue from Contracts with Customers

The Group has adopted IFRS 15 'Revenue from Contracts with Customers' at 1 January 2018.
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 impacts of the new standard has been undertaken including a review of the Group's performance obligations, treatment of variable consideration and the timing of revenue recognition. This assessment has shown there are no material impacts on revenue for the Group.

(e) IFRS not yet applied

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2018 reporting periods and have not been early adopted by the group. The group's assessment of the impact of these new standards and interpretations is set out below.

International Financial Reporting Standard (IFRS) 16 'Leases' (replacing IAS 17).

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 the year ending 31 December 2019. Adoption of the new standard will have a material impact on the Group. Adoption of the new standard has also been assessed for the Company and the new standard is expected to have an immaterial impact on the Company.

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 on balance sheet, 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 finance expense.

The lease liability has been measured at the present value of the remaining lease payments, discounted using the incremental borrowing rate at transition. The right-of-use asset is measured at its carrying amount as if the standard had been applied since the commencement of the lease, discounted using the incremental borrowing rate at transition. Where data is not available to enable this measurement to be made, the right-of-use asset is measured at an amount equal to the lease liability. Transition recognition exemptions relating to short-term and low value leases have been applied as well as practical expedients taken, where available, to simplify the transition process.

The Group has collated information on leases held at the 31 December 2018 for an evaluation of the impact of IFRS 16. It is estimated that on transition the lease liability and the right-of-use asset brought on balance sheet will be valued at approximately £48.5 million. Net current assets will be £13.2 million lower, due to the presentation of a portion of the liability as a current liability.

The group expects that the impact on the income statement for 2019 will be a reduction in the net profit before tax by approximately £0.5 million as a result of adopting the new rules with the operating lease expense recognised under the existing standard (IAS 17) (Full year total operating lease cost 2018:£15.3 million) being replaced by depreciation and finance costs. There will be no overall impact on the Group's cash and cash equivalents.

The group will apply the standard from its mandatory adoption date of 1 January 2019 using the modified retrospective approach. Under this approach, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings on 1 January 2019, with no restatement of comparative information. All right-of-use assets will be measured at the amount of the lease liability on adoption (adjusted for any prepaid or accrued lease expenses).

There are no other new standards, amendments to existing standards, or interpretations that are not yet effective that would be expected to have a material impact on the Group.

f) Accounting Policies

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.

1 Accounting policies continued

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 initially recognised at fair value on the date that a derivative contract is entered into, and they are subsequently remeasured to their fair value at the end of each reporting period. The accounting for subsequent changes in fair value depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. The group designates certain derivatives as either:

- hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedges);
- hedges of a particular risk associated with the cash flows of recognised assets and liabilities and highly probable forecast transactions (cash flow hedges); or
- hedges of a net investment in a foreign operation (net investment hedges).

At inception of the hedge relationship, the group documents the economic relationship between hedging instruments and hedged items, including whether changes in the cash flows of the hedging instruments are expected to offset changes in the cash flows of hedged items. The group documents its risk management objective and strategy for undertaking its hedge transactions.

The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months; it is classified as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Trading derivatives are classified as a current asset or liability.

The Group enters into forward exchange contracts and the fair value 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.

Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in the cash flow hedge reserve within equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss, within other gains/(losses).

Where option contracts are used to hedge forecast transactions, the group designates only the intrinsic value of the options as the hedging instrument. Until 31 December 2017, the group classified foreign currency options as held-for-trading derivatives and accounted for them at fair value through the profit and loss (FVPL).

Gains or losses relating to the effective portion of the change in intrinsic value of the options are recognised in the cash flow hedge reserve within equity. The changes in the time value of the options that relate to the hedged item ('aligned time value') are recognised within other comprehensive income (OCI) in the costs of hedging reserve within equity.

When forward contracts are used to hedge forecast transactions, the group generally designates only the change in fair value of the forward contract related to the spot component as the hedging instrument. Gains or losses relating to the effective portion of the change in the spot component of the forward contracts are recognised in the cash flow hedge reserve within equity. The change in the forward element of the contract that relates to the hedged item ('aligned forward element') is recognised within OCI in the costs of hedging reserve within equity. In some cases, a Group company might designate the full change in fair value of the forward contract (including forward points) as the hedging instrument. In such cases, the gains or losses relating to the effective portion of the change in fair value of the entire forward contract are recognised in the cash flow hedge reserve within equity.

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.

Further information about the derivatives used by the Group is provided in note 23 below.

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.

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. Assets begin to be depreciated from the date they become available for use. 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 arises when a company acquires another business and 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.

1 Accounting policies continued

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

In respect of acquisitions prior to 1 January 2004, goodwill is included on the basis of its deemed cost, which represents the amount recorded under UK GAAP which was broadly comparable save that only separable intangibles were recognised and goodwill was amortised. This is in accordance with IFRS 1.

Other intangibles

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

Amortisation

Amortisation is charged to the income statement 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	1 – 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.

Financial assets

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the group has transferred substantially all the risks and rewards of ownership.

At initial recognition, the group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss. Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

There are three measurement categories under IFRS 9 into which debt instruments may be classified, these are;
- Amortised cost;
- Fair value through other comprehensive income (FVOCI);
- Fair value through the profit and loss (FVPL)

All material financial assets of the Group are held at amortised cost. Financial assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as separate line item in the statement of profit or loss.

Trade and other receivables

Trade receivables are recognised at the transaction price (as defined in IFRS 15) if the trade receivables do not contain a significant financing component. Other receivables are measured at fair value on initial recognition.

Following the adoption of IFRS 9, from 1 January 2018, the Group assesses, on a forward-looking basis, the expected credit losses associated with its trade and other receivables carried at amortised cost and fair valued through other comprehensive income (FVOCI). The impairment methodology applied depends on whether there has been a significant increase in credit risk. For trade receivables, the Group applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognised from initial recognition of the receivables. See note 23.

Where specific receivables are known to be 'bad' or it becomes apparent that payment is 'doubtful' then a credit loss allowance of 100% is applied.

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. This includes management's best estimate of overheads to be absorbed in the cost of inventory and discounts to be received from suppliers. 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 financial assets, 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. Financial assets are assessed using an expected credit loss model.

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 in the income statement whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

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.

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.

1 Accounting policies continued

Provisions

Provisions are recognised in accordance with IAS 37 'Provisions, Contingent Assets and Contingent Liabilities'. Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are made for property dilapidations for the estimated costs of the repairs over the period of the tenancy where a legal obligation exists.

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.

Guaranteed Minimum Pensions (GMPs) must be equalised across males and females, and as a result of clarity in legislation the Company have added 1.1% to the liabilities as at 31 December 2018. This is an approximate scheme-specific allowance calculated by the scheme actuaries, which takes into account high-level summary data of the Scheme. The Company has allowed for the additional liability in respect of GMP equalisation as a past service cost, which has gone through 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.

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 64 to 72.

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. The primary performance obligation is the transfer of goods to the customer. Revenue from the sale of floorcoverings is recognised when control of the goods is transferred to the customer (which is typically the point at which goods are received by the customer), at an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods. Provision for returns, discounts and other allowances are reflected in revenue at the point of recognition.

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. Rebates received for the financial year are deducted from cost of sales. Rebates recoverable at the end of the financial year are accrued within other debtors.

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.

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.

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.

1 Accounting policies continued

Taxation

Income tax comprises current and deferred tax. Tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the Statement of Financial Position date, and any adjustment to tax payable in respect of previous years.

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

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

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

Non-underlying items

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

2 Segment reporting

As at 31 December 2018, the Group had 63 operating segments in the UK and four 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	
	2018 £000	Restated* 2017 £000	**2018 £000**	Restated* 2017 £000	**2018 £000**	Restated* 2017 £000
Revenue						
External revenues	**604,150**	593,476	**104,273**	99,064	**708,423**	692,540
Reportable segment underlying operating profit	**45,163**	44,765	**488**	1,271	**45,651**	46,036
Reportable segment assets	**304,645**	297,325	**42,591**	44,515	**347,236**	341,840
Reportable segment liabilities	**(168,184)**	(179,016)	**(25,219)**	(25,021)	**(193,403)**	(204,037)

* The results for the year ended 31 December 2017 have been restated to reflect changes made for the year ended 31 December 2018 reported in note 1.

During the year there were no inter-segment revenues for the reportable segments (2017: £nil).

