Preliminary results for the year ended 31 March 2016

27 May 2016

Highlights

- Progress in all key focus areas leads to year on year growth
- Important progress in Enterprise market
- Accelerated fibre deployment in Hull and East Yorkshire
- National network asset disposal for £90m, with associated book profit of £44.5m
- Strong net year end funds of £7.4m, reflecting network sale proceeds and increase in net cash inflow from operations
- Proposed final dividend of 3.94p (2015: 3.58p); full year dividend of 5.91p (2015: 5.37p)
- Dividend guidance for next two years reiterated at a minimum of 6.0p per annum

Financial performance

Paul Simpson

Chief Financial Officer

Summary financial results

	Mar 16 £m	Mar 15 £m	
Revenue	349.2	348.0	0.4% growth
EBITDA	74.9	74.3	0.8% growth
EBITDA %	21%	21%	Consistent margin
Operating profit	50.9	57.2	£6.9m increase in D&A
Adjusted basic EPS (pence)*	7.54	7.91	As above
Adjusted net cash inflow from operations**	62.4	50.8	Improvement in working capital
Net funds / (debt)	7.4	(99.3)	National network proceeds
Full year dividend per share (pence)	5.91	5.37	In line with guidance

All amounts are before exceptional items.
* Adjusted basic EPS is basic EPS adjusted for exceptional items (including the tax impact of the exceptional items).
**Adjusted net cash inflow from operations adjusted for £18m VAT balance due to national network disposal, paid post year-end.

Segment performance

FY16 existing segments

	Revenue		EBITDA	
	Mar 16	**Mar 15**	**Mar 16**	**Mar 15**
	£m	**£m**	**£m**	**£m**
KC	104.5	104.8	56.3	56.4
Kcom	249.9	248.6	26.1	25.7
PLC	(5.2)	(5.4)	(7.5)	(7.8)
	349.2	**348.0**	**74.9**	**74.3**

FY16 on new segment basis

	Revenue		Contribution	
	Mar 16	**Mar 15**	**Mar 16**	**Mar 15**
	£m	**£m**	**£m**	**£m**
Hull and East Yorkshire	104.5	104.8	71.2	71.3
Enterprise	147.7	141.6	29.8	25.9
SMB National	102.2	107.0	24.3	25.9
Total Contribution			**125.3**	**123.1**
Eliminations/shared costs	(5.2)	(5.4)	(50.4)	(48.8)
			EBITDA	
KCOM	**349.2**	**348.0**	**74.9**	**74.3**

For FY17, our operating segments are Hull and East Yorkshire, SMB National, Enterprise and Shared. KCOM has one EBITDA with segment profitability now being measured at contribution level (gross margin plus certain direct costs).

Enterprise

	Mar 16 £m	Mar 15 £m	Movement £m
Revenue	**147.7**	**141.6**	**4%**
Margin	**44.4**	**43.4**	**2%**
Margin %	*30%*	*31%*	
Contribution	**29.8**	**25.9**	**15%**
Contribution %	*20%*	*18%*	

Continued success in cloud communications

- HMRC growth due to high project activity in year, delivering services such as debt management, tax-credits and multi-channel
- Position as trusted technology partner has led to the recent contract win with BUPA and preferred supplier status with Shoosmiths
- Strong progress in consultancy and project delivery, with recent additional contract wins with ATOC

Non renewal of certain contracts anticipated in the year, due to refocusing technology partners and exiting certain legacy activities, with annualised revenue impact of approximately £27m

Hull and East Yorkshire

	Mar 16 £m	Mar 15 £m	Movement
Revenue			
Consumer	54.7	53.4	2%
B2B	31.2	30.3	3%
Wholesale	11.6	12.0	(3%)
Contact & Publishing	7.0	9.1	(23%)
	104.5	**104.8**	**-**
Contribution	**71.2**	**71.3**	**-**
Contribution %	*68%*	*68%*	

Consumer and B2B growth of 3% in part due to strong take up of fibre:

- Consumer increase of 2%, reflecting primarily an increase in ARPU
- 1,700 business have taken fibre, of which 1,000 benefitted from the government's superfast broadband initiative
- 50% take-up of fibre for businesses passed

Fibre roll-out further accelerated targeting 150,000 premises passed by December 2017

SMB National

	Mar 16 £m	Mar 15 £m	Movement £m
Revenue			
Partners	47.1	50.4	(7%)
SMB	55.1	56.6	(3%)
	102.2	**107.0**	**(4%)**
Margin	**36.8**	**36.7**	**0%**
Margin %	*36%*	*34%*	
Contribution	**24.3**	**25.9**	**(6%)**
Contribution %	*24%*	*24%*	

- Continue to experience growth in the broadband and related connectivity despite a background of a maturing market
- Partners revenue impacted by certain declining or ceased contracts

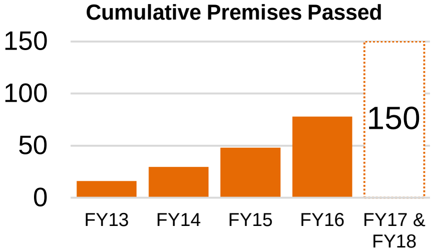
Sale of national network

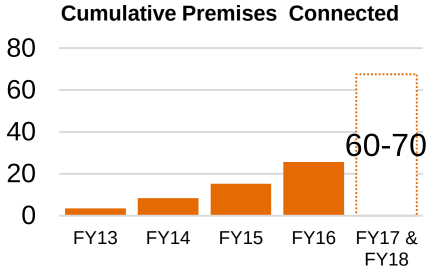
Key Metrics	£m
Sale Proceeds	90
Associated costs	(3)
Net funds	**87**
Tax effect in year	7

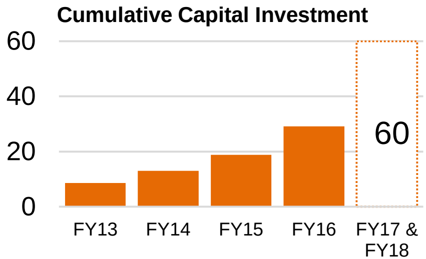
	Mar 16 £m
Proforma EBITDA	**70**

- National network asset disposal for £90m strengthening the balance sheet
- Net funds position at the year-end included £18m VAT due to timing paid post year end
- Tax impact going forward of £12m in allowances lost over future years
- Net additional costs paid to CityFibre for continued use of the national network - full year impact is £4m

Fibre roll-out







- Commitment to reach 150k premises by December 2017
- Level of take-up remains high, with 26k premises connected by the end of FY16 (both consumer and business)
- Current deployment methodology and capital investment is a function of both:
    - Passing costs – fixed for each geographic area that is fibre enabled
    - Connection costs – are variable based on customer demand for fibre
- Acceleration of current deployment methodology means investment over next two years is equivalent to cumulative spend to the end of FY16 (£29m) and will take overall investment to £60m
- Average ARPU uplift of consumers remains approximately £5 per month. Based on current experience of passing and connecting costs, payback varies dependent upon take up in area:

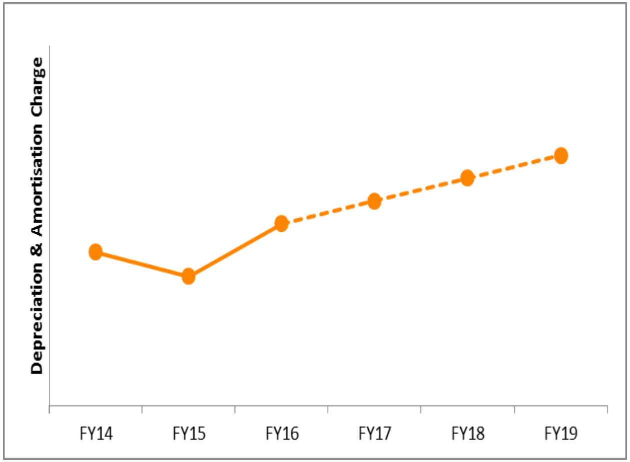
Take Up	30%	50%	100%
Payback (years)	15	11	8