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

	2018 £000	2017 £000
Profit for the year		
Total profit for reportable segments	**45,651**	46,036
Non-underlying items	**(2,942)**	(2,399)
Unallocated expense	**(1,378)**	(2,253)
Operating profit	**41,331**	41,384
Finance income	**709**	578
Finance expense	**(1,593)**	(1,243)
Profit before taxation	**40,447**	40,719
Taxation	**(6,943)**	(7,797)
Profit for the year	**33,504**	32,922

	2018 £000	2017 £000
Assets		
Total assets for reportable segments	**347,236**	341,840
Unallocated assets:		
Properties, plant and equipment	**88,879**	89,379
Deferred tax assets	**516**	648
Cash and cash equivalents	**12,573**	16,646
Total assets	**449,204**	448,513
Liabilities		
Total liabilities for reportable segments	**(193,403)**	(204,037)
Unallocated liabilities:		
Employee benefits	**(5,888)**	(12,716)
Income tax payable	**(6,730)**	(6,339)
Deferred tax liabilities	**(8,063)**	(6,847)
Total liabilities	**(214,084)**	(229,939)

	UK £000	Continental Europe £000	Reportable segment total £000	Unallocated £000	Consolidated total £000
Other material items 2018					
Capital expenditure	**2,579**	**1,139**	**3,718**	**666**	**4,384**
Depreciation	**2,058**	**751**	**2,809**	**2,466**	**5,275**
Non-underlying items	**1,262**	**466**	**1,728**	**1,214**	**2,942**
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

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:

2 Segment reporting continued

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

	UK		Continental Europe		Total	
	2018 £000	Restated* 2017 £000	**2018 £000**	Restated* 2017 £000	**2018 £000**	Restated* 2017 £000
Revenue						
Residential	**400,710**	417,799	**57,046**	52,074	**457,756**	469,873
Commercial	**203,440**	175,677	**47,227**	46,990	**250,667**	222,667
	604,150	593,476	**104,273**	99,064	**708,423**	692,540

* The results for the year ended 31 December 2017 have been restated to reflect changes made for the year ended 31 December 2018 reported in note 1.

3 Profit before tax

The following are included in profit before tax:

	2018 £000	2017 £000
Depreciation on property, plant and equipment	**5,275**	4,914
Amortisation of intangible assets	**1,763**	931
Profit on sale of property, plant and equipment	**(50)**	(45)
Operating lease rentals		
Plant and machinery	**11,923**	11,014
Land and buildings	**3,566**	2,197

Non-underlying items of £2,942,000 relate to non-recurring costs relating to personnel changes, GMP equalisation, a release of contingent consideration, intangibles amortisation relating to businesses acquired acquisitions fees, and the related tax of £807,000 on these costs, see table below.

	2018 £000	2017 £000
Non-recurring people costs	**836**	677
GMP equalisation	**1,214**	–
Release of contingent consideration	**(1,384)**	–
Amortisation of acquired intangibles	**1,763**	931
Acquisitions related fees	**513**	791
	2,942	2,399

Auditor's remuneration:

	2018 £000	2017 £000
Audit of these financial statements	**111**	87
Amounts received by the Auditor and their associates in respect of:		
Audit of financial statements of subsidiaries of the Company	**276**	175
Corporate finance services	**–**	91
	387	353

4 Staff numbers and costs

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

	Number of employees			
	Group		Company	
	2018	2017	**2018**	2017
By sector:				
Floorcoverings	**2,593**	2,430	**–**	–
Central operations	**22**	19	**22**	19
	2,615	2,449	**22**	19
By function:				
Sales and distribution	**2,401**	2,276	**–**	–
Administration	**214**	173	**22**	19
	2,615	2,449	**22**	19

The aggregate payroll costs were as follows:

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Wages and salaries	**84,147**	80,961	**2,801**	3,383
Equity settled share-based payment expense (note 21)	**1,478**	1,218	**739**	403
Social security costs	**10,775**	10,402	**445**	538
Pension costs (note 20)	**6,839**	5,126	**1,967**	883
	103,239	97,707	**5,952**	5,207

5 Emoluments of key management personnel

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

	2018 £000	2017 £000
Short-term employee benefits	**1,652**	2,474
Equity settled share-based payment expense	**638**	507
	2,290	2,981

Short-term employee benefits comprise salary and benefits earned during the year and bonuses awarded for the year. Further details on Directors' remuneration, share options and long-term incentive schemes are disclosed in the Remuneration Report on pages 64 to 72.

6 Finance income and expense

	2018 £000	2017 £000
Interest income:		
Bank interest	**709**	540
Other	**–**	38
Finance income	**709**	578
Interest expense:		
Bank loans, overdrafts and other financial expenses	**(1,331)**	(770)
Net interest on defined benefit plan obligations (note 20)	**(232)**	(473)
Other	**(30)**	-
Finance expenses	**(1,593)**	(1,243)

7 Taxation

Recognised in the income statement

	2018 £000	2017 £000
Current tax expense:		
Current year	**8,775**	8,548
Adjustments for prior years	**(810)**	(567)
	7,965	7,981
Deferred tax expense:		
Origination and reversal of temporary differences	**(938)**	(39)
Effect of change in tax rates	**–**	(27)
Adjustments for prior years	**(84)**	(118)
	(1,022)	(184)
Total tax in income statement	**6,943**	7,797

	2018 £000	2017 £000
Tax relating to items (charged)/credited to equity		
Current tax on:		
Income and expenses recognised directly in equity	**(38)**	(150)
Deferred tax on:		
Share options	**169**	(138)
Income and expenses recognised directly in equity	**46**	(18)
Deferred tax on other comprehensive income:		
Defined benefit plans	**1,628**	1,729
Cash flow hedge	**–**	(43)
Total tax reported directly in reserves	**1,805**	1,380

Factors that may affect future current and total tax charges

The UK headline corporation tax rate for the period was 19% (2017: 19.25%). The UK tax rate will be further reduced to 17% with effect from 1 April 2020 which was enacted during 2016. The majority of the deferred tax balance in respect of UK entities has therefore been calculated at 17% (2017: 17%) on the basis that most of the balances will materially reverse after 1 April 2020.

In addition, a 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

	2018		2017	
	%	£000	%	£000
Profit before tax		**40,447**		40,719
Tax using the UK corporation tax rate	**19.0**	**7,685**	19.3	7,836
Effect of change in UK tax rate	**0.0**	**20**	(0.1)	(30)
Effect of change in overseas tax rate	**(0.9)**	**(382)**	(0.1)	(27)
Non-deductible expenses	**1.3**	**516**	1.6	646
Effect of tax rates in foreign jurisdictions	**0.0**	**(2)**	0.1	57
Adjustments in respect of prior years	**(2.2)**	**(894)**	(1.7)	(685)
Total tax in income statement	**17.2**	**6,943**	19.1	7,797
Add back tax on non-underlying items		**807**		179
Total tax charge excluding non-underlying items		**7,750**		7,976
Profit before non-underlying items		**43,389**		43,118
Adjusted expected tax rate excluding non-underlying items		**17.86%**		18.50%

8 Current tax liabilities

The Group's current tax liability of £6,730,000 (2017: £6,339,000) 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 £394,000 (2017: £1,329,000) represents the amount of income tax payable in respect of current and prior year periods which exceed any amounts recoverable.

At 31 December 2018, the Group held a current provision of £1,726,859 (2017: £2,342,715) in respect of uncertain tax provisions. Liabilities relating to these open and judgmental matters are based on an assessment as to whether additional taxes will be due, after taking into account external advice where appropriate. The Group expects this uncertain tax provision to decrease in the next 12 months.

9 Earnings per share

	2018 £000	2017 £000
Earnings		
Earnings for underlying basic and underlying diluted earnings per share	**35,639**	35,142
Earnings for basic and diluted earnings per share	**33,504**	32,922

	2018	2017
Number of shares		
Issued ordinary shares at 31 December	**85,363,743**	85,363,743
Effect of weighted average of shares held in treasury	**(1,501,085)**	(1,183,451)
Weighted average number of ordinary shares for the purposes of basic earnings per share	**83,862,658**	84,180,292
Effect of diluted potential ordinary shares:		
Weighted average number of ordinary shares at 31 December	**83,862,658**	84,180,292
Dilutive effect of share options	**674,621**	549,488
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**84,537,279**	84,729,780
Earnings per share		
Basic	**40.0p**	39.1p
Diluted	**39.6p**	38.9p

At 31 December 2018, the Company held 1,523,370 shares (2017: 856,458) in relation to treasury stock and shares held in trust for satisfying options and awards under employee share schemes. These shares have been disclosed in the treasury reserve and 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 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
Balance at 1 January 2018	**119,867**	**37,138**	**89**	**157,094**
Acquisitions	**1,021**	**300**	**–**	**1,321**
Additions	**396**	**3,514**	**474**	**4,384**
Disposals	**(272)**	**(931)**	**–**	**(1,203)**
Reclassification	**–**	**90**	**(90)**	**–**
Effect of movements in foreign exchange	**447**	**221**	**1**	**669**
Balance at 31 December 2018	**121,459**	**40,332**	**474**	**162,265**
Depreciation and impairment				
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
Balance at 1 January 2018	**27,753**	**27,710**	**–**	**55,463**
Depreciation charge for the year	**2,466**	**2,809**	**–**	**5,275**
Disposals	**–**	**(850)**	**–**	**(850)**
Effect of movements in foreign exchange	**199**	**130**	**–**	**329**
Balance at 31 December 2018	**30,418**	**29,799**	**–**	**60,217**
Net book value				
At 1 January 2017	93,157	9,777	–	102,934
At 31 December 2017 and 1 January 2018	92,114	9,428	89	101,631
At 31 December 2018	**91,041**	**10,533**	**474**	**102,048**

At 31 December 2018, the cost less accumulated depreciation of long leasehold property held by the Group was £7,250,000 (2017: £7,430,000).

Company investment properties and plant and equipment

	Investment properties £000	Plant and equipment £000	Under construction £000	Total £000
Cost				
Balance at 1 January 2017	103,396	72	–	72
Disposals	–	(62)	–	(62)
Balance at 31 December 2017	103,396	10	–	10
Balance at 1 January 2018	**103,396**	**10**	**–**	**10**
Additions	**190**	**2**	**474**	**476**
Disposals	**–**	**(3)**	**–**	**(3)**
Balance at 31 December 2018	**103,586**	**9**	**474**	**483**
Depreciation				
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
Balance at 1 January 2018	**20,253**	**8**	**–**	**8**
Depreciation charge for the year	**1,686**	**2**	**–**	**2**
Disposals	**–**	**(3)**	**–**	**(3)**
Balance at 31 December 2018	**21,939**	**7**	**–**	**7**
Net book value				
At 1 January 2017	84,835	36	–	36
At 31 December 2017 and 1 January 2018	83,143	2	–	2
At 31 December 2018	**81,647**	**2**	**474**	**476**

At 31 December 2018, the cost less accumulated depreciation of long leasehold property held by the Company was £7,250,000 (2017: £7,430,000).

Investment properties were last valued by an independent professional valuer on 17 January 2017. The valuation of the investment properties at that date was £85.3 million. The Company will obtain an updated valuation for the year ended 31 December 2019.

11 Intangible assets – group

	Goodwill £000	Order book £000	Customer relationships £000	Brand names £000	Non-compete £000	Total £000
Cost						
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
Balance at 1 January 2018	**36,981**	**6,202**	**5,443**	**4,996**	**–**	**53,622**
Addition (note 24)	**4,427**	**272**	**1,345**	**1,950**	**31**	**8,025**
Balance at 31 December 2018	**41,408**	**6,474**	**6,788**	**6,946**	**31**	**61,647**
Amortisation						
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
Balance at 1 January 2018	**3,197**	**5,690**	**45**	**28**	**–**	**8,960**
Charge for the year	**–**	**650**	**659**	**450**	**4**	**1,763**
Balance at 31 December 2018	**3,197**	**6,340**	**704**	**478**	**4**	**10,723**
Net book value						
At 31 December 2017 and 1 January 2018	33,784	512	5,398	4,968		44,662
At 31 December 2018	**38,211**	**134**	**6,084**	**6,468**	**27**	**50,924**

Cumulative impairment losses recognised in relation to goodwill is £3,197,000 (2017: £3,197,000).

Impairment tests for cash-generating units containing goodwill ('CGU')
Goodwill is attributed to the businesses identified below for the purpose of testing impairment. These businesses are the lowest level at which goodwill is monitored and represent operating segments.

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

	Reported segment	2018 £000	2017 £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 of Companies Limited	**UK**	**22,955**	22,955
Mitchell Carpets Limited	**UK**	**345**	345
McMillan Flooring	**UK**	**96**	96
CECO (Flooring) Limited	**UK**	**2,240**	–
Dersimo BV	**Continental Europe**	**1,313**	–
Ashmount Flooring Supplies Limited	**UK**	**437**	–
Rackhams Limited	**UK**	**410**	–
Other	**UK**	**1,366**	1,329
		38,221	33,784

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 (2017: 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 2017, and applying the following key assumptions.

Key assumptions
Cash flows were projected based on actual operating results, the approved 2019 business plan and management's assessment of planned performance in the period to 2023. For the purpose of impairment testing the cash flows were assumed to grow into perpetuity at a rate of 2.0% beyond 2023.

The main assumptions within the operating cash flows used for 2019 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 10.7% (2017: 10.4%) has been used for impairment testing adjusted to 11.6% (2017: 11.3%) 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 risk of material impairment.

12 Investments in subsidiaries
Summary information on investments in subsidiary undertakings is as follows:

	£000
Cost	
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
Balance at 1 January 2018	**120,640**
Share options granted to employees of subsidiary undertakings	**740**
Balance at 31 December 2018	**121,380**
Carrying value	
At 1 January 2017	90,707
At 31 December 2017	120,640
At 31 December 2018	**121,380**

A full list of the Group's subsidiaries are listed on page 133. There were no impairments recognised on the Company's investments in subsidiaries in the year ended 31 December 2018.

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	
	2018 £000	2017 £000	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Property, plant and equipment	**–**	–	**(6,146)**	(7,552)	**(6,146)**	(7,552)
Intangible assets	**–**	–	**(2,399)**	(2,097)	**(2,399)**	(2,097)
Employee benefits	**1,315**	2,892	**–**	–	**1,315**	2,892
Other items	**–**	558	**(317)**	–	**(317)**	558
Tax assets/(liabilities)	**1,315**	3,450	**(8,862)**	(9,649)	**(7,547)**	(6,199)
Set-off of tax	**(799)**	(2,802)	**799**	2,802	**–**	–
	516	648	**(8,063)**	(6,847)	**(7,547)**	(6,199)

Movement in deferred tax during the year

	1 January 2018 £000	**Brought in on acquisition £000**	**Recognised in income £000**	**Recognised in equity £000**	**31 December 2018 £000**
Property, plant and equipment	**(7,552)**	**–**	**1,406**	**–**	**(6,146)**
Intangible assets	**(2,097)**	**(614)**	**315**	**(3)**	**(2,399)**
Employee benefits	**2,892**	**–**	**220**	**(1,797)**	**1,315**
Other items	**558**	**87**	**(919)**	**(43)**	**(317)**
	(6,199)	**(527)**	**1,022**	**(1,843)**	**(7,547)**

Movement in deferred tax during the prior year

	1 January 2017 £000	Brought in on acquisition £000	Recognised 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)

Company

Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2018 £000	2017 £000	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Property, plant and equipment	**–**	–	**(6,172)**	(6,287)	**(6,172)**	(6,287)
Employee benefits	**647**	1,795	**–**	–	**647**	1,795
Other items	**38**	54	**–**	–	**38**	54
Tax assets/(liabilities)	**685**	1,849	**(6,172)**	(6,287)	**(5,487)**	(4,438)
Set-off of tax	**(685)**	(1,849)	**685**	1,849	**–**	–
	–	–	**(5,487)**	(4,438)	**(5,487)**	(4,438)

Movement in deferred tax during the year

	1 January 2018 £000	Recognised in income £000	Recognised in equity £000	31 December 2018 £000
Property, plant and equipment	**(6,287)**	**115**	**–**	**(6,172)**
Employee benefits	**1,795**	**299**	**(1,447)**	**647**
Other items	**54**	**(16)**	**–**	**38**
	(4,438)	**398**	**(1,447)**	**(5,487)**

Movement in deferred tax during the prior 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)

Unrecognised deferred tax assets and liabilities – Group and Company

At the Statement of Financial Position date, the Group and Company has unused capital losses of £11,197,000 (2017: £10,797,000) available for offset against future chargeable gains. In addition to these there are Dutch tax losses of £1,273,000 (2017: £705,000) and French tax losses of £1,376,000 (2017 £1,125,000). The Directors have considered the probability that the deferred tax assets would be recoverable and concluded that no deferred tax assets should be recognised in respect of these amounts at this time.