- We continue to review deployment methodology in order to optimise cost but most importantly to unlock benefits from improved customer experience and reduced operating cost from a fully fibre enabled network

Investment

Fixed asset additions by category:	FY14	FY15	FY16
	£m	£m	£m
Fibre roll out	4.4	5.8	10.0
Strategic IT Investment	6.6	11.0	1.2
Workplaces	4.1	9.9	6.1
Key investment areas	**15.1**	**26.7**	**17.3**
Other investment	19.5	13.3	18.9
Total investment	**34.6**	**40.0**	**36.2**

Depreciation & amortisation			
On key investment areas	0.7	2.3	8.7



Net funds / debt

	Mar 16 £m	Mar 15 £m
EBITDA reported	115.8	39.5
Working capital movement	5.4	(14.7)
VAT relating to national network disposal	18.0	-
Exceptional items – non cash (impairment)	-	33.9
Pensions	(6.6)	(4.3)
Profit on sale of national network	(44.5)	-
Other operating cash items	(7.7)	(3.7)
Net cash inflow from operations	**80.4**	**50.8**
Capital expenditure - cash	(31.3)	(32.0)
Interest	(2.8)	(5.6)
Dividends	(28.7)	(26.1)
Share purchases & dividend equivalents	(0.5)	(4.6)
Other	(0.3)	-
Proceeds from sale of assets	90.0	-
Decrease / (increase) in net bank debt / funds1	**106.8**	**(17.5)**
Net increase in finance lease liabilities	(0.1)	(6.9)
Decrease / (increase) in net debt / funds	**106.7**	**(24.4)**
Net (funds) / debt: EBITDA ratio[2]	(0.1) x	1.3 x

[1] Net bank debt is net debt excluding finance leases

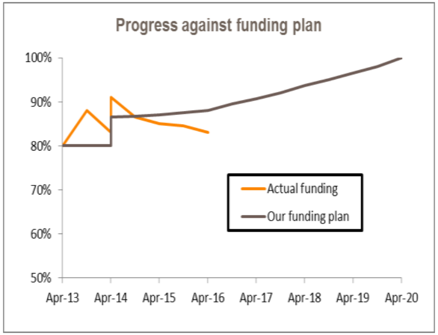
[2] EBITDA is before exceptional items

- The disposal of our national network results in a year end net funds position
- Working capital inflow results in part from timing (including £18m VAT on the transaction paid to HMRC in April 2016), and a 6 day reduction in day sales outstanding at March 2016 compared to March 2015
- Other cash movements related to expected increases in pensions and dividend payments offset by lower interest payments following the repayment of bank debt

Pensions

	Mar 16 £m	Mar 15 £m
Fair value of assets	213.1	208.8
Present value of defined benefit obligation	(227.5)	(240.2)
Retirement benefit obligation	**(14.4)**	**(31.4)**

Assumptions	**%**	**%**
Discount rate	3.45	3.25
RPI	2.95	2.95



- Triennial valuation will show a deficit, on an actuarial basis in excess of the IAS 19 deficit reflected in the financial statements
- Increase in assets due to company contributions, including a £2m prepayment in March 2016, higher investment returns and decrease in liabilities due to increase in the discount rate
- Committed deficit recovery payments over next 3 years are £6.7m plus inflation

	FY17	FY18	FY19	FY20	FY21
Asset backed rental payments	2.7	2.7	2.8	2.8	2.9
Deficit Recovery (Per March 13 Triennial valuation)	6.7	6.8	6.9	6.9	-
Agreed	**9.4**	**9.5**	**9.7**	**9.7**	**2.9**
Additional Budgeted for Deficit Recovery	1.0	1.0	1.0	1.0	-
Total Budget	**10.4**	**10.5**	**10.7**	**10.7**	**2.9**

Excludes KC Data scheme

Continuing our transformation journey

Bill Halbert

Chief Executive Officer

A year of further progress

- Launch of business under a single brand
- Simplified and unified business
- Growing disruptive reputation in the enterprise market
- Continued high take-up of fibre in Hull and East Yorkshire
- Tightened market focus
- Disposal of national network asset creates strong balance sheet with capacity to invest

We make life easier and better for our customers by creating greater value from the way they interact, collaborate and connect with what matters to them.