14 Inventories

	Group		Company	
Goods for resale	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Balance as at 31 December	**132,704**	131,566	**–**	–

Cost of sales consists of the following:

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Material cost	**475,701**	472,208	**–**	–
Processing cost	**3,648**	2,228	**–**	–
	479,349	474,436	**–**	–

The cost of inventories within cost of sales stated above includes movements in the provision for obsolete inventory of £211,000 release (2017: £727,000 release).

15 Trade and other receivables

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Trade receivables	**89,100**	94,652	**–**	–
Prepayments and accrued income	**4,924**	5,105	**274**	392
Other receivables	**24,983**	28,211	**213**	468
Derivative assets used for economic hedging:				
Other derivatives at fair value	**–**	8	**–**	–
Amounts due from subsidiary undertakings	**–**	–	**23,004**	20,460
	119,007	127,976	**23,491**	21,320

Other receivables include balances totaling £145,000 that fall due after more than 1 year (2017: £120,000).

£1,281,000 (2017: £1,198,000) 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:

	2018 £000	2017 £000
UK	**1,009**	995
Continental Europe	**272**	203
	1,281	1,198

16 Cash and cash equivalents

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Cash	**44,005**	42,030	**12,573**	16,646
Bank overdrafts	**(221)**	–	**–**	–
Cash and cash equivalents per Statement of Financial Position	**43,784**	42,030	**12,573**	16,646

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, increased 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 latest 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 2018 were £112,779,000 (2017: £112,464,000).

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

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Current liabilities				
Bank overdraft	**221**	–	**–**	–
Interest-bearing loan	**236**	233	**–**	–
	457	233	**–**	–
Non-current liabilities				
Interest-bearing loans	**6,805**	6,519	**–**	–
	6,805	6,519	**–**	–

The Group has undrawn borrowing facilities at 31 December 2018, which amounted to £105,517,000 (2017: £105,712,000). 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 2018 and there were no breaches.

The undrawn borrowing facilities are as follows:

	Interest rate %	**2018 £000**	Interest rate %	2017 £000
UK	**1.80**	**97,500**	1.57	97,500
Netherlands	**1.98**	**1,563**	2.03	1,313
France	**1.30**	**2,472**	1.30	3,107
Switzerland	**1.50**	**3,983**	1.65	3,792
		105,518		105,712

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 2018 £000	**Cash flows £000**	**Acquisitions £000**	**Foreign exchange movements £000**	**At 31 December 2018 £000**
Cash at bank and in hand	42,030	**(831)**	**2,615**	**191**	**44,005**
Bank overdraft	–	**(218)**	**–**	**(3)**	**(221)**
	42,030	**(1,049)**	**2,615**	**188**	**43,784**
Debt due within one year	(233)	**–**	**–**	**(3)**	**(236)**
Debt due after one year	(6,519)	**(211)**	**–**	**(75)**	**(6,805)**
	35,278	**(1,260)**	**2,615**	**110**	**36,743**

18 Trade and other payables

	Group		Company	
Current	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Trade payables	**142,382**	149,594	**788**	1,343
Taxation and social security	**17,069**	17,954	**2,114**	2,112
Non-trade payables and accrued expenses	**21,826**	22,751	**4,424**	3,519
Amounts due to subsidiary undertakings	**–**	–	**26,900**	34,806
Derivative liabilities used for economic hedging:				
Other derivatives at fair value	**23**	–	**–**	–
	181,300	190,299	**34,226**	41,780

Included within current non-trade payables and accrued expenses is an amount of £nil for accrued interest on unsecured bank loans (2017: £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	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Non-trade payables and accrued expenses	**2,592**	4,938	**2,007**	4,938
	2,592	4,938	**2,007**	4,938

Non-current non-trade payables and accrued expenses for the Group in 2018 relate to discounted deferred consideration for Domus Group of Companies Limited and Betu Holdings Limited, the holding company of CECO (Flooring) Limited, see note 24 (2017: Domus Group of Companies Limited). The Company has discounted deferred consideration for Domus Group of Companies Limited in both 2018 and 2017.

19 Provisions

	Property 2018 £000	Property 2017 £000
Balance at 1 January	**2,048**	1,531
Acquired on acquisition	**224**	195
Charged/(credited) to the income statement:		
Additional provisions	**–**	322
Utilisation of provisions	**(23)**	–
Balance at 31 December	**2,249**	2,048

The property provisions relate to property dilapidations.

20 Employee benefits

During the year, the Group operated UK and Swiss defined benefit plans and defined contribution plans in the UK, France and the Netherlands.

UK defined benefit plan

The Headlam Group plc Staff Retirement Benefits Scheme is the principal defined benefit plan which provides pensions in retirement and death benefits to members. The majority of members are entitled to receive pensions from age 65, equal to either 1/50 or 1/60 of final salary for each year of service that the employee provided, depending on which section of the plan the member is part of.

The plan is a registered scheme under UK legislation. The plan is legally separated from the Company and assets are held independently of the Company's finances.

The plan is subject to the scheme funding requirements outlined in UK legislation.

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.

There have been no amendments, curtailments or settlements made to the plan during 2018.

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 2017 and revealed a funding deficit of £2,388,000.

The main annual rate assumptions at 31 March 2017 used by the actuary for the 2017 valuation 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%.

Under the schedule of contributions dated 10 May 2018, Company contributions were fixed at 51.6% of pensionable salaries each month. The Company is expected to pay contributions of £1,170,000 over the next accounting period for the accrual of benefits.

In accordance with the recovery plan dated 26 March 2015, payments were made to the plan during 2018 of £747,000 towards the deficit.

Under the recovery plan dated 10 May 2018 the Company is not due to pay any contributions over the next year.

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 19 years.

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 is affiliated to the Collective Foundation 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 collective foundation is reinsured for risk benefits with Swiss Life insurance company.

There have been no amendments, curtailments or settlements made to the plan during 2018.

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 scheme funding valuation of the plan was as at 31 December 2018 and revealed that the plan was overfunded. This overfunding is appropriate to Swiss legislation and cannot be considered in the context of IAS 19R. 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 2018 revealed a funding deficit of £2,965,000 (2017: £2,591,000). The Group is expected to pay £338,000 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 19.55 years.

Defined benefit obligation

In the UK there is no contractual agreement or stated Group policy for allocating the net defined benefit liability between the participating subsidiaries and as such the full deficit is recognised by the Company, which is the sponsoring employer. The participating subsidiary companies have recognised a cost equal to contributions payable for the period as advised by a professionally qualified actuary. The Company recognises a cost equal to its contributions payable for the period net of amounts recharged in relation to the Group deficit to the participating subsidiary companies.

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Present value of funded defined benefit obligations	**(125,101)**	(139,048)	**(111,592)**	(126,308)
Fair value of plan assets	**119,576**	126,709	**109,031**	116,560
Net obligations	**(5,525)**	(12,339)	**(2,561)**	(9,748)
Other long-term employee benefits	**(363)**	(377)	**–**	–
Total employee benefits	**(5,888)**	(12,716)	**(2,561)**	(9,748)
Analysed as:				
Current liabilities	**–**	(2,235)	**–**	(2,235)
Non-current liabilities	**(5,888)**	(10,481)	**(2,561)**	(7,513)
Total employee benefits	**(5,888)**	(12,716)	**(2,561)**	(9,748)

20 Employee benefits continued

Movements in present value of defined benefit obligation

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
At 1 January	**139,048**	141,947	**126,308**	128,002
Current service cost	**2,254**	2,488	**1,462**	1,628
Past service costs	**1,214**	(511)	**1,214**	–
Interest cost	**3,063**	3,479	**2,966**	3,410
Net remeasurement losses/(gains) – financial	**(14,874)**	6,827	**(14,464)**	7,527
Net remeasurement (gains)/losses – demographic	**(1,005)**	(4,598)	**(1,006)**	(4,598)
Net remeasurement (gains)/losses – experience	**281**	(6,552)	**553**	(6,221)
Benefits paid	**(5,914)**	(3,740)	**(5,577)**	(3,592)
Contributions by members	**370**	384	**136**	152
Effect of movements in foreign exchange	**664**	(676)	**–**	–
At 31 December	**125,101**	139,048	**111,592**	126,308

Movements in fair value of plan assets

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
At 1 January	**126,709**	119,339	**116,560**	109,719
Interest income on plan assets	**2,831**	3,006	**2,753**	2,957
Return on assets, excluding interest income	**(7,036)**	4,804	**(6,619)**	4,265
Contributions by employer:				
Future service contributions	**1,351**	1,222	**1,031**	895
Past service deficit contributions	**747**	2,164	**747**	2,164
Contributions by members	**370**	384	**136**	152
Benefits paid	**(5,914)**	(3,740)	**(5,577)**	(3,592)
Effect of movements in foreign exchange	**518**	(470)	**–**	–
At 31 December	**119,576**	126,709	**109,031**	116,560

The fair value of the plan assets were as follows:

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Equities	**36,557**	58,062	**33,577**	55,194
Government debt	**18,244**	14,760	**18,244**	14,760
Corporate bonds	**19,209**	29,630	**14,829**	25,415
Annuities	**4,870**	5,074	**4,870**	5,074
Hedge funds	**22**	2,918	**22**	2,918
Other	**40,674**	16,265	**37,489**	13,199
	119,576	126,709	**109,031**	116,560

Expense recognised in the income statement relating to defined benefit obligation

	Group	
	2018 £000	2017 £000
Service cost	**3,468**	1,977
Net interest on the net defined benefit liability (note 6)	**232**	473
Total	**3,700**	2,450

Service costs and net interest are charged to Administration expenses and Net finance costs respectively. Included within the service cost for 2018 is an amount of £1,214,000 for guaranteed minimum pensions ('GMP') equalisation, this is included within non-underlying costs. GMPs must be equalised across males and females, and as a result of clarity in legislation the Company have added 1.1% to the liabilities as at 31 December 2018.

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

	Group	
	2018 £000	2017 £000
Net remeasurement – financial	**(14,874)**	6,827
Net remeasurement – demographic	**(1,005)**	(4,598)
Net remeasurement – experience	**281**	(6,552)
Return on assets, excluding interest income	**7,036**	(4,804)
	(8,562)	(9,127)

Principal actuarial assumptions are as follows:

	UK		Swiss	
	2018 %	2017 %	**2018 %**	2017 %
Discount rate	**2.7**	2.4	**0.8**	0.8
Future salary increases	**3.4**	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 S2PA tables with future improvements from 2007 in-line with the CMI mortality projections model CMI_2017 with a long-term rate of improvement of 1.5% per annum.**	96%(M)/98%(F) of the S2PA 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.		
UK post-retirement – current pensioners	**96%(M)/98%(F) of the S2PA tables with future improvements from 2007 in-line with the CMI mortality projections model CMI_2017 with a long-term rate of improvement of 1.5% per annum.**	96%(M)/98%(F) of the S2PA 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.		
Swiss scheme	**–**	–	**BVG 2015**	BVG 2015

20 Employee benefits continued

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

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Non-pensioner male	**24.1**	24.3	**24.1**	24.3
Pensioner male	**22.4**	22.5	**22.4**	22.5
Non-pensioner female	**26.0**	26.1	**26.0**	26.1
Pensioner female	**24.2**	24.2	**24.2**	24.2

Company

The principal actuarial assumptions for the Company are the same as those disclosed for the UK above.

Sensitivity analysis

The tables below for the UK and Swiss defined benefit plans show the impact on the defined benefit obligation of changing each of the most significant assumptions in isolation.

UK defined benefit plan

		Impact on scheme liabilities 2018		Impact on scheme liabilities 2017	
Effect in £millions	Change in assumption	**Increase**	**Decrease**	Increase	Decrease
Discount rate	0.25% movement	**(5.3)**	**5.6**	(6.3)	6.8
Rate of inflation (RPI)*	0.25% movement	**4.8**	**(4.5)**	5.7	(5.3)
Salary increases	0.25% movement	**1.1**	**(1.1)**	1.3	(1.3)
Assumed life expectancy	one year movement	**5.3**	**(5.3)**	6.1	(6.2)

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

The figures in the table as at 31 December 2018 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 2017 have been calculated by applying the same percentage increase or decrease as at 31 December 2018.

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

Swiss defined benefit plan

		Impact on scheme liabilities 2018		Impact on scheme liabilities 2017	
Effect in £millions	Change in assumption	**Increase**	**Decrease**	Increase	Decrease
Discount rate	0.25% movement	**(0.6)**	**0.7**	(0.6)	0.7
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)**	0.1	(0.1)

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

The figures in the table as at 31 December 2018 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 2017 have been calculated by applying the same percentage increase or decrease as at 31 December 2018.

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	2018 £000	2017 £000	2016 £000	2015 £000	2014 £000
Present value of defined benefit obligation	**(125,101)**	(139,048)	(141,947)	(115,849)	(117,639)
Fair value of plan assets	**119,576**	126,709	119,339	97,167	96,190
Deficit	**(5,525)**	(12,339)	(22,608)	(18,682)	(21,449)

Company	2018 £000	2017 £000	2016 £000	2015 £000	2014 £000
Present value of defined benefit obligation	**(111,592)**	(126,308)	(128,002)	(102,766)	(106,297)
Fair value of plan assets	**109,031**	116,560	109,719	86,601	86,907
Deficit	**(2,561)**	(9,748)	(18,283)	(16,165)	(19,390)

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 2018 is £363,000 (2017: £377,000). This is 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 £3,371,000 (2017: £3,149,000). Contributions amounting to £175,000 (2017: £180,000) in respect of the December 2018 payroll were paid in January 2019.

The total Group cost of operating the plans during the year was £6,839,000 (2017: £5,126,000) and, at 31 December 2018, there was an amount of £346,000 (2017: £316,000) owed to the plans, being employer and employee contributions due for December 2018, which was paid in January 2019.

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 share price 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 1 May 2018 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 64 to 72.

21 Share-based payments continued

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

Grant date/employees entitled	Number of instruments 2018	2017	Vesting conditions	Contractual life of options
Five-year Sharesave scheme granted to other employees 10 May 2013	–	36,662	Continuous service	01/07/18 – 01/01/19
Five-year Sharesave scheme granted to other employees 8 May 2014	**52,347**	52,661	Continuous service	01/07/19 – 01/01/20
Headlam Group Co-Investment Plan 2008 granted to key management 1 May 2015*	–	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	**6,404**	296,593	Continuous service	01/07/18 – 01/01/19
Five-year Sharesave scheme granted to other employees 5 May 2015	**166,036**	204,855	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	**176,048**	219,801	Continuous service	01/07/19 – 01/01/20
Five-year Sharesave scheme granted to other employees 4 May 2016	**36,701**	47,044	Continuous service	01/07/21 – 01/01/22
Headlam Group Performance Share Plan 2008 granted to key management 5 July 2017*	**239,045**	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	**104,064**	216,906	Continuous service	01/07/20 – 01/01/21
Five-year Sharesave scheme granted to other employees 3 May 2017	**19,157**	34,725	Continuous service	01/07/22 – 01/01/23
Headlam Group Performance Share Plan 2008 granted to key management 9 April 2018*	**328,596**	–	Awards will vest between 25% and 100% for performance between 'threshold' performance and 'maximum' performance	10/04/21 – 08/04/24
Three-year Sharesave scheme granted to other employees 1 May 2018	**504,141**	–	Continuous service	01/07/21 – 01/01/22
Five-year Sharesave scheme granted to other employees 1 May 2018	**75,549**	–	Continuous service	01/07/23 – 01/01/24
Total share options	**1,870,735**	1,736,813		

* Further details are provided on pages 64 to 72 of the Remuneration Report.

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

	Weighted average exercise price 2018	**Number of options 2018**	Weighted average exercise price 2017	Number of options 2017
Outstanding at the beginning of the year	**249.3**	**1,736,812**	230.9	1,794,868
Exercised during the year	**203.2**	**(525,905)**	172.2	(466,602)
Granted during the year	**238.6**	**1,007,865**	261.8	502,931
Lapsed during the year	**391.1**	**(348,037)**	346.9	(94,385)
Outstanding at the end of the year	**230.1**	**1,870,735**	249.3	1,736,812
Exercisable at the end of the year	**340.0**	**6,404**	–	–

The weighted average share price for options exercised during the year was 455.4p (2017: 591.0p).