Enterprises

Organisations with complex needs look to us to help them integrate and leverage technology including contact, collaboration and cloud-based services

Our customers in this market include →

NFU Mutual
AVIVA
ATOC
Bupa
HM Revenue & Customs
SHOOSMITHS

Businesses

We help businesses embrace the power of technology to become more successful

Our customers in this market include →

The Range
Hull College Group
FootAnstey
Furniture Village
Lifeboats
RSPB

Consumer and small businesses

Customers across Hull and East Yorkshire can choose from our range of voice, broadband and TV services to suit their needs

Our customers in this market include →

More than 140,000 customers in Hull and East Yorkshire

Consumer and small businesses

Fibre deployment accelerated

Take-up of over 40%

Future-proof capability

Over the top service development

SMB

Focus at higher end of market

Declining revenue in some service areas

No material investment planned

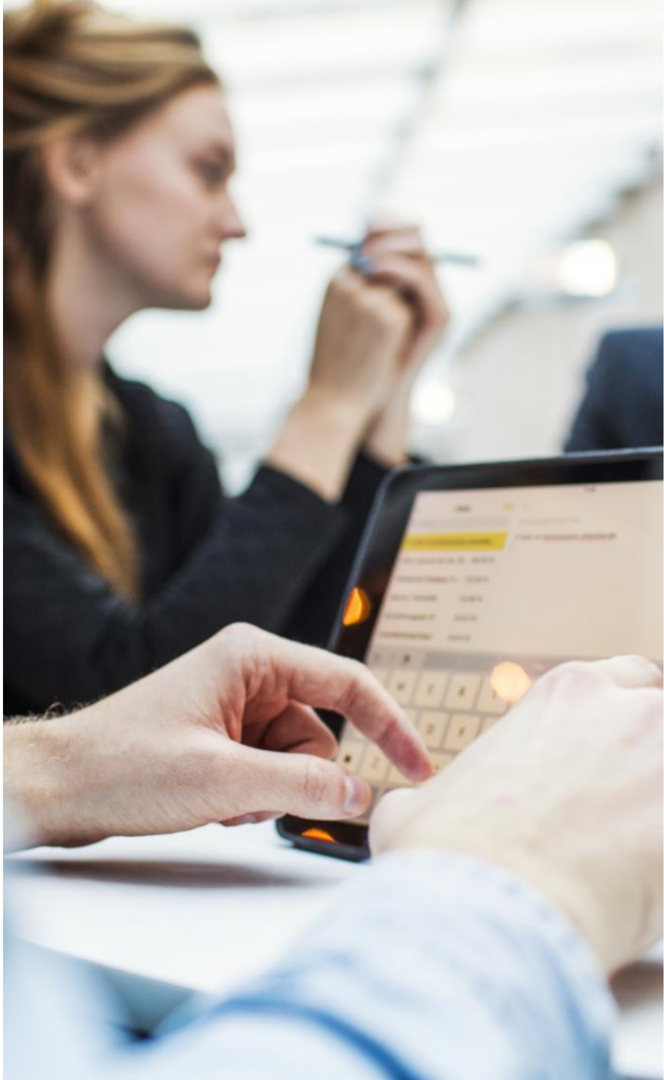
Enterprise

Growing reputation

Further business from existing customers

New customers

Combined capability focused on technology-enabled business transformation



Outlook

- Exploit growth opportunities in enterprise and regional market
- Continued fibre deployment and related fibre enabled services
- Increased investment in coming year
- Further investment in our systems capability to facilitate our journey towards an efficient single business
- Transformation of our existing network technologies
- Minimum 6p per share dividend in each of the next two financial years