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 2.0 years.

The fair value of services received in return for share options granted are measured by reference to the fair value of share options granted. In order to estimate the fair value of the services received the Company uses an appropriate option pricing model, either the Black–Scholes or the Monte Carlo option pricing model.

It is expected that the options will be exercised as soon as they reach maturity.

The expected volatility is based on historic volatility calculated over the weighted average remaining life of the share options.

Details of share options granted during 2018 are shown below:

2018		**Three-year Performance Share Plan 2008**	**Three-year Sharesave scheme**	**Five-year Sharesave scheme**
Number of options		**328,596**	**582,621**	**96,648**
Fair value at measurement date:				
No performance conditions		**–**	**167.9p**	**156.2p**
Performance conditions	EPS 80% & TSR 20%	**374.9p**	**–**	**–**
Share price at 31 December		**410.0p**	**410.0p**	**410.0p**
Exercise price		**–**	**354.0p**	**354.0p**
Expected volatility		**66.1%**	**66.1%**	**56.9%**
Option life		**three years**	**three years**	**five years**
Dividend yield		**5.4% p.a.**	**5.4% p.a.**	**5.4% p.a.**
Risk-free rate of interest		**0.9% p.a.**	**0.8% p.a.**	**1.1% p.a.**

Details of share options granted during 2017 are shown below:

2017		Three-year Co-Investment 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		585.0p	585.0p	585.0p
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.

21 Share-based payments continued

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

	Group		Company		Subsidiaries	
	2018 £000	2017 £000	**2018 £000**	2017 £000	**2018 £000**	2017 £000
Total expense recognised	**1,478**	1,218	**739**	403	**739**	815

22 Capital and reserves

Share capital

	Ordinary shares	
	2018	2017
Number of shares		
In issue at 1 January and 31 December – authorised	**107,840,000**	107,840,000
In issue at 1 January and 31 December – fully paid	**85,363,743**	85,363,743

	2018 £000	2017 £000
Allotted, called up and fully paid		
Ordinary shares of 5p each	**4,268**	4,268
	4,268	4,268
Shares classified in Shareholders' funds	**4,268**	4,268
	4,268	4,268

At 31 December 2018, the Company held 1,523,370 shares (2017: 856,458) in relation to treasury stock and shares held in trust for satisfying options and awards under employee share schemes. These shares 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 represented 1.8% (2017: 1.0%) of the issued share capital as at 31 December 2018 with a nominal value of £76,169 (2017: £42,823).

In the period from 1 January 2019 to 6 March 2019 no shares were purchased by the Company.

Ordinary shares

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company.

Dividends

	2018 £000	2017 £000
Interim dividend for 2017 of 7.55p paid 2 January 2018	**6,372**	–
Final dividend for 2017 of 17.25p paid 6 July 2018	**14,597**	–
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
	20,969	25,729

Interim dividends for 2018 of 7.55p per share (2017: 7.55p per share) are not provided for at 31 December 2018, but are recognised in the financial statements when the dividend is paid. The dividend was paid on 2 January 2019 and totalled £6,322,000.

The final proposed dividend of 17.45p per share (2017: 17.25p per share) will not be provided for until authorised by shareholders at the forthcoming AGM. There are no income tax consequences. The cost of the final proposed dividend will be £14,612,000.

The total value of dividends proposed but not recognised at 31 December 2018 is £20,934,000 (2017: £20,969,000).

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 arises from cash and cash equivalents, contractual cash flows of debt investments carried at amortised cost, at fair value through other comprehensive income (FVOCI) and at fair value through profit or loss (FVPL), favourable derivative financial instruments and deposits with banks and financial institutions, as well as credit exposures to wholesale and retail customers, including outstanding receivables.

For Headlam Group plc credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's trade receivables.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset and, as at the Statement of Financial Position date, in the Directors' opinion, there were no significant concentrations of credit risk likely to cause financial loss to the Group.

The Group has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed on all new customers requiring credit and these are frequently reviewed by management to limit exposure. Businesses must obtain central approval from Executive Directors or senior executive management for credit limits in excess of £10,000. The Group does not require collateral in respect of financial assets.

The credit control procedures described above, coupled with the diversified nature of the Group's trade receivables, lead the Directors to believe that there is limited credit risk exposure and that the credit quality of these assets is robust.

Other receivables comprise amounts due to the Group which historically have been received within three months of the year-end. The Directors have considered the inherent risk profile of other receivables at the year-end and are of the view that this historical experience will prevail for the foreseeable future and accordingly consider the credit quality of these assets to be robust.

Cash and cash equivalents represent deposits with reputable financial institutions in the UK and Continental Europe and hence, the Directors consider the credit quality of cash and cash equivalents to be robust.

23 Financial instruments continued

Impairment of financial assets

The Group has trade receivables for sales of inventory as financial assets that are subject to the expected credit loss model. While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial.

The carrying amount of financial assets at the Statement of Financial Position date was:

	Group		Company	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Trade and other receivables (note 15)	**114,083**	122,863	**23,217**	20,928
Derivative assets (note 15)	**–**	8	**–**	–
Cash and cash equivalents (note 16)	**44,005**	42,030	**12,573**	16,646
	158,088	164,901	**35,790**	37,574

The fair values of the above financial assets at both 31 December 2018 and 2017, are deemed to approximate to carrying value due to the short-term maturity of the instruments.

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

	2018		2017	
Group	**Gross £000**	**Impairment £000**	Gross £000	Impairment £000
Not past due	**85,822**	**(154)**	85,038	–
Past due 0 – 30 days	**2,851**	**(242)**	8,330	(415)
Past due 31–120 days	**3,417**	**(2,594)**	3,972	(2,273)
	92,090	**(2,990)**	97,340	(2,688)

All other receivables and derivative financial assets are not past due (2017: not past due).

The Company had trade receivables of £nil (2017: £nil).

The Group applies the IFRS 9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables.

The expected loss rates are based on the payment profiles of sales over a period of 36 months before 31 December 2018 or 1 January 2018 respectively and the corresponding historical credit losses experienced within this period. The historical loss rates are adjusted to reflect current and forward-looking information on macroeconomic factors affecting the ability of the customers to settle the receivables. The group sells its goods predominantly to the countries in which it is resident and therefore any changes in GDP and unemployment rates have been considered when looking to adjust the historical loss rates.

To measure the expected credit losses, trade receivables have been grouped based on shared credit risk characteristics and the days past due. The loss allowance provision as at 31 December 2018 is determined as follows;

	Not past due	**Past due 0-30 days**	**Past due 31- 120 days**	**Total**
31 December 2018				
Expected loss rate	**0.2%**	**8.5%**	**75.9%**	
Gross carrying amount – trade receivables	**85,822**	**2,851**	**3,417**	**92,090**
Loss allowance	**154**	**242**	**2,594**	**2,990**

The loss allowance provision for trade receivables as at 31 December 2017 is the same as the balance reported and therefore no restatement is necessary through the opening retained earnings for 1 January 2018.

The maximum exposure to credit risk for trade receivables at the Statement of Financial Position date by geographic region was:

	Group 2018 £000	Group 2017 £000	Company 2018 £000	Company 2017 £000
UK	**76,640**	81,989	**–**	–
Continental Europe	**12,460**	12,663	**–**	–
	89,100	94,652	**–**	–

During the year the Group's impairment loss as a percentage of revenue amounted to 0.19% (2017: 0.17%).

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 2018, cash and cash equivalents covered the amounts of borrowings maturing in the next 12 months with a net positive liquidity of £43,548,000 (2017: £41,797,000). 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 2018 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	**221**	**(221)**	**(221)**	**–**	**–**	**–**
Unsecured bank loans	**7,041**	**(7,335)**	**(313)**	**(310)**	**(6,712)**	**–**
Trade and other payables	**164,508**	**(164,508)**	**(164,508)**	**–**	**–**	**–**
Derivative financial liabilities						
Other derivatives	**23**	**(23)**	**(23)**	**–**	**–**	**–**
	171,793	**(172,087)**	**(165,065)**	**(310)**	**(6,712)**	**–**

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 2018 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	**32,112**	**(32,112)**	**(32,112)**	**–**	**–**

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)	–	–

The value of the Group's and Company's financial liabilities as detailed above at 31 December 2018 and 2017 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.

23 Financial instruments continued

The table below sets out the Group's accounting classification of each class of financial assets and liabilities at 31 December 2018 and 2017.

31 December 2018	Fair value through profit or loss (FVPL) £000	Amortised cost £000	Total Carrying Value £000
Cash and cash equivalents	–	**44,005**	**44,005**
Bank overdraft	–	**(221)**	**(221)**
Borrowings due within one year	–	**(236)**	**(236)**
Borrowings due after one year	–	**(6,805)**	**(6,805)**
Trade payables	–	**(142,382)**	**(142,382)**
Non-trade payables	**(416)**	**(24,002)**	**(24,418)**
Trade receivables	–	**89,100**	**89,100**
Other receivables	–	**24,983**	**24,983**
Provisions	–	**(2,249)**	**(2,249)**
Derivative liability	**(23)**	–	**(23)**
	(439)	**(17,807)**	**(18,246)**

31 December 2017	Other derivatives at fair value £000	Amortised cost £000	Total Carrying Value £000
Cash and cash equivalents	–	44,005	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 liability	(8)	–	(8)
	(8)	(21,190)	(21,182)

All derivative financial instruments not in a hedge relationship are measured at fair value through the profit or loss. 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	
	2018 £000	2017 £000	**2018 £000**	2017 £000
Variable rate instruments				
Financial assets	**44,005**	42,030	**12,573**	16,646
Financial liabilities	**(7,262)**	(6,752)	**–**	–
	36,743	35,278	**12,573**	16,646

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 2017.

	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 2018								
Variable rate instruments	**367**	**(367)**	**–**	**–**	**126**	**(126)**	**–**	**–**
31 December 2017								
Variable rate instruments	353	(353)	–	–	166	(166)	–	–

Commodity risk

The Company and Group are exposed to the commodity risk of rising fuel prices however on 31 December 2018 there were no commodity transaction swaps entered into by the Group.

Foreign currency risk

The Group and Company are exposed to movements in currency exchange rates arising from transaction currency cash flows and the translation of the results and net assets of overseas subsidiaries. The currencies giving rise to this risk are primarily the euro, Swiss franc and US dollar.

The Group and Company use forward exchange contracts to hedge their foreign currency transactional risk. A future foreign currency contract would be entered into where there was a known requirement for the currency due to planned imports that are not invoiced in the functional currency of the acquiring company. These forward exchange contracts would have a maturity of less than one year after the Statement of Financial Position date. The Group also enters into foreign currency contracts at spot rate where the amounts are not frequent or material. Gains and losses on currency contracts recognised as a liability at 31 December 2018 amounted to £23,000 (2017: asset of £8,000).

Hedge ineffectiveness

Hedge effectiveness is determined at the inception of the hedge relationship, and through periodic prospective effectiveness assessments to ensure that an economic relationship exists between the hedged item and hedging instrument. For hedges of foreign currency purchases, the Group enters into hedge relationships where the critical terms of the hedging instrument match exactly with the terms of the hedged item. The Group therefore performs a qualitative assessment of effectiveness. If changes in circumstances affect the terms of the hedged item such that the critical terms no longer match exactly with the critical terms of the hedging instrument, the Group uses the hypothetical derivative method to assess effectiveness. In hedges of foreign currency purchases, ineffectiveness may arise if the timing of the forecast transaction changes from what was originally estimated, or if there are changes in the credit risk of Headlam Group plc or the derivative counterparty. The Group now enters into forward rate agreements containing a delivery period in which the entity can drawdown the currency as they require it, subject to a final delivery date. This has enabled the Group to match the forward rate agreements to the hedged item with accuracy.

For the 12-month period to 31 December 2018, 1.2% (2017: 3.1%) of the Group's operating profit was derived from overseas subsidiaries and at 31 December 2018, 17.5% (2017: 18.8%) 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.

23 Financial instruments continued

The exposure to foreign currency risk was as follows:

2018	Group Euro amount £000	Group Other amount £000	Group Total £000	Company Euro amount £000	Company Other amount £000	Company Total £000
Trade and other receivables	**336**	**3**	**339**	**–**	**–**	**–**
Cash and cash equivalents	**2,791**	**38**	**2,829**	**244**	**–**	**244**
Trade and other payables	**(7,569)**	**(1,324)**	**(8,893)**	**–**	**–**	**–**
	(4,442)	**(1,283)**	**(5,725)**	**244**	**–**	**244**

2017	Group Euro amount £000	Group Other amount £000	Group Total £000	Company Euro amount £000	Company Other amount £000	Company 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

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 2017.

	Group 2018 £000	Group 2017 £000	Company 2018 £000	Company 2017 £000
Euro	**(444)**	(501)	**24**	5
Other	**(128)**	(125)	**–**	–

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 forward currency contracts which were fair valued in accordance with level 2 (2017: 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. During the year 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 2018 and 31 December 2017.

24 Acquisitions
On 2 March 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of Dersimo BV ('Dersimo') located in the western Netherlands. Dersimo is a full service distributor of both soft and hard floors from a combination of well-known manufacturer brands as well as its own carpet and vinyl designs which are manufactured as a private label. The Dersimo acquisition is complementary to the Company's market-leading core business which supplies a high volume of small orders into both the residential and commercial sectors and increases the Company's presence and geographical coverage in the Netherlands.

On 30 March 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of BETU Holdings Limited (a non-trading holding company) the parent company of CECO (Flooring) Limited ('CECO'). CECO is a leading provider of flooring and wallcovering products to retail and commercial customers throughout Northern Ireland and the Republic of Ireland. The CECO acquisition diversifies and broadens the Company's overall position in the commercial specification market.

On 1 July 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of Ashmount Flooring Supplies Limited ('Ashmount')a floorcovering distribution business based in Tottenham, North London. The Ashmount acquisition expands the Company's presence in commercial products in Greater London, a geographic area in which the Company has historically had a low market share.

On 28 September 2018, a subsidiary company of Headlam Group plc entered into an agreement to acquire 100% of the share capital of Rackhams Limited ('Rackhams') located in Highams Park, East London. Established in 1935, Rackhams is a leading provider of retail and commercial products to customers in Greater London and the surrounding counties with a strong Rackhams 'brand' having been developed in recent years. The Rackham's acquisition expands the Company's presence in commercial products in Greater London, a geographic area in which the Company has historically had a low market share.

On 26 October 2018, a subsidiary company of Headlam Group plc completed the acquisition of all the trade and assets of Garrod Bros Ltd ('Garrod Bros') located in Enfield, North London. Established in 1827, Garrod Bros is a leading provider of commercial flooring products and accessories to customers in Greater London. The Garrod Bros acquisition expands the Company's presence in commercial products in Greater London, a geographic area in which the Company has historically had a low market share.

Both the Rackhams and Garrod Bros acquisitions are currently subject to a merger inquiry by the Competition and Markets Authority ('CMA').

The acquired businesses contributed revenues of £13.7 million and an operating profit of £0.6 million to the Group for the year ended 31 December 2018. If the acquisitions had occurred on 1 January 2018, pro-forma revenue and operating profit for the year ended 31 December 2018 would have increased to £717.7 million and £42.0 million respectively.

24 Acquisitions continued

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	–	3,598	3,598
Goodwill	653	(653)	–
Property, plant and equipment	1,321	–	1,321
Inventories	2,545	(233)	2,312
Trade and other receivables	3,225	(44)	3,181
Cash at bank and in hand	2,615	–	2,615
Trade and other payables	(3,160)	(83)	(3,243)
Provisions	(74)	(150)	(224)
Borrowings	(435)	–	(435)
Deferred tax	(2)	(525)	(527)
Net identifiable assets and liabilities	6,688	1,910	8,598
Goodwill on acquisition		4,426	4,426
Consideration			13,024
Satisfied by:			
Cash			11,356
Deferred and contingent consideration			1,668
			13,024
Analysis of cash flows:			
On completion			10,921
Borrowings repayment			435
Cash acquired			(2,615)
			8,741

Professional fees of £0.5 million were incurred in relation to acquisition activity and have been expensed to the income statement within non-underlying administration expenses.

The book value of receivables given in the table above represents both the gross contracted and fair value of amounts receivable. At the acquisition date, the entire book value of receivables was expected to be collected.

Goodwill of £4.4 million arose on the acquisitions, there were also intangible assets on acquisition of £3.6 million which were attributed to brand names, order book, non-compete agreements and customer relationships. During the year £0.5 million of intangibles have been amortised to the income statement on these acquisitions.

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.

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 CECO was financed by initial cash consideration of £4.3 million paid on completion and satisfied from the Group's existing cash and debt facilities and deferred consideration of £1.4 million. On 3 August 2018 the first of the deferred consideration of £400,000 was paid.

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.

Prior year acquisitions
In the prior year the Group acquired Mitchell Carpets Limited, Domus Group of Companies Limited and its subsidiary entities and the business and certain assets of McMillan Flooring.

The fair values of the assets and liabilities acquired have been reconsidered as part of the hindsight period but no adjustment was considered necessary. In relation to Domus Group of Companies Limited the contingent consideration has been decreased as a result of a change in forecast future profitability.

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 to £721.9 million and £44.6 million respectively.

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 from 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. The contingent consideration has been further reduced as at 31 December 2018 based on the EBITDA achieved to date.

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:

	2018			2017		
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	**4,560**	**10,359**	**14,919**	3,243	9,569	12,812
Between one and five years	**9,176**	**18,420**	**27,596**	7,341	16,796	24,137
More than five years	**6,059**	**1,862**	**7,921**	4,478	641	5,119
	19,795	**30,641**	**50,436**	15,062	27,006	42,068

	2018			2017		
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**	**13**	**39**	26	8	34
Between one and five years	**105**	**17**	**122**	105	10	115
More than five years	**1,776**	**–**	**1,776**	1,802	–	1,802
	1,907	**30**	**1,937**	1,933	18	1,951

The Group leases the majority of its motor and commercial vehicles on terms that range between three and seven years and during the year ended 31 December 2018, total operating lease expense of £15,489,000 was recognised in the Consolidated Income Statement (2017: £13,211,000).

26 Capital commitments

Group

During the year ended 31 December 2018, the Group entered into commitments to purchase property, plant and equipment for £743,000 (2017: £358,000). These commitments are expected to be settled in the following financial year.

Company

At 31 December 2018, the Company had no commitments to purchase property, plant and equipment (2017: £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 50 and 51.

As at 31 December 2018, Directors of the Company and their immediate relatives controlled 0.9% of the total voting rights of the Company (2017: 0.8%).

Non-Executive Directors receive a fee for their services to the Board.

Other than as disclosed in the Remuneration Report, there were no other transactions with key management personnel in either the current or preceding year. The cost charged to administrative expenses relating to share plans of key personnel amounted to £638,000 (2017: £507,000).

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 2018 £000**	Highest during the year £000	Balance at 31 December 2017 £000
Amounts due from subsidiaries	**24,605**	**24,605**	20,460	20,460
Amounts due to subsidiaries	**(26,900)**	**(26,900)**	(34,806)	(34,806)

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 2018 £000	For year ended 31 December 2017 £000
Rental income	**7,971**	7,971
Dividends received	**32,208**	38,378
Recharge of operating expenses	**3,380**	3,140
Interest income	**379**	163

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.

29 Group subsidiaries

Company	Type	Place of incorporation
HFD Limited	Trading	Great Britain*
MCD Group Limited	Trading	Great Britain*
CECO (Flooring) Limited	Trading	Great Britain******
Domus Tiles Limited	Trading	Great Britain*
Rackhams Limited	Trading	Great Britain*
Headlam BV	Trading	Netherlands**
Dersimo BV	Trading	Netherlands*****
LMS SA	Trading	France***
Belcolor AG	Trading	Switzerland****
Headlam (European) Limited	Holding Company	Great Britain*
Betu Holdings Limited	Holding Company	Great Britain******
Headlam Holdings BV	Holding Company	Netherlands**
Headlam SAS	Holding Company	France***
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*
Yourfloors Plc	Dormant	Great Britain*
Crossforge 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*
Ashmount Flooring Supplies 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 these 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.
***** Registered address for this Dutch subsidiary: Noordzee 12, 3144 DB, Maassluis, the Netherlands.
****** Registered address for these UK subsidiaries: Unit 5 Carryduff Business Park, Comber Road Carryduff, Belfast, County Down, BT8 8AN

FINANCIAL RECORD

	2018 £000	Restated*** 2017 £000	Restated* & *** 2016 £000	Restated* & *** 2015 £000	Restated** & *** 2014 £000
Trading results					
Revenue	**708,423**	692,540	677,722	639,260	620,803
Gross profit	**229,074**	218,104	210,205	198,693	188,649
Overheads	**(184,801)**	(174,321)	(169,133)	(161,916)	(157,187)
Underlying profit before net financing costs	**44,273**	43,783	41,072	36,777	31,462
Net financing costs	**(884)**	(665)	(966)	(1,153)	(1,162)
Underlying profit on ordinary activities before tax	**43,389**	43,118	40,106	35,624	30,300
Taxation	**(7,750)**	(7,976)	(7,601)	(7,213)	(6,515)
Underlying profit on ordinary activities after taxation	**35,639**	35,142	32,505	28,411	23,785
Profit before tax	**40,447**	40,719	38,179	35,624	30,300
Shareholder value					
Paid interim and final dividend per share	**24.8p**	22.55p	20.70p	17.50p	15.30p
Paid special dividend per share	**–**	8.00p	6.00p	–	–
Proposed dividend per share	**25.0p**	24.8p	22.55p	20.70p	17.50p
Earnings per share	**40.0p**	39.1p	36.8p	33.8p	28.6p
Underlying earnings per share	**42.5p**	41.7p	38.7p	33.8p	28.6p
Net assets					
Non-current assets					
Property, plant and equipment	**102,048**	101,631	102,934	104,677	106,875
Intangible assets	**50,924**	44,662	10,388	10,388	10,013
Deferred tax assets	**516**	648	1,138	629	515
	153,488	146,941	114,460	115,694	117,403
Current assets					
Inventories	**132,704**	131,566	126,037	118,165	115,591
Trade and other receivables	**119,007**	127,976	128,934	120,300	118,962
Cash and cash equivalents	**44,005**	42,030	59,343	63,932	47,589
	295,716	301,572	314,314	302,397	282,142
Total assets	**449,204**	448,513	428,774	418,091	399,545
Current liabilities					
Bank overdraft	**(221)**	–	(4)	–	–
Other interest-bearing loans and borrowings	**(236)**	(233)	(224)	–	(204)
Trade and other payables	**(181,300)**	(190,299)	(183,304)	(171,375)	(165,240)
Employee benefits	**–**	(2,235)	(2,169)	(2,171)	(2,933)
Income tax payable	**(6,730)**	(6,339)	(6,824)	(6,974)	(6,073)
	(188,487)	(199,106)	(192,525)	(180,520)	(174,450)
Non-current liabilities					
Other interest-bearing loans and borrowings	**(6,805)**	(6,519)	(6,493)	(20,000)	(22,818)
Trade and other payables	**(2,592)**	(4,938)	–	–	–
Provisions	**(2,249)**	(2,048)	(1,531)	(1,087)	(787)
Deferred tax liabilities	**(8,063)**	(6,847)	(4,077)	(4,533)	(3,931)
Employee benefits	**(5,888)**	(10,481)	(20,781)	(16,843)	(18,803)
	(25,597)	(30,833)	(32,882)	(42,463)	(46,339)
Total liabilities	**(214,084)**	(229,939)	(225,407)	(222,983)	(220,789)
Net assets	**235,120**	218,574	203,367	195,108	178,756

* The balance sheets for 2015 and 2014 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.

*** The Condensed Consolidated Interim Income Statement for the years ended 31 December 2017, 2016, 2015 and 2014 have been restated to reclassify a number of items between revenue, cost of sales, and operating expenses in order to more appropriately reflect their nature. Consequently, these adjustments mean the earlier periods are presented in a consistent manner with the year ended 31 December 2018.

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Financial Calendar

Statutory Meeting and Announcements	
Annual General Meeting	24 May 2019
Interim results announced	28 August 2019
Final results announced	March 2020

Dividend Dates	
Final dividend for 2018, if approved, payable to qualifying shareholders on the register as at 7 June 2019	1 July 2019
Interim dividend for 2019 declared	28 August 2019
Interim dividend for 2019 payable	2 January 2020

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